



Hilton Worldwide Holdings, Inc.

Q2 2015 Earnings Call

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C O R P O R A T E P A R T I C I P A N T S

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Kevin Jacobs, *Executive Vice President and Chief Financial Officer*

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C O N F E R E N C E C A L L P A R T I C I P A N T S

Harry Curtis, *Nomura Securities International, Inc.*

Joe Greff, *JP Morgan*

Smedes Rose, *Citigroup*

Felicia Hendrix, *Barclays*

Shaun Kelly, *Bank of America*

Jeff Donnelly, *Wells Fargo Securities*

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Chad Beynon, *Macquarie*

P R E S E N T A T I O N

Operator:

Good morning. My name is Leanne and I will be your Conference Operator today. At this time, I would like to welcome everyone to the Hilton Worldwide Holdings Q2 2015 Earnings. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question and answer session. If you would like to ask a question during this time, simply press star, then the number one on your telephone keypad. If you would like to withdraw your question, please press the pound key.

Thank you. Christian Charnaux, you may begin.

Christian Charnaux:

Thank you, Leanne. Welcome to the Hilton Worldwide Second Quarter 2015 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 the forward-looking statements, and forward-looking statements made today are effective only as of today. We undertake no obligation to publicly 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 www.hiltonworldwide.com.

This morning, Chris Nassetta, our President and Chief Executive Officer, will provide an overview of our second quarter results and will describe the current operating environment, as well as the Company's outlook for the remainder of 2015. Kevin Jacobs, our Executive Vice President and Chief Financial Officer, will then provide greater detail on our results and outlook. Following their remarks, we will be available to respond to your questions.

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

Christopher Nassetta:

Thanks, Christian. Good morning, everyone, and thanks for joining us today. We're pleased to report another strong quarter, with Adjusted EBITDA and earnings per share above the high end of our guidance.

We continue to feel great about the fundamentals, which should continue to support strong performance going forward. As a result, we've raised our full-year Adjusted EBITDA and EPS guidance. Given our confidence in the outlook and the significant deleveraging we've achieved, we are also pleased to commence returning capital to shareholders, with the declaration this morning of our first quarterly cash dividend. Kevin will cover this in more detail later in his remarks, but we intend to grow our dividend over time as earnings grow, and we believe we should be able to initiate a share buyback program next year.

Turning to our performance in the quarter, system-wide comp RevPAR grew 5.2% on a currency neutral basis. May was somewhat softer than expected, largely due to weaker transient business caused by weather in the southern and central US, and demand declines across oil and gas markets, impacting quarterly RevPAR growth by approximately 100 basis points. However, transient growth for the quarter

was still relatively strong, up over 5% system-wide, and strengthened significantly in June, continuing into July.

Group business was strong in the quarter, as system-wide group revenue increased over 6% at our comparable Americas Owned and Operated hotels, largely driven by company meetings that were up over 10% in the quarter, with particular strength in the Chicago, New Orleans and Hawaii markets.

Favorable mix shifts also continued to support ancillary spend, with F&B at owned and operated hotels growing 7% in the quarter.

Group position continues to track up in the mid-single-digits for the balance of this year and into 2016. We expect to see a strong second half of the year in group, with the fourth quarter outpacing the third quarter, largely due to holiday shifts.

Turning to development, our system growth continues to both lead the industry and gain in momentum. According to STR, we increased our industry-leading position in both pipeline and rooms under construction in the quarter.

We are on track to have a record number of signings this year, roughly 90,000 rooms, continuing to grow the largest pipeline in our Company's history, all with de minimus amounts of our capital and no acquisitions.

In the quarter, we opened 82 hotels, totaling more than 11,000 rooms, bringing our total supply to 4,440 properties and more than 730,000 rooms. With the opening of the Hilton Aruba Caribbean Resort and the Hilton Garden Inn Guatemala City earlier this month, we are now present in 97 countries and territories. Including all approved deals, our pipeline stands at nearly 265,000 rooms. As of today, we have 1 million rooms open or under development, and expect to be in 100 countries and territories by the end of the year.

Net unit growth adds to our ability to serve customers anywhere in the world for any travel need they have, driving significant loyalty to our system that continues to enhance our industry-leading RevPAR index premiums. To serve even more customers, we continue to globally deploy our existing brands and launch new brands, like Home2, Curio and Canopy, and soon a new mid-scale brand.

We now have nearly 60 Home2s open, with over 225 more in the pipeline. Year to date, we have signed or approved nearly 80 new Home2s, and continue to build significant momentum with developers. Curio just celebrated its first anniversary, with nearly 50 properties and 13,000 rooms open or in various stages of development, and with its first international hotels opening this month in the Caribbean, Europe and Latin America. We also continue to see tremendous interest from owners within Canopy, with over 20 hotels and 3,500 rooms either in the pipeline or with signed Letters of Intent. We expect the first Canopy to open Reykjavik, Iceland, early next year.

We intend to launch our new mid-scale brand in the first quarter of 2016, largely targeting new customers for our system at a price point below the Hampton brand. We believe the target market is about 40% of US room night demand, demand that our current system largely does not serve. We have already received tremendous interest from our owners on this brand and our goal is to have a system size larger than Hampton over time, with next to no capital investment on our part.

Our portfolios of brands, from Waldorf to Hampton, and soon to include our mid-scale brand, are linked together by our Hilton Honors Program, and our enhanced Honors app is at the center of making our system more rewarding and attractive to guests. Fully integrated into our back-end systems, the Honors app allows guests to check in and select a room at over 4,100 hotels globally today, with straight-to-room capabilities via a digital key now rolling out at scale, with hundreds of hotels expected to offer this service

by year end. Our award-winning Honors app has been downloaded nearly 5 million times, and nearly one in four Honors arrivals are using digital check-in and room selection today, totaling nearly 5 million digital check-ins to date and approaching 1 million mobile check-ins per month. Guest feedback has been really positive, with the Honors app receiving the highest average Apple Store customer rating amongst all hotel apps since its relaunch.

Now, let me update you on the outlook for the remainder of the year. Overall, the fundamentals of the cycle remain very solid and we continue to expect 5% to 7% system-wide RevPAR growth in 2015.

In the US, we expect 5% to 7% RevPAR growth for the full year, supported by favorable supply and demand dynamics and growing group business, particularly in the fourth quarter. Although we expect continued pressure from softening European and Japanese inbound travel, decreases should be mitigated by continued upticks in inbound travel from other markets, particularly from China, and strong domestic leisure business.

For the Americas region outside the US, we anticipate mid-single-digit RevPAR growth for the full year, supported by solid transient in Mexico, Peru and Columbia, which should more than outweigh challenges in Brazil where economic softness continues.

We maintain our mid-single-digit RevPAR growth expectations for Europe, although prolonged challenges in France and Eastern Europe continue to temper regional performance. Leisure trends remain very strong particularly throughout Spain and Italy, as robust international inbound travel and greater local demand drive strong transient business.

For the Middle East and Africa region, we forecast low-single-digit RevPAR growth for the year, as decreasing inbound demand from Russia, Germany and Turkey continues to weigh on results in Saudi Arabia and the UAE. This inbound weakness should be largely offset by strengthening fundamentals and easy comparisons in Egypt.

In the Asia-Pacific region, we continue to expect high-single-digit RevPAR growth, supported by strong fundamentals in Japan, positive momentum in Thailand and solid performance in China. We continue to forecast 6% to 8% RevPAR growth in China for the full year, despite decelerating economic growth, due mostly to our favorable market mix and rising market share.

In summary, we're very pleased with our second quarter performance, as well as the setup for the remainder of this year and into next. We also remain very focused, first and foremost, on creating long-term value for shareholders, including exploring possible structural options for the Company. I know many of you are curious about the potential for timeshare or real estate spin opportunities, and I can tell you that we continue to explore all options and still plan to give you a full update before the year is out.

With that, I'm going to turn the call over to Kevin for further details on the quarterly results and the outlook for the rest of the year. Kevin?

Kevin Jacobs:

Thanks, Chris, and good morning, everyone. During the quarter, our RevPAR growth of 5.2% was driven by a 3.4% increase in average rate and a 1.3 percentage point increase in occupancy. In actual dollars, system-wide RevPAR increased 2.9%. RevPAR growth was 5.8% for the first half of the year, roughly two-thirds driven by rate.

Diluted earnings per share adjusted for special items was \$0.25, an increase of 19% versus the prior year period and above the high end of our guidance.

Adjusted EBITDA was \$777 million, an increase of 15% year-over-year, beating the high end of our guidance by approximately \$17 million, as fee growth significantly outperformed expectations and FX headwinds were lower than expected. We attribute \$5 million to \$10 million of the beat to timing items that should normalize during the back half of the year. For the quarter, enterprise-wide Adjusted EBITDA margins were up 320 basis points year-over-year to 41.8%.

Management and franchise fees were \$434 million in the quarter, up 17% over the second quarter of 2014, driven by strong franchise sales, new unit growth, and accelerated timing of certain items, including change of ownership and termination fees.

We continue to grow fees by increasing effective franchise rates. Through the second quarter, we have approved the relicensing of over 275 hotels this year, more than double the pace of last year, resulting in a net increase of franchise rates from 4.6% to 5.5% in those hotels, or an estimated fee increase of more than \$10 million annually.

For the fee business overall, we expect growth in the back half of the year, particularly the fourth quarter, to decelerate relative to the first half. Again, this is mostly owing to accelerated timing of fees booked earlier in the year than we initially anticipated, tougher comparisons to last year, and some one-time items that benefited prior year results.

The ownership segment posted Adjusted EBITDA for the quarter of \$318 million, up approximately 9% versus the prior year. Results were driven by robust fundamentals and were boosted by performance in Chicago, Japan, New Orleans, and the recently acquired 1031 Exchange assets in Florida and San Francisco outperforming their underwriting. Cost savings, including lower energy prices, further fueled the segment's outperformance and supported margin expansion of 200 basis points.

Timeshare Adjusted EBITDA was \$86 million in the quarter, up 21% versus the prior year period. Performance was in line with our expectations and we continue to expect timeshare Adjusted EBITDA of \$335 million to \$350 million for full year 2015.

We continue to grow our timeshare supply with fee-for-services deals that require no capital on our part, including two recent capital-light deals, a condo/hotel conversion in Orlando and a new-build tower in Myrtle Beach. Our current timeshare supply totals nearly 136,000 intervals, or about six years of sales at our current pace, with over 83% of those developed by third parties.

Finally, our corporate and other segment was \$61 million for the quarter, slightly better than expectations.

Moving on to regional results:

In the US, RevPAR grew 5.0% year-over-year at comparable system-wide hotels. As Chris mentioned, results were pressured by severe weather and flooding in key areas of the country, demand declines across key oil markets, most notably Houston, where RevPAR dropped 5.7% in the quarter, as well as by tough year-over-year comparisons. More broadly, we continued to see solid fundamentals, supported by increasing rate and strong leisure transient revenue, which was up over 8% in the quarter.

Trends in New York improved sequentially, aided by both transient and group performance. Inbound travel to the US from Continental Europe declined 1% through June, which has impacted gateway cities. However, some markets, like San Francisco and Hawaii, have seen increased demand from other countries, including China and Australia, mitigate weaker European travel.

In the Americas outside the US, RevPAR grew 6.8%, driven primarily by strength in Mexico, Peru and Chile, which was somewhat offset by Brazil, where performance was hit particularly hard given prolonged economic softness from lower commodity prices.

RevPAR in Europe increased 4.6%, as solid leisure trends supported by rising inbound travel offset softer group volumes in Germany, Spain and the UK. Inbound travel from the US to continental Europe rose 6% year to date through June, and strong vacation bookings continue into the third quarter.

The Middle East and Africa region posted modest RevPAR growth of 2.5%. Despite the sustained recovery in Egypt, declining inbound continued to weigh on fundamentals on the Arabian Peninsula.

In the Asia-Pacific region, RevPAR gains of 9.4% were driven by nearly 19% growth in Japan, which benefited from strong transient rates, as well as continued improvement in Thailand and strong trends in China. Corporate and leisure demand, coupled with market share gains, supported over 10% RevPAR growth in mainland China, despite some softness in the country's broader economy.

Turning to capital allocation, we reduced long-term debt by \$175 million in the quarter and prepaid an additional \$350 million on our term loan this month using the net proceeds from the Hilton Sydney sale. This brings total debt reduction year to date to \$750 million.

As Chris mentioned, we will begin returning capital to shareholders through a quarterly dividend of \$0.07 per share, payable on September 25, to shareholders of record on August 14. We intend to grow the dividend over time and maintaining a target payout ratio of 30% to 40% of recurring cash flow, which we define as Adjusted EBITDA, less debt service, capex, taxes and working capital.

Our goal remains to achieve an investment grade credit rating, which we believe will maximize equity value over the long term. Going forward, we anticipate returning recurring cash flow in excess of a market dividend to shareholders through programmatic share buybacks. Based on our anticipated credit profile, we believe this could occur in the second or third quarter next year.

We ended the quarter with a net debt to Adjusted EBITDA ratio of 3.7 times and expect to end the year below 3.5 times after factoring for dividend payments.

In terms of our outlook for the full year, we are maintaining system-wide RevPAR growth guidance of between 5% and 7% on a comparable currency neutral basis. Adjusting for the sale of the Hilton Sydney which closed earlier this month, we are raising our full-year Adjusted EBITDA guidance range by \$20 million at the midpoint to \$2.82 billion to \$2.87 billion. Our full-year guidance continues to assume approximately \$60 million related to FX impacts for the year.

For the third quarter of 2015, we expect system-wide RevPAR to increase between 4.5% and 6.5% on a comparable currency neutral basis, Adjusted EBITDA of between \$730 million and \$750 million, and diluted EPS adjusted for special items of \$0.21 to \$0.23.

Further detail on our second quarter results and updated guidance can be found in the earnings release we distributed earlier this morning.

This completes our prepared remarks. We would now like to open the line for any questions you may have. In order to speak to as many of you as possible, we ask that you limit yourself to one question and one follow-up. Leanne, can we have our first question, please?

Operator:

At this time, if you'd like to ask a question, please press star, one. Our first question comes from Harry Curtis from Nomura. Your line is open.

Harry Curtis:

Good morning, everyone.

Christopher Nassetta:

Good morning.

Harry Curtis:

Hey, I just wanted to ask you a bigger picture question. Investors' single biggest concern is that the lodging demand and pricing are decelerating, that the cycle is over, so I wonder if you could give maybe a bit more meat around the bone, that gives you confidence that Hilton can enjoy pricing power in the 5% to 7% range for an extended period, that the cycle really has ample room to run.

Christopher Nassetta:

Harry, I'm happy to do that, and I know that's prime on everybody's minds, particularly given what I've seen, and volatility in the markets, and as others have reported. I think my philosophy on this is quite simple and, frankly, quite consistent, which is I think we're in a very, very nice part of the cycle. I don't feel any different in that regard than I felt over the last several quarters. I think that is supported—not to over-simplify it, but I think it is supported by the basic laws of economics, okay, and that is as I look at the world or I look at the US market, which still represents a large part of—nearly 80% of our EBITDA, we have an economy that is certainly not roaring but is showing reasonably stable growth, with the potential to have a slight uptick in growth. The demand for rooms, hotels rooms follows very closely, it's on a very high correlation to that, so we are seeing decent demand growth for rooms that is being matched by historically—continuing historically low supply levels. So, it was less than 1%, we're now ticking a little bit over 1% in 2015, it will go up a little bit from there, recognizing the 30-year average is 2.5%—and by the way, in my history of many, many cycles, it is not at the average that you typically run into supply problems, and I think we're long, long way from the average.

So, I think if the US economy maintains moderate growth rates, based on what we can see from the standpoint of where the pipeline is and what supply growth is going to be, I think you've got several years of running room where you can feel good. Now, every quarter can be a little bit different here and there, depending on transient things that go on, like we had go on in May, or the way groups cycle through, but it should clearly, in my opinion, support growth, which is what I have been saying very consistently over the last couple of years, and for the next couple of years, it should clearly support growth in the 5% to 7% range, which is what we have been delivering.

If you break it down by segments, I think it should make you feel good. It makes me feel good. You look at what's going on in transient, you know, you had a little hiccup in May, but related to very specific things, but June has been very strong, it's strong in the highest rated segments, the transient, leisure transient is quite strong, and then you go to the group side, and we gave you some of the stats, but the group pace has been good, the position is good, both for the rest of the year and looking out to 2016, quite strong. It's strong in company meetings, which is, you know, honestly, where you'd really like as much as anywhere to see it show that strength.

So, not only do the laws of economics and sort of the macro conditions make me feel good, when I look at the micro conditions of the various important segments of our business and where they're going, and what we see on the books and consumer behavior, it makes me feel awfully good.

And the last point, because I know this is on everybody's minds, so worth taking a little bit of time on, I know that—my sense is that people have been getting sort of less enthusiastic about the cycle over the last six or eight weeks. What's interesting is I sit at this very table—I'm in our boardroom—every Monday

morning and I talk to my whole team around the world, including the three Presidents that run our mega-regions, and I end the week talking to the three of them, as well, and I'm going to tell you, over the last six or eight weeks, they haven't been—by region, and I'm now saying amongst all of them, they haven't been getting slightly more negative or neutral, they've been getting slightly more positive in their views of what's going on in our three big mega-regions.

So, again, that's anecdotal, but, I mean, you know, just sort of the atmospherics of what we see in real hard data and the atmosphere—the data that we see, hard data, makes you feel good, but the atmospherics, I should say, around just how our teams feel around the world about where things are going is quite positive, as well. So, I think the—I will declare, from my and our point of view, we think the cycle is alive and well, we're very confident in being able to deliver what we're suggesting to you that we're going to deliver this year, and we think that the good times continue.

Harry Curtis:

That takes care of it for me. Thanks.

Operator:

Our next question comes from the line of Joe Greff from JP Morgan. Your line is open.

Joe Greff:

Good morning, everybody, and ...

Christopher Nassetta:

Good morning, Joe.

Joe Greff:

Thanks for the perspective, Chris. Kevin, when you're looking at the 3Q guidance, the 4.5% to 6.5%, which I think is probably reassuring relative to what others had talked about for the 3Q, on a currency adjusted basis, how do you see that, and then what's the assumption for the US properties in that 4.5 to 6.5?

Kevin Jacobs:

Yes, sure. The 4.5 to 6.5, I assume you mean the 4.5% to 6.5% is FX neutral, so what would it be at actual rates. I think it would be a point to two lower than that at actual rates. Then, the US is consistent with that outlook.

Joe Greff:

Got it. Then, in the last couple of quarters, we've seen relatively stronger growth ...

Christopher Nassetta:

And, Joe, we covered it sort of indirectly. The reason it's a half tick down really has everything to do with sort of the holiday calendar in the third quarter. The effect of the calendar is shifting some business, is weighting fourth quarter, particularly on the group side, more than the third quarter. The full second half of the year looks great, but there's a little bit more weighting in fourth versus third, and so that half a point is a reflection of that.

Joe Greff:

Would you expect the second half US to be consistent with the growth that you saw in the first half?

Christopher Nassetta:

Generally, yes.

Joe Greff:

Great, that's it for me. Thanks so much, guys.

Operator:

Our next question comes from the line of Smedes Rose from Citigroup. Your line is open.

Smedes Rose:

Hi, thanks. I guess just along the same lines here, so in order to achieve the higher end of your RevPAR for the growth, we're going to need to see RevPAR kind of pick up at a pretty hefty pace through the second half, and I know you have your range there, but if you had to kind of lean one way or the other, would you be kind of towards the higher or kind of the mid part of that range?

Christopher Nassetta:

Well, I'd say a couple things. I think you're doing the math right, so, yes, it does imply a pickup, and I do think that's what you will see. I think you will see, sequentially, the third quarter RevPAR numbers be higher than second quarter, and I think the fourth quarter—at least as we look at our forecast, particularly given the really strong group pace—will be higher than the third quarter. I would say for the full year, you know, we gave you a range, I'd probably direct you to the middle-ish of the range.

Smedes Rose:

Kevin, just to clarify, in the management and fee income for the quarter, you said there were \$5 million to \$10 million of sort, for lack of a better word, one-time items in there. That's all in that line?

Kevin Jacobs:

Yes.

Smedes Rose:

Okay. Even if you adjust for those, it seems like growth in the second quarter was a little above the high end of your range, and I'm just wondering, through the back half of the year, are you just sort of being—you know, trying to be conservative there, or is there something that would kind of slow down that pace of growth?

Kevin Jacobs:

No, I think there's a couple of things that play into it, Smedes. One is the timing, as you mentioned. I mean, there are some things that materialized earlier in the year than we thought, and then in the fourth quarter of last year we had some one-items that created a little bit tougher comps on a growth rate basis.

Smedes Rose:

Okay. Can you quantify what the amount was in the fourth quarter last year?

Kevin Jacobs:

Yes, we could take you through some of the modeling offline, I wouldn't want to get into specifics now.

Smedes Rose:

All right. Thank you.

Operator:

Your next question comes from the line Felicia Hendrix from Barclays. Your line is open.

Felicia Hendrix:

Hi, thank you. Just switching gears for a moment to your pipeline, Chris, both your new unit openings and your development pipeline seems to be increasingly weighted towards the US, now about 54% international versus—I believe it was about 60 when you guys had your IPO. So, I'm just wondering what do you think is causing the shift in international markets, you know, what do you think gets the new construction development reinvigorated.

Christopher Nassetta:

You've got those numbers exactly right. At the IPO, it was 60/40 and now it's 54/46, and I think—here's what I'd tell you, I mean, obviously, different parts of the world move in a different cadence. The US development side, particularly in the limited service space, has been picking up steam, you can see it in our numbers and some others' numbers, and other parts of the world, including Europe, slowed down and now are picking up steam. Asia-Pac, compared to where it was, has slowed down somewhat. I'd say the Middle East is generally consistent.

What I love—and we did talk a lot about at the IPO—is that at our scale and with the breadth of chain scale diversification we have, we have the ability to sort of ebb and flow with market conditions and win everywhere. So, the idea is there are going to be times where, you know—and we saw it for the five years leading up to maybe last year, that China and Asia-Pacific are roaring, and there are going to be times—and the US and Europe were very slow. Now, Asia-Pacific is slowing somewhat modestly and Europe is finally stabilizing, improving a bit on the development side, and the US is starting to pick up some steam.

This is one of the great things about diversification, that as that's going on we are making sure that we're really thoughtful about our development strategy, making sure we have the right resources in the right place, that we're layering our brands in the right way that is satisfying both the consumer demand, obviously, but also where the capital is flowing in these various parts of the world, and the idea is that if we're intelligent and strategic about how we do that, we're going to keep growing, and we're going to grow at an accelerated pace, no matter what's going on in the world, because the world's a big place and it's a diversified world, and we're going to be able to continue to gain momentum by being intelligent.

So, what we've seen is just what I said, the US and Europe now are picking up a little bit, providing a little bit more of the growth. In 2010 through 2013, when we went public, the US had little or nothing going on, Europe was in stays, and Asia-Pacific was a bit part of the story. That's why I like our story, frankly,

relative to others, is that we can do this. We've got 12 of the best brands with the highest market share, great development teams around the world, and we push and pull and are very strategic about what we're doing around the world to continue to grow our base of hotels, to better serve customers for any need anywhere in the world they want to be.

Felicia Hendrix:

Thanks, and if I could just bring you back to the quarter results for a second, you gave us some very helpful color on the weaker transient business in May. Can you just help us understand what percentage of your system-wide room count ended up being affected by the weather and the weaker energy demand, just to drive the 100-basis-point decline in RevPAR?

Christopher Nassetta:

I would guess, you know, if you combine it—I don't have the exact numbers, so, Felicia, we'll have to get back to you, but not insignificant. I would say probably, because it was a large swath of the limited service system and franchise system that was really impacted, I would guess 20%, but I'll ask Christian and Jill to get it. We did do the math, I just don't have the number of hotels.

Felicia Hendrix:

Okay.

Christopher Nassetta:

But not insignificant.

Felicia Hendrix:

Okay, great. Thank you.

Operator:

Our next question comes from the line of Shaun Kelly from Bank of America. Your line is open.

Shaun Kelly:

Thanks, and thanks for taking my question. So, just to maybe switch gears and talk a little bit about strategic alternatives, Chris, you alluded to a little bit about this in your prepared remarks. So, the first question I have is, you know, last quarter the only thing we could talk about was M&A and this quarter made it five questions in without asking about it, so how does M&A fit into the strategic alternatives, because you sort of alluded to real estate and timeshare, but didn't mention that. So, how are you thinking about that today and has that changed at all?

Christopher Nassetta:

No, I think it has not changed. I think we think about it very consistently, with what I've articulated, and Kevin and others have articulated before, and that is we feel really good about the attributes of the Company as they stand and our ability to expand those attributes organically, meaning launching new brands, and as a result, be able to lead the industry in growth and do it in a very capital-light way, which we think is going to drive the best returns on equity in the business. I've been pretty clear in saying you would never say never. I mean, we look at everything that's out there, generally, and if we found anything that sort of went through our filter of being highly strategic for us and economically compelling in terms of

value, you know, value enhancing to the Company, it would be something that we'd consider. I will say I don't really see anything that's out there right now that gets through that filter, and that's because of a good problem we have, which is, getting back to what I started with, we have pretty much, in our view, what we need to be successful. We're going to launch brands, as we talked about, mid-scale. We just launched two new brands last year, and Home2 not too long before that. But, given the base size of the Company, our scale, our geographic distribution, our existing chain scale distribution, and importantly, 10,000 owner groups that we have an amazing relationship with, we think that the higher return answer for investors, all investors, including ourselves, is to really focus on our organic growth. So, in a simple way, I would say we are not particularly acquisitive, but we are always trying to be intelligent and thoughtful.

Shaun Kelly:

That's very helpful. Then, my follow-up would just be, you know, when we think about the other two alternatives and some of the more organic things you can do, the real estate, the REIT group, which you know better than anyone, the valuations there have come off fairly significantly in the last few weeks. Clearly, these things are volatile, but the question is does it change, or does the recent change in valuation have a material impact on the way you guys are sort of viewing that longer term set of alternatives for the real estate side?

Christopher Nassetta:

No, I don't think so, Shaun. I mean, we're really trying to look at this, as I've described a couple times, through a very long-term lens, which is, when you think about the Company, is it best—do we think we can create the most value for shareholders over the long term in our current setup or another setup, and so it is very much a long-term view. We've done a considerable amount of work in looking at all the options. As you can imagine, it's quite complex structurally, manageable but quite complex, and we want to be really thoughtful about the value levers, because we're not in the business of doing things for practice, we're in the business of doing things that we think are going to create long-term value.

We have done a lot of work, we'll continue to do a lot of work, and as I said, certainly, before the end of the year, I think we can lay out the rationale for how we want to move forward. But, these recent ups and downs, I think, when we're looking through a longer term lens, at least what I've seen so far, doesn't really have any material impact on our thinking.

Shaun Kelly:

Thank you very much.

Operator:

Our next question comes from the line of Jeff Donnelly from Wells Fargo. Your line is open.

Jeff Donnelly:

Good morning, Chris. I guess, maybe, to put a finer point on it, is in broad strokes, how are you thinking then about your 2016 RevPAR growth, either domestically or globally, just as compared to the pace in '15, do you think it's going to hold or accelerate, or even decelerate?

Christopher Nassetta:

I'll go back to what I started saying at the IPO. I feel really good, as I said earlier today, Jeff. I think we will be in that 5% to 7% range. We have not started to dig in into our budgeting process, that will actually

start to kick off in a couple of weeks, but we're in regular dialogue around the Company and with all of our regional heads about their views of this year and next, and obviously looking at the pace of bookings, and I think that the cycle is alive and well. I stand by what I said, which is I think we will be able to, for the next couple of years at least, deliver RevPAR growth in that zone, and that's what we will aiming towards.

Jeff Donnelly:

I apologize, I got on a little late. Can you talk about your perspective on trends and pricing in China in the next 12 months versus the past 12, just given some of the headlines we've been seeing and kind of the market falling at a low with consumption and whatnot?

Christopher Nassetta:

You know, China, obviously, the economic growth story there is one of a bit deceleration. I think they're going to great lengths to stabilize their markets to keep consumer confidence high, because in the end, you know, they're transitioning that economy to be a consumption-led economy, not unlike ours and many of the other more mature economies. I suspect there'll be some bumps and bruises along the way, as there always are in these things, but that the underlying fundamentals of 1.3 billion people that are, no question, have ups and downs, but are gaining in wealth, is going to allow them, over an extended period of time, to accomplish their objectives. I think they have been reasonably smart and I suspect they'll continue to be reasonably smart.

We are seeing reasonably healthy results in the market. I think the hotel space there is in its nascent stages of development and growth. I mean, there's certainly some markets, some of the core markets that maybe have had more development than others, but if you look at the representation per room, of thousands of people per room—or rooms for a thousand people, rather, in China, it is still much, much lower than any of the more developed Western economies. So, I think, any stat you look at, the next 10, 20, 30 years, and China will have ups and downs, but will be a rise up, meaning you're going to continue to see a massive amount of development, because you're going to have a massive amount of demand coming from their consumers, and more people visiting China.

When you look at the current trends—well, I gave you the number, we had a great second quarter, we still think we'll be 6 to 8 for the full year. Some of that is we're getting a network effect and we're gaining market share. I only think that gets better. I think this story is much more—I've been saying this for two years, by the way, and that's why we've done what we've done—I think it's becoming very much a mid-market story. It's not that you're not going to build more Hiltons and Waldorfs and Conrads, but you're going to build fewer of them, and the market's going to fill in, like it did in other parts of the world, the US, in particular, which is the most segmented, with mid-scale kind of brands. We've very aggressively trying to do that, because that's what's going to build our infrastructure and our network and distribution, which is going to create that network effect like we have in other parts of the world, Europe, the US, predominantly in Europe, Europe, as well. So, we feel very good about China.

I mean, if you look at deals being signed in China, it reflects everything I just said. When you look at the stats here today, we've signed exactly the same number of deals in China this year as last. Last year, 17% of them were limited service, this year 53% for limited service, okay? So, there's still full service and above getting done. It's just a very different profile. My guess is you fast-forward a year, I think you're going to see the same thing. I actually think we'll sign more deals in the first half of next year. I think our deal flow will accelerate, the size of the hotels will become much smaller, we'll have a velocity of more deals, more distribution, more in the mid-scale and limited service side of the business. That's what's going on. That doesn't mean it'll ebb and flow and you'll have surges over time at the high end of the business, as well, but that's what sort of got—in China, the low end of the business got very built out, the high end of the business got reasonably built out. It's really the middle that's sort of missing, which is why we focused on it, and I think for the next three, four, five years, that's where the demand is, that's where

they don't have enough capacity. Thus, I think the economics are good. The money is going to flow to that segment.

Jeff Donnelly:

Great. Thank you.

Operator:

Our next question comes from the line of Thomas Allen from Morgan Stanley. Your line is open.

Thomas Allen:

Hey, good morning. So, a bigger picture on the mid-scale brand launch you're going to do, I think you said in early 2016, or maybe later this year. If you look at supply growth in the US, the one chain scale that's actually seeing decline in supply growth in the US is actually the mid-scale segment, and most of the future construction is in upper mid-scale and upscale. So, what gives you guys the confidence that you can—you know, clearly, developers are choosing to build these other kind of slightly higher chain scale properties over mid-scale, so what gives you guys the confidence that you can kind of launch a brand and change that dynamic?

Christopher Nassetta:

Everything you just said gives us the confidence that we can do it. I think why you're seeing what you're seeing there, with all due respect to the products that out there, there is no good mid-scale property. That's why we're doing it. If you think about the history of it, and I've said this certainly in one-on-one meetings, and I think maybe on one of these calls, I mean, Hampton was initially targeted to be in that segment. It has just been so successful that it's grown up out of it. So, it's in upscale, you know, technically. I think this year it'll be close to \$115 average rate in the system. As a result, there is a huge swath, 40% of the demand base in the US markets, and similar sort of stats as you go around the world, that we find we're not serving as much as we want to because they can't afford, basically, our lowest chain scale product. So, we think there's a big customer base out there that wants it.

But, to your point, the reason there's not been a lot of development, I don't think the products justify development. The reason that we're taking so long to get this right is we're not just going out and saying, you know, just do a Hampton lookalike, we're recreating this segment, and we're doing it in a way that it's going to be unlike anything anybody's done. It's going to be an all new build, against product that's out there that is almost no new build, to your point, that's going to be very appealing to the customer, and, importantly, that is engineered both to build and operate in a very simplistic way, to be able to drive returns, like we've done with Hamptons. It'll be a lower investment, but we're trying to drive a similar type of return. We've been working with our ownership groups, we're way down the path, and we think we've cracked that code.

So, we think we're going to do something—the reason I think this will be thousands of hotels is because the demand is there. The reason nobody's building this is because there's no product that resonates with the customer, and these types of products aren't delivering returns to owners, so they don't build them. They're building Hampton and Garden Inn and Courtyard and Fairfield, whatever. We think we're going to give them an alternative to serve a customer base we're not serving, and to make great returns, and then have a product that the customer loves, because they have such bad choices now.

In terms of, like, fast-forward down the road—we're not ignoring the high end of the business, by the way, we have amazing momentum in the luxury space with Conrad and Hilton, and doing amazing things with Curio and Canopy, we gave you some of the stats, but in terms of number of units and when you fast-

forward five and 10 and 15 years down the line, this can be a mega-brand that generates mega-EBITDA, because this can be thousands—be smaller hotels, but they're going to be thousands of them, just as we've done with Hampton.

Thomas Allen:

Thanks, and as my follow-up, I think the first question you guys are asked—you know, I think Harry highlighted that investors' top concern is just around the cycle. I think investors' second highest concern is just around the threat from the sharing economy, and I'm often, and people are often accused of being too flippant around that threat. Can you kind of address that? Thanks.

Christopher Nassetta:

Yes, Airbnb or HomeAway, or any of the above, I guess.

Thomas Allen:

Exactly.

Christopher Nassetta:

You can imagine that we've sat around this table as a Management Team, you know, with our Board of Directors talking about it and, really—and we've talked with the Airbnb folks, and lots of others in the industry. In the end, I won't pontificate, I view it as a different sort of customer looking for a different type of experience. It's a real business for sure, a growing business for sure, but what it really is at its core is a leisure value adventure sort of need that it's fulfilling. That is not what we are. I mean, we are some leisure, yes, but we're not trying to be the cheapest. We're trying to be the highest quality product and service, so that people will pay a premium, and we're not trying to provide an adventure in that sense, meaning we want it to be very high-quality products and service, so you know exactly what you're getting.

So, I think the proposition, when customers, our customers are coming to us, what they're looking for is something different than what they're looking for when they go there. I'm not going to say there is zero overlap, that none of our customers ever use them, but I think they use them for a different need, and I think largely, as we look at it, statistically, okay—and every market's a little different and we can talk about New York, whatever, but if you look at the broad business for those guys, I think it is growing the pie more than anything. I think it is stimulating more travel that wouldn't have occurred, and in the end, I think that's a good thing. Getting people traveling more is fantastic, because we think once they're travelling and they get the bug, they're eventually going to come stay with us, because we're going to be able to satisfy a different kind of need that they're going to have, particularly as they sort of, you know, grow up and move up in their careers, and families, and all of those things, where what they're looking for may be a little bit different.

So, I'm not saying—I'm not trying to be a Pollyanna and say we don't think about it, we don't care, we dismiss it. We think about it a lot, we talk about it a lot, but both, you know, anecdotally and with hard statistics, I think in the end they are not impacting and I do not think they have a material impact on us. I think they make our pie bigger, and ultimately stimulating people to travel more is, net net, I think a good thing.

Thomas Allen:

Thank you.

Operator:

Our next question comes from the line of Carlo Santarelli from Deutsche Bank. Your line is open.

Carlo Santarelli:

Hey, guys, thanks for taking my question. I was just wondering—I know within the context of your group pace for 2016, Kevin, I believe you said mid-single-digits. Could you guys talk a little about the tenure of maybe some of your group discussions over the last several months and relative to when we had this conversation at the end of April, and then maybe provide a little bit of color on in-the-quarter, for-the-quarter trends?

Christopher Nassetta:

Yes, I would say group tenure is the same. I mean, I don't think there's any material difference. I think, you know, we're looking at a year next year that's going to be another very good year, we're looking at having a good position, so that means we don't have as much capacity available for people. So, I think that continues to give us incrementally a bit more leverage. I wouldn't say it's moved a whole lot either way. I mean, if anything, I think our leverage levels for group bookings have gotten a little stronger.

If I look at sort of to back that up, even in the quarter, but certainly going forward, the majority of our group growth is coming through rate, so I think is as good a reflection as anything that the leverage level we're getting is growing, not diminishing, and it should be, you know, the more we build out a bigger group base, the more selective we can be and there's less sort of capacity for people to book, so we can drive higher rates. In-the-quarter bookings were strong, I think they were Q2, forward-looking, up in the high single-digits from a pace point of view, so quite good

Carlo Santarelli:

Great. Thanks, Chris.

Operator:

Our next question comes from the line of David Loeb from Baird. Your line is open.

David Loeb:

Good morning.

Christopher Nassetta:

Good morning, David.

David Loeb:

I want to come back to China for a minute. I wanted to ask about your agreement with Plateno. There have been some press accounts that suggest that Plateno and Jin Jiang are getting together. Will that have any impact on your deal with them?

Christopher Nassetta:

No. I mean, we've been in a pretty constant dialogue with them as that has been evolving, as you might imagine, and I think our view of a combination of Jin Jiang and Plateno is that together they are even

stronger and an even better partner for us in what we're trying to do and, in our discussions with them, I don't think it changes their commitment to what we're trying to do at all.

David Loeb:

Great, thanks. You've covered all the other important stuff already, so thank you.

Christopher Nassetta:

Okay. Thanks, David.

Operator:

Our next question comes from the line of Wes Golladay from RBC Capital Markets. Your line is open.

Wes Golladay:

Hey, good morning, everyone.

Christopher Nassetta:

Good morning.

Wes Golladay:

Are you seeing any headwinds on the cost side from developers in the US, particularly in the select service?

Christopher Nassetta:

Well, I mean, the answer is yes, but not in a way that's slowing down our ability to add to our pipeline. There's no question that there's more construction going on, not just in hotels—incrementally, obviously, a bit more in hotels, but across the board more infrastructure spending going on, you're starting to see construction in the other areas of real estate, home building is picking up. So, there's no question that the costs to build are going up higher than the sort of average inflationary increases, but given the strength of the business in terms of the growth in RevPARs, I think it has generally been keeping up enough that the deals that really make sense are getting done.

That is a reason, by the way, and I have articulated this before, that I have such confidence in the supply side of it, which is that not all deals make sense. There's a reason that there is basically two companies that make up more than half of what's getting built in the US, and those are the two companies, ourselves included, that have very, very high market share that allow the economics to work. The reason why the other stuff isn't getting done is because costs to build have been going up and they're high, and if you don't have the high market shares, the economics don't work. So, it's sort of a good news story for us, because we've got that market share, we can continue to build our pipeline when others can't, and the cost increases that are going on in construction, which are not insignificant, are keeping a bit of a lid on overall supply, and I think will continue to do so. I think as the US economy, you know, sort of seasons this recovery a little bit more, I think that will continue to be problematic.

Wes Golladay:

Okay. Now, switching over to China, how are the developers funding their projects over there, and can you give us a brief overview of the profile of the developers?

Christopher Nassetta:

Well, the profile is changing. I'd say in the big full service and luxury stuff that is still a component of what's in our pipeline and getting done, and we're still signing some of those deals new, those are very large companies that are in a lot of different businesses, and in many cases partially government owned, either local or nationally, in national government, and that's sort of been the pattern. There's a spattering of publically listed Hong Kong-based real estate companies in there, but a lot of those deals have been done by very big Chinese conglomerates that own lots of different, or are in of different industries and have some government ownership.

What's shifting in that is, as we're going to more of a limited service makeup, because that's where the demand is, as I already described, and where the money is flowing, it's changing, not unlike in the United States, where you're getting smaller players, entrepreneurial players, much less of the big conglomerates and much more diversified smaller entrepreneurial individuals, small companies, families that are making those kinds of investments. That, I think is a really good thing, that's a natural thing, that's exactly—if you look at the Hampton system in the US as an example, it is massively diversified, and largely our owners are small families and small businesses. I think that is increasingly what you're going to find happening in China as you shift the business to more of a limited service business. For us, that's going to create, I think, a great diversified base of owners. That lowers risk and also provides more avenues of growth.

Wes Golladay:

Okay. Thanks a lot for taking the question.

Christopher Nassetta:

Yes.

Operator:

Our next question comes from the line of Robin Farley from UBS. Your line is open.

Robin Farley:

Great, thanks. I think most of my questions have been answered, maybe just to circle back to one topic for little more clarification, which is the potential for spinning out of REIT. I mean, I think just maintaining your RevPAR guidance is kind of a victory, given the lower RevPAR guidance from a number of others out there. It sounds like you're saying that kind of lower valuations out there wouldn't deter your interest in a REIT spin, but maybe it's fair to say it would change the potential timing of it.

Christopher Nassetta:

Not necessarily. Again, I think the lens we're going to look at, which is what I would hope all shareholders would want us to look through, is how do we create the best long-term value for everybody, and so, I think when you're doing that, you've got to be very careful, in my mind, of looking at any sort of snapshot in time of, you know, of what it was three months ago or yesterday, or what it might be a month from now. I think it is sort of—when you look at the different pieces of our businesses, it's a bunch of different filters that you're looking at. It's relative valuations, it's tax efficiencies, it's opportunities to activate in different ways various businesses, all against incremental costs of what might be more G&A to have more than one enterprise, as compared to what we have today, and I think all of those things are factors. Not to complicate it too much and not to dangle the carrot out there too much, but those are the sort of factors that we are filtering through as we go through it, and obviously we're cognizant of what's going on in the

market, but we're trying to take a long view on where relative valuations—we think relative evaluations have been and will be.

Robin Farley:

Great. Thank you.

Operator:

Our next question comes from the line of Steven Kent from Goldman Sachs. Your line is open.

Steven Kent:

Hi, good morning.

Christopher Nassetta:

Good morning.

Steven Kent:

I have two questions. First, just a better sense for cash use. You generally have been paying down around \$200 million in debt every quarter. Now, you'll be paying around \$70 million with the dividend. What will happen to the rest of the \$130 million or so? Is that going to go towards debt? You mentioned buybacks, but is there some kind of pacing that you're thinking about, or how do you think about that? Then, separately, there was the other adjustment line item and the adjusted EBITDA bridge, and I just wanted to understand what that is and how we should be thinking about that other adjustment line over the next couple of quarters?

Kevin Jacobs:

Sure, Steve, it's Kevin. I think, on dividends versus use of cash, I think our other uses of cash are going to stay very similar, we're not going to change our overall outlook on our capital allocation, and we do still, as I said in my prepared remarks, want to achieve investment grade, and I think as we've said to you all along, that we thought that target range for our balance sheet was between 3 times to 4 times leverage, I think we've refined that a little bit as we've gotten into it, where we're targeting a range of 3 times to 3.5 times, and so we think we're going to finish the year at 3.4 times with the dividend. So, that gives us a little bit of room to go towards getting into sort of the middle of that range, so you would see the other use would be continued debt paydown in the back half of the year.

Then, on the other line item, it's pretty straightforward. The lion's share of that is severance related to the Waldorf Astoria transaction, which was effectively a transaction cost as part of the overall transaction, where we're picking up 80% of the severance deal, and that's all baked into that line item.

Steven Kent:

That other line will go back to roughly around \$20 million or so per quarter?

Kevin Jacobs:

Yes, yes.

Steven Kent:

Okay. Thank you.

Operator:

Our next question comes from the line of Bill Crow from Raymond James. Your line is open.

Bill Crow:

Hey, good morning.

Christopher Nassetta:

Good morning, Bill.

Bill Crow:

Just to clarify, Kevin, you had earlier suggested \$800 million debt reduction for the year. You're now increasing that. I'm just trying to build that same bridge between the \$1.1 billion and \$1.3 billion of capital available to reduce debt and return to shareholders against \$800 million debt reduction and \$130 million, \$140 million of dividends?

Kevin Jacobs:

Yes, I think the difference, Bill, is the Sydney paydown. So, it's \$800 million or so—well, it's \$800 million or so, I think was the prior number, I'm not—to be honest, I'm not sure exactly what number you're referring to, but I think it was our prior guidance number, and then that moved up to 1.1 to 1.3 when we sold Sydney and had the Sydney paydown in there, and so now all you would do is you would take the dividend amount and that would be part of the 1.1 to 1.3. Does that answer the question?

Bill Crow:

Yes, I guess I thought your actual debt retirement paydown number was \$800 million for this year, which you've essentially hit already, but you're increasing that number, it sounds like, right?

Kevin Jacobs:

Well, we increased it last quarter, our guidance went up to \$1.1 billion to \$1.3 billion last quarter when we reached agreement on Sydney.

Bill Crow:

Okay, of debt reduction, okay, very good. Chris, couple of quick topics. Marriott signed a marketing and distribution agreement with TripAdvisor, I wanted to get your thoughts on that, any goal of reducing commissions paid out. Then, the other topic, Chris, is as you think about this potential to divide up the Company, and knowing that you're kind of allergic to G&A, would it not make sense to look for an existing REIT platform that already has the G&A commitment that might make the economics work better?

Christopher Nassetta:

Okay, happy to answer these both. On Trip, obviously, I'm not going to get into where we might be with any particular party. We've had some discussion with them, those discussions are ongoing, unclear where they will end up, but we may do something with them. The reason we would, would be because

the terms that we get with them are consistent with basically the three pillars that we have in dealing with any of our distribution partners, and that is: one, we want complete control of our inventory; two, we want to have the ability to price differentially to our most loyal customers, otherwise known as our Honors members; and three, we want to have very efficient margin structures or commission structures with them; and I'd say, not a pillar, but sort of the overarching philosophy is always going to be that we want to have the most direct relationship we can have with our customer.

So, everything we're doing, and we talked about in the prepared comments about our Honors app and straight-to-room, and all of what we're doing with CRM, is all around trying to shift as many people into our direct channels, because, number one, we want to have that direct relationship, and two, it's the most cost-efficient way for us to be able to distribute our product. It will always, obviously, be, you know, we will have distribution partners. I don't see a world where we're going to get everybody to come direct to our channels, the more the better, and when we're going to have distribution channel partners, like potentially three or four others that we are all aware, we are very, very focused on making sure it sort of meets the standards of our three pillars.

So, what we do with Trip, I don't know. If we can meet the standards of our three pillars, we may do something with them.

On the spin, I don't want to get—yes, there is, theoretically, a rationale for if you decided at some point you wanted to separate the real estate—and, yes, I do not like incremental G&A—that there would be a way to do it that would be more efficient than doing it ourselves, when I say we will look at all options, we will look at that option, as well.

Bill Crow:

Thank you.

Operator:

Our next question comes from the line of Vince Ciepiel from Cleveland Research. Your line is open.

Vince Ciepiel:

Hi, thanks for taking my question. I had a question on owned margin. They've been impressive in the quarter and year to date. When you look at RevPAR growth in your owned business, it's equally been driven by occupancy and rate. So, is there anything going on with costs there and how should we think about margins progressing into the second half?

Kevin Jacobs:

Yes, Vince, it's Kevin. We certainly had some things go our way in terms of costs in the quarter, energy being a predominant cost that's been down due to what's going on in the oil markets, and we continue to work our labor management systems to run the properties as efficiently as we can, and so if we achieve RevPAR growth that is in excess of inflation, particularly, as you point out, if it comes more from rate than occupancy, we should be able to continue to drive margin growth.

Vince Ciepiel:

Great, thanks. Then, a different topic, the last couple—or, actually, the last couple of years, Hampton, Doubletree and Garden Inn have led your guy's guidance as RevPAR growth. I noticed they were more in line with the system average this quarter. So, I guess, first, how much of that's related to kind of the

weather/Texas impact you alluded to? Then, second, you guys provided kind of a positive longer term outlook. Is part of that those brands leading system-wide RevPAR growth going forward?

Christopher Nassetta:

Yes, I think it is partially a result of those brands being more impacted by the things that impacted Q2, for sure, but, as we've said a couple calls ago, we do believe that RevPAR growth levels are going converge as between the lower segments and the upper segments, and I think when we look at the balance of the year and we look into the next year—and, frankly, year to date even, sort of extracting out the weather impact—we believe that's happening. The upper end of the business is definitely catching up, which is I think a good thing, and a natural thing, as the group base continues to build, because the upper end is more driven by that group base.

Operator:

Our next question comes from the line of Joel Simkins from Credit Suisse. Your line is open.

Joel Simkins:

Yes, good morning guys. I can't believe we've made it 67 minutes without timeshare, but timeshare obviously has continued momentum for you. Can you just give us a little bit of color on what you're seeing out there in this business, whether it relates to tour flow, package size, willingness to use financing, and then are you seeing some additional opportunities with this to continue to feed some owned hotel inventory or some of those 1031 assets to this business?

Christopher Nassetta:

Yes, (inaudible) timeshare, but we didn't spend a ton of time on it, but it's doing incredibly well, as I look at it against others that are reporting. I mean, our tour flow numbers are way up in the quarter, up 9%, VPG is up 7.5%. We expect those kinds of numbers, plus or minus, for the full year. So, our timeshare business is hitting on all cylinders, and it's doing it, honestly, in a very different way, as we've talked, than all of our competitors, in the sense that we've got the vast majority, now over 80% of our inventory, that we're doing it that a very capital-light way. I think 60%, roughly, of our sales in the quarter were in the capital-light segment. So, we have really, I think—I know I've really transformed this business over the last three or four years, and we continue to build momentum. I know there's always a question like, "Well, is it sustainable and can you keep building the inventory?" and I think we have proven—our inventory numbers have been moving up, you know. Even as the economy gets stronger and people thought, "Well, there won't be broken deals," we've proven, just because of the returns we can deliver, that we're able to find more and more counterparties that want to do this with us. We announced, in Kevin's comments, a couple of deals, we did it quickly and gently, but we just did another in the quarter, another couple of capital-light deals. So, Kevin may want to add to it. I think this business is cranking, it's hitting on all cylinders. Our team is doing an amazingly good job.

Kevin Jacobs:

Yes, I think, as it relates to the consumer, Joel, I mean, consumer confidence is up, right, and so is timeshare. It is, at the end of the day, a consumer product driven by how the consumer feels about their own outlook and their own balance sheet, and so you are seeing—as Chris mentioned, you're seeing very high levels of sales growth, more people willing to go on tours. On the margin—we haven't really changed the financing profile of the business that much, but on the margin, the consumer willing to borrow a little bit more to stretch for that product because they feel good about their own balance sheet.

Then, the last thing, Joel, I didn't quite follow the question as it related back to the 1031. Were you asking if there are timeshare opportunities specifically at those assets?

Joel Simkins:

Yes, those assets, or just how you continue to think about parsing out a couple of floors in some of your owned hotels to these types of projects, particularly urban locations?

Kevin Jacobs:

Yes, I think we continue to think about those kinds of things. The 1031s, you know, there's the urban hotel in San Francisco, you know, who knows, but I think, as Chris mentioned, we're finding really good capital-light deals to do, so we look at those first, and then we always continue to look at opportunities for value enhancement in our properties, including at the 1031s. I'm not sure that there will be any major projects there, but we're certainly finding good ROI projects to do in that portfolio. Whether or not they will be in the timeshare space, I'm not sure, but we will create value in those hotels.

Christopher Nassetta:

In the owned segment, including properties that we have owned for a period of time, there are two or three incremental opportunities over time to take pieces of existing hotels. More potentially, it's the New York Hilton, and we've talked a little bit about Hawaii, in Waikoloa, and there are one or two other urban markets where I think we have some opportunities that we're moving down the path on and at the appropriate time we'll make sure we let you guys know about them.

Joel Simkins:

That's very helpful. One quick follow-up, if I may, here. Chris, you called out some very interesting mobile check-in stats, and I certainly recognize this isn't all about cost savings, but it sounds like you've had some pretty high adoption rates, so, clearly, the consumer wants to control their experience. So, in terms of that small base of the hotels you're deployed that currently, are you seeing any real meaningful kind of front-of-the-house, back-of-the-house efficiency opportunities?

Christopher Nassetta:

Not yet, because it's too early in the process. I mean, right now, we're not trying to drive costs down, as you pointed out. Eventually, I think there are opportunities to drive costs down and/or repurpose people, but at the moment we're using those people to sort of help retrain our customers. So, not unlike, you know, if you look at how the airlines did this and they went to online check-in and kiosks, in the beginning there's a lot of work and training and human resource effort to get people to adopt, understand it, make sure it's work. So, we're in that stage, but the adoption rates are huge.

By the way, I didn't note it, but the satisfaction rates are off the chart. Think about it, it's a real simple philosophy. Everybody wants what you want and I want, they want choice and control in the palm of their hand, and they want to interact with us just like they're interacting with so many other businesses in their everyday life. The hotel business, honestly, over time, probably hasn't kept up with that. We're trying to not only keep up with it, but get ahead of it. I do think ultimately it's going to build increased loyalty and market share, it's going to create cross-sell opportunities and up-sell opportunities that I think are going to be meaningful, and it's going to create cost efficiencies, okay. Incremental extra cost now, I'd say it's sort of neutral, but ultimately there will be cost efficiencies as we get broad adoption.

Joel Simkins:

Thank you.

Operator:

Our next question comes from the line of Chris Agnew from MKM Partners. Your line is open.

Chris Agnew:

Thanks very much. Good morning.

Christopher Nassetta:

Good morning.

Chris Agnew:

I agree with your sentiments on Airbnb, but just wanted to follow up with a question. Is the risk that the rapid growth of alternative accommodation is holding back pricing power, or even has the potential to hold back pricing power for the industry, given that these types of accommodation can come into their own when there's compression? So, how do you think about the risks that pricing power is maybe weaker than in previous cycles, or what it should be given favorable supply demand conditions in the industry? Thanks.

Christopher Nassetta:

Yes, not to be a Pollyanna, I mean, obviously, any type of supply could have the effect of taking away our pricing power, and there may be markets where there is some impact, but it's not an impact, as we look at it, enough that we can measure, and as I said, I think it's just a different kind of customer. The largest part of our base of customers is really a business customer for a business purpose. I know they're trying to get in that business and good luck, and I'm sure they'll build the business, but I just don't think, in terms of the core customer that we're serving and what that core customer is telling us that they want from us, that they are enough similarities where the overlap is creating a really credible alternative that's affecting pricing power in a meaningful way, as we study it. Again, you can probably pick micro-markets and there'd be exceptions to it, but, broadly, we are not seeing. I don't expect to see it.

Chris Agnew:

Thank you.

Operator:

Our next question comes from the line of Chad Beynon from Macquarie. Your line is open.

Chad Beynon:

Great, thank you very much. With respect to corporate negotiated rate budgeting and the timing of these conversations with your partners in the next couple of months, acknowledging that the majority of the leverage is in your favor, as you've spoken about, how important is the timing of these conversations against a potential Fed rate increase, and how important is the size of that increase in these negotiations, maybe some anecdotes over the past couple of cycles, what you've seen during other periods when rates were increasing? Thanks.

Christopher Nassetta:

Yes, it's a good question. I'm going to have to admit I haven't actually scientifically done the correlations on Fed increases while we're in negotiations on corporate rates, so I can't give you an exact answer. Here is what I'd say, though, anecdotally. I do think we have more pricing power. So, if we were in the sort of low to mid-single-digits this year, I would expect we'd be in the mid to higher single-digits, just because we do have incrementally more pricing power. While increasing rates could have an impact, the net results of increasing—the reason rates would be going up, to begin with, is if the economy is stronger. If they're going up faster than people expect, it just means ultimately the economy is stronger than everybody expects. The economy being stronger is advantageous to us, meaning the economy being stronger is creating more demand for room nights. There's the same amount of capacity, essentially, because there's very limited new capacity coming on. It should incrementally give us more pricing power. Not that I want rates to go up fast, don't get me wrong, but if rates started going up at a faster clip, I think it's reflective of our business. Ultimately, we are—we re-price every day and it's ultimately reflective of our business being very, very strong, and I think gives us more leverage in the negotiation.

Chad Beynon:

Okay, thanks, and can you provide us with the percentage of your managed properties that paid IMS during the quarter versus last year?

Christopher Nassetta:

Yes, I think it was in the low 50s versus—it was in the low 60s this year versus low 50s last year.

Chad Beynon:

Okay. Thank you very much.

Christopher Nassetta:

You bet. Okay, is that—I guess we're done with questions. So, thanks everybody for joining the call. We appreciate the time today, obviously pleased with the quarter, very excited about the way we think the second half of the year is going to play out and looking forward to getting back with you after our third quarter end. Take care. Have a great day.