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# Hilton Worldwide Holdings, Inc. (HLT)

Q2 2020 Earnings Call

## CORPORATE PARTICIPANTS

**Jill Slattery**

*Vice President & Head-Investor Relations, Hilton Worldwide Holdings, Inc.*

**Kevin J. Jacobs**

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

**Christopher J. Nassetta**

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

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## OTHER PARTICIPANTS

**Carlo Santarelli**

*Analyst, Deutsche Bank Securities, Inc.*

**Thomas G. Allen**

*Analyst, Morgan Stanley & Co. LLC*

**Shaun C. Kelley**

*Analyst, Bank of America Merrill Lynch*

**Robin M. Farley**

*Analyst, UBS Securities LLC*

**Joseph Greff**

*Analyst, JPMorgan Securities LLC*

**Richard J. Clarke**

*Analyst, Sanford C. Bernstein Ltd.*

**Stephen Grambling**

*Analyst, Goldman Sachs & Co. LLC*

**Smedes Rose**

*Analyst, Citi Investment Research*

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Good morning, and welcome to the Hilton Second Quarter 2020 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Jill Slattery, Vice-President, Investor Relations. Please go ahead.

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**Jill Slattery**

*Vice President & Head-Investor Relations, Hilton Worldwide Holdings, Inc.*

Thank you, Chad. Welcome to Hilton's second quarter 2020 earnings call. Before we begin, we'd 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 speak only to our expectations as of today. We undertake no obligation to publicly update or revise these statements. For a discussion of some of the risk factors that could cause actual results to differ, please see the risk factor section of our most recently filed Form 10-K as supplemented by our 10-Q filed on May 7, 2020.

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](http://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 second quarter results. Following their remarks, we'll be happy to take your questions.

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

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**Christopher J. Nassetta**

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

Thank you, Jill. Good morning, everyone. And thanks for joining us today.

Before we get started, I'd like to offer our sympathies to all those affected by the recent explosion in Beirut. Our thoughts are with our team members and everybody impacted by this tragic event. It goes without saying that these past several months have been challenging. While we have continued to navigate the global coronavirus pandemic and its impact on our business and the communities we serve globally, here in the US, we have also witnessed tragic acts of social injustice, leading to difficult, but necessary discussions regarding systemic inequalities. For more than a century, our hotels have been a welcoming place for all, a place where we bring together people of all backgrounds and connect them to the light and warmth of our hospitality. Now, more than ever, Hilton remains committed to fostering an inclusive culture and driving positive change in our communities and society more broadly.

Building on the work we have been doing, we have set even more aggressive leadership diversity targets across our corporate and hotel teams. As we announced yesterday, we're happy to welcome Chris Carr to our board of directors. Chris brings several decades of executive leadership across global consumer companies, and we look forward to his insights and diversity of thought as we focus on our near-term recovery and long-term growth opportunities.

Unfortunately, the new reality of our business required us to adapt our organizational structure moving forward. During the quarter, we took additional measures to further reduce costs, including the reduction of approximately 2,100 corporate roles globally and the extension of previously announced furloughs. These were very difficult decisions, as our company's culture has always been centered on supporting our team members who deliver hospitality for our guests. Through these challenging times, I'm proud of how our team has continued to live our Hilton values, to have integrity, to deliver exceptional guest experiences and to be leaders in our industry and in our communities.

We are working hard to restore confidence to travel again and have taken a number of measures to enhance the safety of our team members and guests. In June, we launched Hilton CleanStay in collaboration with Lysol and the Mayo Clinic to provide industry-leading hygiene practices in our properties all around the world. Our new elevated standards include modifying housekeeping procedures and adjusting common areas in our hotels to support social distancing. As part of the program, we also recently launched Hilton EventReady, which sets new standards for cleanliness and customer service for meetings and events. Additionally, we are requiring everyone inside our hotels in the US to wear face coverings in all indoor public spaces.

Long before COVID-19, we had invested heavily in technology to give our Hilton Honors members access to seamless and contactless experiences with our Hilton Honors app. Today, our Honors members can benefit from features like digital check-in, room selection and the ability to message with hotel team members from their own device. Additionally, Digital Key allows for contactless check-in and checkout at the vast majority of our hotels globally. Combined with our new approaches to cleanliness, we think these are important initiatives on the road to reassuring guests of a safe experience at our hotels as travel resumes, while still delivering exceptional customer service.

Turning to the quarter, as expected, the pandemic and the related decreases in global travel and tourism materially affected our second quarter results. System-wide RevPAR declined 81% year-over-year, with all regions and chain scales meaningfully impacted. Approximately 20% of our system-wide properties had temporarily suspended operations at some point in the first half of the year. Today, nearly 80% of those hotels have reopened, including all of our hotels in China and the majority of our hotels in the United States. In Europe, we're seeing steady progress on re-openings, as restrictions ease and demand gradually return. Today, more than 96% of our system-wide hotels are open and operating.

In terms of demand, we're seeing meaningful improvements off the lows in April, with monthly sequential increases throughout the quarter and into July. System-wide occupancy rebounded from a low of roughly 13% to approximately 45% currently, with all major regions improving. In Asia Pacific, performance is largely driven by rebounds in both leisure and business transient travel in China, where occupancy is more than 60%. In the Americas, occupancy is over 45%, boosted by an increasing demand for limited service hotels and drive-to leisure markets. During the Fourth of July weekend, nearly 800 hotels in the US ran over 80% occupancy.

Across Europe, Middle East and Africa, occupancy is generally around 30%, although easing government restrictions and continued re-openings should help drive further improvements there. As we look to the fall, assuming no significant disruptions to the current environment, we hope to see a continuation of the modest pickup in business transient demand, which would help offset slower leisure demand post-summer. However, we remain cautious given the uncertainty surrounding the virus and its overall impact, including the reopening of schools and offices.

While we continue to adjust to new ways of interacting, one thing remains consistent: our focus on doing what is right for our guests and their evolving travel needs. For that reason, we made a number of changes very early on. We introduced and have since extended the most flexible cancellation policies in the industry, and we're among the first global hotel companies to implement rewards extensions to help Honors members maintain their points and status. Through our partnership with American Express, we also enhanced our co-branded credit cards to include more ways for Honors members to earn rewards during this time and provide cardholders with greater flexibility and even more points now to use for future travel.

From a development perspective, activity was disrupted given the broader macro challenges; yet we were still able to add 7,000 rooms to our system and achieve 4.8% net unit growth versus the same period last year. Monthly openings increased sequentially throughout the quarter, and in June, openings in the Americas were nearly 15% higher than last year. Additionally, we continue to be encouraged by conversion opportunities, which should help mitigate the impact of construction delays. For the full year, we expect net unit growth to be in the 3.5% to 4% range. It will take time for development to fully recover, but we're confident that we have the brand and the commercial engines to continue taking a disproportionate share of the global pipeline.

In the quarter, we signed several notable luxury deals, including the Waldorf Astoria, Tokyo, the Conrad Costa del Sol in Spain, and the OCEANA in Santa Monica, which will join our LXR portfolio. On the conversion side, we saw positive momentum across our DoubleTree, Curio and Tapestry brands. As an additional testament to the strength of our development strategy, during the quarter, we signed a management license agreement with Country Garden, one of the strongest players in the Chinese property market to exclusively develop Home2 Suites properties in China. We expect this partnership to produce more than 1,000 hotels over time and look forward to introducing a new brand and segment to the Chinese market. As one of Hilton's fastest growing and award-winning brands, we think Home2 is well positioned to capture additional growth opportunities in the extended stay, mid-scale segment in China.

Taking the current landscape and uncertainties into considerations, we have a clear path forward. I am very proud of what we have been able to accomplish during these difficult times, and I'm confident that we will emerge stronger. I think we have demonstrated our flexibility, resiliency, and an ability to embrace change, all while continuing to do what's best for our people and the future of our business.

With that, I'm going to turn the call over to Kevin for a little bit more detail on the second quarter results.

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### Kevin J. Jacobs

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

Thanks, Chris, and good morning, everyone. In the quarter, as Chris mentioned, system-wide RevPAR declined 81% versus the prior year on a comparable and currency-neutral basis, with decreases across all chain scales and regions. Decreases were largely driven by occupancy declines, with rate pressure from increased competition for lower-rated business further impacting results. We did, however, see sequential improvement throughout the quarter, particularly in China and the US. Adjusted EBITDA was \$51 million in the second quarter, declining 92% year-over-year. Results reflect the significant reduction in global travel demand due to COVID-19 and the subsequent temporary suspension of operations at more than 1,000 hotels at some point in the quarter.

Revenue declines were mitigated by greater cost control at the corporate and property levels. Management and franchise fees decreased 77% to \$135 million, driven by RevPAR declines and unfavorable timing of license fees. Our ownership portfolio posted a loss for the quarter, due to significant closures, fixed operating costs and fixed rent payments at some of our leased properties. Results were mitigated by cost control tactics across the portfolio. Diluted loss per share adjusted for special items was \$0.61.

Turning to liquidity, we ended the quarter with total cash and equivalents of nearly \$3.6 billion, following a number of actions taken early in the quarter to enhance our position and increase our financial flexibility. Additionally, our cash burn during the second quarter was lower than expected, partially due to the timing of certain payments. As we look at the balance of the year, we remain confident that we have ample liquidity to continue to navigate the current environment and prepare for recovery.

Further details on our second quarter can be found in the earnings release we issued earlier this morning. This completes our prepared remarks. We would now like to open the line for any questions you might 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:** Certainly. We'll now begin the question-and-answer session. [Operator Instructions] Our first question will come from Carlo Santarelli with Deutsche Bank. Please go ahead.

**Carlo Santarelli**

*Analyst, Deutsche Bank Securities, Inc.*

Hey, Chris, Kevin.

Q

**Christopher J. Nassetta**

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

Hey, good morning, Carlo.

A

**Carlo Santarelli**

*Analyst, Deutsche Bank Securities, Inc.*

Good morning. Chris, you talked a little bit about, obviously we're seeing demand come up a little as we see that in the data and that you expect kind of a modest business transient demand somewhat offset a waning leisure as we move out of the summer vacation months. Bigger picture, as you think about the second half of this year, could you talk a little bit about how you foresee kind of the shape of the recovery in aggregate?

Q

**Christopher J. Nassetta**

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

Yeah, I'd be happy to. Obviously, that is the big question. And I certainly have a view, although I think there's obviously still enough uncertainty out there where it's hard to be confident in the view. But my view really hasn't changed, Carlo, a whole lot from the last call. And if I think about the shape of the recovery so far, which has gone from a low of basically a little over 10% to now running 45% and moving our way up to 50%, while those are still terrible numbers, that is a lot of improvement over a relatively short period of time.

A

And if you go back to what I said on the last call, that's sort of what we had expected. I mean, things are sort of moving fairly close to what we would have expected. I said on the last call and I sort of say the same thing, I think we're going to – you're going to see a step change from very, very low levels as you start to reopen the world, where you're going to get 40% to 50% occupancy levels by the end of the summer, early fall. And then it's going to be a grind up because as you get through the health elements of this crisis, you're going to be dealing with an economic crisis or a recessionary environment, and businesses and individuals have been impacted. And so, you're going to be on a grind up from there.

And that's sort of what I think is happening. I think as you go into the fall, what I would hope is that we're going to be in that 45% to 50% range. You're going to see leisure trail off, as you always do, but I think a little less so, it will take a little longer for that to bleed off because a lot of kids aren't going back to school, or they are, but virtually. A lot of offices aren't opening up, and so their people are going to be virtual. So, they have a lot more flexibility to sort of extend the leisure travel season. And we can already see early tell-tale signs of that because it's been very hard to get availability in certain locations in July and August. So, they're extending into September and maybe into October. So, I think you'll have a little bit heavier leisure business as you go into the fall, which will be helpful, because that's been a significant part of the business.

And you will, I think, continue to see some movement up in business transient. We saw it through the quarter. I mean, if you look at our managed business transient segment, which would typically be, like last year in June was 20% of our business. In June of 2020, it was 18% of our business. Now, it's a little bit different makeup of business traveller than probably it was last year for the last decade or two or three, but nonetheless it was business-related travel. So, you are starting to see that come back. Not rapidly, but slowly. And I do think, all things being equal as you get into the fall, you will see that continue.

So, I think you're going to hopefully cross over with the pickup – dropping off of leisure, a slight pickup in business. And you're going to sort of hang out in that arena and be grinding slowly but surely as we have been our way up. Even with the recurrence of COVID in a bunch of parts of the country, we stepped back for two or three weeks if you look at the data, and then we started the march back – grind back up again. And the grind up again will depend on the trajectory of the overall recovery. I think, my own view, as I said it last time, I think it is two or three years to sort of get back to the demand levels that we were experiencing in 2018 and 2019. But I think that is sort of the broader trajectory.

We will be in the hopefully 45%, 50% range and then moving our way steadily, slow and steady up from there. I do think there's a decent likelihood – I'm not a health expert, but I am certainly talking to a lot of them and folks in the government and the like on a daily basis. I do think there is a reasonably good chance that we will have not just a vaccine, but a suite of different vaccines that get approved sometime in the fall that will have different levels of effectiveness but combined will be reasonably effective. And I think that's going to help. Obviously, that's going to sort of, I think, help move us a little more rapidly through the health issues and then just into the economic issues.

I do think, if you get that, you'll see some step change in mobility and thus travel, particularly business travel, just because that incremental person that is reticent to travel without it is going to have more confidence to do it. But I still think – I stand by what I said. I think you could well probably have a step-change up on the occurrence of that. You will, even without it, continue grinding up. And then it will take some time to get – because I don't think we should be under any illusion that even with a vaccine, we're going to be back at 2018 or 2019 levels of business, transient travel demand for a period of time just because the economic impact has been significant. And it will work out over the next two or three years, but it will take time to.

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**Carlo Santarelli**

*Analyst, Deutsche Bank Securities, Inc.*

Q

Very helpful, Chris. Thank you very much for that. And then just if I could one follow-up. [indiscernible] (20:05) obviously the 3.5% to 4% down from what you said before, but in the current environment, certainly not bad. Could you talk a little bit about kind of what the components of that look like, what you're seeing in terms of conversion activity, how aggressive you've been able to be, et cetera, on that front?

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**Christopher J. Nassetta**

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

A

Yeah. I mean, it's obviously, Carlo, lower than what we thought pre-COVID. It's higher than what we thought last quarter. It's moved up a tick. I think we said last quarter about midpoint of our guidance, which would be in the low 3s and now we're – midpoint of our current guidance is in the high 3s. And I would probably – with what I see today, I'd probably, that based on what we're seeing it would be towards the higher end of that if all goes well. I think conversions are going to play a role in it. They certainly will be. We have a lot of momentum there in terms of the deals that we're signing and that are in active discussions. I think those are up circa 50% from where they were last year in conversions. Some of that will translate into this year, and a lot more of it will translate into next year. So, I think a larger component of that will be conversions.



But the latest data that I'm seeing is probably 4 points, 5 points, 6 points. I think it will be significantly more than that next year just because the world sort of while conversions are obviously sort of in keeping with what's going on in the broader environment, we went through a period of time of three or four months where sort of nothing was getting done. Now, we're in lots of active discussions. Those deals need to be negotiated. In some cases, you need to do CapEx work, property improvement programs and get it into the system. And so, a bunch of that is going to happen this year. As we said, we'll have meaningful incremental percentage this year, but I think a lot more just timewise by the time things get done will be into next year.

And I do think the combination of that with the properties that were new construction that got delayed because of the freezing of time during particularly most of the second quarter will mean next year will be a better NUG year. I don't think it will be back to where we were yet. I think it will take a couple years to get back to where we were. But I just think the math of how NUG is going to work is going to – it does strongly suggest that our 3.5% to 4% is sort of the low point in this cycle. And then next year is better, and then we're moving our way back to a more stabilized environment.

I mean, what's interesting – you didn't ask it, but somebody will. We're still – there are a few months that everybody is frozen. We're still signing a lot of deals and getting a lot of deals under construction. I mean, I wouldn't hold me to it because data is not perfect these days in the sense that it's hard to know exactly what people are going to do. But our best guess is that we will probably sign – our signings may be down circa 20%, our starts right now look like they're down circa 10%, and then we already talked about NUG.

So, that's why the pipeline numbers are looking good is we're still signing lots of deals that we're eventually going to open, and we aren't opening them as fast. So, the math becomes pretty simple to explain there. So, I've been surprised, honestly, to the good on activity on the development side on all fronts. I've been surprised on how many deals we're getting signed. I've been surprised to the good on how many are going under construction. And as I said, our NUG numbers are sort of inching up, which is a pleasant surprise.

So, we're still working hard in the Country Garden deal. I think it's a testament to the fact that we're not crying in our milk. We've got a business to run. We've got great brands. This too shall pass. We will get back to a more normalized environment. And we got to be forward-looking because we've got to deal with the current environment, which I think we have quite well, but we also have to look forward on Country Garden, which we were working on pre-COVID obviously if it got done is a testament to the fact that we're dealing with the here and now and we're also dealing with the future, all at the same time, which is what we get paid to do.

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**Carlo Santarelli**

*Analyst, Deutsche Bank Securities, Inc.*

Great. Chris. Thank you very much.

Q

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**Operator:** The next question comes from Shaun Kelley with Bank of America. Please go ahead.

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**Shaun C. Kelley**

*Analyst, Bank of America Merrill Lynch*

Hi. Good morning. And thanks for taking my question.

Q

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**Christopher J. Nassetta**

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

A



Hey, Shaun.

**Shaun C. Kelley**

*Analyst, Bank of America Merrill Lynch*

Q

Hi, Chris. So just wanted to maybe follow up. I mean, obviously some very difficult decisions were made in the quarter as it relates to kind of the broader corporate cost structure and operating structure for Hilton here. How can you help us think about what happens as trend lines continue to improve? And what parts of this, of these reductions need to come back because these were really volume-driven piece of the business versus how much of this, kind of go forward, you can actually rethink or possibly be a little bit more efficient going forward? Just any thoughts or color on that.

**Kevin J. Jacobs**

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

A

Yeah. Hey, Shaun, it's Kevin. I'll take this one. I'd say, look, obviously it's going to be a combination of both of those things, right? We do have parts of our business – that's obviously a very complicated business. There are parts that are sort of purely volume, and there are parts where it's not as much volume and we can be more efficient. I'd say the way to think about it is, for our corporate costs, for our corporate G&A, we gave you guidance last time that it would be down around 25% to 30%. We're coming in right along those lines. Most of the moves that we ended up making were largely thought through when we gave that guidance if not final decisions had been made, but it was certainly factored into our guidance.

I'd say, in that part of the business, the way to think about it is most of the costs will be sustained. The cost savings will be sustainable. There will be some elements of furloughs and salary reductions that obviously won't repeat themselves and create a touch of a headwind. And then, of course, that's offset by the fact that the reductions in force then get annualized going forward, which will be largely permanent savings. And so as the business comes back, some level of inflationary type expense growth you should expect to come back. But I'd say for some period of time, it should be quite sustainable.

**Shaun C. Kelley**

*Analyst, Bank of America Merrill Lynch*

Q

Thank you very much.

**Christopher J. Nassetta**

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

A

Sure.

**Operator:** And the next question will be from Joe Greff with JPMorgan.

**Joseph Greff**

*Analyst, JPMorgan Securities LLC*

Q

Good morning, Chris. Good morning, Kevin.

**Christopher J. Nassetta**

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

A

Good morning.

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

Hi, Joe.

A

**Joseph Greff***Analyst, JPMorgan Securities LLC*

Question you mentioned and referred to the nice occupancy gains where the portfolio is in that 45% to 50% range. I think you referenced the 50% in one of the answers to the questions. I was hoping maybe you can frame it – maybe you said it and I missed it – but are you doing or tracking from a rate perspective? Maybe you can kind of put it in perspective of 3Q to the July RevPAR trend and kind of benchmark that against the industry data domestically and globally. And then I have a follow-up.

Q

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

Yeah. I would say weighted, our performance weighted for the industry is maybe a touch better when you adjust for the difference in methodology. Which is that we're keeping all of our hotels, even the hotels that closed temporarily or are still closed, in our comp set. If you – and Star (sic) [STR] is not – if you adjust for that, and we're on top of or a little bit better.

A

I'd say, on the rate side of things, we have seen improvement. Basically for the quarter, at the beginning of the quarter, rate was down of the – like April was almost 90% down in RevPAR, about 35% down in rate. If you look at July, that's 25% down. If you look at where the trend line is going in August and beyond, it's coming down.

I mean, I think the rate thing is a really – we've had a lot of discussion about it here because lots of questions on, is the industry going to maintain rate integrity and all that. I think what is really behind the rate issue, as we dig into the data, and it doesn't take much digging because there's not that much data these days or not as much as normal, it's really a mix issue, which is we have – the traditional customer of ours particularly has been a higher rated leisure and a higher-rated business traveler. There's just not as many of them at the moment traveling for all the reasons that you guys know. And so, it's a different sort of population, not entirely, but largely different than we're used to which is much more – not to be judgmental, but a much lower-end, lower price point customer.

And so, the issue for all of us in the industry – and I can't speak for what others have done, I speak for us is we have owners that are really hurting and we're trying to do everything we can to help them because no business is built for sort of what was happening, which is like limited or no revenue and then very, very low levels of revenue. And so, in this very difficult time, along with our consultation with our owners, our view was whatever business is out there, to help them, we need to go after it.

And so what's happened is the rates have come down largely as a result – I mean, I'm not going to say there isn't rate pressure broadly in an environment like this. Everybody expects a bargain. So, yeah, there's rate pressure broadly. But if you look at the data, if you look at the math, the bulk of it is just mix. We are now – in this environment, we have gone after directly some through the OTAs but largely through our own channels with Honors and all of our marketing campaigns and marketing spend, lower funnel has been going after that lower-rated leisure traveler because it has been the bulk of what is out there to get. And we need to help our owners get to the other side of this.

And so, when you mix that in, it's just – it starts even pre-COVID at a much lower price point. So I think that's what's going on with ADR. I think while there will be pressure on ADR because of the economic issues that have

been caused as a result of COVID and it would be silly to say there won't be. I think you will get – I think the pressures that you saw in the second quarter that are still ongoing, when you get back to what I'll call a new normalized environment where you have many more of our traditional travelers, higher-end leisure and higher-end business transient travelers on the road again, I think this will right itself quite rapidly.

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**Joseph Greff***Analyst, JPMorgan Securities LLC*

Q

Great. And one of the answers is a nice segue to my follow-up question. Based on what we were able to ascertain from the release, it doesn't seem that any kind of third party collections issues was a significant working capital or free cash flow drag in the 2Q. One, is our premise there correct? And then, two, has there been any trend change in the 3Q? And would you anticipate maybe just more broadly that if there are issues there would be some sort of lag? Or how do you view that? And that's it for me. Thank you.

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

A

Yeah, thanks, Joe. I'd say, look, what I'd say generally on the collections and broadly working capital side is obviously relative to the guidance we gave you last quarter, things generally went better than we thought. And I'd say that's across the board in terms of the buckets in the managed portfolio and in terms of payment of fees and the like.

We do – in this environment, we have built some receivables. We are sort of collecting at a slower pace than normal, which is completely understandable given what is going on in the world and given what our owners are going through. But I'd say, again, largely better than we thought. Sort of obviously everything that's happened was captured in the numbers. Nothing has really changed so far in the third quarter, although we should point out that it's still early in the third quarter and there's a lot of year left. But so far it's been going quite well.

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**Operator:** Thank you. The next question comes from Stephen Grambling with Goldman Sachs. Please go ahead.

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

Q

Thanks. I'm going to actually follow up on that last question on working capital and also tying in reimbursed costs. How should investors think about how these will trend in a more sustained recovery? I mean, do you just get back to breakeven or could you actually get incremental revenue or income in from those relative to the expenses?

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

A

Well, revenue doesn't get recognized – collections doesn't affect the way we recognize revenue. And so, I think you could see on the P&L that in the funded part of the business or the reimbursable part of the business, we did spend more than we earned in this quarter, which is completely normal if you think about what's going on in the world and how quickly revenues declined. I think from a cash basis, we would expect the vast majority of it will be repaid. And so you should think about there will be a flip-around on the cash side, it doesn't necessarily correspond with what you're seeing on the P&L on the revenue side.

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

Q

Got it. And then you also referenced on the distribution side a little bit on the OTAs here. I guess, prior to COVID, I think there was a heavy direct booking campaign and there was maybe some hope that consumer preferences may change such that in a downturn you might start to see less focus or less emphasis on the OTAs. Given the current environment, I guess in some ways would argue for more inventory going to the OTAs. Are you seeing that change in behavior? Or if there is any other data point that you can provide that might glean some insight there.

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**Christopher J. Nassetta**

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

A

Yeah, it's a good question. And I think I sort of touched on it indirectly. Yes, in this environment, you just heard what I said about the biggest bucket of demand, which is the lower priced leisure demand, that would typically favor OTAs. That is typically what we have used over time the OTAs for, to supplement the other pools of our demand that we have very direct access to. And so, you would think this would mean that our distribution channel mix would be shifting in that way. But reality is it has not.

Our direct channels in part because of what we've been doing because we do want to continue to build direct relationships with customers of all sorts, including these customers who we hope may not have been our typical customer before but we hope will adopt our system during COVID and post-COVID and will add to the complement of customers that we have.

And so, the OTA business, from a distribution point of view, has held relatively constant. Our direct channels are growing at a faster pace. And that is, as I said, that is because of our actions. Not so much in what we're doing with the OTAs, but very much how we're spending our marketing dollars and how we are orienting our Honors programs to access that type of customer.

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**Stephen Grambling**

*Analyst, Goldman Sachs & Co. LLC*

Q

Makes sense. Thanks so much. Best of luck in the back half and through the rest.

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**Christopher J. Nassetta**

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

A

Thanks.

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**Operator:** Our next question is from Thomas Allen with Morgan Stanley. Please go ahead.

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**Thomas G. Allen**

*Analyst, Morgan Stanley & Co. LLC*

Q

Hi. Good morning. So you guys have obviously had a long experience operating hotels and salons. Some hotels in the past, over a lot of hotels. Just big picture, how are you thinking of the overall hotel operating cost structure will change in the future versus pre-COVID levels? Thanks.

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**Christopher J. Nassetta**

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

A

Yeah, Tom, it's a really good question and I would say that deserves a good answer, as always. I will give you an answer. I'm not in a position at the moment yet to be highly specific but I will certainly answer it directionally. And

the fact of the matter is we're spending probably more time on that right now inside our organization than any other single thing that we are doing for all the things you would guess.

In the early stages of COVID and continuing our effort with our owners – because we need to help them bridge this very difficult time – had been to provide a tremendous amount of flexibility against our standards of all sorts, in terms of food and beverage standards, operating, across the board. And the reality is doing a lot of work with our customer base. That's what they expected. Everybody knows we're in a different world, and that things are going to be different.

We will get back to a more normalized world, but we want to use this opportunity to really dive very deeply into each and every brand, which we are doing, both the CapEx and OpEx standards to see if we can't drive far greater efficiency.

Now, the trick is, and the needle that we are not just trying but we will thread is, we have the best brands in the business and those brands have the highest premiums in the industry. In COVID world, it's like anarchy out across the world but we're going to get out of that in the not too distant future and these brands will continue to have the premiums.

But the reality is, like any business over time and any industry, you add things, you add things – I would argue we all have been better at adding things than taking things away. And so what we're doing in a simple way, working very closely with customers, is figuring out what are the things that are most important to driving those premiums and what are the things that don't matter. And if the things that don't matter or they were from yesteryear and they might have helped ten years ago but they don't matter as much today then we don't need to be doing those things.

And then, looking just at the engineering, particularly in the limited service space, of every single element of the hotel, like food and beverage to the penny on cost per occupied room and the like.

And so I am – I'm not just optimistic. I'd say we are going to find for our ownership community significant savings, at the same time, I believe finding a way to make these brands even better and even more relevant to customers because we will lean in heavier to the things that matter and get out of the things that don't matter.

So I know in the end, you guys like to translate everything to a model and would like to be able to model for the ownership community what that means. I can't tell you because we're right – we're literally deep in the middle of it. And we've got a very large group of our most important and knowledgeable owners that are at the table with us. We're in constant communication with a broad array representing our customer base. And I think it's really exciting work that, if you were to take an 2018 or 2019 sort of normalized demand level, we will clearly be driving in every one of our brands higher margins just because we're going to – necessity, I've said this too many times in my career, which bums me out. But necessity becomes the mother of invention. Well, I think our brands are the best and drove great margins and we've got disproportionate share of pipeline because our brands perform better top line and bottom line than our competitors. That's not good enough. Right now, our owners are suffering. It's going to be a long dig out, and we know we can create greater efficiencies and at the same time not in any way threaten but enhance our premiums.

Thomas G. Allen

*Analyst, Morgan Stanley & Co. LLC*

Helpful. Thank you.

Q

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

**Robin M. Farley**

*Analyst, UBS Securities LLC*

Q

Great. Thanks. I wonder if you could give us a little color on the conversations that you're having with your corporate customers. I don't know if this is a little too early for when you would normally have corporate pre-negotiated rates discussions. But are corporate buyers just sort of saying, hey, we don't even need to have this conversation? Call me in six months or, you know, I guess if you could give us a little insight into what your big buyers of business travel historically are saying?

**Christopher J. Nassetta**

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

A

Yeah, I mean, it is a little early, Robin but it's a really good question. And I'd ask it too.

I think next quarter we'll have a heck of a lot more to say because we'll have had a lot more conversation. I would say – and I'm going to put it into three big buckets, okay? I think a third, a third, a third and I'm being more scientific than reality. But sort of in my own head, that's how it plays out.

A third of our big corporate customers are super understanding of what's going on, and they're of the belief that whatever deal we had should just continue on and they want to be supportive in this environment. They probably for a period of time are going to be traveling less, but they want to sort of continue on with the basic pricing parameters that they had. And they've signed up for that. I would say – and again, we're just quite early in the season of this dialogue. So it could change. I'd say a third of them don't know. Okay? They're sort of like, gosh, I don't know what to do. This is a crazy world. I sort of hear what you're saying. Maybe we should just keep going but they're sort of contemplative. And then, a third are saying, it's a really crazy world and we've got to get a better deal. Okay? We're suffering. If we're going to travel and we're going to stay with you, we've got to get a better deal. And I would say that's as much as I know at the moment.

I think, in the end, that third that are in the middle, I think half of them go both ways. I think it's sort of 50/50. When I talk to our sales teams and it's all anecdotal for the record. It's not like this is scientific data, but I'm talking to them all the time, every single week at least once. They'll say it's sort of half our big corporate customers get it. They want to be supportive. They're not going to beat us up. And half are sort of like, nah, I've got to get a better deal because my world blew up too.

So we'll see how it plays out. As I said, there will be an environment where you get through the health situation and you're in an economic downturn. There's going to be, as there always is, some pressures on rate. People are going to expect a bargain for everything, most things that they're doing. My own belief is that that will not be intense pressure, certainly not reflective of what you're seeing in the current environment.

As I said to an earlier question, much of the rate degradation, the bulk of the rate degradation as far as I can tell at this point is really just the mix. It's just a different customer base. There'll be pressure, but not this kind of pressure on rates as you get to a more normalized environment.

**Robin M. Farley**

*Analyst, UBS Securities LLC*

Q



That's great. Thank you. And maybe just as my follow-up, still thinking about sort of intentions of travelers, can you give color on, for group bookings, obviously I'm sure things like we hear from others are canceling through Q1. But are new group bookings coming in for next year? Or not really? Is there a pause in even people ...?

**Christopher J. Nassetta**

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

A

Yes. They are. Intentions keep picking up. I mean, you're right. I think all of – what we're seeing broadly is – a lot of it – we're doing some group. By the way, in the second quarter we did like 10% of our volume was group. I think it will be higher in the third and fourth quarter, for what it's worth, so. But again, it's not our typical groups. It's like – it's groups related to the crisis. It's businesses in small group meetings where they just have to do it, but their offices aren't really open yet. I mean – and we're getting a lot of that kind of stuff. But I mean it's obviously a small fraction of what it typically would be. I do think it will keep picking up. Because those sort of other types of groups are going to keep picking up as the year goes on.

But the traditional bigger group meetings and all that that are kind of our bread and butter in the fall, those are going to keep getting kicked out. A bunch of them are still on the books for the rest of the year, but I think a lot of that will wash out. And it's day-by-day you sort of see that washing out. And people are kicking the can into next year with again the hopes that the health crisis will have passed and or through a vaccine, herd immunity, whatever is going to happen. And the further we go in the year, the further they sort of kick it out because there's a lot of noise in the system and it makes them nervous about wanting to spend a lot of time and money planning a meeting they might have to cancel.

So, I would say where it starts to stiffen up a bit is starting in Q2 of next year. I think people, the psychology of it is for third and fourth quarter, you'll see groups, but it's sort of group meetings out of necessity or replacement for something what happened in your office. And that will pick up as time goes on. But the core sort of traditional group business is going to kick forward to Q2 through Q4 of next year. And we are both moving business that is canceling. We're moving every bit we can, which is most of it to a future date. And we're booking new business. I mean, we are booking tens of millions of dollars a week of new business for periods in the future, most of which is starting in the second quarter of next year.

So a lot of it will – again you get – it's like there's so many unknowns. You get a vaccine, it changes the game on a lot of these things. Again, you still have an economic situation to deal with, and people have still been damaged in that way. But I think it frees up, it creates a decent amount of momentum because the fear goes away. So I think we just have to see where all of this goes through the fall. I mean, again, I feel pretty good about where things are going with vaccines. There are – certainly there is lot of data out there that says as you get to the later part of this year and early next, even if you don't have a vaccine, you're going to be at a point of herd immunity because enough people are either naturally – have the natural antibody T cells or have been exposed in a way where it just can't spread the same way that it has. Again, I'm not a health expert. Like you, I read a lot of stuff. I think we just have to sort of get, watch it really carefully in the fall.

And on the current course, I think all segments will continue to grind up. Group will obviously be the longest lag because people require spending, planning. And right now most people don't want to do that. Right? They don't want to do that because they're afraid that they're wasting time and money.

**Robin M. Farley**

*Analyst, UBS Securities LLC*

Q

Does that mean actually that what you have on the books for second half of next year is actually kind of ahead of what it would normally be? In other words, versus the same time last year for this course?



**Christopher J. Nassetta**

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

A

No. I don't have the data in front of me, but, no, I don't think that's the case. Not yet. Not yet. I think it could eventually build to that, and if things go well, it will, I think. But not at the moment, no. We're not where we were.

**Robin M. Farley**

*Analyst, UBS Securities LLC*

Q

Thank you. Thanks very much.

**Operator:** The next question will be from Richard Clarke with Bernstein. Please go ahead.

**Richard J. Clarke**

*Analyst, Sanford C. Bernstein Ltd.*

Q

Good morning. Thanks very much. One of your competitors said a couple of days ago that they were expecting business travel to see a behavioral change. And about a 10% behavioral change. Am I right in thinking you don't adhere to that? And I guess their point was they would have to make up for that with alternative revenue sources, whether that's skewing more towards leisure or using the hotels in a slightly different way. Is that something also you're looking to contemplate going forward?

**Christopher J. Nassetta**

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

A

Well, I think that – I didn't mean to imply anything on that, as far as I was concerned. And so if I did, that's not what I meant. But in answer to that question, I would say – I mean, there's a raging debate about that that I think will be ongoing over the next three years. My belief is that from having done this for 37 years – and while we haven't had a pandemic like this, we've had lots of other things, lots of other similar things that have disrupted the environment – that in the short to intermediate term, you are definitely going to have a substitution effect because people, businesses have been damaged. And as a result, they're going to have to have, find ways to cut costs and save money. And so they're going to substitute Zoom in for certain types of meetings, and it will have an impact in the short to intermediate term.

I think over the long-term, there will be – and by the way, as a result, we of course are looking as we are now at every opportunity of how we utilize all of our rooms and all our public spaces and everything else in creative ways to be able to supplement and find different pockets of demand, whether that be leisure, or whether that be using rooms as offices in an environment where people aren't opening offices because we have a safe environment where people can be socially distanced by definition, et cetera. We're doing all those things.

I personally believe when you wake up in two or three years and you can – we'll all mark this moment and let's talk in three years, I think we'll have a raging debate that business travel will never be the same. And it may look like that because businesses have been hobbled, a lot of them. And it will be lower for a while. I've already said. I think it takes two or three years to get back. I think what we'll find when we wake up in three years, it will be more like it was in 2018 and 2019 than it is.

Now, there will be a substitution effect. There will be different – there will be certain types of business travel that probably forever will change. Whoever said 10%, God bless them. I'm not smart enough to figure that out. I've read a bunch of pundits have had views. I don't know. But at the same time like every other time, there will be other things and other need for travel that will emerge. And so I think while it will take a few years to get back, I

think, one way or another, we will have similar levels of demand both for business transient and group. People will want to congregate. People will have to meet, will have to build relationships. If anything that Zoom and WebEx I think has taught us is, it's really hard to build a real relationship this way. So maybe a bunch of internal meetings. Or there were some things – I mean, that's all we're doing. There are some things that I think will be – what percentage I don't know – will sort of become a more permanent way of doing things. But they will be supplanted by other forms of travel, where people are going to be out traveling for things that they haven't been traveling for.

And so short, intermediate term, we absolutely have scrambled every jet we've got to think about a weaker business transient demand environment to fill those gaps. We and I believe longer term it will recover to similar levels.

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**Richard J. Clarke**

*Analyst, Sanford C. Bernstein Ltd.*

Q

If I can just ask you a quick follow-up. Obviously, on your franchise agreements, the fee structure is heavily skewed towards room revenue. Is there a need to sort of reopen franchise agreements to make sure that you are aligned with the hotels to drive all these alternative sources of revenue as well?

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**Christopher J. Nassetta**

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

A

Well, I don't think so. I mean, the reality is in a big full-service hotel, our fees are generally based on both food and beverage and rooms and other revenues. So in the big complex hotels we already do that. In a limited service hotel, let's be honest, they're pretty much only rooms. So we don't have a lot of other infrastructure or capacity in the facility in most limited service.- like a Hampton Inn, there isn't a lot of meeting space. And by the way, that's part of room revenue in any event. There isn't – it's a small lobby. It's a different animal. And so it really is rooms. In those hotels if you don't have your traditional customers, what other ways can you sell rooms? Like I said, you can sell them as office space. You can do – there are things that – you can sell them as dormitories, which we're doing like crazy, right?

We've done dozens and dozens of deals across the country with universities. We're doing all those things. But all that flows through room revenues, and I think the incentives are properly aligned already generally.

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**Richard J. Clarke**

*Analyst, Sanford C. Bernstein Ltd.*

Q

Great. Thanks very much.

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**Christopher J. Nassetta**

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

A

Yes.

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**Operator:** The next question is from Smedes Rose with Citi. Please go ahead.

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**Smedes Rose**

*Analyst, Citi Investment Research*

Q

Hey, thanks. I just wanted to ask you, kind of going back to your pipeline, when you talk with your developers, what are they saying or telling you in terms of how banks are thinking about financing new construction at this point?

And maybe kind of – if you could talk about it relative to kind of franchise, limited service properties and then maybe anything you're seeing on the full-service side.

**Kevin J. Jacobs**

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

A

Yeah, I think it's a good question, Smedes. I think it's a little early. I'd say what people are saying. Everybody's being – I mean look, we're in the middle of a global pandemic, right. So I think everybody is being a touch more conservative about everything. I mean, that's why you sort of see, you hear Chris talking about us pivoting towards conversions and the like.

I'd say, generally speaking, though, projects that make sense can still get financed. There's a ton of capital in the world. Rates are low. If people are willing to equitize, if they have the equity if they're willing to equitize a little bit more, they can get deals done and they and their lenders can collectively – can collaboratively look towards the future and say, hey, look, we're going to open this thing up into – hopefully open this thing up into a new cycle. And so generally people are still working on that stuff.

And then, as it relates to the mix, what we were already seeing was much more demand in the smaller, limited service type hotels. The bigger more complicated full service hotels largely didn't get built a lot this cycle because the recovery never justified them. Building costs kept going up. Labor costs kept going up.

And so they really weren't all that active in terms of construction anyways. So it's really not that precise of an answer I think because it is a little early. But you should assume a little bit more conservatism across the board.

**Smedes Rose**

*Analyst, Citi Investment Research*

Q

Thanks. And then, Chris, can I just follow up with you. You talked a little bit about the operating model. That question came up earlier. Just one thing that's come up with owners is the idea of suspending housekeeping during a guest stay and making that just kind of a permanent part of the hotel operating business. Do you think that's really on the table? And does that meaningfully change the margin from an owner's perspective, kind of all else equal?

**Christopher J. Nassetta**

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

A

Yeah, we're right in the middle of that, Smedes. So I don't really have an answer. Everything is on the table, first of all. I mean, we're – that along with literally hundreds of other things are on the table. That's probably one of the bigger things. We have agreed already with our owners in the short to intermediate term to do that as part of our launch of CleanStay because we think it is a better protocol for cleanliness to not have third parties in the room.

And so we clean the room. We seal, literally put a seal on the door. And only if a customer requests it – so it's an opt-in – do we have somebody come in and do a limited cleaning. That obviously, based on the fact that people have been not opting in at a high rate, that has helped from a margin point of view. We also think it's helpful from a cleanliness point of view, which is why it was part of CleanStay.

What we're doing is using this moment, which at a minimum that will go through this year to figure out with our customers what they really want. I mean, what we're trying to do is thread the needle with our customer and owner community to make sure that what I said in my earlier comments that we are ultimately giving our

customers what they want so they'll pay a big premium for our product, and we're doing it in a way that drives the best margins humanly possible for our owners. And we have to satisfy both constituencies.

And so what we're doing between now and the end of the year is looking at a lot of data. We're doing it so we now have a real test that is system-wide that is live, that is allowing us to look at data, to see the behavior of the consumer, to talk to consumers about their views on this. And so it's definitely on the table, but we don't yet have enough data to have an answer. And I think the idea is that we will through the rest of this year be studying it and figure out based on that data what the right answer is.

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**Smedes Rose**

*Analyst, Citi Investment Research*

Q

Great. Thank you. Appreciate it.

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

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**Christopher J. Nassetta**

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

Thanks, everybody, for the time. Obviously, Q2 not a shining moment in our 100 year history, but I guess this is what happens when you have a global pandemic, we found out. I've lived through lots of different things over the years, and this is certainly has stretched the limits of I think what all of us have seen. But I'm really, as I said in my comments, I'm very proud of how we responded. We've taken a difficult situation I think in our – managing our way through it quite well.

Our team has been working tirelessly. Fewer of them working even harder. And I feel as good as I did pre-COVID about the long-term prospects of this business. It may not feel that way to you all right now, but I do think that when we wake up in two or three years, we will be back on track and this business will be performing, as will the industry quite well.

We look forward to talking to you after Q3. Every quarter we learn a lot. So I suspect we'll have a little bit better visibility into the trajectory of recovery, maybe even have some knowledge on vaccines, all of us, et cetera. So we'll look forward to catching you up after Q3. Take care and be well.

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

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