# Hotels - What's going on with 2018 corp. rate negotiations? Flat to up slightly

## But big pushback on 48+ hr cancellation terms. It appears many hotels caved in.

**C. Patrick Scholes**
212-319-3915
patrick.scholes@suntrust.com

**Bradford Dalinka**
212-303-4190
bradford.dalinka@suntrust.com

Gregory J. Miller
212-303-4198
gregory.j.miller@suntrust.com

Jeffrey Stantial
212-590-0993
jeffrey.stantial@suntrust.com

**What's Inside**

Insights provided by our corporate travel agency contacts on how they are handling corporate room rate negotiations for 2018

### What's Incremental To Our View

Negotiated transient corporate demand (where there are set rates for corporate accounts) represents one of the most important pieces of business for branded full-service hotels. Corporate room rates can drive revenue management strategies; consequently, the corporate room rate negotiations that have taken place recently will be influential towards RevPAR in 2018. **Over the past month we spoke with our corporate travel agency contacts and came away with three important takeaways:**

**We asked:**

1. **What were you targeting for corporate rate growth for 2018?** With negotiations generally wrapping up/finalized for many companies, **our contacts indicated they were negotiating for flat-to-up-slightly pricing in 2018. Our contacts suggest that this pricing was achieved (*there were far stickier negotiations on cancellation policies,* as discussed below).** We compare these results to Hilton's (HLT, $79.29, Buy) 3Q17 earnings call comments of corporate negotiate rate growth of +2-3% and Marriott's (MAR, $134.40, Hold) earnings call comments of "low single-[digits]". With the exception of fast growing industries, our general expectations for negotiated volume (room night demand) is flattish growth y/y, which is in line with HLT and MAR's comments.
   - **Our takeaway:** Expectations going into the negotiation period were generally modest (not unexpected considering the mediocre transient corporate demand environment in 2017.) Thus, the results from our sources are largely in-line with MAR and HLT's 3Q earnings call commentary.
2. **How did negotiations compare to last year?** There was one significant difference that we uncovered -- the new cancellation policies were extremely poorly received by corporations and that some hotels pushed back hard to keep the cancellation policies in place. Realistically, a 48 or 72-hour cancellation window is problematic for corporate travel agencies as a portion of corporate travel is relatively last minute/second and travel plans change quickly (particularly in roles such as sales). Our contacts suggested that there was some divergence on how corporations negotiated cancellations with the hotels. Particularly as negotiated rates are only one piece of the negotiation (cancellation policies, amenities, etc. also play factors), some corporations appeared to push harder than others. The big picture result is we believe some corporations were able to negotiate for the elimination of the multi-day cancellation policy (meaning: back to the historical 4 or 6 PM day of cancellation time). Other companies might have agreed to a 24-hour cancellation policy (instead of 48 or 72 hours) albeit with other perks.

- **Our takeaway: There are a lot of ramifications from this discovery.**
  - **First: it is news for us that the longer cancellation windows has had significant pushback.** We suspect that the average leisure traveler might have protested less (their travel dates are more fixed and often made more in advance) and has far less negotiation power.
  - **It is also news that for this year, the hotel companies might have conceded in some respects to corporate negotiated customers. In our view, this would suggest concerns from hotels regarding the strength of 2018 demand (of all customer segments, but particularly corporate transient).** Most of these negotiations took place before the tax bill (discussed below) and if the bill had passed sooner it is possible the hotels would have had a stronger position from which to negotiate.
  - **The above said, we believe it may be only a matter of time in which large corporations will have to accept 48 or 72-hour cancellation policies, which will lead to a desirous fee stream to the C-corps and REITS.** Hotel executives have pointed to the airlines as an example where cancellation fees/penalties are accepted practice.

3. **How did the tax bill play into your negotiations?** We preface that corporate rate negotiations began months before the tax bill was signed and by the time the bill was passed, corporate rate negotiations were in the process of finalizing. Thus, we believe that hotels were unable to assume a re-acceleration of corporate demand resulting from the tax bill when negotiations commenced and it was too late for hotels to renegotiate significant rate increases in December post-the tax bill passing. Similarly, we assume that many corporations did not assume any significant volume increases in their travel budgeting.
   - **Our takeaway: While the tax bill likely did not play a big impact in most corporate rate negotiations, there may be some positive consequences in terms of demand resulting from the tax bill down the road (positive to Lodging C-corps and REITS).** As we discuss in our coda, we believe that for many full-service hotels where there is relatively limited supply growth and high weekday occupancy, there may be more opportunities for hotels to push last-minute "rack" rates higher if corporate demand rebounds post-the tax bill. We believe this case is more muted in the Upscale space due largely to more significant supply growth.

**In our view, the major outstanding question on the corporate demand front for 2018 will be the amount of non-negotiated corporate volume room nights, specifically the last-minute bookings at rack rates.** This source of room demand is quite variable and often volatile depending on the macroeconomic environment. Even if negotiated demand volumes are relatively flat y/y, we believe that there will likely be at least a modest pickup in corporate demand simply from companies that decide to allocate more resources to travel following the tax bill passing (this would occur after many corporations have finalized their annual budgets, so we expect some conservatism from many corporations towards increased travel spending).

- We have yet to see clear evidence of increased forward corporate demand in our bookings intelligence (but no material deceleration over the past 16 months either) but as we weigh the puts and takes of existing high overall weekday occupancy and relatively low supply growth for many markets (particularly for full-service hotels), we believe that revenue managers may have some room to push weekday rack rates in 2018, likely at low-single-digit percent increases y/y.
- Nevertheless, we continue to expect low single digit RevPAR growth from corporate demand in 2018 with any tax cut related strength at least partly offset by approx. 40bps. of additional y/y new hotel supply.

### HLT: Valuation and Risks

We apply a blended multiple of 14.7x (9.5x for Owned/leased and 15.0x for Managed/franchised) to our 2018 adjusted EBITDA estimate to derive a 12-month price target of $77.

Risks include:

**Press reports (**FT, Bloomberg, etc.) **have indicated possible financial difficulties at HNA, a 25% holder of HLT shares.** If HNA should have to liquidate HLT we believe this would create near-term pressure on the shares. Separately, HNA interests (as a travel industry conglomerate) could conflict with other shareholders.

**Growth trajectory could disappoint.** Pipeline growth could either slow down or projects scheduled for construction could be cancelled, which would diminish system growth for the firm and disappoint investors.

### MAR: Valuation and Risks

Our price target of $108 for MAR is derived by applying a 14.8x target EV/EBITDA multiple (a blended average of the industry average multiples for each business segment) to our estimate for 2018 EBITDA.

Upside Risk: Significant U.S macroeconomic improvement results in large recovery in transient corporate demand (and consequential >400 bps RevPAR improvement). Owned assets sell for premium prices relative to MAR expectations.

Downside Risk: 2018 is a recession year in the US. Geopolitical and policy risks negatively impact lodging demand.

## Companies Mentioned in This Note

**Hilton Worldwide Holdings Inc.** (HLT, $79.29, Buy, C. Patrick Scholes)
**Marriott International, Inc.** (MAR, $134.40, Hold, C. Patrick Scholes)

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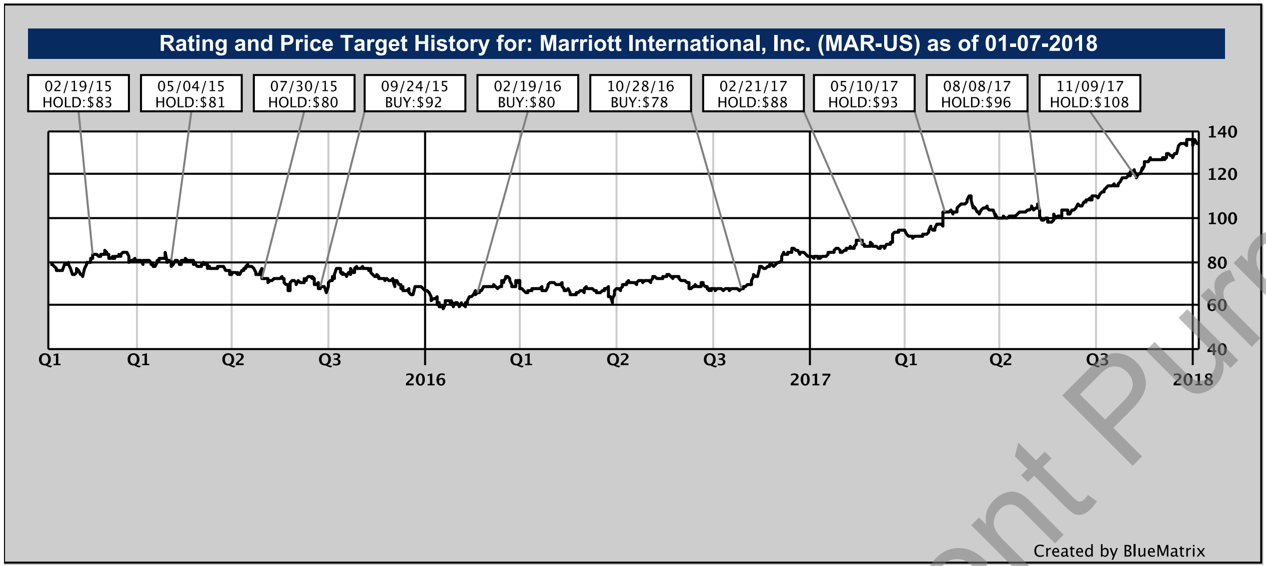


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