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Hilton Worldwide Holdings, Inc. (HLT)

Q2 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the Hilton Second Quarter 2021 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's prepared remarks, there will be a question-and-answer session. [Operator Instructions] Please note this event is being recorded.

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

Jill Slattery

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

Thank you, Chad. Welcome to Hilton's second quarter 2021 earnings call. Before we begin, we would like to remind you that our discussions this morning will include forward-looking statements. Actual results could differ materially from those indicated in 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'll refer to certain non-GAAP financial measures on this call. You can find reconciliations of non-GAAP to GAAP financial measures discussed in today's call in our earnings press release and on our website at ir.hilton.com.

This morning, Chris Nassetta, our President and Chief Executive Officer, will provide an overview of the current operating environment. Kevin Jacobs, our Chief Financial Officer and President of 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.

Christopher J. Nassetta

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

Thank you, Jill. Good morning, everyone, and thanks for joining us today. As I think our second quarter results demonstrate, we continue to make significant progress towards recovery, working hard to serve all of our stakeholders – for our guests, to deliver a reliable and friendly experiences in a very demanding environment; for our team members, to maintain an award-winning culture by creating an inclusive, safe and welcoming environment, full of opportunities; for our owners, to drive value through premium market share and efficient and effective operating models; for our communities, to remain a positive force for good at a time when it is needed most; and, finally, for our shareholders to maximize profits, free cash flow, and, overall, total returns.

We're pleased to see that our diligence and determination are beginning to pay off. As much of the world reopens, the pent-up demand for travel we've been anticipating is happening. While the pace of recovery varies and COVID variants remain a risk, we are seeing significant sequential improvement in every major region.

In the second quarter, systemwide RevPAR grew 234% year-over-year. Compared to 2019, RevPAR was down 36%, improving 17 percentage points versus the first quarter, with June RevPAR improving 24 percentage points

versus the first quarter and down only 29 points versus 2019. Additionally, 30% of systemwide comparable hotels exceeded 2019 RevPAR levels in June.

Adjusted EBITDA was \$400 million, up 684% year-over-year. Performance was driven by strong leisure demand and rate growth. For the second quarter, US leisure demand exceeded prior peak levels with rates at 90% of prior peaks. This positive momentum continued into July, with systemwide and US leisure room nights and rate exceeding 2019's levels.

Business transient also increased meaningfully throughout the quarter, with June RevPAR for the segment increasing 20 percentage points from the first quarter. We saw improving results in small and medium-sized businesses and positive momentum across larger accounts. In June, business transient room night demand was 70% of 2019 levels, with rates over 80% of 2019 levels. We continue to see progress in July with similar room night demand and rates at 90% of 2019 levels.

Group performance in the quarter also improved sequentially, driven primarily by social groups, given seasonally higher leisure demand. Overall group demand increased nearly 20 percentage points sequentially from the first quarter, ending June at more than half of 2019 levels. Additionally, group bookings for next year are at rates above 2019 peaks.

Approximately 99% of our hotels are now open and operating, including some of our largest urban and group properties. In the last few months, we were thrilled to celebrate the reopenings of the legendary Palmer House Hilton, the Chicago Hilton and the Hilton San Francisco Union Square. As government restrictions loosen and more people are vaccinated, we continue to see positive momentum in demand and an increasing ability to push rate.

For July month-to-date, systemwide demand is 85% of 2019 levels, with rates equal to 2019. In the US, July RevPAR is roughly 85% of 2019 levels. And in China, RevPAR is now above prior peaks. With increasing transient bookings, digital traffic and group sales leads, we are optimistic about the forward trends.

Turning to development, we delivered another robust quarter of growth, with net units increasing 7% year-over-year, ahead of expectations due to strong openings in the US and fewer overall removals. During the quarter, we added 119 hotels, totaling nearly 20,000 rooms and celebrated the five-year anniversary of Tru with the opening of its 200th property. With nearly 270 hotels in development, Tru continues expanding across the US and Canada, as well as moving into new markets in the Caribbean and Latin America.

We were also thrilled to celebrate the highly anticipated opening of Resorts World Las Vegas last month, marking the first ground up resort development on The Strip in over a decade. The property features three of our premium brands, Hilton, Conrad and LXR and adds 3,500 rooms to our portfolio. With expansive meeting and event space, 120,000-square-foot casino, 40 world-class food and beverage options, and a concert and entertainment venue with capacity for 5,000 attendees, this spectacular property raises the bar for Las Vegas and delivers on our long-standing promise to return to The Strip.

Along with the recently opened Virgin Hotels Las Vegas, Curio, we now have more than 30 properties totaling 11,000 rooms across 12 brands in the city. Las Vegas is also the first US market to house all three of our luxury brands.

Earlier this month, we debuted our premier meetings and events focused brand Signia by Hilton with the opening of the Signia Orlando Bonnet Creek. The property will undergo a multi-phase transformation featuring the addition

of more than 94,000 square feet of multi-functional meeting and event space, designed for an elevated meeting experience. In the quarter, we also broke ground on the nearly 1,000-room Signia Atlanta scheduled to open in 2023.

Our exceptional brands and industry-leading RevPAR premiums continue to drive a high-quality pipeline. In the quarter, we signed nearly 26,000 rooms, up 40% year-over-year and increasing from our first quarter pace, given strength in the Americas and Asia Pacific regions.

We ended the quarter with approximately 401,000 rooms in development, more than half of which are under construction. We had a record number of conversion signings in the quarter, representing 40 hotels and accounting for approximately 30% of our total signings, including the Conrad Chia Laguna Sardinia; the Conrad Shanghai, which will be our largest Conrad in Asia with more than 725 rooms; and the Hotel 1000 LXR, located just steps away from Seattle's iconic Pike Place Market.

Further expanding our all-inclusive and luxury portfolios, we announced the signing of three beach front resorts in Mexico earlier this month. The Hilton Vallarta Riviera All-Inclusive Resort, the Hilton Tulum All-Inclusive Resort and the Conrad Tulum will add more than 1,500 rooms to our existing 70-hotel portfolio in Mexico, demonstrating our commitment to continued expansion across the region and to growing our all-inclusive resort footprint. Travelers will soon be able to choose from an even wider variety of Hilton-branded all-inclusive resorts globally.

We expect positive development trends to continue and remain confident in our expectations to deliver mid-single digit net unit growth over the next several years. For 2021, we expect net unit growth in the 5% to 5.5% range, above prior expectations, given the pace of openings year-to-date.

Delivering on guests' desire for more flexibility in their travel experience and solving a long-time travel frustration, last month, we launched Confirmed Connecting Rooms, a first in the industry. This innovative technology enables guests to easily book and instantly confirm at least two connecting rooms. As families and friends begin to reunite, reconnect, and travel again, we're excited to create a seamless travel experience from booking through stay.

We continue to prioritize unique opportunities to engage our nearly 120 million Honors members, driving value for them through our enhanced partnerships and points redemption offerings. In the quarter, membership grew 10% year-over-year. On average, our premium members are staying with us even more frequently than in 2019. For the quarter, Honors members accounted for 58% of occupancy, reaching a high of 61% in May, only 2% below May of 2019.

As we head into the back half of the year, we know it's critical to lead with our culture, which recently earned us the number one spot on DiversityInc's list of Top 50 Companies for Diversity.

We were also thrilled to invite all of our team members to return to our headquarters last week. The energy and excitement in the office is palpable and we're thrilled to be back, fostering a collaborative environment which allows for innovative thinking as we remain focused on our strategic priorities and the bright future ahead.

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

Kevin J. Jacobs

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

Thanks, Chris. And good morning, everyone. During the quarter, systemwide RevPAR grew 233.8% versus the prior year on a comparable and currency-neutral basis as recovery accelerated, driven by strong global vaccine

rollouts, relaxed government restrictions and surging leisure demand, particularly in the US. As Chris mentioned, systemwide RevPAR was down 36.1% compared to 2019. Performance was largely balanced between occupancy and rate growth.

Adjusted EBITDA was \$400 million in the second quarter and those results reflect relaxed travel restrictions and strengthening global demand.

Management and franchise fees grew 220%, demonstrating the resiliency of our fee-based business model. Additionally, results were helped by continued cost control at both the corporate and property levels.

Our ownership portfolio posted a loss for the quarter due to the more challenged demand environment throughout Europe and Japan and related suspensions of hotel operations. Fixed operating costs further weighed on performance.

Overall, the ownership segment performed better than expected, largely due to continued cost control. For the quarter, diluted earnings per share adjusted for special items was \$0.56.

Turning to our regional performance, second quarter comparable US RevPAR grew 234% year-over-year and was down 31% versus 2019. Demand improved sequentially throughout the quarter, with occupancy averaging roughly 70% in June. Strong leisure demand, combined with improving business transient trends, drove rate improvement across the US with weekend ADR finishing June down mid-single digits as compared to 2019 rate and weekday rates down in the high single digits.

In the Americas outside the US, second quarter RevPAR increased 390% year-over-year and was down 54% versus 2019. While limited international travel weighed on overall performance, easing restrictions and strong leisure demand drove improving trends in June.

In Europe, RevPAR grew 470% year-over-year and was down 72% versus 2019. While the region saw month-over-month improvement, rising COVID cases and prolonged travel restrictions continued to weigh on performance.

In the Middle East and Africa region, RevPAR increased 287% year-over-year and was down 35% versus 2019. Performance benefited from strong domestic leisure demand, with rate now nearly recovered to 2019 levels in July.

In the Asia Pacific region, second quarter RevPAR grew 143% year-over-year and was down 33% versus 2019. RevPAR in China was down less than 9% as compared to 2019, with rising COVID cases in June temporarily disrupting strong performance trends in April and May. However, as Chris mentioned, China has since rebounded with RevPAR now trending above 2019 levels. In the rest of the Asia Pacific region, performance was tempered due to lockdowns in India and continued travel restrictions across Japan.

Turning to development, as Chris mentioned, in the second quarter, we grew net units 7%. Our pipeline grew sequentially, totaling 401,000 rooms at the end of the quarter, with 62% of pipeline rooms located outside the US.

Despite the challenges brought about by the pandemic, developer appetite for Hilton brands remains strong across the globe. As travel restrictions ease, regions prepare for recovery and owners focus on growth opportunities, development activity and interest is gaining momentum. For the full year, we expect signings to increase in the high-single to low-double-digit range year-over-year. We expect net unit growth of 5% to 5.5%.

Turning to the balance sheet. During the quarter, we fully repaid the outstanding \$1.2 billion balance on our revolving credit facility. As we look ahead, we remain confident in our balance sheet and financial flexibility as we move forward into the recovery and move closer towards our target leverage.

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 may have. We would like to speak with all of you this morning, so we ask that you limit yourself to one question.

Chad, can we have our first question please?

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] And the first question will come from Stephen Grambling with Goldman Sachs. Please go ahead.

Stephen Grambling

Analyst, Goldman Sachs & Co. LLC

Q

Thanks. You gave some great color on NUG, but I'd like to peel back the onion a bit more. Specifically, can you discuss how net unit growth expectations have evolved over the quarter as we look around the world, where your increased confidence comes from across things like brands' adds, deletions, conversions and how the financing environment is changing as we consider not only this year, but sustained growth beyond? Thanks.

Christopher J. Nassetta

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

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Yeah. Stephen, thank you. Good question. And happy to give a little bit more color. If you think about around the world on the development side, I think so goes the recovery sort of so goes the development is probably the simplest way to think about it. So, versus our earlier expectations and why we're a bit more optimistic, obviously, and have raised our outlook for the year, is largely driven by what we are seeing in faster recovery in the US and faster recovery in Asia, really China. And I'd say those are sort of the largest drivers.

If you think about recovery, that's where – as we suggested in the prepared comments, that's where we see the steepest slope of recovery. Europe is, obviously – we knew would be lagging and isn't contributing as much as the US and China is at this point. But, obviously, our expectation there is, as the UK and Europe continue to open, we'll see a meaningful uptick there. So, I think it's pretty much that simple. Slope of recovery steeper, more activity on the development side in terms of both signings and openings, people are back at it and picking up steam.

On the conversions, I'd say just modestly better. As you would note from prior calls, we've had high expectations for conversions. We have some great conversion brands. The system is performing at the highest levels from a market share point of view than it's ever performed in our history, and I think that's a great leading indicator for opportunities to convince folks who are independents to come into the fold as well as folks that have weaker brands that are looking for a better performance to come into the fold. Both of which are happening and a little bit better than our expectations.

And so, while we had – we expected things to pick up in the conversion area, I would say this year and then leading into next because some of the signings will take some time. Most of them happen pretty quickly, but some of them will take time in terms of CapEx for property improvements programs and the like. It's modestly better than what were pretty high expectations.

In terms of the financing environment, there's a lot to discuss. I think to – so we can get to lots of other questions, I think the simple answer is it's improving. The world's a big place. So, again, following the slope of recovery, the US and China, I would say, the financing markets are recovering most rapidly because markets are efficient. And the performance is starting to really pickup, not just from an occupancy, but you're getting back to rate levels very rapidly, probably more rapidly than I've ever seen in my 40 years of doing this.

What happens is the lender community starts to have more confidence. Rates are, obviously, hyper low and have been low and lenders need yield, and so the more comfort they get that recovery's afoot and that there's going to be a recovery back to where we were and then beyond, the more they're willing to take the risk a little bit further down on the risk spectrum and underwrite it.

And so, you're seeing pretty robust financing markets in China. The US is still – has a ways to go. You can look at the data out there. It's not anywhere near where it was, but it's improving. And my expectation is as you get into the fall, and I'm sure we'll talk about this, I'll leave it for other questions, and our belief, my belief is that we're going to continue to have very strong recovery in the fall and into next year, you're going to continue to see a gradual increase in financing that's available certainly here in the US. I think Europe will take a little longer. So, a ways to go. Not saying it's back anywhere near where it was. It's a long way off. Sort of off, but off the floors of what we had seen last year.

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

Thank you.



Operator: The next question is from Carlo Santarelli with Deutsche Bank. Please go ahead.

Carlo Santarelli*Analyst, Deutsche Bank Securities, Inc.*

Hey, guys. Thanks for taking my question. So, Chris, could you talk a little bit about how you guys plan to use key money in development spend? And obviously, in light of the financing environment that you just talked about and the way that's coming around, is it something you guys maybe rely on a little bit more in the near term and then start to wean away from it as we get more comfortable with kind of the outlook for new unit growth and things of that nature?



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

Yeah. That's a good question. If you look at the numbers, we had a little bit higher key money in the quarter than we would typically have. What I would say is I don't see anything that – I don't think anything is changing materially, meaning still over 90% of the deals that we are doing are dry deals. We're not spending – we're not using the balance sheet anyway. So, there's not any material shifts, given what's going on in the broader macro environment, the financing markets. Nothing material that's shifted.



The reason you're seeing a little bit heavier key money spend right now is a super positive story, in the sense that both things that we've been working on for a long time and/or opportunities that have arisen because of the pandemic have sort of come together in an unusual way this year.

So, example, some of the bigger key money expenditures are iconic assets for our portfolio, largely resort-oriented that we've been working on that will be generational. It will be in the system for decades and decades and decades. So, the Waldorf Astoria in Monarch Beach in Laguna. I've literally been working on that deal one way or another for 20 years, I think, between Host and here. That's in the system, an incredible addition to the Waldorf brand.

Resorts World, which I talked about in my prepared comments, 3,500 rooms on The Strip. We're basically the only major player on The Strip with a massive meetings platform and 3,500 rooms. We've been working on that for a number of years. Not a crazy amount of key money by any means, but relative to our normal expenditures, significant.

And then, the deals that I talked about in Mexico, the three deals, 1,500 rooms in Puerto Vallarta, and then in Tulum, these are incredible assets that were either existing, in the one case, in PV, was an existing hotel that was operating with another brand. And in the case of Tulum was developed literally over 20 years to get the entitlements with another brand. And because of COVID and what has happened in the industry, presented an opportunity for us. And so, that allowed us to enter the zone on hotels that would have taken us a decade to sort of pull together. And in a matter of 6 or 12 months, we're going have these purpose-built incredible hotels in the system.

And so, I know a long answer, but I view all of those, and then there's some others that I'm not even mentioning, but those are the big ones as like incredible progress for us in all-inclusive, in resorts and in luxury. And those deals just don't come around that often.

We're getting a few more of them now, as I said, aided by COVID. So, maybe I would say, our spending overall is going to be up probably this year and next year relative to 2020. But 2020 was a depressed year. If you look at it versus our normal run rate, like 2017, 2018 and 2019, honestly, I think our overall CapEx is sort of going to be within the ranges that we would have been. But again, I don't see anything – we don't see anything material. We still think over 90% of our deals are going to be dry. And when we have these really unique opportunities, even with key money, they're very nice returns for us, and they're incredibly, I think, strategic and important to the system.

Carlo Santarelli

Analyst, Deutsche Bank Securities, Inc.

Q

Great. Thanks, Chris. That's super helpful, and I appreciate it.

Operator: The next question will be from Joe Greff with JP Morgan. Please go ahead.

Joseph Greff

Analyst, JPMorgan Securities LLC

Q

Good morning, Chris. Good morning, Kevin. Good morning, Jill.

Christopher J. Nassetta

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

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Good morning, Joe.

Kevin J. Jacobs

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

Good morning, Joe.

A

Joseph Greff

Analyst, JPMorgan Securities LLC

Given significant progress we've seen in the operating environment, given your balance sheet and where your leverage ratios are heading by the end of this year, I was hoping you could give us an update on how you're thinking about what you're looking at, which might be obvious? And how you're looking at the timing of resuming capital return?

Q

Christopher J. Nassetta

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

Great. Great question. I figured I'd get it, and I figured I'd get it early. So thank you. I know that's on everybody's mind. And we have obviously talked a bunch about it. We – ultimately, that's a decision we'll go to our board with. We have an upcoming meeting. We've had broader dialogue, but we haven't pinned it down.

A

But I said on the last call that I was pretty confident that we would be reinstituting a return to capital program next year. I still feel that way. Obviously, the slope of the recovery is even steeper, so I would say – the update to that would be I feel confident that we're going to do it in the first half of next year. The exact date and time, to be determined when we talk to our board.

But I think you should read the results of second quarter, you should read the commentary that Kevin and I gave in our prepared comments, plus everything you're hopefully going to get in color to say that we're very optimistic. We're not – we read the papers. I talk to a lot of people. We're not oblivious to the Delta variant and things that are going on in the world. But we're confident because we think we will power through that. Trends that we see real time are very strong and improving. We feel really good about what's going to happen in the fall. And so, yeah.

Every quarter that goes by, I think we feel better and better about where the recovery is going. And so, that should ultimately translate into our feeling better about starting to return capital because we'll be generating real significant free cash flow.

In my mind next year, and we do not need to hoard it, our belief has always been that, as I said in my prior answer, we're going to be able to keep growing with very little use of our own balance sheet. And so, we're going to give it back to folks. So, my expectation is in the first half of next year that that program will resume and we'll be having some discussion with our board in the very near future.

Joseph Greff

Analyst, JPMorgan Securities LLC

Thank you very much.

Q

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

Shaun C. Kelley

Analyst, BofA Securities, Inc.

Q

Hi. Good morning, everyone.

Christopher J. Nassetta

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

Hi, Shaun.

Shaun C. Kelley

Analyst, BofA Securities, Inc.

Good morning, Chris. You mentioned a couple times now just talking about that recovery in the fall, so I was hoping we could dig in there a little bit? I know you are sort of probably right at the cusp of when you have too much color you can actually share on the corporate side. But can you talk about how that is starting to firm up, be it September, October? And what data you have?

And then, last quarter, you talked a little bit about an exit trajectory for the year of possibly something in the down 30% (sic) [70%] range, and I appreciate it may be a little early to give an update to that, but kind of how you're thinking about that relative to maybe where we were three months ago?

Christopher J. Nassetta

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

Yeah. Totally fair question. That's the \$64,000 question I think everybody's trying to figure out. So, I'll give you – we do have some data points, and I'll give you my opinion on top of it. We've obviously seen, as Kevin and I both described in the nuggets we gave in our comments that you wouldn't find in the press release, we've seen really nice recovery. And that recovery has been across the board. Obviously, most of the – the greatest strength in leisure, but significant pickup in business travel, and significant pickup while – further to go in the group side. And we continue to see that, notwithstanding the Delta variant and all the things going on.

Like I got just last night – as an example, systemwide US occupancy was 74%. Trailing seven-day 74%. That's with the urban – that's with some urban hotels not even open. And those are in the comp set, with all of our urban – so all of the urban hotels. Obviously, the urban environment has been lagging a little bit.

So, what that says to you, like last night, if we're running 74%, that's not leisure. While we have a lot of leisure-oriented hotels, we have a lot of business-oriented hotels. And so, midweek occupancies at that level are definitely reflective of business travel being back. And we've seen it literally – it's funny sort of post Memorial Day, you just saw a shift. You just saw a shift where weekday occupancies, on any given night, went up 10 or 20 percentage points. And that was business travel dominated by small and medium-size businesses, by the way.

But even pre-COVID, keep in mind, 80% of our business travel was small and medium-size businesses. Right? So, that's sort of currently what's going on. I know your question is forward looking, and I promise you I'm going to get to that.

I think the trajectory, my own view, and I think the data sort of supports this is, as you get into August, what's going to happen is you're going to continue have massive surge in leisure travel because everybody wants to get out, notwithstanding again the Delta variants and the like. We've not seen impact in sort of consumer behavior from that. So I think you're going to have continued very good strength in the leisure.

I do think in August, as you always do, you will see business transient fall off a little bit, right? Just because people are going to be – like they always do, they're going to be not traveling for business as much and going on

more vacations, and it's sort of the last hurrah before maybe a lot of people are going back to work, and the kids are finally going back to school, and all that fun stuff.

But when you get to the fall and limited – we have limited data, obviously, this far out. So, this is – I gave you data points that I have real time today. When you get 60, 90 days out, business transient stats, a lot of the bookings haven't occurred. So, this is where it gets into my view of what I think will happen. I think you get after Labor Day, I do believe – I'm not a health expert, but I'm talking to a lot of them, I do believe we will have powered through the Delta thing. If you look at the stats on hospitalization and the like, they're really not terrible.

If you look at what's happened in the UK, and we're sort of three or four weeks behind them, the patterns there right now are quite good. The infection rate is down 50% on a trailing 12-day basis over there. So, I think there is a lot of reasons to be optimistic that we sort of power through that.

And when we get to the fall, here is what I think we do know. Kids are going back to school. We'll debate whether they're wearing masks or not. Some places, yes. Some – but they're going back to school. I'm pretty confident in that. And offices are opening. They may open at different times. Some people, you're reading they're going to push it a month or whatever. Obviously, I said we're open. We're open and operating here at all of our headquarters. But you're going to have people back at work, which means with kids in school, with babysitters, and with people in the office, you're going to have more propensity to want to travel.

And when we talk to customers, again, I can't give you the booking data because it's too far out. But when we talk to customers, anecdotally, it supports all of that. When you get into the fall, people are going to be traveling. There's both pent-up demand, okay, of things they've been needing to do and then there's just demand generally for folks to be able to run their businesses. And so, I think as you get into the fall, you're going to see the natural reduction in the leisure, as we always do. Because now kids are in school. They weren't last year. Kids are in school. People are back in the office. They don't have as much time to go on vacation.

I do believe, again, can't prove it, but my belief is leisure will be elevated for a while because we're still living in a bit of a hybrid world, but I think business transient will come back. Group will, obviously, take a little longer gestation period, but group will definitely be coming back. The booking trends into the third, particularly the fourth quarter, are much better than they've been. And I think we're motoring forward.

In terms of – last time, I believe I said that I think we'd be back to sort of 70% by the end of the year of 2019 levels. And, obviously, I feel better. So, while we're not giving guidance, so I'm not going to do it, we're not ready to start doing that. There's still enough uncertainty where we want to wait. We do do forecasts. Okay? It's not Camp Runamuck here. We are looking at our numbers.

And I'd say our view is demand levels, probably – RevPAR levels are probably in the US and globally somewhere circa 80% versus the 70% I thought in our current thinking. Demand levels, probably back to 85%. So, we're getting there. Again, much, much – I said last time, recovery's been much steeper than we thought. I say it again today. Just things have been coming back more quickly than we would have thought. We knew they'd come back. Obviously, you all know I've been optimistic about their recovery, but it's even better than I would have thought.

I think one of the most surprising things, although it shouldn't be to any of us, because as I kid our team, the laws of economics are alive and well. The most surprising thing is how quickly rate comes back. But that's – again, that's just demand. Right? We're pricing demand. We're being really smart about it. But I do believe when we look back on this recovery, the most unusual thing relative to any other period in my almost 40 years of doing this will be just the rapid return of rate.

Shaun C. Kelley*Analyst, BofA Securities, Inc.*

Thank you for all the detail.

Q

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

Yes.

A

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

Smedes Rose*Analyst, Citigroup Global Markets, Inc.*

Hi. Thanks. I just wanted to follow up on that. Hi. I wanted to follow up a little bit on that. I think in your opening remarks, you said that your group bookings are trending greater now in 2022 than they were in 2019, which I think is a pretty big positive increase sequentially from what you've mentioned on your first quarter call. And I was just hoping you could maybe talk a little bit more about the competition of those groups and what you're seeing on the rate side? And maybe just kind of a little more color around folks' willingness to book group at this point?

Q

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

Yeah. A great question. Still building. What I said is that all of our bookings for 2022 are at rates that are greater than 2019. So, to be specific, rate. I didn't say volume. Volume's still a bit off, just because it takes time to build the book. So, my expectation is we get closer to next year and into next year, in the year, for the – later in this year, particularly when you get past this Delta, this Delta wave, and then in the year for the year will be a barn burner year, bigger than anything we've ever seen in the year for the year simply because people have to meet. It takes time to plan it. They want to sort of get through their budget season to know how much money they have. But I'm not worried about the volumes next year. Again, they're not where we were at 2019. They're close, but they're not there, but the rate's above.

A

Honestly, what I've been saying to our teams is, be really careful. There's going to be a monumental amount of demand. We don't want to give it away. We want to make sure that we're pricing. Even though we're not at the volumes now, my expectation very strongly is it's all going to fill in. It just takes a little bit longer, given the reason for this recession being a health issue and sort of getting through the final stages of that, in my opinion, is required before you really get the momentum on the volume. And so, that's why rates are up, is because we're being super disciplined, recognizing that there's a limited amount of meeting space. There's going to be a gargantuan amount of demand, and we can be a bit patient, I think, given what's going on.

Smedes Rose*Analyst, Citigroup Global Markets, Inc.*

Great. Thank you.

Q

Operator: Next question is from Thomas Allen with Morgan Stanley. Please go ahead.

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

Q

Thanks. So on net unit growth, you've obviously seen some great progression in terms of your guides and you gave some helpful color earlier. But do you think you can get back to the 6% to 7% growth you were putting up pre-COVID? And if so, when?

Christopher J. Nassetta

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

A

Yes. I do. And I think it's probably sometime between 2023 and 2024. Kevin?

Kevin J. Jacobs

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

A

Yeah.

Christopher J. Nassetta

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

A

Kevin is also Head of Development. So, I want to make sure he has – before I commit him. Yeah. I think it's sometime in 2023, 2024. I would...

Kevin J. Jacobs

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

A

Probably more 2024.

Christopher J. Nassetta

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

A

Probably more 2024, just because you've got to get through – when you look at starts last year, you'd look at – if you look at the progression, you'll see when we're done. Last year, we were down in starts. This year we'll be down modestly, not nearly as much as last year in starts. And I think that's the bottom. And then, I think next year, we'll be ramping up in starts. And I think if you just play that through, that's what gets us in the mid-single-digits for the next sort of couple of years, two or three. And then, I think you're back in business in the 6% to 7% range.

Kevin J. Jacobs

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

A

Yeah. If the average construction time or gestation period in the pipeline is two-and-a-half or three years, you've got to be two-and-a-half or three years past the bottom before you get back to your old run rate.

Thomas G. Allen

Analyst, Morgan Stanley & Co. LLC

Q

Helpful. Thank you.

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

Robin M. Farley

Analyst, UBS Securities LLC

Q

Great. Yeah. I wanted to ask about the pipeline as well. You mentioned that conversions were – I think you said 30% of signings. I'm wondering what percent of openings that was in Q2 and maybe what you expect it to be for the full year?

And then, just on the theme of pipeline, you mentioned mid-single-digits for the next two or three years. And I think last quarter, you had said that 2022 might be kind of in the 4% to 5% range, but maybe lower than this year, just given that there was some kind of construction catchup this year. So, I'm wondering, with the higher unit growth rate here in 2021, does that carry through to sort of continued conversion into 2022? Or in fact does it – is it bringing forward some things you thought would open in 2022 that kind of bring forward into 2021, and so maybe we'd still see that slightly lower rate, closer to 4% next year than the 5% for 2022? Thanks.

Christopher J. Nassetta

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

A

Yeah, Robin. Thanks. All good questions. I think I've got it all. I'll try to go in order. I think on the conversion front, openings were lower. I don't remember the exact percentage, but they're circa 10% of openings for the quarter. And that was just timing. I'd say last year, we were sort of 19%, 20% of openings. I think this year it will be that, or maybe a little bit higher, given sort of the number of signings we had in the second quarter. And so, I think that's a good way to think about it.

Look, we are doing more conversions. Very happy with the conversions in second quarter. A really nice mix between hard brands, soft brands, conversions from independents, conversions from other brands, regionally. So, very happy with that. But that said, our pace of deliveries of new builds is going up as well. So, it's sort of hard – it's a little bit harder for that percentage to move. And, of course, that's all baked into our outlook.

The idea of – I'll do the third one next. The idea of 2022 being affected, not as much. I think 2022 is going to be about what we expect, maybe a little bit of timing pull forward, replaced by a little bit more conversion. So, 2022 is about the same as we thought.

And then, yeah, you picked up on – we said 4% to 5% for the next several years. We were not pointing to any one specific year when we said 4% to 5%. And now, we're saying mid-single digits, which of course 4% to 5% is mid-single digits. So, it's about the same. But I think what you're hearing is a little bit more optimism about the future of net unit growth, given what's been going on lately.

Robin M. Farley

Analyst, UBS Securities LLC

Q

Great. Thank you very much.

Christopher J. Nassetta

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

A

Sure.

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

Richard J. Clarke

Analyst, Sanford C. Bernstein & Co. LLC

Q

Hi. Thanks for taking my questions. Just wanted to ask your, sort of, opinion, your thoughts on labor shortages in the US. There's been some commentary around drops in service levels. Obviously, it's across the whole industry. But how much truth is there in that? Or is it working the other way? You actually being able to realize some sort of bigger efficiencies by working with less on the hotel side level?

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

A

Yeah. Thanks, Rick. It's a great question. Labor shortage is a real issue. Probably the single biggest issue that we're dealing with. It is definitely not just for Hilton, but industry – all service industries and manufacturing and a lot of your supply chain issues that you're reading about every day. All of this is sort of interconnected to not having enough labor.

At a high level, I think it will largely resolve itself over the next couple of quarters, in the sense that I think there are a lot of complex reasons behind it. Some of it is obviously health. People still don't feel like, particularly with the Delta variant now, that they should go back to work. Some people, because they're worried about their health because – we haven't had kids in school, so we don't effectively have daycare. There are women in the workforce where it's been most dramatically impacted because they have to stay home to take care of kids.

And then, some of the government programs that were really important last year in the depths of this crisis have – aren't as important right now when there's a ton of opportunity for employment. And that is unemployment insurance, the federal top-up. But that goes away in early September. So, I think when you get kids back in school, we get past these – hopefully, the last wave with Delta and unemployment insurance goes away in the early fall, I think you're going to start to see a significant easing of the issues on the labor side.

In terms of what it – its impact on margins, given that we're able to – while are service issues all of us are having, we're obviously working awfully hard to deliver great service and I think we are doing a very good job given the difficult circumstances, we are doing it with less labor. And so, ironically, given demand and given the ability to price the demand, margins are, in many cases, unbelievably high because you're getting effectively rates that are consistent with what you had before, and you can't get the labor. So, you just have less cost. That obviously is a temporary thing. You're going have to have more labor ultimately in the hotels.

Having said that, long term, we've done a bunch of things in the crisis in terms of testing and learning on different ways to change the operating model, particularly as it relates to housekeeping and food and beverage. And then a whole host of smaller things, where we think we can deliver a greater experience for our customers and do it more efficiently. And so, I think when it all gets flushed through and we're on the other side of this and through the stresses and strains on the labor issues we're talking about, I think we have developed a plan to have higher margin businesses across all the major brands. And so, yeah, it's a big issue. We're spending a lot of time on it, but I do – as the old adage goes, this too, I think, shall pass.

Richard J. Clarke*Analyst, Sanford C. Bernstein & Co. LLC*

Q

Thanks very much.

Operator: And the next question is from Bill Crow with Raymond James. Please go ahead.

William A. Crow*Analyst, Raymond James & Associates, Inc.*

Q

Thanks. Good morning.

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

A

Hey, Bill.

William A. Crow

Analyst, Raymond James & Associates, Inc.

A clarification and a question. The clarification is, I think you mentioned that RevPAR was down 29% in June relative to 2019 numbers. And did you say that it was going to be closer to 20% down in the fourth quarter as we pivot to business travel?

Christopher J. Nassetta

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

Yes, I did.

William A. Crow

Analyst, Raymond James & Associates, Inc.

That's the clarification.

Christopher J. Nassetta

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

Yeah.

William A. Crow

Analyst, Raymond James & Associates, Inc.

The question I guess goes to your discussion about rate being the biggest surprise. And I'm just – I'm wondering if we're already at a point where we can declare victory over rate integrity, maybe for the first time in any recovery. Right? Or do we have to wait until we get into business travel and really see what lies beneath this leisure surge?

Christopher J. Nassetta

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

Yeah. On the first one, I've answered it. Maybe you didn't hear it because – and I apologize talking over you. But yes on the first. That's what I said to clarify the first question.

You know me, Bill. I tend to feel – under-promise, over-deliver is my theory in life. So, I don't want to declare victory yet on rate. I meant what I said. I've been doing this a long time and been through bunches of recessions at this point. And what I'm seeing is very atypical. And I do believe that, into the fall and next year, we're going to continue to have robust demand and improvement. So, I think the rate story, as I said in my earlier comment, when we look back on it, I think that's going to be the real difference in recovery here. But I don't know about declaring victory. George W. Bush did it on an aircraft carrier. It didn't work out for him.

William A. Crow

Analyst, Raymond James & Associates, Inc.

Didn't work so well.

Christopher J. Nassetta

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

Yeah. But listen, it's nice to see. It's nice to see. Again, it's just a function of demand. And then being smart in how you price demand.

William A. Crow

Analyst, Raymond James & Associates, Inc.

All right. Thank you.

Q

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

Patrick Scholes

Analyst, Truist Securities, Inc.

Hi. Good morning, everyone.

Q

Christopher J. Nassetta

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

Good morning.

A

Patrick Scholes

Analyst, Truist Securities, Inc.

Quick question here. This is just a sort of – sort of looking for another ballpark answer. But with the labor issue out there, what percentage of your hotels right now aren't able to sell full inventory due to staffing shortages?

Q

Christopher J. Nassetta

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

I can't. I don't have a scientific answer for you. I would say sort of atmospherically, I think it's a relatively small percentage of our portfolio. It's definitely – there are definitely some hotels that can't because I've talked to some owners and I was with a bunch of owners out of Dallas this week. And labor was probably the number one topic because it's what everybody's talking about. But I'm not – I'm just giving you the atmosphere because I don't have hard data on it.

A

Patrick Scholes

Analyst, Truist Securities, Inc.

Okay.

Q

Christopher J. Nassetta

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

I think that it is an issue, but not a significant issue. And, by the way, it's helping – to a degree, it's also helping with rate because in some markets where they can't, they're reducing capacity and driving rate, which, by the way, back to Bill Crow, when we're done with it, maybe we can declare victory that we were actually really smart about not only rate recovery, but sort of how we manage occupancy versus rate to drive the best profitability.

A

So, in the hotels where they are having issues, in many of them – and I can think of a few who I just talked to, are having great success in sort of moderating occupancy levels down and then driving it on the top line. And net-net, they're making more money than if they had the incremental labor and they opened up the capacity. Their profitability is higher. So, it's not all a bad story.

Long-term, obviously, the labor issues, we have to sort. I already gave my answer. I do think they'll sort. There are a bunch of things we're doing to make sure that our system has unique opportunities to access labor. And,

ultimately, to deliver the kind of service we want to deliver, we do need to get more labor in the hotels. But at the moment, from an owner point of view, in many cases, yeah, some are limiting capacity. But I think it is a relatively small percentage.

Patrick Scholes

Analyst, Truist Securities, Inc.

Okay. Thank you for the color on that.

Christopher J. Nassetta

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

Yes.

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

David Katz

Analyst, Jefferies LLC

Hi. Good morning, everyone.

Christopher J. Nassetta

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

Morning, David.

David Katz

Analyst, Jefferies LLC

Thanks for taking my question. Two questions, if I may. Within the sort of franchise fees line item, we're sort of in a moment where it's – candidly, nothing's easy to model, I assume, for either of us. But that one in particular was much larger than what we had. And I know there is a number of things in there. Getting to franchise fees should be straightforward. But, Kevin, if you could give us just a little insight on the other pieces that are in there, right? There is credit card fees and there's some royalties in there and sort of how those flow, a little modeling help would be welcome.

Kevin J. Jacobs

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

Yeah. David, it's hard and easy all at the same time. Basically, overall fee growth was a bit lower than overall RevPAR growth. Thus, your question. And the real – the short answer is, yeah, license fees are growing. By the way, they're growing really strongly. I think license fees were up something like 80% in the second quarter, but that's obviously a lot less than RevPAR growth at 234%. And so, just the math ends up being a little bit less than RevPAR. And so, when we're in this period of RevPAR growth being sort of at these really elevated rates because of the crazy comps, we're going to be a little bit lower than fee growth. On a long-term basis, it should be about one to one.

David Katz

Analyst, Jefferies LLC

Got it.

Christopher J. Nassetta

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

A

So that's kind of sort of the easiest way I can sort of lay it out.

David Katz

Analyst, Jefferies LLC

Q

Got it. And...

Christopher J. Nassetta

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

A

But like we just said, it's hard to model, though. Sorry about that.

David Katz

Analyst, Jefferies LLC

Q

That's okay. Whatever you got, we'll take. If I may ask a similar question around sort of owned and leased, it's not – certainly not the biggest part within your model. But if you don't mind my asking, any color on sort of how that recovers and grows out in the future would be helpful as well.

Kevin J. Jacobs

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

A

Yeah. Totally fair question. I sort of telegraphed it a little bit in our prepared remarks. Again, pretty straightforward. That portfolio is concentrated in places like the UK, Central Europe and Japan, in particular, that are just behind in the trajectory of recovery. So, all the things we talked about. There's nothing structural there. It's just that it's behind. It obviously was loss-making this quarter. It will probably be loss-making next quarter just because of the level of recovery and what's going to be needed in those parts of the world. And we think it's sort of breakeven-ish in Q4. We'll see what happens. Again, it's dependent on recovery and the world opening up a little bit.

And then, the last thing I'd say is, obviously, it's going to grow more quickly than the core business, so it's going to contribute positively to our growth going forward because it's going to be growing off a much lower base.

David Katz

Analyst, Jefferies LLC

Q

Perfect. Appreciate the help. Thanks.

Kevin J. Jacobs

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

A

Sure.

Operator: The next question is from Vince Ciepiel with Cleveland Research. Please go ahead.

Vince Ciepiel

Analyst, Cleveland Research Co. LLC

Q

Thanks for taking my question. I wanted to come back to the Honors contribution, which sounded really high. I think you said around 60% which is maybe a few points under 2019. And that's all while business transient is still, I think, 30 points off. I think that usually over indexes to brand direct. So, just curious how you think this direct

contribution evolves through the pandemic? Usually, there's a narrative that OTAs take share. But it seems like your direct business is really impressive. How do you think it evolves over the course of the next year?

Christopher J. Nassetta

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

A

Yeah. Over the next year is probably harder to judge. Over the next several years, obviously, our objective is to continue to enhance the value proposition for Honors such that, as I've been saying for a long time, you're sort of crazy not to be a member of Honors. You get all the technology. You get a little bit of a discounted rate. You get the points. You can use the points to shop on Amazon, buy a concert ticket at Live Nation, go travel the world and get rooms or food and beverage or a spa treatment or whatever. It's very much an opportunity to sort of create value. And if you're not an Honors member and you're staying with us, you're sort of silly. Just because you're effectively giving away value.

And so, that happens to be true. Obviously, we've been trying to, over the years, as I've talked about many times on these calls, sort of go high and low. Make sure that for our most frequent travelers, it's a really relevant program, which I think we've done. But infrequent travelers as well. And that's probably been what's most game-changing for us, and I think it's helped us sort of over the last five years, lead the industry in percentage of occupancy represented by loyalty, which is we've made it relevant to somebody that travels two or three days a year and not just 60 or 100 days a year because it's a currency effectively and there's a value proposition that works for them.

And so, being specific about it, we want to continue that. My own view is we were running in the 60s pre-COVID. My goals are much higher for that pre-COVID and I'm not letting up. COVID set us back. But I think COVID also provided opportunities. And as you pointed out, in May, we were effectively only a couple points different than we were in 2019. Why? Why would that be when our core traveler is not back. Well, I think it's two things. One, in May and June, our core travelers started to come back. Number two, we worked really hard in how we sort of shifted our upper funnel and lower funnel strategies for marketing to attract customers into the system that were traveling during COVID that weren't our core customers. And so, we were able to get a bunch of those folks to say, gosh, I would like to be an Honors member and sign up. And then realize this is a really good value proposition.

So, the whole thing during COVID has been to basically say, let's go really hard after the customer that maybe wasn't our core, wasn't an Honors member, make sure they really understand the value proposition, and then keep them in the system. And then, when our core customer comes back, obviously, we believe we've got a great value proposition they understand. And when you put one and one together, you hope to get three. And so, the objective would be not to get back to where we were because that wasn't the objective pre-COVID. It's to get significantly beyond that.

Why? Because we believe it's a better experience for our customer. The better the value proposition, the happier they are. The better experience with the technology, the happier they are. From an ownership and system point of view, we lower our distribution costs. It's the lowest cost distribution channel we have. So, for all the right reasons, we want to continue to build very direct relationships.

My belief is, when you wake up in two or three years, while COVID has obviously been a difficult time for everybody in the industry, including us, I do think it afforded us an opportunity to accelerate some of those efforts.

Vince Ciepiel

Analyst, Cleveland Research Co. LLC

Q

Thanks.

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 additional or closing remarks.

Christopher J. Nassetta

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

Thanks, everybody, for the time today. Obviously, we covered a lot of territory. And you can probably tell from my comments, we're obviously pleased with Q2 relative to where the business has been industrywide and the company. And we're very bullish about – while we know there are risks out there, not oblivious to that, we think those are all reasonably manageable. We're very bullish about not just the second half of the year, but very bullish about recovery as we go into 2022 and beyond.

We'll look forward – appreciate your time. We'll look forward to catching everybody up after we finish our third quarter. Take care. And have a great day.

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

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