IHG®

HOTELS & RESORTS

Q3 2021 Trading Update

Friday, 22nd October 2021

Introduction

Stuart Ford

Good morning everyone and welcome from me to IHG's conference call for the third quarter 2021 trading update. I am Stuart Ford, Head of Investor Relations at IHG and I am joined this morning by Paul Edgecliffe-Johnson, our Chief Financial Officer and Group Head of Strategy.

Just to remind listeners on the call that in the discussions today the company may make certain forward looking statements as defined under US law. Do please refer to this morning's announcement and the company's SEC filings for factors that could lead actual results to differ from those expressed in, or implied by, any such forward looking statements.

For any analysts or institutional investors who are listening via our website, may I remind you that in order to ask questions you will need to dial in using the details on page two of the RNS release. The release, together with the usual supplementary data pack can be downloaded from the Results & Presentations section of the Investors tab of ihgplc.com. With that, I will hand over to Paul.

Third Quarter 2021 Trading Update

Paul Edgecliffe-Johnson

Good morning everyone. I will start as usual with a review of our trading performance. You will see that in this morning's announcement we are comparing our performance against both 2020 and 2019, but I will focus my comments on the latter as it is the most meaningful. Starting with comparable RevPAR for the Group, which increased to $68, only 21% below 2019. This was a significant sequential improvement from the declines of 36% in the prior quarter and 51% back in quarter one. Strong domestic leisure demand resulted in rate recovering to almost parity with 2019 and saw occupancy down only 15 percentage points. Absolute occupancy was around 60% in the quarter, and a number of markets achieved occupancy and rates back at 2019 levels in the summer.

The stronger trading, particularly in the Americas franchise estate, has also led to further improvements to our RevPAR sensitivity which is now trending closer to $14 million per point of RevPAR. As a reminder, our revPAR sensitivity is referring to 2021 versus 2019 and is calculated before cost savings. In regard to savings, we remain on track to deliver a sustainable $75 million reduction in fee business costs whilst still reinvesting for growth. Further to these we now expect around $25 million of additional temporary cost reductions for this year only, largely driven by vacancy rates for corporate roles and other headcount related costs.

Turning now to our regional performance, in the Americas RevPAR was 10% lower. Rates exceeded 2019 levels and absolute occupancy recovered to 66%. Standout occupancy performances included 70% across the Holiday Inn Express estate and 80% in our extended stay brands which exceeded 2019 levels. In the US RevPAR was only 7% under the 2019 level and was ahead for Holiday Inn Express and our Extended Stay brands. Strong demand over the peak summer months resulted in July RevPAR being ahead of 2019 by 2% in non-urban locations where we have nearly 3,000 hotels or around 90% of the estate.

It is worth pausing for a moment to focus a little more on the trends we saw in the US during the quarter across business demand, group activity and leisure demand. Leisure demand stayed strong with room nights consumed slightly up on 2019. Rates were up by almost 10%. We have seen that essential business travel demand has been resilient throughout Covid. What we are now seeing is increasing amounts of discretionary business travel demand coming through. This resulted in overall business room nights consumed down only 12% in the third quarter with rate down less than 5%, a marked improvement on the prior two quarters. Group demand has similarly seen improvement each quarter and group pricing is holding firm. While room nights consumed was still down nearly 30%, rate was down only 8%. The strong rate environment across each demand segment is encouraging as we continue to see demand build back.

Turning now to Americas system size, we opened around 3,000 rooms leading to gross growth of 3.3% year-on-year. We signed more than 4,000 rooms taking our Americas pipeline to 97,000. Encouragingly, the pace of development activity picked up through the quarter with signings accelerating in September. We have also seen a sequential pickup in deal applications through the year, particularly during the third quarter.

Moving now to Europe, Middle East, Asia & Africa where RevPAR was down 43%. Performance within the region continued to vary, reflecting the differing levels of travel restrictions. In the UK RevPAR improved to only 22% below 2019. London, which has a higher weighting towards international demand, saw RevPAR 51% below. This compared to markets outside London achieving 95% 2019’s RevPAR. Continental Europe improved to a 48% deficit and the Middle East to a 39% deficit as restrictions eased. In contrast, Australia saw a deficit of 68%, impacted by the reintroduction of travel restrictions.

With the general reopening of travel and increasing demands across the region, the number of temporarily closed hotels was down to just 28 at the end of September, compared to more than 200 at the start of the year. We opened over 4,000 rooms resulting in gross growth of over 5% year-on-year and signed a further 2,200 rooms into our pipeline. Conversions accounted for half of the signings in the period, and we expect development activity to pick up further in the fourth quarter.

Turning now to Greater China where RevPAR fluctuated significantly in the quarter. July RevPAR was down just 6% as the recovery continued and benefitted in particular from strong domestic leisure demand. The reintroduction of temporary restrictions meant that the August deficit was 55%. With restrictions then lifting again, September RevPAR swiftly recovered to a 26% deficit. Across Mainland China, Tier 1 cities continued to see a greater level of RevPAR deficit, down 32%, given their historical weighting to international inbound travel. RevPAR in Tiers 2-4 cities which are more weighted to domestic and leisure demand saw a 26% deficit. In July, Tier 4 was over 40% ahead of 2019 RevPAR levels, given the strong demand in resort locations including Sanya.

Net system size in the region increased by 10.6% year-on-year to 5,300 rooms added in the quarter. We signed 6,300 rooms into the pipeline. Covid restrictions held back some development activity in the period and we expect the signings pace to pick up significantly in the fourth quarter.

Moving now to the Group system size, our strong openings momentum continued with 5.2% gross growth year-on-year. The one-off quality initiatives we have underway this year mean that as expected after exits this netted down to a system size that was flat year-on-year.

Further rapid progress has been made on a review that covers around 200 Holiday Inn and Crowne Plaza hotels. Over 90 hotels have already exited or are confirmed to exit, with more than 40 further hotels committed to improvement plans. Year-to-date this review accounted for around two-thirds of our removals. By contrast the rate of removals year-to-date across other brands has been broadly in line with their annual removals rate of around 1.5% which we have seen for the last five years.

We remain on track to conclude this review by the end of this year.

Our 91 hotel signings took our pipeline to 270,000 rooms. Signings accelerated over the course of the quarter and this trajectory is expected to carry on through the fourth quarter as owner interest in doing deals with us continues to strengthen.

To conclude, trading continued to significantly improve, driven by strong domestic leisure demand and a strong pricing environment. We are encouraged by the return of more corporate travel and group bookings.

We saw over 5% gross openings growth and outside of the Holiday Inn and Crowne Plaza review, our removals rate for other brands in line with our annualised rate of around 1.5%.

Signings pace improved through the quarter and we expect this to significantly pick up again in the fourth quarter.

Looking at the very short-term, fluctuating Covid restrictions may well still make trading volatile in certain markets but looking further ahead the strength of our brands, platforms and scale underpins our confidence to exceed prior levels of profitability and to deliver industry-leading levels of net system size growth in the coming years.

Q&A

Jamie Rollo (Morgan Stanley): Morning everyone, I have got three questions please. First Paul, is there anything you can give us on any early indications on the corporate negotiation season? It may be too early. Otherwise, any colour on recent trading, any expectations on Q4 and whether that corporate recovery can continue and therefore you could see Q4 RevPAR similar or better to Q3, which is what I think consensus is looking for.

Secondly on the signings, in the Americas they were still half 2019 levels. I appreciate in EMEAA and China there are other aspects dragging it down but given the market was fully open, why is that still quite weak and how does that frame your thinking about openings going forwards?

Then just one more. On the savings, $25 million temporary, they have been there now for nearly two years. Are we going to end up putting in $100 million of permanent savings, do you think from next year? Thank you.

Paul Edgecliffe-Johnson: Thanks Jamie. In terms of the first question and what we are seeing in the corporate rates renegotiation process, I think our corporate customers are very keen to lock in pricing. The pricing environment has continued to be very strong and, as I referenced, leisure pricing has been in many markets well up on 2019. That is one of the key things that our customers are looking for, to make sure that the prices are not going up too much in 2022. However, it has been constructive conversation so far but nothing particular I can pull out of it.

In terms of recent trading, we are continuing to see this continued rebound in corporate demand and we certainly saw that through the third quarter. Looking at industry numbers beyond, yes, it is continuing. It is not an immediate bounce back to where we were in 2019 but it is encouraging to see and the rates that are being achieved are also encouraging to see. It is sequentially quite a significant improvement on what we saw in the first half.

In terms of signings, yes, we are pleased with the step-up in signings in the third quarter that we saw in the US. It is still below what we saw in 2019 of course. Remember, that there is quite a long lead time for a deal to go from when an owner starts to get interested in doing a signing with us to actually getting ink on a page and a legal contract in place. For quite an extended period of time our owners have been focused on stabilising their businesses, looking after their teams, etc. It will take a while before that normalises. What we have seen though and very encouraging, is a big step up in the pre-applications. People are calling us and saying they want to look at a new site with us, signing letters of intent and also in the lending environment the regional banks have been calling our owners more to say, 'We are open for business. We want to lend on your project.' That is a good early indicator as to a step back up in the signings level in due course.

On the savings, the $25 million additional, the intent is not that this becomes part of the permanent savings because we are a growth business, and we are wanting to have all the resources and all the muscle in place to be able to deliver that level of net system size growth which we aspire to. It is tough to find people of the calibre that we are looking for so we have had some positions open this year, but our intent is to fill those. It is not our intent to run with $100 million. We hope we will find the people to take that down to $75 million.

Jamie Rollo: Thanks. Just back on the Q4 numbers, I know you do not formally guide but any thoughts on market expectations for revPAR to be down circa 21%, similar to Q3? Does that sound reasonable?

Paul Edgecliffe-Johnson: I think it will partly depend on what we see in China. I think what we have seen is China can be very volatile. If you look back on what we saw in the third quarter it went from -6% to -50% to -25% sequentially by month. Quite where it ends up will depend on what restrictions the Chinese government puts in place. If we see it fully open again I think it will very quickly go back to a very strong level of trading there. With restrictions it will be tougher and that is quite a big swing factor, so it is very difficult to call with that factor still in mind.

Jamie Rollo: Sorry, are you saying China needs to be fully open and back to normal for you to be down 21% or could it be better than that if China gets back to normal?

Paul Edgecliffe-Johnson: I am saying it is a big swing factor in what will be printed for the Group as a whole and it is impossible to tell where that is going to come out right now. If it comes out at -10%, which it could for China, then that will be a positive. If it comes out at -50% if things all close down, then that will be a negative. It is impossible to call that at the moment.

Vicki Stern (Barclays): Firstly, on achieving unit growth back to 4.5%+ from next year, could you walk us through again the building blocks in terms of that confidence? Obviously you have signalled the lower churn but perhaps more colour on the gross openings side and really why there is that level of confidence in getting back to those 2018/2019 levels from next year. Within that, is there much expectation of conversion activity, for example?

Second question, following up on Jamie's really, can we talk about how you see the signings momentum then phasing over the next few questers? Obviously there are a lot of unknowns but assuming things continue to open up, given those pre-indications that you have been getting, how do we think about how quickly you could get back to pre-Covid levels of signings over the next year or so?

Then finally on pricing, if you could give more colour what you think is driving that strength that we are seeing in price even on the leisure side. I would not have thought pre-Covid that we would have seen a recovery as swift in leisure even if the demand was coming back as quickly in terms of price. Given your comments there on the rates indications, you guys wanting to lock in decent rates at this stage, how sustainable do you think that positive pricing dynamic is as we look into next year, perhaps with a more normal business/leisure mix? Thank you.

Paul Edgecliffe-Johnson: Thanks Vicki. In terms of our level of confidence in getting back to the level of growth that we were seeing before, I think if we look at what we have seen year-on-year in terms of our gross growth, the 5.2%, and then if you think about normalised level of exits of 1.7%, that would have delivered us 3.7%. What we are saying is we are expecting it to be similar to what we saw in 2018. You are talking about then something starting with a four. Yes, you would have to see a few more openings than we saw this year but not a lot. A few thousand and then if you think about the step-up that we are seeing and sequentially we have been seeing, I think it is pretty reasonable when you look at just trading to-date. Nothing more than that. You look at the very large pipeline. You look at the number of brands that are very attractive for converting, so with Vignette, with voco in particular, there are a lot of owners who would like to move their hotels across into these brands and take benefit of all the revenue delivery that we have. That is what is driving that.

In terms of the signings momentum, it is a hard one to be precise on because deals will get signed when the deal is ready and when we are confident on the project. What I think is very encouraging is the number of new enquiries. Remember, our owners want to do more hotels with us and as long as the debt capital is available then they will sign up. Once they have their existing business stabilised, which broadly in the US they do, it is a question of when rather than whether we get back to the sorts of levels that we saw before.

In terms of pricing and what is driving that, one of the statistics that frankly surprised me slightly was just the level of price that was being achieved from our leisure guest over the summer months. 10% ahead of what we were seeing in 2019. I think it is the supply and the demand, plus the levels of inflation that we are seeing in the broader economy. It might be ahead of 2019 on a nominal basis but if you think about it on a real basis with some years of relatively high levels of inflation it is closer to parity on a real basis. I think that then high level of demand for leisure is then translating through into the pricing that we are seeing in business and the pricing that we are seeing in group. I think that will be sustained as I think we will have a very strong leisure summer next year as well. We will continue to get good pricing off the back of that.

Bilal Aziz (UBS): Good morning everyone, thanks for taking my questions. Three quick ones from me please. Firstly, apologies if I missed it but what was conversions as an extension of the gross additions into this quarter? How do you think that number evolves going into next year?

Secondly, you spoke about China into Q4. Just a quick comment on the US please. Are you expecting leisure to soften into Thanksgiving and Christmas, or do you think both leisure and business will improve into Q4?

Then very finally just on your sensitivity which you said is now closer to $14 million to 1% of RevPAR, can you perhaps flesh out what the next level of improvement will be driven by in EMEAA? Then it will start to gradually improve and you intend to see into next year, please. Thank you.

Paul Edgecliffe-Johnson: Thanks Bilal. Conversions, you did not miss it, I do not think we talked about it. We do not give that level of granularity on a quarter normally. However, conversions were about 25%. Higher in EMEAA but lots of demand for our conversion brands given the revenue that they deliver and the strong benefits to owners, which is encouraging to see.

In terms of leisure, will we see it soften into the Thanksgiving season? I think there is a lot of leisure demand out there for people wanting to travel and frankly given how strong the summer season was there are some people who have not managed to take all the trips they would like to have done. Leisure has, across the industry, continued to be very good. I think that the Thanksgiving season probably for the industry will be strong. Then it will probably soften a bit in the build up to Christmas, which is the normal pattern. I think there is nothing else that we can particularly say at that point.

In terms of the sensitivity going into next year it really all does depend on when the remaining owned and leased hotels and big management contracts get back to their normal level of profitability. Remember, it used to be $13 million of sensitivity per point of RevPAR. It went up and now it is trending close to $14 million. It will come back in due course. It is an output rather than an input so we will keep you in the loop as we trend through 2022.

James Ainley (Citi): Morning everybody. Three questions please. Firstly, if I look at the industry data in the US by segment it looks like Holiday Inn and Crowne Plaza underperformed quite materially. Why do you think that is? Perhaps if you purged the data for those hotels you are exiting, we would have a slightly different picture. I am interested in your perspectives on that.

Secondly, related to that hotel review or those 200 hotels, it looks like rather more are choosing to exit now than the last time you gave us the numbers. Where do you think you might land on that review in terms of the exits and the re-investors?

Then the third question on labour supply more broadly, how do you think your hotels are faring? Are you still seeing some limits to occupancy or services in hotels? Do you see any signs of labour availability easing? Thank you.

Paul Edgecliffe-Johnson: Thanks James. In terms of Holiday Inn and Crowne Plaza and the comparisons you made in your statement, I think the thing worth remembering is that Holiday Inn in particular has historically, given the nature of the brand a lot of them were built some time ago, they are the higher level of group business in there and a higher level of business travellers normally than a typical Hotel Indigo hotel which would have been a small box, sort of old boxes in there. That is really the differential you are seeing.

In terms of Holiday Inn and Crowne Plaza and the exit rate, it is very much in line actually with what I have guided to and what we are expecting to see. 90 who have now exited or said they are going to exit, 40 who have signed up so it is a similar proportion is what I would expect to see by the end of the programme. Maybe 120 or 130 or so going and the remainder committing to a significant improvement, which will be great because it will significantly raise the quality of those brands. That will help us grow them over the long-term. It is a really important initiative there.

In terms of labour supply there is a lot that we are doing for our owners through our Procurement teams and our Human Resources teams to help find people for the hotels. That is of course one of the benefits of being part of a large system like ours is that we have those linkages. We have also been providing owners with labour rostering tools and our plans as to how they make the most of the people that they have. It is still clearly a challenge and I think it is going to stay a challenge to find everybody that the hotels need. Our owners are very resourceful. They are an army of entrepreneurs out there who are very skilled at running their own businesses and they know their local markets. I think they are very well placed to do that with our help. Thanks James.

Alex Brignall (Redburn): Morning, thanks for taking the questions. All on a similar theme of signings and opening rates please. The first one is on that lag time between signings and openings. Clearly you are talking about a strong 2022 and 2023. If you look at the Financial Crisis the slowdown came after that. Obviously, you have got a strong pipeline so theorising or making assumptions about current signings rate but at the current signings rate that we have now, when would that start to drop through into lower openings? It is encouraging to hear the comments about applications and there is some data out from CodeStar about land acquisitions for hotels and usage which this year are still 80% below the levels in 2019. I guess for someone who is not anywhere near as close to the data as you guys, what is the order of events? Presumably buying the land comes first, then an application and then a signing. If you could just explain how that might work chronologically?

Then on conversions you have given numbers on conversions as a percentage of total. Could you talk about conversions on an absolute level versus pre-pandemic? I think and I could very well be wrong, that on an absolute level they are still below the level that we saw pre-pandemic. I guess my question is, why would that be? Should we not see conversions on an absolute basis go up versus pre-pandemic if it is not needing new financing to build? Why might they actually be down? Thanks very much.

Paul Edgecliffe-Johnson: Thanks Alex. In terms of signings to openings in the period that it takes, as you would imagine it varies significantly across the brands. For an InterContinental which might be part of a large complex, you could be talking 60 months. Some are done more rapidly but it does take some time. By contrast, with an avid, for example, by the time you break ground to when the hotel opens can be less than a year. One of the great attractions for owners of the avid brand and similarly with Candlewood, Holiday Inn Express, is that they are relatively simple boxes to build. The key thing is getting the hotel signed, and signed with good owners. Then get the ground broken and then once the ground is broken the hotel will manifest a certain period afterwards. That has always been the case and there is no real change there.

In terms of the order in which things happen, the key for an owner to be able to get debt financed is to have an application approved by us. Obviously, you will need the debt finance to acquire the land. The key thing for an owner is getting our franchise signed up. Often, they will have rights over a land, or they will have land identified but it does not mean that they will necessarily own the land. Some do. They may have it as part of a historic arrangement they made or have another hotel on it that they are deconstructing to build our new one. There is a variety but you have to get the contract with us normally first.

In terms of conversions, they have stepped up significantly and in EMEAA more conversion discussions than we have ever seen before. I would actually have to look at the numbers and refresh my mind as to what we used to do back in 2019 on an absolute basis but we have seen owners having to focus on their operating businesses more and on building their next hotels less. That will mean that you see fewer hotels getting done so that will be the reason if there is an absolute differential. Nothing else behind it. Thanks Alex.

Alex Brignall: Thanks very much Paul.

Stuart Ford: Many thanks, no further remarks from me. Paul, anything to add?

Paul Edgecliffe-Johnson: Thanks everybody for listening and look forward to catching up with you very soon. Have a great day.

[END OF TRANSCRIPT]