THOMSON REUTERS STREETEVENTS

# EDITED TRANSCRIPT

FCH - Q1 2016 Felcor Lodging Trust Inc Earnings Call

EVENT DATE/TIME: APRIL 26, 2016 / 4:00PM GMT





THOMSON REUTERS

## CORPORATE PARTICIPANTS

**Stephen Schafer** *FelCor Lodging Trust Incorporated - SVP of IR*

**Rick Smith** *FelCor Lodging Trust Incorporated - CEO and President*

**Michael Hughes** *FelCor Lodging Trust Incorporated - CFO*

## CONFERENCE CALL PARTICIPANTS

**Chris Woronka** *Deutsche Bank - Analyst*

**Bryan Maher** *FBR Capital Markets - Analyst*

**Shaun Kelley** *BofA Merrill Lynch - Analyst*

**Lukas Hartwich** *Green Street Advisors - Analyst*

**Patrick Scholes** *SunTrust Robinson Humphrey - Analyst*

## PRESENTATION

**Operator**

Good afternoon. My name is Carol, and I will be your conference operator today. At this time, I would like to welcome everyone to the FelCor first-quarter earnings release call.

(Operator Instructions)

Thank you. I would now like to turn the call over to Mr. Stephen Schafer.

---

**Stephen Schafer** - *FelCor Lodging Trust Incorporated - SVP of IR*

Thank you, and good morning. On behalf of the management team, I would like to welcome you to our first-quarter earnings conference call. With me today are members of our management team, including Rick Smith, our President and CEO; and Michael Hughes, our Chief Financial Officer. Following their remarks, we will take your questions.

Before I turn the call over to Rick, let me remind you that with the exception of historical information, the matters discussed on this conference call may include forward-looking statements within the meaning of the Federal Securities Laws. These forward-looking statements are expressions of current expectations, and are not guarantees of future performance.

Numerous risks and uncertainties and the occurrence of future events may cause actual results to differ materially from those currently expected. These risks and uncertainties are described in FelCor's filings with the SEC. Although we believe our current expectations to be based upon reasonable assumptions, we cannot assure you that our expectations will be attained, or that actual results will not differ materially. And with that, I will turn the call over to Rick.

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Thanks, Steve, and good morning. We had a solid first quarter. Our strong and well diversified portfolio once again outperformed the industry in upper upscale segment, with 4.7% RevPAR growth.

Additionally, The Knick exceeded our expectations for the first quarter, with EBITDA $379,000 better than expected. While Q1 is the softest quarter of the year for New York, and sentiment for the City is negative, the hotel is certainly moving in the right direction.

Based on travel patterns to date, and discussion with our corporate accounts, we have not seen any downward trend in corporate transient travel, which was up 1% to budget, despite corporate profits ex-energy being down a bit in the first quarter. However, we will continue to monitor both corporate travel patterns and profits very carefully, as we move through the second quarter and adjust mix as necessary, to combat any such rising trends. We also remain fairly insulated from new supply, except in New York.

While trends and sentiment have certainly moderated, the majority of our submarkets are still experiencing positive demand growth, which allowed us to increase both rate and occupancy during the quarter. As such, we are cautiously optimistic moving forward, and are reiterating our full-year guidance.

Our focus for the remainder of the year continues to be asset sales and internal growth, primarily selling the five hotels which we are marketing. While transaction volume has decreased, we have made steady progress overall, with one short-term setback. Let's go through each now.

The Nashville Holiday Inn. We had previously agreed to sell the hotel, and are currently finalizing the contract. We are resolving a structural issue relating to the ground lease, and expect to sign the contract within two weeks.

Esmeralda. We have been through the first round of bids, and are currently receiving best and final offers. We expect to be under contract with the winner sometime in late May.

The Knick. We have completed the introductory outreach to more than 80 investors. There are several that are very interested, and are working their preliminary due diligence. We expect to meet with each of them in May, and will begin to discuss pricing seriously. Preliminary price discussions have been good but we will need to see where that goes, once preliminary diligence is complete. The buyers are all highly qualified, and the process is going according to plan.

Morgans and Royalton. Unfortunately, the potential buyer that was under LOI just recently fell out, and the LOI was terminated. We are currently re-engaging other interested properties for both properties. We will keep you informed on that process, as it progresses.

While termination of this deal is disappointing, it is not an uncommon occurrence, and nothing we didn't experience on a number of the 98 hotels we have previously sold. With the continued progress on the other hotels, we remain confident that we will accomplish the asset sales this year at attractive pricing. Proceeds from the asset sales will go toward paying down debt and the stock repurchase program, which will enhance shareholder value. To date, we have purchased 5.2 million shares of stock at an average price of $6.85 under the program. As asset sales solidify, and while the stock continues to trade at a significant discount to NAV, we will ramp up the program.

Our second area of focus this year is internal growth, including the continued outperformance of our portfolio, the last substantial increase in the Wyndham guarantee, the ramp-up of the Knick, and moving forward with our near-term redevelopment projects. As I've already covered the first three areas, I want to focus on the two redevelopments currently underway:

Phase one of the Vinoy redevelopment and work at Kingston Plantation are currently in progress. These projects will add significant value to the properties, by enhancing club membership and high-end group business that will allow us to adjust customer mix, and drive overall rate. The unlevered IRRs for each of these projects is north of 15%.

Additionally, there will be no displacement from these two projects this year, as the project at Kingston is free-standing, and phase one at the Vinoy is at the golf course and club. We expect to spend approximately $15 million this year on these projects, which will be paid from free cash flow. We expect to complete both in early 2017.

We have announced our upcoming analyst and institutional investor day. The meeting will be held at the Knick on May 26. We will be providing an update on the Company, and our going-forward plan, followed by a Q&A session and tour. We look forward to seeing you there.

A couple things before I turn the call over to Michael. With the clean-up portion of our transformation complete, we are in great position moving forward. With our restructured balance sheet, we have the best maturity profile of any lodging REIT.

Once the asset sales are complete, we will have significant liquidity and leverage of roughly 4 times. The combination of these will allow us to manage effectively through any economic cycle. The asset sales also further improve overall quality of our portfolio.

As we move forward with low leverage, a great maturity profile and improved and outperforming portfolio, less volatility than peers due to the Wyndham deal, and many internal opportunities to grow earnings, we remain positioned to increase shareholder value more than our peers. With that, I will turn the call over to Michael.

---

**Michael Hughes** - *FelCor Lodging Trust Incorporated - CFO*

Thanks, Rick, and good morning. As Rick mentioned, we had a solid quarter. Portfolio RevPAR grew 4.7%, exceeding the industry and the upper upscale segment by 200 and 280 basis points respectively, and we grew market share by 1.2%. ADR drove over two-thirds of our RevPAR growth, leading to good flow-through.

Several markets were particularly strong this quarter, especially on the West Coast. Our Los Angeles area hotels increased RevPAR 21%, and gained significant market share. Our five San Francisco Bay area properties grew RevPAR 12% during the quarter, helped by the Super Bowl and the Embassy Suites Mandalay Beach resort grew RevPAR 21%. Philadelphia, Myrtle Beach and Atlanta experienced 11%, 9% and 8% RevPAR growth respectively, and our Wyndham Houston Medical Center's RevPAR grew 6.6%, despite the 9.5% RevPAR decline for the Houston market.

However, there were a few weak spots. RevPAR at our Boston hotels declined 1.5%. Multiple severe storms contributed to last year's occupancy, making the comparison to prior year particularly challenging. Nonetheless, we continue gaining market share at the Fairmont Copley Plaza.

Austin's RevPAR declined 3%, as the Texas Relay shifted from March to April. We expect a strong rebound in April, which is up 17.4% month to date. Additionally, our South Florida properties only grew RevPAR 1.5%, reflecting in part the impact of the Zika virus state of emergency declared in Dade and Broward counties. Despite this challenge, we benefited from stronger cruise business in Fort Lauderdale, where RevPAR increased 8% at our Embassy Suites.

Our balance sheet is in great shape, and will continue to improve as we complete the planned asset sales. Our long-dated debt maturities and low fixed rates insulate us from capital markets disruption, giving us substantial flexibility to operate our business and pursue opportunities. We are using that flexibility to take advantage of the significant discrepancy between our current stock price and our NAV. During the first quarter, we repurchased 3 million shares of common stock, at an average price of $6.51. To date, we have purchased 5.2 million shares, at an average price of $6.85. We intend to continue repurchasing our common stock, and trading below NAV, and expect to increase the program in conjunction with completing the asset sales.

We are affirming our full-year 2016 operational outlook. For the year, we forecast a 3.5% to 5.5% RevPAR increase at our same store hotels. We have also raised the low end of our guidance to reflect updated asset sale timing. We have forecast adjusted FFO per share between $0.93 and $0.99, and adjusted EBITDA between $242 million and $256 million. Additionally our outlook assumes NOI from our Wyndham hotels equals the 2016 guaranteed amount. And with that, we are ready to take questions.

---

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions)

Your first question today comes from the line of Chris Woronka from Deutsche Bank. Your line is open.

---

**Chris Woronka** - *Deutsche Bank - Analyst*

I guess first question would be related to the Morgans and Royalton coming out of LOI. It seems as if your guidance doesn't -- you don't anticipate any incremental disruption there. Is that right, despite the fact that the process is -- there's going to be another sale process going on?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

No, I mean, everybody's been aware of what's been going on since the very beginning of the year. That's just going to continue, so we don't see any further disruption there.

---

**Chris Woronka** - *Deutsche Bank - Analyst*

Okay. And then, I know it's fairly recent. You got to re-engage with interested bidders. But internally do you think pricing changes dramatically, or do you think you had other guys that are in the same ballpark?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

It's a little early to be able to gauge that, Chris. We are in the process of, like I said, re-engaging and starting those conversations back up. We'll have to see where that comes.

Could there be some change in pricing? Could be. Still think the pricing will be attractive, though. We're not going to give anything away.

---

**Chris Woronka** - *Deutsche Bank - Analyst*

Fair enough. And then just on the Knick, thanks for the update on performance, relative to your budget. I guess what -- can you give us maybe a rough number, I know first quarter is a very low period in New York, I mean, but as the hotel ramps up, is it fair to say that the first quarter is going to be a really small part of the year for EBITDA?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Oh, Lord, yes, as with most hotels in New York, maybe all hotels in New York, it is an extremely low quarter, and extremely soft. Things start to pick up in March, but really, when you get into April and the rest of the year, is when New York is better.

---

**Chris Woronka** - *Deutsche Bank - Analyst*

Right. Just a quick follow-up there. Has your customer mix changed at all relative to your, I guess, initial underwriting as you deal with some of the supply increases and some of the, I guess, structural underlying changes in the market?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Well, yes, I mean, there's -- look, there's various things at play here. First of all, at stabilization in a stabilized market, we still assume the mix will end up at the right place, and at the place that it needs to be. But given the combination of the ramp-up and the combination of the soft market, certainly it is ever-evolving. The mix is ever-evolving, and we are working on rate right now.

I mean, trying to shift to a little more group, given the softness of the market, and with corporate being flat to slightly negative, certainly during the first quarter. And so we're -- it's a work in progress, as you go through with the combination of the ramp-up, and the softer market, it is a work in progress. Good news is, the Revenue Manager on-board, the Director of Sales on-board, the GM that's on-board, we've had some team changes, and we are really pushing in the right direction, and we're very pleased with the direction that we're heading.

---

**Chris Woronka** - *Deutsche Bank - Analyst*

Okay. Very good. Thanks, Rick.

---

**Operator**

Your next question comes from the line of Joseph Greff from JPMorgan. Your line is open.

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

I think we lost him, operator.

---

**Operator**

Moving to the next question in queue is from Bryan Maher from FBR. Your line is open.

---

**Bryan Maher** - *FBR Capital Markets - Analyst*

Quick question. Your results and your commentary, I think many people, or at least we construe as certainly more positive than negative, and maybe more so for your portfolio than others. But can you weigh in on some of the negative commentary we're hearing from one or two lodging REIT competitors, who are seemingly quite bearish, particularly as it relates to the cycle, and give your view on the bigger picture lodging lay of the land for US?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Well, I mean, certainly like I said, I mean, sentiment fundamentals are moderating. I mean, in the first quarter, really for the first time, corporate profits ex-energy was down. And so it starts to -- when that starts to happen, you start to watch very closely what travel trends are for corporate transient. Corporate group, yes, a little bit, but corporate transient is really the key metric to be watching there, and we're not seeing anything yet.

I think we do have a very strong portfolio, a diverse portfolio. We are in very strong sub-markets. We're not seeing anything yet which leads us to be cautiously optimistic. I mean, we are -- now, as far as our competitors, I can't speak to what they're seeing within their own portfolio, and I use the words cautiously optimistic purposely, because it is getting to a point where the moderation is something that has to be watched carefully.

You have to watch your mix. Have you to watch for trends as far out as you can possibly see them, so that you can start managing mix accordingly. And I think the whole year's going to be like that. So I think we just have to stay on top of it.

But what we're seeing in our portfolio right now, and what we have seen to date, what our -- by talking to our corporate customers and by seeing the actual bookings, and the pace of bookings going forward, we haven't seen that downward trend yet, and we will continue to adjust group as needed, if we start to see that, as well as other channels. So it's not like we're jumping for joy, and we think we're in the height of the upturn, or anything of that nature. But we are cautiously optimistic, because we haven't seen those trends yet, and we're still gaining share. I'm not sure everyone can say that.

Certainly, the industry was at 2.5, the upper upscale was around the same, and there are people coming in below that. Well, they're losing share, and we're gaining share, and supply is lower in our markets. New York is the only market that we really have any impact. We're not giving up rate yet. And back to supply real quick, there's new supply in Houston, but we've got the Wyndham guarantee. Plus we're at the Medical Center where the supply is vastly less pronounced and less impactful.

And we're in really good spot in Miami, where there's been some new supply. Nashville is still on fire. Even though there's been new supply there, it hasn't hurt. We don't have anything in the other markets.

I think that helps us, as well. We're not as impacted by new supply. So I think the combination of all those things makes us feel reasonably good, but very aware of the trending from a supply/demand standpoint, from a corporate profit standpoint, and we will continue to watch those and move forward accordingly.

---

**Bryan Maher** - *FBR Capital Markets - Analyst*

Thanks. That's helpful. I don't want to put words in your mouth, but would you say that it's safe to say that some of the curmudgeon-ness out there might be more portfolio, and/or product specific?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Yes.

---

**Bryan Maher** - *FBR Capital Markets - Analyst*

And then just a second question, when you look at your sales and recognizing Royalton and Morgans, minor setback here, your range for the year was high, low, baked on, I think you said one for the second quarter, and maybe the balance for the third, and then the high estimate was all five in the fourth. As you sit here today, how do you really feel between those two points, the sales process will play out?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

I think it remains to be seen, when things start heading back positively on Morgans and Royalton. Certainly, we feel good on the other three being able to move forward. But these deals take on a life of their own, and certainly the folks we're talking to on the Knick are never in a hurry, relative to their counterparts in the states. And so we feel very good on timing, from a standpoint of Nashville.

We expect that one structural issue, which is just a release issue, and by the way, if we can't get there with the ground lessor, there is an alternative solution that will allow us to get there. So we feel good about being able to put that to bed in the next couple of weeks, get that signed, so we look at that being in the summer. Assuming the -- we feel good about the second round in the best and final round at Esmeralda. We should be able to work the contract fairly quickly, once that's done. So that's late summer, early fall.

The Knick is going to take some time, and we're just going to have to play that out, in accordance with the pace that the eventual buyer typically moves. And Morgans Royalton, we'll just have to see.

As far as the market goes, there's been a decrease, a fairly substantial decrease in transaction volume. I think that we're in pretty good shape on three of the five. We'll see how that impacts us on Morgans and Royalton going forward.

But overall, we still remain confident that we'll be able to get this done. We sold 98 hotels, so we know how to sell hotels, and we sold 98 hotels that weren't near the quality of the ones that we're selling now. So we've just got to play it out.

**Bryan Maher** - *FBR Capital Markets - Analyst*

Thanks. That's helpful. And then just lastly on the Knick, are you still leaning towards wanting to do more of a JV, or are you more willing to do a wholesale sale, particularly in the backdrop of Morgans and Royalton? And that's all I have.

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

I mean, the Knick is its own beast, and whatever happens with Morgans and Royalton is not going to influence that. We would like to sell a JV interest, that is our first option. Again, it comes down to what we can get done, what we can't get done, and what the pricing differentials are there that will allow us to make a more informed decision once we get to the end of the day.

There's a lot of reasons to want to stay in the Knick. It's a great property. Value over the long term is just going to continue to accrete. We do feel very confident about getting the property to stabilization.

Leaving the New York market, right now, it seems good to people that are thinking about New York for the next year or two, but from a long-term perspective, and from an overall quality of portfolio perspective there's a lot of rationale to remain in the New York market, to some degree. So there's a lot of varying factors and we're just going to have to play that by ear as we move forward, see what our opportunities are, and what makes the most sense long-term for our shareholders.

**Bryan Maher** - *FBR Capital Markets - Analyst*

Thanks, Rick.

**Operator**

Your next question comes from the line of Shaun Kelley from BOA. Your line is open.

**Shaun Kelley** - *BofA Merrill Lynch - Analyst*

Just wanted to maybe just follow up a little bit more. You've already given plenty of color on this, but to the extent you can, and appreciate these conversations can change, but Rick, I think you made an allusion to the fact that maybe there's some foreign buyers interested in the Knick. Any more color on the buyer composition, or at least some of the parties that have shown some interest, who that is. Clearly, you can't give us specifics but just like are these international? Is it sovereign wealth? Where are the deep pockets?

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

I'm not going to get into buyer names, but it is, I would I say, 80% of the interest is foreign, and it is mostly from Asia. But I'm not going to get into too much more than that and tell you what kind of companies they are, because you can back into things. It's still preliminary. Their diligence is still preliminary. So I don't want to get too far you ahead of ourselves on that. There is strong interest, but we have to see where that goes.

**Shaun Kelley** - *BofA Merrill Lynch - Analyst*

That's helpful. I think that's all from me. Thanks.

**Operator**

Your next question comes from the line of Lukas Hartwich from Green Street Advisors. Your line is open.

---

**Lukas Hartwich** - *Green Street Advisors - Analyst*

Rick, can you just maybe talk about broadly, what you're seeing in the transaction market and asset values?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Well, we haven't seen a whole lot of change in asset values, certainly nothing that we're talking about on anything. But the transaction market, volume-wise, has certainly decreased fairly substantially during the first quarter, and that could be part where the cycle's headed. And it could be part access to capital. But by and large, the people that we've been talking to are still pretty good.

Morgans and Royalton falling out didn't really have anything to do with that. It had to do with something else entirely in -- as far as we have been led to believe. So we haven't seen any real substantial change.

Could we be heading to a place where pricing moderates a little bit? Yes, potentially. And we've always known that, which is why we wanted to push the process, and started pushing the process as soon as we could. But we haven't seen anything yet, Lucas.

---

**Lukas Hartwich** - *Green Street Advisors - Analyst*

That's really helpful. Thank you. And then also, can you just provide an update on what you're seeing in terms of group production trends, and group pace for the year?

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Group pace has been really good for us. Group is looking good overall. I think pace for the year is up about 12 and transient's only up slightly. It's good that there's still expansion on the transient, but it's also part of the strategy, coming into this year, with things moderating, or the expectation that things would moderate from transient growth standpoint. We are mixing a little bit further into group which explains some of our pacing, but we expect good remainder of the year, particularly third and fourth quarter, from a group standpoint.

---

**Lukas Hartwich** - *Green Street Advisors - Analyst*

Great. That's it from me. Thanks.

---

**Operator**

(Operator Instructions)

Your next question comes from the line of Patrick Scholes from SunTrust. Your line is open.

---

**Patrick Scholes** - *SunTrust Robinson Humphrey - Analyst*

Two questions. First question, as far as the Morgans and Royalton falling out, can you specify a reason why the buyer backed out? I know you have hinted at it, but can you give us more color on that?

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Well, I can't tell you what's in their head, and what they were going through internally. I can tell you that clearly they came to a point that they couldn't move forward on, so they -- as a ruse, they threw out a massive REIT trade, which was silly. And it was a REIT trade of the nature that was totally inconsistent with every discussion during the entire process, with the specific language in the LOI, with the specific language in the contract.

I'm not talking about pricing, I'm talking about structure, that made the deal non-tenable. And they knew it made it non-tenable, so they knew it would kind of get them off the hook. They made a decision for whatever reason internally, that they weren't going to be able to move forward, even though they were a qualified buyer. And so it's just -- we moved on.

**Patrick Scholes** - *SunTrust Robinson Humphrey - Analyst*

Was this a Chinese or international buyer?

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

No, it was not.

**Patrick Scholes** - *SunTrust Robinson Humphrey - Analyst*

And then last question, on the Esmeralda, I'm aware that market, Palm Springs and the desert area, they get a lot of demand from Western Canada, and certainly Western Canadian economy not doing so well. Is that having any impact on the appetite for the asset?

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

No, that's not really having any appetite. We had a good process. We went out to a lot of people, both domestic and international, and we had some fairly good reaction to it.

Everybody loves the property. And then, when the first round of bids came in, there were some -- a good enough amount of activity, that made us think that doing a best and final round made sense. So we'll see where that goes. So far, that didn't really -- as far as we know, that didn't really affect any of the bidding, and we're pretty happy with those that we're going back to for the second round. And assuming that pricing holds, we'd be happy with where we were coming out.

**Patrick Scholes** - *SunTrust Robinson Humphrey - Analyst*

Okay. I have one last question. I think you mentioned that -- what did you say that your transient pace was for the rest of the year?

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

2%.

**Patrick Scholes** - *SunTrust Robinson Humphrey - Analyst*

Okay. And along that, in your transient customer, is that -- what's the split between business travel and leisure travel? And I guess what I'm getting at here is, I guess I'm kind of confused because you started saying that you're not seeing any slow down in transient business, but then you're saying it's 2% RevPAR, and in my view that's not a terribly strong number.

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

What I said was that I'm not seeing any decline in corporate travel. And that's important. When corporate profits start to sag, removing energy from it, there is a strong chance that you're going to start seeing some decline in corporate transient travel, and we're not seeing that. We're seeing continued expansion.

It's small expansion. It's certainly moderated significantly. But overall transient's up 2%, rack's up 19%. We're seeing still good signs, solid signs, but not phenomenal signs, by any stretch of the imagination.

We're not trying to say that corporate travel's booming. It is moderating, no question about it. But we, based on all of our conversations with a lot of corporate clients, guys that we deal with on an ongoing basis, and based on what we've seen from actual bookings and so forth, we're not seeing any decline, and that's very important as it relates to our overall numbers for the year.

---

**Patrick Scholes** - *SunTrust Robinson Humphrey - Analyst*

Okay. Thank you for the clarification.

---

**Operator**

We have no one else in queue at this time.

---

**Rick Smith** - *FelCor Lodging Trust Incorporated - CEO and President*

Okay. Thank you everyone, for joining us, and we'll talk to you next quarter.

---

**Operator**

This concludes today's conference call. You may now disconnect.

---