

Choice Hotels (CHH)

\$90.70 (As of 06/05/20)

Price Target (6-12 Months): **\$95.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 05/26/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:F

Value: D

Growth: D

Momentum: D

Summary

Shares of Choice Hotels have outperformed the industry in the past year. However, the company's shares have declined sharply in the past three months due to the coronavirus pandemic. Recently, the company reported first-quarter 2020 results, wherein earnings and revenues surpassed the Zacks Consensus Estimate. However, the bottom line declined year over year. Owing to the outbreak, the company has also suspended dividend payouts. Moreover, stiff competition and high cost of operations are adding to woes. However, continuous enhancement of the mid-scale brand and the acquisition of the WoodSpring brand and transformation and advancement of the Comfort and Cambria brands, are likely to drive performance. Further, continual expansion strategies through acquisitions and franchise agreements are adding to the positives.

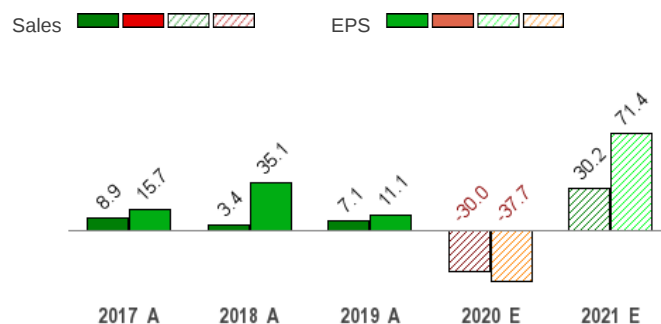
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$109.26 - \$46.25
20 Day Average Volume (sh)	389,611
Market Cap	\$5.0 B
YTD Price Change	-12.3%
Beta	1.37
Dividend / Div Yld	\$0.90 / 1.0%
Industry	Hotels and Motels
Zacks Industry Rank	Bottom 19% (205 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	18.8%
Last Sales Surprise	9.9%
EPS F1 Est- 4 week change	16.8%
Expected Report Date	NA
Earnings ESP	0.0%

P/E TTM	21.4
P/E F1	33.7
PEG F1	3.4
P/S TTM	4.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	205 E	288 E	297 E	248 E	1,017 E
2020	218 A	149 E	200 E	206 E	781 E
2019	218 A	318 A	311 A	268 A	1,115 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.60 E	\$0.99 E	\$1.24 E	\$0.79 E	\$4.61 E
2020	\$0.76 A	\$0.28 E	\$0.70 E	\$0.65 E	\$2.69 E
2019	\$0.84 A	\$1.19 A	\$1.37 A	\$0.92 A	\$4.32 A

*Quarterly figures may not add up to annual.

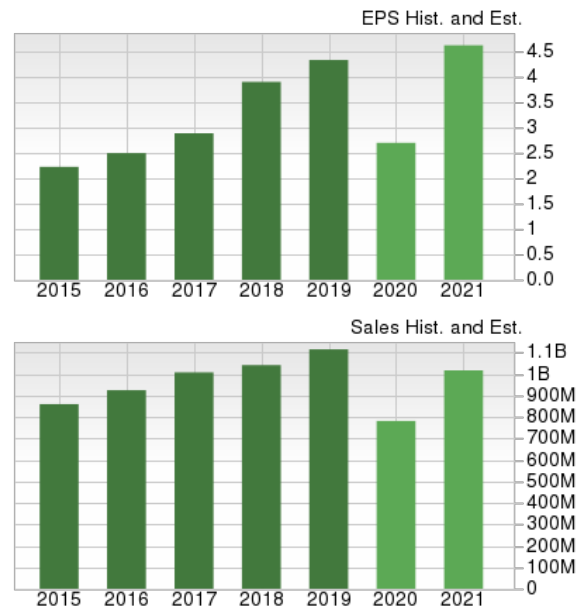
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 06/05/2020. The reports text is as of 06/08/2020.

Overview

Choice Hotels International is one of the largest hotel franchisors globally. As of Dec 31, 2019, the company had more than 7,153 running hotels. This hotel chain is spread across 40 countries and territories internationally, and is present in 50 states domestically and the District of Columbia.

Comfort Inn, Comfort Suites, Quality, Clarion, Clarion Pointe, Sleep Inn, Econo Lodge, Rodeway Inn, MainStay Suites, Suburban Extended Stay Hotel, WoodSpring Suites, Everhome Suites, Cambria Hotels, and Ascend Hotel Collection (collectively, the "Choice brands") are the company's proprietary brand names.

Choice Hotel's primary business segment is hotel franchising, representing 97% of the total revenues. While domestic franchising operations are conducted through direct franchising relationships, international franchise operations are carried out via a combination of direct and master franchising relationships.



Reasons To Buy:

▲ **Strong Brand Recognition & Impressive Earnings Trend:** Choice Hotels' riveting growth potential depends on the continual expansion of its brands. In fact, the company's portfolio of well-segmented brands is getting evidently stronger. With continuous enhancement of the mid-scale brand, acquisition of the WoodSpring brand, and transformation and advancement of the Comfort and Cambria brands, Choice Hotels is poised for growth. Notably, its earnings also surpassed analysts' expectations for 16 straight quarters.

Continual expansion strategies through acquisitions and franchise agreements are major positives.

▲ **Franchise Business Lends Economies of Scale:** The company's 97% of revenues are generated from the franchise business. Choice Hotels gains from economies of scale associated with the franchise business. Accordingly, higher fee from franchisees and transference of cost burden to franchises provide the company with operational advantages. Apart from royalty fees and procurement services revenues, Choice Hotels also collect marketing and reservation system fees to provide support activities for the franchise system. Franchising, as we believe, will facilitate ROE expansion and earnings growth over the long term. Meanwhile, the company's solid commitment toward franchisee profitability is driving incremental revenues. The number of domestic franchised hotels and rooms as of Dec 31, 2019, increased 1.6% and 2.9%, respectively, from the year-ago levels.

▲ **Continual Expansion Bodes Well:** Choice Hotels relies heavily on expansion in both domestic and international markets. Despite the coronavirus pandemic, the company awarded nearly 60 new agreements in first-quarter 2020. During fourth-quarter 2019, the hotelier was awarded 307 domestic franchise agreements, improving 7% year over year. Alongside domestic growth, the company continues to expand its international footprint in new countries. Key international operating markets include Spain, Colombia, Panama, the Caribbean and Canada. Relatively new to the midscale portfolio, Clarion Pointe - part of the popular Clarion brand, is experiencing great success. With more than 30 domestic franchise agreements in 2019. As Clarion Pointe brand is resonating with guests, the total number of Clarion Pointe hotels open or awaiting conversion since the brand launch has now surpassed 50 hotels. Meanwhile, in 2018, the company announced an alliance with Sercotel, a leading hotel operator and franchisor based in Spain. This alliance will enable the extension of Choice Hotels' global footprint in Spain and other markets, as well as the creation of opportunities for additional hotel development across Europe and Latin America.

The Cambria brand has been doing solid business. In 2019, the brand opened 11 new hotels, representing over 1,700 upscale rooms in major markets like Boston, Houston and Phoenix. It ended the year with the opening of its 50th Cambria hotel, the brand's largest property just outside Disneyland in Anaheim, CA.

▲ **Woodspring Acquisition Adds Value:** Apart from constant franchise expansions, Choice Hotels has added 239 extended-stay hotels in 35 states to its portfolio through the acquisition of Woodspring Suites in 2018. In 2019, the extended stay domestic pipeline grew by 13% year over year to 315 hotels. This was primarily driven by the continued expansion of the Woodspring brand. In 2018, the company completed opening of additional 12 WoodSpring hotels in top markets like Chicago, Seattle, Charlotte and Detroit. Currently, Choice Hotels has 270 Woodspring hotels. By the end of 2020, it expects to see Woodspring operating 300 hotels. Additionally, in Jan, 2019, the company finalized an agreement with a developer to build more than 27 additional WoodSpring Suites over the next four years.

In January 2020, the company further strengthened its extended stay presence by introducing Everhome Suites, an all-new construction midscale brand in the extended stay segment. Multiple developers have already committed to build 13 Everhome Suites hotels in Austin, TX and Los Angeles market. Nonetheless, it expects to open its first Everhome Suite in 2021.

Reasons To Sell:

- ▼ **Coronavirus Likely to Hurt 2020 Results:** The Hotel and Motels industry is currently grappling with the coronavirus pandemic and Choice Hotels isn't immune to the trend. Owing to the outbreak, the company has already suspended quarterly dividend payouts. It has also taken certain actions to reduce operating expenses. Moreover, the CEO and the board of directors have agreed to a pay cut for 2020. The board has also decided to furlough part of its corporate workforce in Europe. Further, non-essential and discretionary capital expenditures have been eliminated. Notably, the company has withdrawn 2020 guidance.
- ▼ **High Debt a Concern:** A strong balance sheet will help a company tide over the ongoing crisis. At the end of Mar 31, 2020, the company's long-term debt stands at \$1,208.9 million, up from \$844.1 million at 2019-end. As a result, the company's debt-to-capitalization of 103.7%, compared with 102.8% at the end of Dec 31, 2019. Moreover, the company ended first-quarter fiscal 2020 with cash and cash equivalent of \$322 million, which may not be enough to manage the high-debt level.
- ▼ **High Costs Hurt:** Despite the positive synergies to be realized from acquisitions and focus on franchising, Choice Hotels is shouldering high costs from operations. Total operating expenses in 2018 increased 20.1% year over year. Total operating expenses in 2019 increased 9% to \$781.2 million. In first-quarter 2020, total operating expenses increased 5% from the year-ago quarter to \$171.8 million.
- ▼ **Cutthroat Competition:** The hotel industry is highly competitive, as major hospitality chains with well-established and recognized brands are continuously expanding their global presence. Choice Hotels is continuously facing intense competition from both large hotel chains and smaller independent local hospitality providers. Increasingly, the company also faces competition from new channels of distribution in the travel industry. Additional sources of competition include large companies that offer online travel services as part of their business model such as Alibaba, search engines such as Google, and peer-to-peer inventory sources such as Airbnb and HomeAway that allow travelers to book stays on websites that facilitate the short-term rental homes and apartments from owners, thereby providing an alternative to hotel rooms. Unless the company counters these competitions with appropriate strategies, it may pose a concern for its future profitability.
- ▼ **Cyclical Nature of the Industry Poses Concern:** The hospitality industry is cyclical, and a worsening of global economic conditions might in turn dent Choice Hotels' revenues and profits. Consumer demand for services is closely linked to performance of the general economy, and is sensitive to business and personal discretionary spending levels. Decline in consumer demand due to adverse general economic conditions, poor travel patterns, lower consumer confidence and high unemployment can lower revenues as well as the profitability of the company. These factors can also reduce its management and franchise fee revenues.

Cyclical nature of the industry, the coronavirus outbreak, stiff competition and high cost of operations remain concerns for Choice Hotels.

Last Earnings Report

Choice Hotels Q1 Earnings Surpass Estimates, Decline Y/Y

Choice Hotels reported first-quarter 2020 results, wherein the top and the bottom line surpassed the Zacks Consensus Estimate. However, the top line was almost flat compared to the prior-year quarter, while the bottom line declined year over year.

The lodging franchisor reported adjusted earnings of 76 cents per share, surpassing the consensus mark of 64 cents. However, the bottom line dropped 9.5% from the prior-year number due to a rise in operating expenses.

In the quarter under review, total revenues came in at \$218.2 million. Although the figure topped the consensus mark of \$214 million, it remained relatively flat compared to the prior-year levels.

The coronavirus pandemic is hurting demand and occupancy. The company expects it to affect operations in the future as well. Owing to the unprecedented nature of the crisis, the company has withdrawn its 2020 guidance. Meanwhile, to boost liquidity, the company has temporarily suspended dividend payouts and share repurchase programs.

Franchising & Royalties

Domestic royalty fees totaled \$66.3 million, down 12.2% year over year. Also, domestic system-wide RevPAR declined 15% year over year. Average daily rate (ADR) inched down 3.8% and occupancy was down 610 basis points compared with the prior-year quarter's level.

The company's newly-executed domestic franchise agreements were 58 in the first quarter. As of Mar 31, 2020, the number of domestic hotels and rooms rose 1.2% and 2.7% year over year, respectively.

Operating Results

Total operating expenses increased 5% from first-quarter 2019 to \$171.8 million. However, adjusted EBITDA declined 8.3% from the prior-year quarter to \$69.2 million.

Balance Sheet

As of Mar 31, 2020, the company had cash and cash equivalents of \$321.9 million compared with \$33.8 million on Dec 31, 2019.

Long-term debt in the same period was \$1,208.9 million, up from \$844.1 million at 2019-end. Goodwill, as a percentage of total assets, was 30% at the end of the first quarter compared with 67.3% at 2019-end.

In the first quarter, Choice Hotels paid out cash dividends of \$12.8 million.

Meanwhile, management repurchased roughly \$0.7 million shares for nearly \$54.1 million under the share repurchase program during the first quarter. As of Mar 31, 2020, the company had 3.4 million shares remaining under the current share repurchase authorization.

Quarter Ending **03/2020**

Report Date	May 11, 2020
Sales Surprise	9.87%
EPS Surprise	18.75%
Quarterly EPS	0.76
Annual EPS (TTM)	4.24

Recent News

Choice Hotels Suspends Dividend on Coronavirus Concerns – Apr 8, 2020

Choice Hotels International have recently suspended dividend payout in an effort to preserve cash and maintain ample liquidity in case of a possible financial crisis triggered by the coronavirus outbreak. Notably, the CEO and the board of directors have agreed to a pay cut for 2020.

Choice Hotels Withdraws 2020 Outlook Due to Coronavirus Fear – Mar 17, 2020

Due to the unprecedented nature of the coronavirus outbreak situation on the global economy, Choice Hotels announced the withdrawal of its first quarter and full year 2020 guidance.

Choice Hotels' Cambria Line Sees Largest Opening in US - Feb 2, 2020

In a bid to expand its footprint in the United States, Choice Hotels International, Inc. announced the opening of Cambria Hotel Anaheim Resort Area — marking its 50th and the largest location opening. The 12-story, 352-room upscale hotel provides guests access to unique amenities, such as a waterpark, outdoor movie wall and putting green.

Choice Hotels' Ascend Hotel Collection Sets Record in 2019 - Jan 23, 2020

Choice Hotels International, Inc. continues to expand through franchise agreements. The Ascend Hotel Collection franchised by the company recently announced that 2019 was a record-breaking development year. The brand executed 96 total contracts and added 76 new properties to its portfolio of resort, historic and boutique hotels. This milestone fortifies Ascend Hotel's status as the industry's largest upscale soft brand.

Valuation

Choice Hotels' shares are down 12.3% year-to-date, but up 5.8% in the trailing 12-month period. Stocks in the Zacks sub-industry and Zacks Consumer Discretionary sector is down by 23% and 8.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector were down by 11.8% and 0.8%, respectively.

The S&P 500 index is down 1% in the year-to-date period, but up 10.5% in the past year.

The stock is currently trading at 21.39X trailing 12-month earnings, which compares to 22X for the Zacks sub-industry, 25.13X for the Zacks sector and 20.53X for the S&P 500 index.

Over the past five years, the stock has traded as high as 29.38X and as low as 12.4X, with a 5-year median of 22.81X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$95 price target reflects 22.40X trailing 12-month earnings.

The table below shows summary valuation data for CHH.

Valuation Multiples - CHH					
		Stock	Sub-Industry	Sector	S&P 500
P/E TTM	Current	21.39	22	25.13	20.53
	5-Year High	29.38	33.79	32.62	22.23
	5-Year Low	12.4	15.64	19.53	15.96
	5-Year Median	22.81	23.64	25.37	19.04
P/S F12M	Current	5.68	2.42	2.28	3.59
	5-Year High	5.68	2.42	3.19	3.59
	5-Year Low	2.52	1.13	1.67	2.53
	5-Year Median	3.73	1.65	2.51	3.02
EV/EBITDA TTM	Current	16.76	15.19	10.42	11.82
	5-Year High	21.06	23.07	17.63	12.85
	5-Year Low	9.93	9.3	8.29	8.25
	5-Year Median	15.39	14.46	12.25	10.8

As of 06/05/2020

Industry Analysis Zacks Industry Rank: Bottom 19% (205 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Hyatt Hotels Corporation (H)	Neutral	4
Hilton Grand Vacations Inc. (HGV)	Neutral	3
Extended Stay America, Inc. (STAY)	Neutral	3
Marriot Vacations Worldwide Corporation (VAC)	Neutral	3
Wyndham HotelsResorts Inc. (WH)	Neutral	4
Hilton Worldwide Holdings Inc. (HLT)	Underperform	5
Marriott International, Inc. (MAR)	Underperform	5
WYNDHAM DESTINATIONS, INC. (WYND)	Underperform	4

Industry Comparison Industry: Hotels And Motels				Industry Peers		
	CHH	X Industry	S&P 500	H	HLT	MAR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Underperform	Underperform
Zacks Rank (Short Term)	2	-	-	4	5	5
VGM Score	F	-	-	F	D	F
Market Cap	5.02 B	3.64 B	23.09 B	6.42 B	24.18 B	35.01 B
# of Analysts	5	5.5	14	8	8	9
Dividend Yield	0.99%	0.83%	1.82%	1.26%	0.00%	1.78%
Value Score	D	-	-	D	F	F
Cash/Price	0.07	0.20	0.06	0.23	0.08	0.06
EV/EBITDA	16.29	14.86	13.17	4.74	16.00	18.64
PEG Ratio	3.40	9.15	3.13	NA	9.15	20.15
Price/Book (P/B)	NA	1.86	3.15	1.73	NA	NA
Price/Cash Flow (P/CF)	17.48	11.59	12.43	10.09	16.19	14.62
P/E (F1)	33.72	62.05	22.80	NA	87.31	121.91
Price/Sales (P/S)	4.50	1.34	2.52	1.34	2.64	1.70
Earnings Yield	2.97%	0.79%	4.19%	-4.73%	1.15%	0.82%
Debt/Equity	-28.03	0.32	0.76	0.54	-11.53	-570.75
Cash Flow (\$/share)	5.19	3.11	7.01	6.29	5.39	7.39
Growth Score	D	-	-	F	D	D
Hist. EPS Growth (3-5 yrs)	19.25%	13.82%	10.87%	15.95%	11.69%	18.59%
Proj. EPS Growth (F1/F0)	-37.69%	-80.76%	-10.79%	-246.34%	-74.39%	-85.24%
Curr. Cash Flow Growth	7.52%	6.82%	5.48%	5.97%	24.59%	-2.82%
Hist. Cash Flow Growth (3-5 yrs)	17.19%	4.04%	8.55%	2.61%	2.71%	21.40%
Current Ratio	2.08	1.45	1.29	1.48	1.42	0.62
Debt/Capital	NA%	57.92%	44.75%	34.90%	NA	93.91%
Net Margin	22.27%	7.93%	10.59%	12.57%	8.08%	4.50%
Return on Equity	-385.30%	3.58%	16.26%	3.58%	-276.10%	231.22%
Sales/Assets	0.79	0.49	0.55	0.58	0.60	0.82
Proj. Sales Growth (F1/F0)	-29.90%	-31.04%	-2.61%	-45.75%	-42.59%	-37.34%
Momentum Score	D	-	-	D	A	F
Daily Price Chg	2.60%	0.33%	2.89%	3.69%	1.00%	3.00%
1 Week Price Chg	3.11%	2.99%	4.60%	4.46%	1.17%	-2.80%
4 Week Price Chg	23.87%	21.58%	15.60%	25.97%	21.28%	25.56%
12 Week Price Chg	26.24%	21.07%	29.34%	21.49%	13.66%	15.21%
52 Week Price Chg	8.39%	-11.16%	2.76%	-12.54%	-4.18%	-16.05%
20 Day Average Volume	389,611	389,611	2,537,324	1,130,158	4,050,571	5,268,723
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	-1.28%	-0.12%
(F1) EPS Est 4 week change	16.79%	-11.90%	-0.08%	-86.85%	-34.82%	-57.23%
(F1) EPS Est 12 week change	-39.77%	-78.48%	-16.19%	-338.10%	-76.40%	-86.48%
(Q1) EPS Est Mthly Chg	-55.24%	-85.71%	0.00%	-80.80%	-185.25%	-321.25%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	D
Momentum Score	D
VGM Score	F

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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