

Case Study: Home Suites (HSE)



DROU ACADEMY

Home Suites (HSE)

Disclaimer: The LBO case background and related corporate, industry, and transaction details are artificially created to provide a demonstration of the credit analysis process of a typical public-to-private LBO transaction. The corresponding credit analysis is provided as a sample for educational and training purposes only and should not be referred to or quoted as investment opinions or analysis.

Synopsis

Client Inquiry: Michelle is a Vice President of Drou Bank Corporation (“DBC”, or “Drou Bank”)’s Leveraged Finance team. One day, Michelle receives a phone call from SperInv, a long-term private equity sponsor client of the bank. SperInv explains that, along with another PE firm (“AllStar”), they are planning to buy a currently publicly traded company (the “Target”). Because DBC has been supportive to their past transactions, SperInv considers DBC a core relationship bank, SperInv would like to invite DBC to be part of the financing for the LBO of the Target. The bank commitment deadline is in one week and half, which means Michelle must receive internal approvals (credit, legal, compliance) and sign the corresponding Engagement Letter and Fee Letter before that.

Non-Disclosure Agreement / Access to Information: Given the confidential nature of the deal, the client sent Michelle a non-disclosure agreement (“NDA”) for DBC’s to sign before further details would be disclosed. The NDA is a legal document that restricts the disclosure of related information to unauthorized third parties.

After signing the NDA, SperInv sent Michelle the deal materials which include the historical financial statements, sources and uses of the LBO, term sheet, financial projection and their assumptions, investor presentation containing details of the transaction, the target company, and the industry.

Form Deal Team: Michelle quickly forms a deal team of three and starts the internal process. Michelle is the deal team leader who oversees monitoring the process and communicating with the external and internal parties involved in the transaction. John, an Associate of the team, will assist Michell in internal processes and work with Mia, an Analyst of the team, to complete the internal credit application and gather documents for internal legal, KYC, and compliance purposes.

Each “Deal Team” is structured to suit the needs of the transaction and the proclivities of the institution, and the staffing supports the requisite roles demanded by the circumstances. A Deal Team is typically comprised of:

Leader – responsible for prosecuting the deal from start to finish, with the team reporting to the Leader. The Leader will generally be the internal and external point person, being responsible for interfacing with the various other bank constituents (Credit, Industry Experts, Product Group, Syndications, and Operations for funding the loan). The Leader will be responsible for dealing with the client and all deal negotiations including loan documentation and pricing and also for establishing in collaboration with Credit and Syndications the “hold” strategy (determining the ideal retention amount, which the institution will retain after selling participations of their underwritten commitment to other banks), and any syndications strategy.

Associate – A Deal Team may also have an Associate, representing a mid-level Credit Analyst, responsible for ensuring the detailed work product and analysis is comprehensively documented in accordance with the institutional demands. The Associate will be responsible for completing the internal documentation, and will likely participate in the loan document negotiation, and will be responsible for directing and executing the financial analysis and due diligence execution and documentation thereof. The Associate will generally have some general Credit Analyst experience and will be bringing their experience and acumen to the transaction in developing the sensitivity analysis required to underwrite the loan application.

Analyst – when the institution is large enough and the transaction warrants it, the Deal Team will be complemented by a supporting staff person, the Analyst, which is generally a less experience d Credit Analyst, learning the intricacies of credit and underwriting and Credit risk Management and Management. The Analyst

will likely be responsible for duties required for day-to-day Credit Risk Management, including monitoring and reporting on the regular reported activities of the borrower in compliance of with the Loan Documents.

Transaction Background

The Target Company – Home Suites (“HSE”)

Home Suites Inc. (the “Company”, or ‘HSE”) together with its subsidiaries, owns, operates, and franchises hotels in the United States. As of December 31, 2022, the Company’s hotel network consisted of 775 hotels operated under the brand name “Home Suites”, of which the company owns 676 and franchises 99. HSE competes against other similar hotel brands in the mid-priced extended-stay segment of the lodging industry. It serves customers who require a week or longer stay. Founded in 1991, the Company is headquartered in New York City, New York.

Transaction Announcement by PE Firms

SuperInv and AllStar announce that the two PE firms have formed a consortium to buy Home Suites, Inc. for \$7.6 billion. This acquisition follows a significant decline of bookings in the U.S. hotel industry due COVID-19 pandemic but since 2020 the industry has rebounded nicely. Home Suites, which specializes in economy temporary housing for healthcare professionals, proved stronger than its peers. The PE firms’ offer of \$22.50 per share represents a premium of 20% to HSE’s share closing price on April 2nd. Shares of HSE, rose more than 22% before the opening bell.

Credit Application - Business Profile

Mia, the analyst of the deal team, completes the following Business Profile as part of the credit application. The Business Profile contains specific information about the company that the credit committee needs to know about the potential borrower of the bank to make a credit decision.

Drou Bank Corporation Internal Application

CREDIT APPLICATION - NEW BORROWER			
<u>Borrower Summary</u>			
Borrower Name	Home Suites Inc. (NYSE: HSE)	Borrower Type:	New Borrower
Borrower KYC No.	KYC in Process	Industry:	Extended Stay Hotel
Sponsor(s)	SuperInv. All Star	Headquarterts	New York, USA
External Rating	Current: BB- (S&P)/Ba2 (Moody's) Expected: B (S&P)/B2(Moody's)	Founded	1991
Internal Rating	DIR 15	Expected Title	Joint Lead Arranger ("JLA")
Total Commitment	Bank Loan -Global \$3,500 MM / Drou Bank \$875MM Bridge Loan: Global \$1,700 MM / Drou Bank \$425 MM Total: Global \$5,200 MM /Drou Bank \$1,300 MM Expected Hold Level Approx. \$90 million at close	Expected Fees	\$19 MM
Admin Bank	Topbank Bank NA	Expected Closing:	Jan-23

Business Profile

Business and History

Home Suites Inc (“Home Suites”, the “Company”, NYSE: HSE)

Founded in 1991, Home Suites is a hotel chain headquartered in New York, United States. It owns, operates, and manages a hotel network of around 780 hotels in the United States. As of December 31, 2022, the company owned and operated 676 hotels with 77,000 rooms with 8,900 employees. It serves customers in the mid-priced extended-stay segment of the Hotel and Lodging industry. The Company also licenses its “Home Suites” brand to third-party franchisees. As of December 31, 2022, the company franchised 99 hotel properties approximately 10,500 rooms.

The Company’s extended stay hotels offer customers an alternative option to traditional rental apartments and hotels. The average length of stay is approximately a month with the flexibility of shorter or longer terms upon clients’ requests. By contrast, the typical length of stay is over 6 months for traditional rental apartments and 3-5 days for traditional hotels. The rooms are fully furnished with in-room kitchens and other complimentary amenities that are normally available in a hotel: breakfast, free Wi-Fi, TVs, and housekeeping service, which is typically provided weekly.

History

1991: The company was founded in New York as a family-owned vacation hotel “Suites”.

1996: The family-owned hotel was acquired by a hotel developing firm, HDeveloper, and started to operate under the brand name “Home Suites”.

1997-2001: The company started to expand through selective acquisitions of extended-stay hotels national-wide.

2003: Home Suites Inc was formally incorporated, as a result of spin-off from HDeveloper, and started to operate as a stand-alone hotel chain company.

2006: The franchise business model was launched to let third parties join the hotel chain via franchise agreements. The company further expanded its footprint in the United States.

2009: Post the financial crisis, the company brought in a new management team. The new management team started the re-evaluation process of the company’s business model and strategies.

2010: As a result of the new management’s re-evaluation process, the company focused its operations mainly on the mid-priced extended-stay segment of the hotel and lodging industry.

2011: The company launched IPO and started to be publicly traded in the New York Stock Exchange under the ticker “HSE”.

2015: Chris Smith joined the firm as CEO as the previous CEO announce his retirement. Chris later hired Daniel Brandel as CFO of the company.

2020: As COVID-19 Pandemic negatively impacted the global economy as well as the lodging industry, the company incorporated new business strategies to provide temporary stay for healthcare providers and offer quarantine services for travelers. The company also won contracts from the local government as a provider of shelters to homeless people to prevent the spread of the virus.

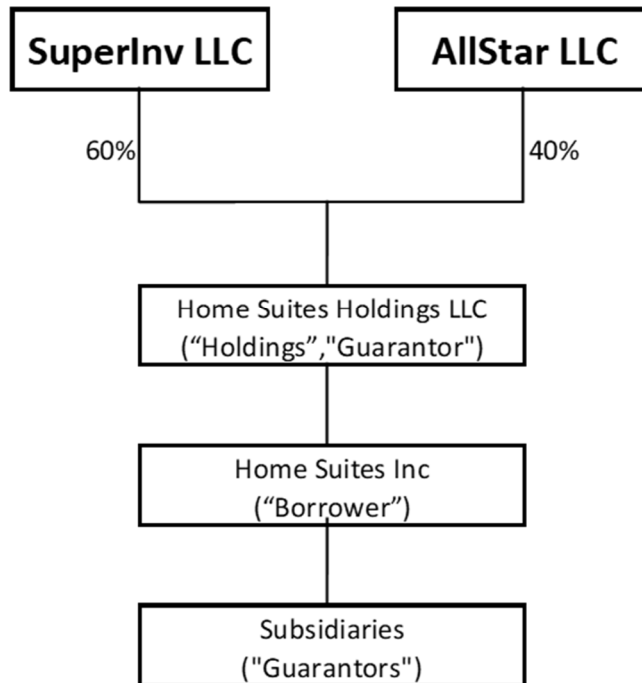
2023: A consortium formed by private equity firms, SuperInv and AllStar, announced the acquisition of Home Suites.

Ownership and Management

Upon the closing of the proposed LBO transaction, the Company will be privately owned by private equity firms SuperInv (60%) and AllStar (40%).

Pro Forma Corporate Structure (post 3/2023 transaction closing)

PROFORMA CORPORATE STRUCTURE



Sponsors

SuperInv

SuperInv, formed in 1990, is a global private equity firm with a focus on real estate and a total of approximately 600 employees managing \$137.2 billion of Total Assets Under Management (“AUM”) as of December 31, 2022. The firm pursues companies in both established and growth-oriented stages. Through its 30 years of investment in real estate, it has acquired several hotel businesses and successfully grown the business with an average Internal Rate of Return (“IRR”) of 32% of its hotel portfolio. SuperInv has a dedicated team consisting of hotel industry experts with an average of over 20 years of experience. Those professionals have proven success in achieving SuperInv’s hotel portfolio companies’ growth and operational improvements.

AllStar

AllStar, incorporated in 1986, is one of the world’s biggest private equity firms with over 750 employees globally and \$201.2 billion of Total Assets Under Management as of December 31, 2020. It has a diversified portfolio, spanning industries, geographies, and strategies. The firm has delivered strong investment results across economic cycles and business stages. It recently closed the fundraising of FUND IV with a total committed capital of \$60 billion. The fund will be designated to investment in categories of real estate on a global basis. Since its inception, AllStar has successfully executed its investment strategies.

Key Executives

Home Suites is led by a management team with extensive industry experience in hospitality, consumer retail, and service businesses. Each key executive has over 15 years of experience and a proven track record of successfully implementing business strategies that bring both growth and improvement to the business.

Chris Smith, CEO of HSE, joined since 2015.

Chris Smith has served as Chief Executive Officer of HSE and has been a member of the board since 2015. Mr. Smith earned a master's degree in Hotel Management from a top business school and has over 20 years of experience in the lodging industry. Prior to joining HSE, Mr. Smith holds various executive roles in other hotel chain brands and successfully grew the businesses during his period of service.

Daniel Brandel, CFO of HSE, joined since 2015.

Daniel Brandel has served as Chief Financial Officer of HSE since 2015. Mr. Brandel is responsible for developing the Company's financial strategy, business performance metrics, and corporate financial reporting. Prior to joining HSE, Mr. Brandel served as CFO of a Global Fortune 500 retail company, from 2010. Mr. Brandel started his career in corporate finance in the late 1990s and served in several publicly traded and private equity backed organizations. Mr. Brandel earned his bachelor's degree and his M.B.A. from top universities. He also obtained a certificate in management accounting.

Charlotte Jones, COO of HSE, joined since 2012.

Charlotte Jones has served as Chief Operating Officer since 2018. Miss. Jones has been with HSE since 2012. Miss. Jones is responsible for managing the hotel's operating. She oversees various corporate functions, including sales, human resources, product and design, rooms, food and beverage, and engineering. Prior to assuming her current position, Miss. Jones served in several senior positions at HSE, including Executive Vice President of Operations and Senior Vice President of Sales. Prior, to joining HSE, Miss. Jones served as a top executive in another hotel chain businesses.

Segments and Geographic Footprint

Segments

The Company operates in two segments:

Owned Hotels (86.3% of total revenue)

The Owned Hotels segment is the Company's primary segment and accounted for 86.3% of total revenue for the fiscal year ended December 31, 2022. Revenues are generated from the operation of 676 Company-owned hotel properties.

Franchised Hotels (13.7% of total revenue)

Revenues of the 99 Franchised Hotels segment are from fees under various franchise and management agreements and accounted for 13.7% of total revenues for the fiscal year ended December 31, 2022. The franchise contracts provide third parties access to HSE's system-wide platforms and/or management services, as well as the right to use the brand name "Home Suites".

Geographic Footprint

As of December 31, 2022, HSE operated in 38 states in the United States with a concentration of popular business and vacation designation states. Out of the total 77,000 (owned) system-wide rooms, 14.8% were in New York, 11.3% were in California, 9.2% were in Florida, 5.9% in Texas, 5.4% in Arizona, and 5.2% in New Jersey.

List of States that count for more than 5% of Total Rooms.

HOME SUITES INC.(HSE)					
State	# of Owned Hotels	# of Franchised Hotels	Total # of Hotels	# of Rooms	% of Total Rooms Owned
New York	99	15	114	12,605	16.4%
California	70	17	87	9,592	12.5%
Florida	58	10	68	7,822	10.2%
Texas	37	8	45	4,996	6.5%
Arizona	37	6	43	4,601	6.0%
Total Owned				77,000	
Total Franchised				10,800	
Customers					
<p>Home Suites' typical customers are:</p> <ul style="list-style-type: none"> - business travelers on business trips, assignments, or training programs. - relocated corporate employees during their search for new houses and apartments to settle; - leisure travelers looking for a longer stay in a home-style apartment with key amenities such as a kitchen while still have access to managed housekeeping services; and - home buyers or anyone in need of a temporary home <p><i>Customers during COVID-19 Pandemic</i></p> <p>As management adopted temporary business strategies during COVID-19 Pandemic in response to declined businesses from traditional customers, Home Suites serviced:</p> <ul style="list-style-type: none"> - healthcare providers who traveled to support regions that reached the maximum capacity of local hospital systems. - people without housing that were sponsored by local governments; and - inter-state travelers looking for quarantine places. 					
Business Strategies					
<p>The management team of Home Suites has been focusing on increasing brand awareness, building a long-term relationship with intuitional clients, and improve service quality to stand out among investors:</p> <ul style="list-style-type: none"> - Increase Brand Awareness: Home Suites has been investing in market campaigns for its brand name to be associated as the to-go extended stay choice with affordable price and high standard quality of services. - Build Long-Term Corporate Relationships: Home Suites has a sales team focused on building partnerships with companies in the finance, consulting, technologies, and construction industries. Home Suites has been a housing provider for those companies' out-of-town assignments and training programs. The corporate partnership has brought Home Suites stable revenue over the years. 					

- **Continues Focus on Quality:** Since the current COO, Charlotte Jones joined the firm as the senior executive overseeing the hotel's operating, Home Suites has implemented long-term and system-wide hotel room renovation and infrastructure upgrades to maintain its industry-leading quality of services.

Temporary strategies during COVID-19 Pandemic:

In 2020, the COVID-19 Pandemic caused both international and national travel restrictions and shelter-in-place orders from local governments for an extended period. As travelers canceled their plans, Home Suites experienced significant disruption in business in the 1st quarter of 2020. The management quickly adjusted to the situations and implemented a temporary strategy to mitigate the impacts on its business:

- formed strategic partnership with healthcare systems as a designated housing provider for traveling healthcare providers
- participated in the local government's shelter program for people without a home
- switched to a contactless service mode that met the requirements for quarantine

Strategies post COVID-19 Pandemic

In addition to its traditional strategies, the management team has been working with the sponsors for a new strategic plan for business recovery and growth post-pandemic:

- **Digital platforms penetration:** To reach potential customers and adjust to consumers' growing preference of searching for travel online, Home Suites will keep upgrading its online booking platform and mobile app as well as continue its online penetration through social media and search engines.
- **Differential pricing and service offering:** Home Suites will expand its service offering to both the luxury segment and the economic segment to offer more options to customers. The Company will launch new brand names for different segments.
- **Growth through Franchising:** Home Suites will focus on growing through hotel franchising and attracting new franchisees, which will bring the Company economies of scale and speed up expansion to other states in which Home Suites currently has a low market share.

Competitions and Market Share

Competitions

Home Suites competes in the highly competitive extended-stay segment of the Hotels and Lodging industry. Competitions come from other extended-stay hotel brands, traditional hotels looking to expanding into the extended-stay segment, as well as alternative lodging businesses such as serviced apartments and private homeowners renting through various digital platforms (websites, marketplace on social media, mobile apps, etc.).

The Company also sees competition in attracting potential franchisees as it's the main source of growing the scale of business. Players in the Hotel and Lodging industry have been aggressively expanding market shares through franchising.

Market Share

Home Suites' business is focused on the mid-price extended stay segment of the industry, which accounted for approximately one-third of the extended-stay rooms in 2020, per ABC research's "Industry Report on Extended-Stay Segment of Lodging Industry" published in February 2021. The Company has approximately 19% market share based on revenue.

Key Competitors

- XX Hotel: direct competitor with approximately 25% market share of mid-price extended stay segment
- YY Hotel: a key player in the Hotel & lodging Industry but currently mainly in the luxury segment, looking to expand into the mid-price segment
- ZZ Hotel: a key player in the economic (low-priced) extended-stay segment

Environmental, Health and Safety Matters

Both the Company’s owned and franchised hotel properties are subject to various regulations that make the hotels responsible for cleaning up hazardous contaminations from the property, natural resource damage arising from those contaminations. The consequences of breaking those laws would be several, resulting in penalties and huge costs of remediation as wells as damages to the Company’s reputation.

Both the private equity sponsors and Home Suites’ management team realize the importance of being in compliance with correspondingly Environmental, Health and Safety regulations and laws. The Company has been and will continue to focus on actively monitoring the emission of hazardous contaminations at or from hotel properties, investing in sustainable and environmental-friendly technologies, and making timely and transparent disclosure of its efforts and results on corresponding matters.

Key Advantages

The Company has the following key competitive advances:

-Seasoned Private Equity Sponsors and Management Team: Both the private equity sponsors, SuperInv and AllStar, have decades of experience in running hotel businesses from various stages and a track record of achieving growth and high returns under the sponsor’ ownership. The current Management team has been successfully running Home Suites for years. During COVID-19 Pandemic, the management team adapted to the new challenges, came up with new strategies quickly, and delivered a relatively stronger performance in 2020 compared to other hotel businesses. This demonstrates the management’s ability and business acumen even through challenging times.

-Well-known Brand Name: Due to the Company’s years of effort in building its brand awareness and through its geographic expansion as well as continuous focus on quality, it ranked as the #2 brand in XYZ Research’s market survey (published in August 2020) on the mid-priced extended-stay segment. The Company holds a 19% market share and currently operates a hotel network in 38 states, making it one of the top players in the segment.

-Proven Resilient Business Model: The Company has benefited from its long-term partnerships with intuitional clients as a housing provider for off-sight assignments and training programs. Corporate travel needs are recurring in nature and thus provide Home Suites with more stable and foreseeable revenue. The Company is also committed to continue expanding its footprint and differentiate service offerings attract more customers.

Key Risks

Risks	Mitigants
<p><i>Cyclical and Seasonality</i></p> <p>As the general Hotel & Lodging industry is cyclical and seasonal in nature, the Company’s business is tied to the economic cycle and subject to seasonal fluctuations. Revenue is generally lower during the 1st and 4th quarters of each calendar year.</p>	<ul style="list-style-type: none"> - Home Suites has a proven resilient business model that focuses on building long-term partnerships with intuitional clients, which brings more reliable revenue streams. - The Management team demonstrated strong business acumen during the COVID-19 Pandemic by deploying new strategies adapted to the challenges when the global economy was heavily disrupted. - Compared to traditional hotels, hotels in extended-stay segment offer home-style rooms with kitchenettes and have been popular among travelers looking for vacation stays during holiday seasons (1st and 4th quarters).

<p><i>Increased Competitions</i></p> <p>The extended-stay segment has been highly competitive and gained increasing attention from traditional hotels as well as private homeowners.</p>	<ul style="list-style-type: none"> - Home Suites is currently the industry-leading player with #2 brand awareness, which makes it the preferred hotel for travelers. - The Company’s new business strategies will focus on digital platforms penetration and differentiated pricing & service offerings, which will compete against industry newcomers. - Compared to private homeowners, well-known hotel chains are a more reliable and safer source of housing with professional high-stand quality of services.
<p><i>Higher Labor and Operating Expenses from Accelerated Inflation</i></p> <p>As the US inflation is expected to rise over the medium term, corporates are facing rising operating costs which will put pressure on margins.</p>	<ul style="list-style-type: none"> - When Home Suites experienced high inflation environments in the past, the Company managed to mitigate the impact by passing through the cost to customers and improving operating efficiencies. - Home Suites’ focus on growth through hotel franchising, which business has higher margins than owned hotels, will improve the over margins of the Company.
<p><i>Tightening Regulations on Environmental, Health, and Safety Matters</i></p> <p>Both the Company’s owned and franchised hotel properties are subject to various regulations on Environmental, Health, and Safety matters. Home Suites are facing tightening rules and rising standards of disclosure.</p>	<ul style="list-style-type: none"> - The Company has been investing in sustainable and environmental-friendly technologies that minimize the impact of hotel operating on environments. - Both the Sponsors and Management are committed to developing enhanced procedures and mandatory training for employees to comply with the regulations. - The Company has also been hiring industry experts and expanding its ESG team to ensure compliance with federal, state, and local laws.

Credit Application – Industry Analysis

After completing the Business Profile, the Deal Team complete a comprehensive Industry Analysis, with the primary original work product being completed by Mia and reviewed for completeness, thoroughness, and accuracy by the Associate and finally by Michelle as the Team Leader. The Industry Analysis part of the credit application focuses on the key characters of the industry in which the borrower competes, the current development and outlook, and any industry-specific factors that could impact the borrower’s business.

Industry

<p>Summaries</p>
<p>The Extended-Stay Segment of the Hotel and Lodging Industry in the United States</p> <p>Extended stay hotels offer apartment-like rooms with kitchenettes with a homely and comfortable feeling. Guests have the flexibility to check out or extended the stay whenever they wish without being bound to a contract or a fixed-term lease.</p> <p>Extended-stay hotels represent a growing segment within the U.S. lodging industry. Based on type, the market is divided into Luxury, Middle (mid-priced), and Economic type extended-stay hotels.</p>

Key Characters

Cyclicality and Seasonality

The overall hotel and lodging industry performance is generally tied to both macro and micro-economic cycles and is seasonal in nature with revenues generally lower during the first and fourth quarters of each calendar year. The extended-stay segment, though, is relatively less cyclical and seasonal. Its flexible terms of stay and apartment-like styles have gained popularity for people looking for temporary homes when settling down in new cities and towns. The extended stay hotels have also become the preferred choice during holiday and skiing seasons.

Higher Barriers to Entry

The lodging industry requires heavy capital investments for the hotel buildings and rooms, corresponding amenities, IT infrastructure, personnel recruiting, and training. Reputations are also key to success in the industry as travelers tend to choose well-known hotel chains for a guaranteed quality of services.

Highly Competitive with New Thread from Private Homeowners

The extended-stay segment is highly competitive. Through years of integration efforts via acquisition and franchising, top plays accounted for more than 50% share of the market. The remaining markets are highly fragmented with many local hotel operators. Traditional hotel brands have also shown interest in the extended-stay segment, which further increases the completions. Furthermore, technology renovations have granted private homeowners' access to the market and travelers via online platforms, mobile apps, and social media marketing.

Growth Drivers

A key indicator of the industry is revenue per available room ("RevPar"), which is calculated by Average Daily Rate ("ADR", price charged per room) times Occupancy Rate. RevPar is impacted by the following factors:

- Economy Growth:** As the economy grows, so does the consumer and business spending, which would result in increased business and leisure traveling thus increasing demand for hotels.
- Growth in International and Domestic Tourist Industry:** Demand from tourists has always been a key driver of the industry and the main source of revenue generation.
- US Housing Market:** Extended stay hotels offer home buyers with temporary housing while doesn't require signing a fixed-term lease. As the housing market grows, so does the demand for extended stay hotels while the home buyers settling the transactions.

Current Trend

The COVID-19 pandemic has caused governments across the globe to implement unprecedented lockdowns and shelter-in-place orders, which adversely disrupted the global economy. The overall hotel and lodging industry is highly tied to the economic cycle, thus also experienced a significant decline in 2020 with RevPar dropped by 41.7% year over year for 2020. As COVID-19 restrictions were partially lifted in 2021 and fully lifter in 2022, the company has seen a significant rebound – higher than pre-covid levels.

The extended-stay segment is relatively more resilient than traditional hotels. Within the extended-stay segment, the mid-priced segment saw the least decline in 2020 with a decline in RevPar below 30% driven by both reduced ADR and occupancy rate. ADR for the mid-priced extended-stay hotels dropped by approximately 15% in 2020. The total supply of rooms in 2020 remained stable as many acquisitions were put on pause due to the pandemic. The industry has seen a significant rebound as COVID-19 travel restrictions were lifted. The Occupancy rates across the US has recovered to pre-covid levels and in many cases higher than pre-pandemic levels.

Industry Outlook

Post pandemic, the extended-stay hotel market is expected to see a recovery back to the pre-pandemic level in 2022. Both ADR and occupancy rate are expected to see a continued recovery for 2023 though there is talk of recession given some challenging macroeconomic data such high inflation and high interest rates as a result the Fed is fighting high inflation rates. ADR is expected to further grow as hotels will pass through increased costs resulting from a rising inflation environment.

Credit Application – Historical Financial Performances

After receiving historical financials from the sponsor, Mia spreads the provided financial statements of HSE into DBC's internal financial summary template and conducts the analysis of historical financial performance with a focus on the most recent fiscal year.

Historical Financial Performance - Operating Assumptions

INCOME STATEMENT							
	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31
(\$000's)	2022	2021	2020	2019	2018	2017	2016
Owned Hotels	1,696,670	1,437,856	1,027,040	1,414,251	1,376,211	1,339,915	1,233,730
Franchised Hotels	270,165	257,300	223,739	47,612	153,859	199,355	290,981
Total Revenue	1,966,835	1,695,156	1,250,779	1,461,863	1,530,071	1,539,270	1,524,712
Cost of Revenue	930,130	755,230	712,512	721,429	715,495	702,654	696,926
Gross Profit	1,036,705	939,926	538,267	740,434	814,576	836,616	827,785
Total Operating Expenses	428,200	372,130	357,814	351,028	359,705	385,091	383,195
EBIT (Operating Income or Loss)	608,505	567,796	180,454	389,406	454,871	451,525	444,590
Interest Expense	139,400	142,600	146,755	140,480	139,618	142,212	153,160
EBT & other Income/Expenses	469,105	425,196	33,698	248,926	315,253	309,313	291,431
Other (Income)/Expenses Net	10,415	12,100	(52,409)	15,582	10,655	31,271	54,187
EBT	458,690	413,096	86,107	233,344	304,598	278,042	237,244
Income Tax Expense	150,650	122,573	29,093	74,871	84,581	91,713	76,663
Net Income	308,040	290,524	57,014	158,473	220,018	186,329	160,581
EBIT	608,505	567,796	180,454	389,406	454,871	451,525	444,590
Depreciation	221,230	210,100	201,916	187,122	94,884	208,662	230,196
Amortization of Intangibles	-	-	-	-	-	-	-
EBITDA	829,735	777,896	382,369	576,528	549,755	660,187	674,786

Figure 2.4

OPERATIONAL METRICS							
	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31
	2022	2021	2020	2019	2018	2017	2016
Average Daily Rate (ADR)	\$ 75.0	\$ 70.0	\$ 62.0	\$ 71.5	\$ 67.2	\$ 66.8	\$ 62.4
ADR Price Increase %	7.14%	12.90%	(13.23%)	6.30%	0.70%	6.98%	
Number of Rooms	77,000	75,100	74,400	74,280	73,800	73,320	73,200
Number of Rooms Increase %	2.53%	0.94%	0.16%	0.65%	0.65%	0.16%	
Revenue at 100% Occupancy per Year	2,107,875	1,918,805	1,683,672	1,937,330	1,810,804	1,786,554	1,667,203
Actual Revenue - owned	1,696,670	1,437,856	1,027,040	1,414,251	1,376,211	1,339,915	1,233,730
Occupancy Rate	80.5%	74.9%	61.0%	73.0%	76.0%	75.0%	74.0%
RevPar	\$ 60.37	\$ 52.45	\$ 37.82	\$ 52.16	\$ 51.09	\$ 50.07	\$ 46.18
RevPar Increase %	15.09%	38.70%	(27.50%)	2.10%	2.04%	8.43%	
Owned Hotels Revenue Growth	18.0%	40.0%	-27.4%	2.8%	2.7%	8.6%	
Franchised Hotels Revenue Growth	5.0%	15.0%	369.9%	-69.1%	-22.8%	-31.5%	
Revenue Growth	16.0%	35.5%	-14.4%	-4.5%	-0.6%	1.0%	
PROFITABILITY RATIO							
Gross Margin	52.7%	55.4%	43.0%	50.7%	53.2%	54.4%	54.3%
EBITDA Margin	42.2%	45.9%	30.6%	39.4%	35.9%	42.9%	44.3%
EBIT Margin	30.9%	33.5%	14.4%	26.6%	29.7%	29.3%	29.2%
INCOME STATEMENT ASSUMPTIONS							
Cost of Revenue % of Revenue	47.3%	44.6%	57.0%	49.3%	46.8%	45.6%	45.7%
Operating Expense % of Revenue	21.8%	22.0%	28.6%	24.0%	23.5%	25.0%	25.1%
Depreciation % of Revenue	11.2%	12.4%	16.1%	12.8%	6.2%	13.6%	15.1%
Tax Rate %	32.8%	29.7%	33.8%	32.1%	27.8%	33.0%	32.3%
CASH FLOW STATEMENT ASSUMPTIONS							
Capex % of Revenue	13.0%	15.0%	11.6%	20.7%	16.2%	11.7%	
Deferred Tax % of Taxes	8.0%	7.3%	35.7%	5.8%	32.2%	-29.3%	
CASH FLOW STATEMENT ASSUMPTIONS							
Accounts Receivable Days	3.8	3.8	4.9	5.1	5.9	6.0	
Inventory Days	0.0	0.0	0.0	0.0	0.0	0.0	
Other Current Assets % of Revenues							
Accounts Payable Days	21.2	24.4	23.3	20.1	18.3	17.2	
Other Current Liabilities as % of Revenues							

Revenues from Owned Hotels segment were stable before 2020 driven by the steady growth of RevPar and the number of rooms. In 2020, the global economy was significantly disrupted by the COVID-19 Pandemic. To combat the spread of the virus, global governments have implemented travel restrictions and shelter-in-place orders, which resulted in cancellations of travelers' hotel booking and revenue decline in the hotel and lodging industry. To mitigate the impact, the management quickly adjusted to the situation and implanted a temporary strategy to offer temporary housing solutions for traveling healthcare providers, people without a home sponsored by local government, and essential travelers subject to mandatory quarantine requirements. Following 2020 pandemic, the recovery shown in 2021 and 2022 has been significant. Revenues has seen increases as a result from higher volume due to higher occupancy rates and more rooms as well as higher prices charged per day.

Revenues from Franchised Hotels segment are mainly royalty fees from franchisees. Revenues declined by double digits from 2016 to 2019 mainly due to the termination of franchise agreements. The majority was due to Management’s quality control efforts since the new CEO and CFO joined the firm in 2015. In order to maintain the high standard of services associated with the brand name, franchised hotels that didn’t meet the quality standard were terminated. In 2020, revenues increased in the Franchised Hotels segment due to new franchise agreements as a result of management’s focus on growth through franchising business.

Gross Margin decline before 2020 was due to the decrease in franchise revenue which is a higher margin component of the total revenue. Margin decline was also a result of industry-wide wage increase especially the hourly wage of temporary workers hired during peak seasons. The Gross margin decline in 2020 was driven by reduced RevPar as a combination of reduced Average Daily Rate and occupation rate during the COVID-19 Pandemic. Following the 2020 pandemic gross margins have significantly recovered from 43% in 2020 to 55.4% and 52.7% in 2021 and 2022, respectively.

EBITDA/EBITDA Margin has improved since 2017 due to Management’s continued effort on operational efficiencies. In 2022, has seen significant improvement following the low levels experienced in 2020 during COVID-19 Pandemic driven by disinfecting products, personal protective equipment (PPE) for employers, and other associated expenses.

Historical Financial Performance – Cash Flows

SUMMARY CASH FLOW ANALYSIS						
	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31
(\$000's)	2022	2021	2020	2019	2018	2017
Net Income	308,040	290,524	57,014	158,473	220,018	186,329
Depreciation	221,230	210,100	201,916	187,122	94,884	208,662
Amortization of Intangibles	-	-	-	-	-	-
Deferred Taxes	12,020	9,000	10,372	4,351	27,209	(26,881)
Cash Income	541,290	509,624	269,301	349,946	342,110	368,110
<u>Working Capital Activity</u>						
Net Receivables	(2,800)	(2,849)	373	6,899	2,171	(889)
Inventory	-	-	-	-	-	-
Accounts Payable	3,370	3,600	6,430	5,000	3,000	2,336
Accrued liabilities	-	-	-	-	-	-
Total Working Capital	570	751	6,803	11,899	5,171	1,447
Other Current Assets/Liabilities	-	-	-	-	-	-
Operating Cash Flow (OCF)	541,860	510,374	276,105	361,845	347,281	369,557
<u>Investment Activities</u>						
Capital Expenditure	(255,175)	(254,496)	(144,530)	(302,606)	(247,871)	(180,095)
Long-Term Investment	(1,195)	(492)	(638)	520	32	(26,705)
Other Long-Term Assets	-	-	-	-	-	-
Total Investment Activities	(256,370)	(254,987)	(145,169)	(302,086)	(247,839)	(206,799)
Cash Flow Before Financing Activity	285,490	255,387	130,936	59,759	99,442	162,758
<u>Financing Activities</u>						
ST Debt	-	-	-	-	-	-
LT Debt	(120,000)	(120,000)	61,183	164,555	(47,113)	(300,607)
Other Long-Term Liabilities	-	-	-	-	-	-
Other Financing Activities	-	-	-	-	-	-
Total Financing Activities	(120,000)	(120,000)	61,183	164,555	(47,113)	(300,607)
Net Change in Cash	165,490	135,387	192,119	224,313	52,329	(137,849)

Operating Activities have generated positive cash flows to the firm. Working Capital has been a source of cash flow to the firm mainly due to Accounts Payable as the firms managed to negotiate favorable terms on payments and accrued expenses especially during the COVID-19 Pandemic and both years following the pandemic. Deferred Taxes is also a source of cash to the firm.

Investment Activities mainly consisted of Capital Expenditure for hotel expansion, renovation, and maintenance. In 2020, Capital Expenditure decreased as many scheduled maintenance and expansion projects were paused due to the COVID-19 pandemic. For 2021 and 2022, the company started to increase their capital expenditures post covid but at much lower levels than pre-covid levels.

Financing Activities' fluctuations were driven by payments and borrowings of long-term debts.

The Company has been accumulating cash in the past two years. In 2020, despite the negative impact of the global health crisis on topline growth, Home Suites generated \$252 million cash and continue to generate post-covid due higher revenue, higher margin and lower capex.

Historical Financial Performance – Liquidity and Ratios:

BALANCE SHEET STATEMENT							
	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31
(\$000's)	2022	2021	2020	2019	2018	2017	2016
Assets							
Current Assets							
Cash And Cash Equivalents	1,045,722	880,232	744,845	552,726	328,412	276,083	413,932
Other Short Term Investments	-	-	-	-	-	-	-
Total Cash and Cash Equivalent	1,045,722	880,232	744,845	552,726	328,412	276,083	413,932
Account Receivables	22,100	19,300	16,451	16,824	23,723	25,894	25,004
Inventory	-	-	-	-	-	-	-
Other Current Assets	-	-	-	-	-	-	-
Total Current Assets	1,067,822	899,532	761,295	569,550	352,135	301,977	438,937
Non-current assets							
Gross Property, Plant and Equipment	6,495,200	6,240,025	5,985,529	5,840,999	5,538,393	5,290,522	5,110,427
Accumulated Depreciation	(2,292,316)	(2,071,086)	(1,860,986)	(1,659,071)	(1,471,949)	(1,377,065)	(1,168,403)
Net Property, Plant and Equipment	4,202,884	4,168,939	4,124,543	4,181,928	4,066,444	3,913,457	3,942,024
Long Term Investments	81,315	80,120	79,628	78,990	79,510	79,542	52,837
Goodwill	64,237	64,237	64,237	64,237	64,237	64,237	64,237
Intangible Assets	41,344	41,344	41,344	41,344	41,344	41,344	41,344
Other long-term assets	15,781	15,781	15,781	15,781	15,781	15,781	15,781
Total non-current assets	4,405,561	4,370,421	4,325,533	4,382,280	4,267,316	4,114,361	4,116,224
Total Assets	5,473,382	5,269,952	5,086,829	4,951,830	4,619,451	4,416,338	4,555,160
Liabilities							
Current Liabilities							
Accounts Payable	55,700	52,330	48,730	42,300	37,300	34,300	31,964
Accrued liabilities	-	-	-	-	-	-	-
Other Current Liabilities	-	-	-	-	-	-	-
Current Portion of Long Term Debt	-	-	-	-	-	-	-
Total Current Liabilities	55,700	52,330	48,730	42,300	37,300	34,300	31,964
Non-Current Liabilities							
Long Term Debt	2,980,346	3,100,346	3,220,346	3,159,163	2,994,608	3,041,722	3,342,329
Deferred taxes liabilities	297,420	285,400	276,400	266,028	261,677	234,468	261,349
Non-Current Deferred revenues	-	-	-	-	-	-	-
Total Non-Current liabilities	3,277,766	3,385,746	3,496,746	3,425,191	3,256,285	3,276,190	3,603,678
Total Liabilities	3,333,466	3,438,076	3,545,476	3,467,491	3,293,585	3,310,490	3,635,642
Stockholders' Equity							
Common Stock	2,131	2,131	2,131	2,131	2,131	2,131	2,131
Additional Paid In Capital	1,312,560	1,312,560	1,312,560	1,312,560	1,312,560	1,312,560	1,312,560
Accumulated Deficit	825,225	517,185	226,661	169,648	11,175	(208,843)	(395,172)
Total stockholders' equity	2,139,916	1,831,876	1,541,352	1,484,338	1,325,866	1,105,848	919,519
Liabilities & Stockholders Equity	5,473,382	5,269,952	5,086,829	4,951,830	4,619,451	4,416,338	4,555,160

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FINANCIAL RATIO ANALYSIS

	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31	Dec 31
	2022	2021	2020	2019	2018	2017	2016

LIQUIDITY RATIOS

Current Ratio	19.2x	17.2x	15.6x	13.5x	9.4x	8.8x	13.7x
Quick Ratio	19.2x	17.2x	15.6x	13.5x	9.4x	8.8x	13.7x
Accounts Receivable Turnover	95.0x	94.8x	75.2x	72.1x	61.7x	60.5x	
Accounts Receivable Days	3.84	3.85	4.86	5.06	5.92	6.03	

SOLVENCY RATIOS

Total Debt / Total Capitalization (Cap Ratio)	58.2%	62.9%	67.6%	68.0%	69.3%	73.3%	78.4%
EBITDA/ Interest (Coverage Ratio)	6.0x	5.5x	2.6x	4.1x	3.9x	4.6x	4.4x
Total Debt / EBITDA (Leverage Ratio)	3.6x	4.0x	8.4x	5.5x	5.4x	4.6x	5.0x
Net Total Debt / EBITDA (Net Leverage Ratio)	2.3x	2.9x	6.5x	4.5x	4.8x	4.2x	4.3x

Liquidity: The Company's liquidity has been improving over the years even during the COVID-19 Pandemic, evidenced by increasing Current and Quick Ratio, higher Accounts Receivable Turnover and shorter Accounts Receivable Days, lower Accounts Payable Turnover and longer Accounts Payable Days, and increasing cash balance.

Total Leverage was over 8 times during 2020 as EBITDA decreased during the pandemic but was lowered significantly in 2021 and 2022. Total debt increased as the Company refinanced existing debt in late 2020 to take an average of lower interest rate resulting from the government's stimulative monetary policy to stimulate the economy.

EBITDA/Interest deteriorated in 2020 and continue to improve in 2021 and 2022.