WHITE PAPER

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CWT SOLUTIONS GROUP

Hotel Industry Consolidation: Marriott's latest mega-merger may be a game changer

Hotel consolidation is not new but consolidation activity has certainly increased over the last two years. Hotel groups continue to grow, with brands tucked under one umbrella and some brands transformed into another. Each of these stories spins a different tale about who, what and why the hotel industry is experiencing consolidation.

These deals did not substantially impact the industry until Marriott announced it would acquire Starwood. With the deal expected to be complete in 2016, the dust appears to have settled with Anbang Insurance Group's bid withdrawal. On the heels of this mega-merger comes the announcement that HNA Tourism Group will acquire Carlson Hotels.

It's clear Chinese conglomerates continue to look for growth opportunities in the hospitality industry, driving the expectation that industry consolidation activity will continue. Our aim here is to provide an understanding of the implications of this consolidation trend on corporate travel programs, along with recommendations about how to prepare programs for the new hotel industry landscape.

Hotel Mergers: Deal Details

The Marriott/Starwood merger has global implications, while most consolidation is focused on specific growth opportunities. Yet depending these deals can impact travel buyers:

- **April 2014, Marriott** strengthened its African portfolio **by acquiring Protea's 116 hotels**, with 10,148 rooms in seven African countries.
- **January 2015, Intercontinental (IHG) acquired Kimpton's 62 hotels**, making IHG the leader in the boutique hotel space.
- **April 2015, Marriott completed deal for Delta's 37 hotels**, making Marriott the largest full-service hotel company in Canada.
- **December, 2015, Accor acquired Fairmont's 115 hotels. This will** triple Accor's assets in the U.S., the world's biggest travel market, and speed up its expansion in China.
- **April 2016, HNA Tourism Group acquires Carlson Hotels 1,400 hotels**, establishing HNA's presence in the US and expanding its footprint outside, increasing HNA's hotel portfolio from 500 to 1,900.

CWT Solutions Group

Carlson Wagonlit Travel

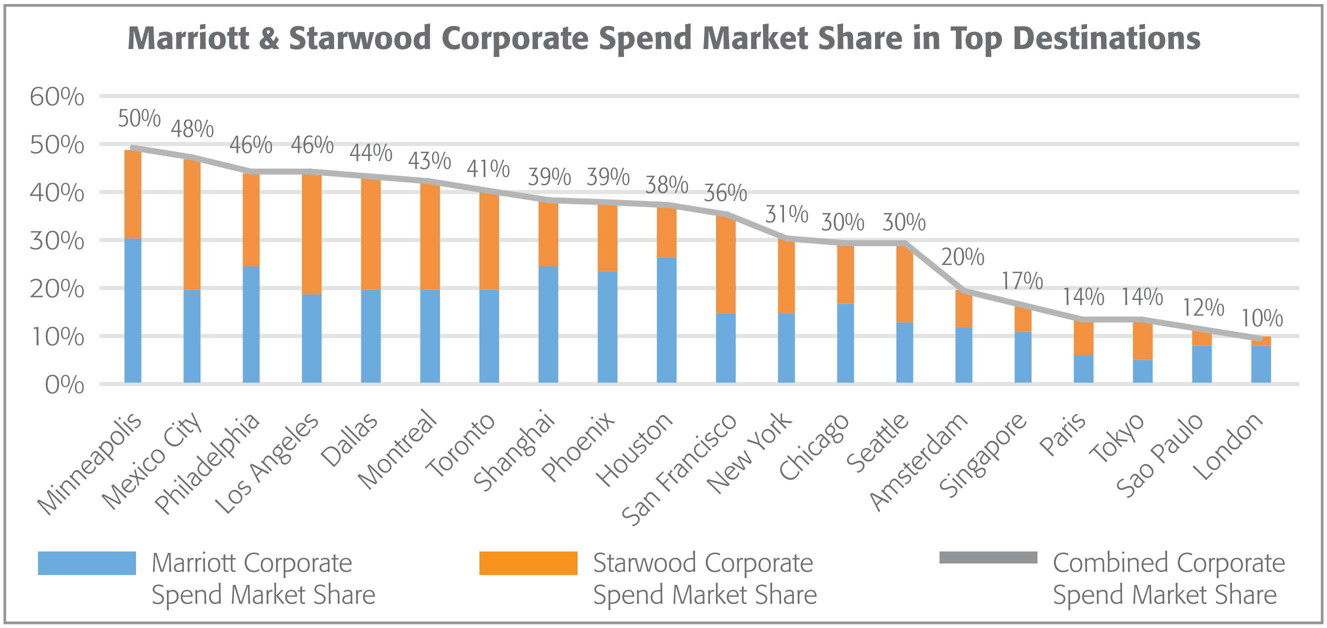
As corporate travel buyers look ahead to fall's RFP season, they should question now what this merger activity means for their hotel program and perhaps consider a different approach. According to the *CWT Solutions Group* hotel team, it is still too early to know the true impact for an individual corporate program, depending on how much they use hotels involved in the recent acquisition activity and in the key markets involved, and the level of willingness to change policies to protect the bottom line. However, there are some educated estimates about the impact of these acquisitions, focusing on: 1) future hotel program negotiations; 2) traveler compliance to hotel programs; and 3) the impact of this acquisition activity on the hotel industry more broadly.

Future Hotel Program Negotiations

Because of the timing, the Marriot/Starwood deal didn't impact 2016 hotel program negotiations. The merger is expected to be finalized by summer 2016, so it also shouldn't have a major impact on 2017 negotiations. However; 2018 will be a very different story and now is the time to start preparing.

With daily room rates and occupancy levels at all-time highs in many major markets, basic economics dictate that less competition will only lead to even higher prices and more challenging negotiations, especially in markets with limited options for corporate travelers. Using CWT aggregate client data, *CWT Solutions Group* hotel team analyzed several top city hotel markets across the globe to determine likely room night market share impact based on the Marriott/Starwood deal. The implications are significant. In 14 of the world's top 20 cities, the new hotel group will have nearly a third of the corporate travel hotel spend, rising to half in some places. See chart below.

Corporate Spend Market Share Impacts Will Be Most Significant in North America



Source: 2015 Full Year Hotel Solutions Client Spend

We don't yet know exactly how the Marriott/Starwood combined entity will approach the corporate travel market. Previous actions, though, give us a clue. Traditionally Marriott has been vocal in reducing discounted corporate pricing in favor of best available rates, while Starwood was used as a competitive alternative, whether it be to simply leverage the competition in negotiations or to actually shift share.

Hotel Chain	% Declined to Bid
MARRIOTT	18%
HILTON	9%
ACCOR	8%
HYATT	7%
STARWOOD HOTELS	5%
INTERCONTINENTAL HOTELS	3%

Source: 2016 CWT Hotel Solutions Data

CWT overall client data indicates Marriott has, more than other chains, chosen not to take part in corporate program RFPs. If this strategy continues, buyers should prepare for an even more challenging environment, particularly in top Marriot markets. Starwood, on the other hand, has been much more likely to take part in bids. We'll have to wait and see the new entity's strategy.

The merger will also reduce the number of hotels involved in the RFP process, which should streamline negotiations. We expect competition to be fierce from other major chains as they look to retain relationships with corporate buyers. And the ability to negotiate in non-preferred markets may actually increase for some clients, with combined Marriott/Starwood volume enabling chain-wide deals once unavailable.

The new entity won't significantly change the class of hotel mix. However, Starwood will fill some gaps in Marriott's portfolio, specifically with its strong international presence, particularly in Asia and Latin/South America, along with Starwood's strong lifestyle brand track record.

Traveler Compliance to Preferred Hotel Program

Another potential area of impact is traveler compliance with the corporate travel program. This is important because one of the best tools corporate travel buyers have in negotiations is the ability to shift traveler spend. If a buyer's combined spend post-merger is

Top 3 Benefits to Corporate Buyers

- Streamline the hotel RFP process
- More aggressive pricing from chains looking to retain share
- Improved Global Coverage from the new entity

Top 3 Threats to Corporate Buyers

- Fewer Competing Properties in Key Markets
- Increases in declines to Bid
- Risk of Increased Traveler Non-Compliance

Estimated Number of Properties by Region

Country/Region	Marriott	Starwood	Marriott & Starwood	Intercontinental	Hilton	Accor	Hyatt
US	3,511	550	4,061	3,303	3,742	9	440
Europe	325	174	499	660	317	3,023	34
Asia	189	295	484	405	128	518	88
Middle East/Africa	152	87	239	107	79	164	22
Canada	132	72	204	172	112	8	6
South/Latin America	83	97	180	216	89	282	34
Caribbean	26	5	31	13	21	3	8
Australia	6	17	23	27	14	207	6
Global	**4,424**	**1,297**	**5,721**	**4,903**	**4,502**	**4,214**	**638**

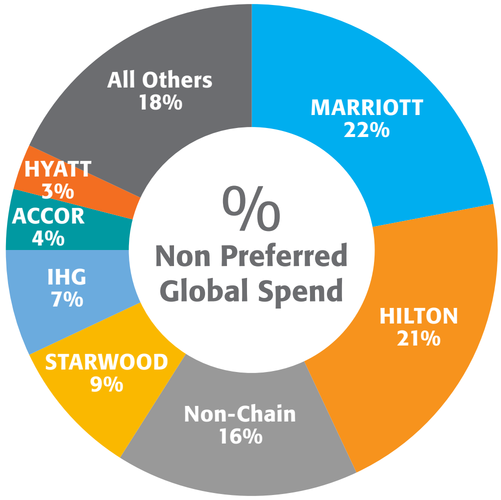
Source: 2015 company annual reports, company fact sheets, company website information, and in certain cases regional numbers are estimated based on room nights or regional revenue where breakouts not available in annual reports.

significantly different, their leverage will also change and buyers should be aggressive from the start.

A key caveat is that this strategy is most effective in mandated programs. As more and more programs have moved to a less mandated approach in recent years, companies may have less influence with travelers and therefore less leverage in their programs.

Mandated or not, buyer beware, however, as CWT Hotel Solutions analysis of client spend also indicates that more than 22% of non-compliant hotel spend occurs at Marriott properties, which are perceived to provide the best rewards. Starwood's loyalty program is also well regarded, and is makes up 9% of non-compliant spend. That means nearly a third of all non-compliant spend is with the new Marriott. This is likely to have a negative impact on buyers' leverage, leading to an important question: do you have company support to enforce your corporate travel policy?

When answering that, it's important to understand why travelers are non-compliant. Do they understand policy? Do they simply disagree? According to a 2015 GBTA survey of corporate travel managers[1], hotel chain loyalty programs is one of the underlying reasons for non-compliant hotel spend. In terms of value, the majority of travelers view reward nights



2015 Full Year Hotel Solutions Client Spend

as the most important loyalty program attribute. Based on an IdeaWorks July 2015 survey[2], the highest reward payback for every dollar spent was the Marriott Rewards Program. While Starwood's reward night value was behind many of the other top chains in the study, Starwood loyalty customers place a premium value on the perks including late checkout, room upgrades and welcome gifts. It isn't possible to predict what the new Marriott loyalty program will entail, but combining two of the most coveted loyalty programs is likely to pose a significant challenge for travel managers.

Marriott Rewards is estimated to have 54 million members while Starwood Preferred Guest has 21 million. While Marriott executives are optimistic loyal travelers will use properties from either brand, they have yet to discuss how they intend to merge the loyalty programs. Perhaps a clue lies in Marriott's CEO, Arne Sorenson, saying the Starwood loyalty program was one of the most attractive reasons for the acquisition.

Another clue could come from the airline mergers of the last decade, which led to significant erosion of loyalty program value for both traveler status and mileage. But hotels are different. There is a relative abundance of choice within the majority of cities, and since hotels are often owned by entities other than the hotel chain, this fragmentation can increase competition not only across chains but even within a chain or brand in the same city. CWT Solutions Group therefore does not foresee the same impact seen in the airline industry. If a hotel loyalty program does not benefit corporations and their travelers, strong competition remains to take share from any new hotel entity and threaten anticipated benefits to the bottom line.

Tips to improve compliance

- Involve Travelers through surveys and internal social media
- Track Compliance Metrics
- Ensure Executive Support and Share Accountability
- Communicate with Travelers not only policy but the reasons behind the policy
- Evolve and Benchmark your policy

[1] Making Hotel Loyalty Programs Work For You and Your Travel Program. [2] IdeaWorks Company; October 2015.

Hotel Industry Outlook

The simple truth in the hotel industry is that size does matter. Volume drives the discussion, whether it's a company using its spend to negotiate or a hotel chain strengthening its own negotiating position.

CWT Solutions Group anticipates there will be an ongoing need for hotels to compete not only with each other, but with emerging industry threats such as OTA consolidation, which reduces hoteliers' ability to set rates, and the onslaught of sharing economy suppliers. Our expectation is that chains will continue to use loyalty programs and preferred traveler rates to drive transactions out of OTAs. On the positive side, large travel management companies (TMCs) will have access to the loyalty rates, to enable tracking and provide at par pricing should these rates drop below the negotiated corporate rates. Similarly, TMCs will look for opportunities to test incremental loyalty programs to improve compliance.

With Marriott's recent acquisition, its global reach has grown significantly and it could trigger more mergers as competitors look to avoid losing market share. Similarly, IHG's acquisition of Kimpton, along with the expansion of lifestyle brands across the industry, points to an increased focus on combatting sharing economy providers. By incorporating common areas, integrating technology, and offering a la carte services, particularly targeting younger travelers, hotel chains are offering a differentiated level of service and thereby driving loyalty in a key shared economy segment.

And while mergers and acquisitions have been making the headlines, other factors are also still very much in play as 2016 budgets are underway and buyers are thinking about the 2017 RFP season.

Hotel prices will be up globally in 2016, with CWT's annual forecast indicating increases as follows: global, 2.5%; Western Europe, 0.7%; Middle East and Africa, 1%; Asia Pacific, 3%; Latin America and the Caribbean, 3.7%; and North America at 4.3%. A key concern for buyers should be whether some of the newly combined hotel entities will push the price increases even further in certain markets.

Hotels will continue to maximize ancillary fees. They have also begun to enforce more stringent cancellation policies and will continue to pursue dynamic pricing agreements as yield management strategies evolve across the industry.

Our expectation is that the hotel acquisition trend will continue as the industry continues to seek opportunities to leverage scale and adjust to changing demographics and market trends.

Prepare early for 2017 negotiations

The integration and alignment of two hotel chains typically requires 12-18 months, which is why the impact will hit in the 2018 negotiating season. However, *CWT Solutions Group* anticipates the new Marriott targeting specific markets as soon as possible, so in some cases the change will take affect sooner. It will also depend on coordination with franchise owners who were once competitors and are now part of the team. Buyers should therefore take some key steps now:

1 Assess key markets: look at share by top chain within key cities or areas within a city, assess alternative hotels and potential savings

- Consider adding new options, particularly where a program previously relied heavily on one brand pre-merger.
- Communicate frequently with your chain account managers throughout the integration and RFP process to understand any nuances of the combined entity.
- Be aware, however, that there is the potential that, in looking for synergies across both companies, the workforce could be cut dramatically and impact your ability to get information.

2 Prepare to have a more flexible approach for 2017 to incorporate alternative suppliers as required

- All buyers should cast a wider net; other hotel suppliers know this is their opportunity to attract new corporate business and buyers may be pleasantly surprised.
- Start negotiations early, by August at the latest, to ensure ample time to respond to unfavorable responses from hoteliers.
- Programs that have been complacent with generally happy travelers are not exempt and may need to engage proactively at an even deeper level to understand future options.

3 Adapt your policy to ensure compliance

- Compliance matters now, more than ever.
- If cost saving is the priority, be direct about it. And consider mandating the program, at least short-term. In doing so, consider more forceful language or consequences for out of policy behavior. With the new Marriott creating more options and majority third of current non-preferred spend going to Marriott, the potential for increased non-compliance and lost spend could easily increase.
- Be prepared for economic ebbs and flows. When economic times are good, policies are relaxed to ensure employee retention and satisfaction while when times are tough, it is prudent for corporate travel programs to clamp down. It is important to stay ahead of these cycles and react quickly to economic changes.

4 Communicate to travelers, engage them in corporate objectives, and create shared ownership in the results

- Make sure employees are both aware of and understand their policy. Most travelers are willing to do the right thing, particularly if the rules are easy to access and understand. It's also important to have good rationale behind policy decisions. Ensuring travelers understand reasons for the policy can make all the difference.
- Engage the internal communications team to emphasize the importance of policy compliance. Develop campaigns to unite travelers for the company's shared goals, including traveler satisfaction, cost effective travel, maximum value, and more.
- Use the traveler feedback channel on a routine basis to ensure travelers' concerns are factored into broader program decisions over time.

While the Marriott/Starwood merger impact may not be known for some time, *CWT Solutions Group* hotel experts suggests buyers should be proactive now, in preparation for the 2017 hotel season, engaging at a deeper level to understand the nuances of their program and ensure they are able to make best-informed decisions for 2017.

Focus now to see the future of hotel programs most clearly

Many questions remain unanswered about how the Marriott/Starwood merger will change both entities. The impact on corporate travel programs and their business travelers is likely to become clearer after the deal closes and implementation begins, around the middle of 2016.

In the meantime, industry experts speculate that coverage and options within the new chain will expand. And, as the size of the deal is sure to change the supplier landscape overall, negotiations may become more challenging in some cases, while new opportunities may be created for others.

Buyers would be wise to simply expect the unexpected, review their program in-depth now to ensure they know their options before 2017 negotiations begin and ensure they, and their travelers, can readily adapt as necessary to ensure maximum value, cost efficiency and traveler satisfaction in 2017 and well beyond.

To learn more about how to manage the changes for 2017 hotel programs, contact your CWT program manager or visit www.cwt-solutions-group.com.