Extended Stay America, Inc. (STAY)
1Q20 Results in Line; Credit Facility Amended, Quarterly Dividend Cut

- No change in our Neutral rating; better-than-peer fundamental performance largely expected; quarterly dividend cut to $0.01/share. Extended Stay’s 1Q20 results were in line with our expectations and likely matched recently heightened Street expectations, in our opinion (link to our earnings preview note). RevPAR growth was over 400 bps better than we were modeling, but nearly 200 bps of greater margin contraction was the offset. Extended Stay’s 1Q20 operating results (and 2Q20 results as well, in our view) should be the best among the hotel companies in our coverage universe. Capex and development spending is being reduced further, and the RevPAR declines appear to have bottomed in early/mid-April, both of which are positives. A 1Q20 earnings summary is as follows:
  - RevPAR: -5.8% vs. Baird at -10%; withdrawn guidance called for flat to +2% growth;
  - Paired share income: $0.07 vs. Baird/Street both at $0.06; and
  - Adj. EBITDA (mil): $97.7 vs. $109-$119 guidance, Baird/Street at $97.0/$95.6.

- Credit facility amendment obtained; quarterly dividend reduced to $0.01/share. The company executed an amendment to its C-corporation credit facility that suspends the leverage covenant test beginning in 2Q20 through the end of 1Q21; the covenant test uses annualized EBITDA for the remainder of 2021. Borrowing costs are unchanged, but the amendment limits share repurchases and dividend payments; a $0.01/share dividend has been declared for 1Q20 (payable in June).

- Balance sheet update: Extended Stay had $725 million of cash on hand at quarter-end and the full $400 million drawn under its two credit facilities. We calculate leverage of 4.5x, which is up from 4.3x at YE2019. Buybacks have been halted since early February, and the reduced quarterly dividend saves $39 million per quarter.

- Fundamentals appear to have bottomed in early/mid-April. March RevPAR growth declined approximately 19%, while April was down approximately 35%. Weekly trends show RevPAR growth bottoming at -40% in early/mid April, but performance has since trended higher to -30% to -25% RevPAR in early May. We model 2Q20 and 2020 RevPAR growth of -25% and -18%, respectively; importantly, all of Extended Stay’s hotels remain open and operational. Overall, the portfolio is acting more apartment-like in the current environment, and management’s continued operational shift focusing on growing the 30+ night stay guests should further reduce top- and bottom-line volatility in the near term, in our opinion.

Valuation Synopsis
Our $12 price target is based on our EV/EBITDA multiple analysis, which applies 9.0x to our NTM+24 EBITDA estimate and is approximately in line with our pre-crisis applied valuation multiples. The stock currently trades at 10.5x NTM EBITDA, which we believe reflects expected near-term fundamental outperformance.

Risk Synopsis
Risks include competition from the major global brand companies, uncertainties regarding development projects and third-party franchisee growth, and the shape/timing of the post-crisis demand recovery.

Extended Stay is the largest owner-operator of extended-stay hotels in the United States with a primary focus on the mid-priced segment.

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Please refer to Appendix - Important Disclosures and Analyst Certification
1 Robert W. Baird & Co. Incorporated makes a market in the securities of STAY.

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