



## Final Transcript

**RED LION: 1<sup>st</sup> Quarter 2012 Earnings Call**  
May 2, 2012/2:00 p.m. PDT

### **SPEAKERS**

Pam Scott  
Jon Eliassen  
Julie Shiflett

### **ANALYSTS**

Jonathan Pong, Robert W. Baird

### **PRESENTATION**

Moderator                    Welcome to today's First Quarter 2012 Earnings conference call. At this time, all participants are in a listen-only mode. Later, we will conduct a question and answer session. [*Instructions given.*] As a reminder, today's conference is being recorded. With that, I'd like to turn the conference over to our host today, Ms. Pam Scott. Please go ahead.

P. Scott                        Thank you. Hello. Welcome to Red Lion Hotels Corporation's First Quarter 2012 Earnings conference call. With us today are Red Lion Hotels President and Chief Executive Officer, John Eliassen, and Chief Financial Officer, Julie Shiflett. Chief Operating Officer George Schweitzer will also be joining us during the Q&A session to answer questions.

Before we get started, I want to remind you that our remarks today contain forward-looking information as defined by the SEC that is subject to a number of risk factors that may cause our actual results to differ materially from those expressed or implied. These risk factors are discussed in detail

in our annual report filed with the SEC on Form 10-K on March 15, 2012. Those reports are available at our Website, [www.redlion.com](http://www.redlion.com) or through the SEC Website at [www.sec.gov](http://www.sec.gov).

We will also be referring to a number of non-GAAP measures. The reconciliation of these measures to their comparable GAAP measures is provided in the table to the press release issued this afternoon. That release is also available in the investor relations section of our Website.

I would like now to turn the call over to Mr. Eliassen.

J. Eliassen

Thank you, Pam. Thank you for joining us today for the First Quarter 2012 Earnings call.

The first quarter has been a very busy time for all of us at Red Lion. For those of you who follow our progress closely, you know that we remain focused on our key operating strategies. During our first quarter we generated RevPAR growth which outpaced midscale hotel segment, resulting in increased total revenue and EBITDA. We continue to implement targeted sales and marketing programs that have allowed us to improve occupancy in what is typically our slowest period without an overall reduction in ADR. We have continued with our asset sale and debt reduction initiatives and are seeing increased interest in our properties held for sale.

We plan to use proceeds from any asset sales to continue to reduce debt and reinvest in our hotels. We remain focused on improving profitability and are confident that the execution of our three-pronged strategy to reduce debt, expand our franchise program, and improve the competitive position of our hotels will enhance value for all of our stakeholders.

That said, we are committed to pursuing all options that will maximize shareholder value. To that end, near the close of the first quarter we announced that our board of directors had authorized Bank of America Merrill Lynch to explore strategic alternatives for the company. Concurrent with executing on our internal strategy, we remain open-minded about all options and intend to evaluate them thoughtfully and carefully. As you can appreciate, this process is ongoing, so we will not be commenting further at this time.

With that, I will now discuss some of our first quarter achievements. Before I turn the call over to Julie for a review of our financial results I

will provide a brief overview of our operational progress during the quarter, a summary of our performance relative to our competition as well as some additional detail on our 2012 outlook, and an update on our asset sale and debt reduction strategy. Julie will then provide more color on our financial results and a review of our balance sheet. After that, we'll open up the call for Q&A.

For the purposes of our discussion today we will be referencing our first quarter results from continuing operations on a comparable basis for all periods presented. This means the numbers we will discuss exclude the performance of the Seattle Red Lion Hotel on 5<sup>th</sup> Avenue which we sold last year. This Seattle property still continues to be operated as a very successful Red Lion franchise.

As I mentioned, we achieved first quarter RevPAR growth for our owned and leased hotels that outperformed the U.S. mid-scale segment. Our RevPAR increased 7.3% year-over-year, primarily driven by a 360 basis point increase in occupancy. Comparatively, RevPAR for the U.S. mid-scale segment increased 5.6%.

During the quarter we implemented a number of targeted marketing and sales initiatives all focused on driving occupancy, and we believe our first quarter results illustrate the success of these initiatives. In what is typically a seasonally slow period of the year we were not only able to drive occupancy growth but we did this while maintaining our average daily rate. We focused primarily on the transient segment and also employed targeted property-specific promotions that provided solid results in targeted markets. For example, this was particularly true in Anaheim.

In addition, we continue to use online travel agency channels to maximize occupancy when appropriate. Red Lion runs system-wide and region-specific seasonal promotions to gain market share in soft demand periods. These promotions are advertised via in-flight airline magazines and through targeted online search promotions, social media, and other traditional media as needed. We expect our marketing strategy, including a planned series of promotions for the balance of the year, to continue to attract our core customer groups while increasing overall brand awareness.

Through our targeted marketing initiatives we have been very successful in growing our transient business over the past year. This reinforces our commitment and focus on this segment through the partnership with TravelClick that we had discussed in our last call. These new property-

specific Websites will be better defining our brand, creating more direct interaction with guests, and drive revenues at a substantially lower cost. The development work with TravelClick is proceeding as planned with pilots scheduled for this summer and a formal launch before the end of the year.

Each Red Lion hotel, both for our company-owned and operated as well as for our franchised hotels, will have its own uniquely focused Web identity with travel information tailored specifically to its region. In addition to listing the attributes of each hotel, the individual Websites will feature nearby attractions and highlight specific information about the particular area. All of the information is designed to convey to our guests the local personality of the hotel and the region in which it's located. We expect this will generate an increase in reservations through our own system, which should translate into improved profitability and margins for all Red Lion hotels, including our franchise locations.

Looking ahead, and based upon industry forecast for the mid-scale hotel segment, we expect RevPAR growth to begin to moderate over the next here quarters. With this industry mid-scale hotel outlook in mind, we are reaffirming our 2012 RevPAR growth of 2% to 4% for the full year. This outlook balances our strong first quarter performance with the continued slow booking pace that we see in many of the markets we serve.

As part of our overall strategy to expand our franchise program and improve our competitive position, we are continuing to focus on lodging development. We are in the process of implementing positive changes in the structure of our franchising team and we are now actively recruiting a replacement for our departing head of lodging development who has accepted a new position effective May 10<sup>th</sup>. We remain in active discussions with a number of owners to potentially franchise hotels in our 11 western state region. To date, our ability to demonstrate the value of the new sales and marketing initiatives has already increased the awareness and the appeal of Red Lion's brand to potential and existing franchisees and we continue to build a strong platform for future franchise growth.

Looking at profitability, comparable EBITDA from continuing operations before special items improved by \$1.7 million year-over-year. The acquisition of the previously leased iStar hotel reduced facility leased expenses by \$900,000 in the quarter. Strong RevPAR results coupled with

seasonal cost containment initiatives and a more targeted mix of promotional initiatives also drove improved profitability.

In addition, we continue with our asset sale and debt reduction initiatives. We have seen increased interest in our properties held for sale, including our hotels in the Denver southeast area; in Medford, Oregon; and in Missoula and Helena, Montana. The sale of these assets will enable us to further reduce debt, expand our franchise program, and continue to reinvest in our hotels to position the Red Lion brand for long-term growth.

J. Shiflett

With this brief update I will now turn the call over to Julie.

Thanks, Jon. Before I begin, I would like to once again state that any discussion of hotel operating results will be based on comparable hotels from continuing operations which exclude the hotel operations from the Seattle 5<sup>th</sup> Avenue property that we sold in June 2011.

Hotel segment revenue of \$28.3 million increased 6.2% year-over-year during the first quarter. Rooms revenue increased 8.5% and food and beverage revenue was 1.8%. Hotel segment expenses for the first quarter increased 3.8%, primarily driven by higher occupancy. To help offset the cost associated with the increased occupancy, we are continually working on a number of margin improvement initiatives, including short- and long-term labor management, energy efficiency, food and beverage pricing, and continued review and adjustment of supply and purchasing contracts.

These initiatives, coupled with a streamlined marketing program that focused our promotional activities on the transient segment and property-specific campaigns, drove a 200 basis point improvement in hotel direct operating margin to 11.1%. While many of these initiatives are designed to improve our long-term profitability, some of these savings may not extend beyond the first quarter as we move into our normally busy summer travel season.

Turning to our other segments, franchise revenue in the first quarter increased 54% to \$1.1 million driven primarily by the addition of our new franchises in Seattle, California, and New Mexico. We also saw an increase in fees associated with higher gross rooms revenue at our existing franchise hotels. Profitability in the franchise segment improved by \$104,000 year-over-year, primarily due to these revenue increases.

Within the entertainment segment, profitability improved due to a favorable mix of shows produced in the first quarter of this year compared to last year. This improvement was despite a \$300,000 decline in revenue

as a result of lower sales volume in the ticketing business. We recently announced our 2012-2013 Best of Broadway Spokane series, which include a 2.5 week run of *Jersey Boys* and a nearly week-long run of the first national tour of *War Horse*.

For the consolidated company, first quarter EBITDA from continuing operations before special items increased \$1.7 million year-over-year to \$1.2 million compared to a loss of \$500,000 in the prior year first quarter. This improvement was primarily due to the reduction in lease payments to iStar, a change in mix of promotional initiatives, and seasonal and permanent cost containment measures. The improvement was partially offset by increased costs associated with higher occupancy.

During the quarter we recorded a pretax asset impairment charge in continuing operations of \$5.9 million related to our assets held for sale. This impairment reflects market value indications received during the marketing process of these properties. These impairment charges are excluded from our EBITDA from continuing operations before special items for the first quarter of 2012 and are identified separately in our operating results.

Turning to our liquidity, as of March 31<sup>st</sup> we had outstanding debt of \$100.2 million, of which \$30.8 million was classified as current as our credit facility matures in March 2013. We were in compliance with all stat covenants at March 31<sup>st</sup> and we have made significant progress over the last year in both reducing and improving the maturity profile of our outstanding debt.

Our strategy is to use the proceeds from our anticipated asset sales to continue to reduce our debt load. In addition, we're continuing to work with our lenders and advisors on alternative sources of funding to refinance our maturing debt.

First quarter capital expenditures totaled \$1.2 million, primarily related to the hotel improvement project. We continue to expect to make \$10 million in total capital improvements during 2012, primarily for our guest room upgrade program and other needs.

As we've stated before, we are always focused on maximizing shareholder value. To that end, we recently announced that the board has made the decision to explore strategic alternatives. These alternatives could include a potential sale of the company or strategic combination with a third party.

The board has formed a strategic alternatives committee comprised of independent directors that is working directly with Bank of America Merrill Lynch. It's important to note that the evaluation of financial and strategic alternatives will not necessarily result in any changes to the company's current business plan or any transaction or agreement.

While this process is ongoing, we continue to advance our three-pronged strategic plan to position the company for growth and value creation. This strategy does include the continued pursuit of transactions for our assets currently held for sale.

Before we turn to the Q&A, a reminder: we will not be providing comments or updates on the ongoing strategic alternatives analysis. We do appreciate your interest in Red Lion. With that, we're ready to take questions. Operator?

Moderator *[Instructions given.]* Thank you, speakers. Just one moment. We will go to the line of Jonathan Pong with Robert W. Baird. Go ahead, please.

J. Pong Hello, guys. Good afternoon. I just want to ask you quickly on the franchise progress in terms of getting to where you guys want to be in a couple years. Can you talk about how that progress is going and what markets are you guys getting a lot of interest from, if any?

J. Eliassen Thanks, Jonathan, for the question. We have continued to build a fairly good backlog of interested parties. It's actually improved quarter-over-quarter in terms of indications of interest, so we continue to work that pipeline. We've had a number of very positive contacts and discussions in the southwest, but we're still, again, staying in the 11 western states where Red Lion has always operated historically.

While Rich Carlson has been here over the last two years, he's done a really good job of building a strong team behind him and under him. They're really working in the field now, both with existing franchisees as well as with the development pipeline, so we're pretty pleased with that process and where we are in that as well.

The other thing that I mentioned in here, too, is we really have linked our sales, marketing, and our revenue management strategies a lot more tightly with our individual franchise locations. We continue to work to build strong partnerships in that way as well, which does set us apart. It really has, I think, helped attract more people into the pipeline to at least discuss

the opportunities with Red Lion. We're pleased with the progress. We still have the same goals of the 30+ hotels by the end of 2013 and beyond to be in the franchise group.

J. Pong                    Maybe an update on assets that you guys have for sale and how soon we could potentially expect to hear news on potential dispositions or movement on that front.

J. Eliassen                The conversations have been positive, as I mentioned. We've had more specific interest, at least in the four that we discussed. I would hope that within the next quarter we would hope to at least be able to make some announcements along those lines, but we are very pleased with the level of interest and the seriousness of the interest that we're seeing right now compared to perhaps six months ago.

J. Pong                    Great. That's helpful. Thanks.

Moderator                Thank you very much. At this point, speakers, we have no further questions in queue. Please continue.

J. Eliassen                Thank you all very much for joining us today. Thanks for your continued interest in Red Lion. As Jonathan mentioned, as we have things to announce we certainly will be making the appropriate public announcements, hopefully on asset sales in the next few months and those kinds of things.

Again, thank you all. We look forward to joining you and having you join us on our next quarterly conference call.

Moderator                Thank you very much. Ladies and gentlemen, this conference will be made available for replay starting today at 4:00 p.m. PST and running through June 2<sup>nd</sup> at midnight. You may access the AT&T Executive Playback Service at any time by dialing 800-475-6701 and entering the access code 245115. International participants will dial 320-365-3844.

That concludes your conference today. We appreciate your participation as well as your using AT&T Executive Teleconference. You may now disconnect.