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Choice Hotels International, Inc. Q3 2008 Earnings Call Transcript

Question-and-Answer Session

Operator

(Operator Instructions) Your first question comes from Steve Kent - Goldman Sachs.

Steve Kent - Goldman Sachs

I have forgotten if you give guidance or give some thoughts on 2009 at this point or whether you wait until the fourth quarter to do that.

Stephen P. Joyce

We fortunately wait until the end of the fourth quarter to give that guidance. Obviously that will give us a little better insight into where we've been tracking and in today's environment you have seen such a wide range of forecasts, I am actually glad we're not giving it until December.

Steve Kent - Goldman Sachs

Then maybe you could just talk a little bit about two points. One, on the royalty rate increases, what's behind some of that royalty rate increase? Is it mix or is it that you're able to get better rates from the people you are signing on?

And then on the pipeline, when we dug a little deeper, it looks like the economy hotels, like Econo Lodge and Roadway, are declining more than the more moderately priced hotels in your brand circle.

David L. White

On the royalty rate, I think what you have to look at there is over the last several years we have had a pretty good track record of gradually increasing that effective royalty rate. And there's a couple key reasons for that. The first one is that one of our sales strategies over the past four or five years has been to discount the effective royalty rate in the early years of these contracts. Obviously this is a contract business, fee-for-service business where we have very long-term contracts for virtually all of these brands. And that effective royalty rate is set at the time of the initial contract.

And so one of our sales techniques, in terms of customer acquisition, has been to discount the early years, so as those discounts burn off that is having an impact on the effective royalty rate.

And then you couple that with the relicensings, although they have been weaker this year than they have been the past two or three years, those relicensing events are also opportunities to essentially

reset the effective rates on these contracts and more aggressively eliminate those discounts. You have seen the burn off of discounts over time.

In terms of the pipeline, I think what you are seeing on the conversion brands and the economy conversion brands, is that frankly, those are predominantly conversion brands, Econo Lodge and Roadway. So when the contract enters the system it comes on line faster than a new-construction hotel does and couple that with the fact that for the third quarter here you saw the number of conversion contracts getting sold declining. It's really those two factors playing out in the pipeline.

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