Hilton Grand Vacations

First Quarter 2019 Earnings Conference Call

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CORPORATE PARTICIPANTS

Robert LaFleur, *Vice President of Investor Relations*

Mark Wang, *President and Chief Executive Officer*

Dan Mathewes, *Chief Financial Officer*

PRESENTATION

Operator

Good morning and welcome the Hilton Grand Vacations' First Quarter 2019 Earnings Conference Call. Today's call is being recorded and will be available for replay beginning at 2:00 p.m. Eastern today. The dial-in number is 888-203-1112 and enter PIN #6391101. At this time, all participants have been placed in a listen-only mode, and the floor will be opened for your questions following the presentation. If you would like to ask a question, please press star, 1 on your touchtone phone to enter the queue. If at any point your question has been answered, you may remove yourself from the queue by pressing star, 2. If you should require Operator assistance, please press star, 0. If using a speakerphone, please lift your handset to allow the signal to reach our equipment.

I would now like to turn the call over to Robert LaFleur, Vice President of Investor Relations. Please go ahead, sir.

Robert LaFleur

Thank you, Leann, and welcome to the Hilton Grand Vacations' First Quarter 2019 Earnings Call. Before we get started, we'd like to remind you that our discussions this morning will include forward-looking statements. Actual results could differ materially from those indicated by these forward-looking statements, and the forward-looking statements made today are effective only as of today. We undertake no obligation to publicly update or revise these statements. For a discussion of some of the factors that could cause actual results to differ, please see the Risk Factors section of our previously filed 10-K or our 10-Q, which we expect to file later today.

We will also refer to certain non-GAAP financial measures in our call this morning. You can find definitions and components of such non-GAAP numbers as well as reconciliations of non-GAAP and GAAP financial measures discussed today in our earnings press release and on our website, investors.hgv.com.

As a reminder, our reported results for both periods in 2019 and 2018 reflect accounting rules under ASC 606 that we adopted last year. Under ASC 606, we are required to defer certain revenues and expenses related to sales made in a period when a product is under construction and then hold off on recognizing those revenues and expenses until the period when construction

is completed. To help you make more meaningful period-to-period comparisons, you can find details of our current and historical deferrals and recognitions in Table T-1 in our earnings release.

Also for ease of comparability and to simplify our discussion today, our comments on adjusted EBITDA and our real estate results will refer to results excluding the net impact of construction-related deferrals and our recognitions for all reporting periods.

Finally, unless otherwise noted, results discussed today refer to first quarter 2019 and all comparisons are against first quarter 2018.

In a moment, Mark Wang, our President and Chief Executive Officer, will provide highlights from the quarter in addition to an update of our current operations and company strategy. After Mark's comments, our Chief Financial Officer, Dan Mathewes, will go through the financial details for the quarter and our expectations for the balance of the year. After that, we will be available for questions.

With that, let me turn the call over to Mark.

Mark Wang

All right. Well, thank you, Bob, and good morning, everyone, and thank you for joining us today. In Q1, Hilton Grand Vacations continued to lay the groundwork for strong future growth and significant value creation. This is most evident in the following ways.

First, we demonstrated the consistency of our business model with solid EBITDA of $102 million, driven by contractual recurring revenues in our resort, club, and financing business lines. We embedded meaningful value into enterprise, with net owner growth of 6.7 percent, which is at the high end of our long-term range. And we're well on our way toward delivering positive NOG for the 27th consecutive year, and our owners remain highly engaged and satisfied.

We originated new loans with a weighted average FICO score of 751, above our current portfolio average of 738, and we continued to leverage our long-term relationship with Hilton to drive healthy tour-flow growth of 6.4 percent.

And, finally, we executed on our dynamic capital allocation framework, completing $200 million of share repurchases under the program we launched in December and yesterday we announced an additional $200 million of repurchase capacity. These actions demonstrate our focus on the overall return to our shareholders.

Looking forward, we remain very confident in our long-term strategy. When we went public, we gained access to capital to accelerate growth while maintaining strong returns. Our experience in Q1 reinforces our conviction in our strategy to invest in inventory that supports the scale and growth we laid out at Investor Day. While we began the investment cycle toward the end of ’17 and into ’18, it’s critical to understand that the vast majority of the new inventory we’ve identified is not yet available for sale — only two properties were the results of investments we’ve made after the spend, and these two projects represent less than 10 percent of the $3 billion in contract sales we’ve logged during this timeframe. And that’s why we’re so excited about what’s coming online, as these properties will improve flexibility at the sales table, ignite demand across the entire base, and allow us to build momentum throughout ’19 and ’20.

In New York, we just started sales at The Central at Fifth, which is the new branding for our just-in-time project on 48th Street. Initial response has been very positive. Additionally, we’ll start sales of The Quin, which remains on track to begin in Q4. We’re very optimistic about what these properties will do going forward.

On top of that, we started sales of our downtown Chicago property through our direct sales teams, and this effort will be complemented later this summer when we open our Chicago Sales Center. And, finally, we’ll start offsite sales of our Liberty Place Charleston property later this year, with onsite sales opening next year.

Looking ahead to 2020, we expect to start selling Cabo, the next phase of Ocean Tower, and our new properties in Maui and Waikiki.

Another source of confidence is that we’re exhibiting strong performance in our recurring businesses, which are doing exactly what they’re supposed to do, namely generating consistent earnings fueled by industry-leading NOG over many years. Together, the adjusted EBITDA contributed by resort, club, rental, and financing grew by 8 percent this quarter. Historically, these business lines represent almost 60 percent of our total EBITDA.

Now, as you saw in our earnings release, we're making some updates to our '19 guidance to reflect first quarter contract sales down 2 percent, as well as timing related to our Cabo project. However, none of the changes to our guidance impacts our long-term growth outlook, strategy, or overall operations. We're adjusting '19 guidance as follows. We're moving contract sales growth to a range of 5 percent to 8 percent; adjusted EBITDA moves down $5 million, with a new range of $445 million to $465 million; and diluted earnings per share moves to a range of $2.61 to $2.77, and we're reiterating our cash flow guidance.

Now, I'd like to provide a bit more detail on the dynamics reflected in our updated guidance. Our continued net owner growth creates a strong need for inventory, but it's not as simple as looking at the total volume of inventory available. It's about the mix and the range of the inventory available across all unit types and geographies. This is part of the reason you heard us consistently beating the drum last year about the need to bring additional inventory online. Q1 of '18 is a great example of what happens when you have that optimal mix of unit types which appeal to the broadest spectrum of customers. This includes owners wanting to upgrade and potential new owners looking at an entry point.

Phase I of Ocean Tower fits that description and helped drive contract sales growth of 14.6 percent in Q1 of '18. During that same period, owner-close rates and VPGs were amongst the highest in my 20 years at HGV. Heading into '19, we knew our inventory mix differed from the beginning of '18, so we expected a lower growth rate in Q1 compared to the rest of the year. Our forecast was tracking through the first two months of the quarter; however, sales in March, which are typically stronger than January and February, were lighter than expected, especially in markets impacted by less available upgrade inventory. However, as more inventory comes online throughout 2019, we expect to see improved traction, and year-over-year comps will become less challenging.

Another driver of the new guidance relates to our Cabo project, which we planned to open in Q4 of '19 but will now shift into '20 due to timing changes related to regulatory approval processes. This is a relatively short delay that crosses calendar years. We still expect Cabo to be in high demand once available, so the shift does not impact the project's expected rate of return.

Before I turn the call over to Dan, I want to reiterate that HGV remains positioned for long-term

growth, adhering to the strategy we outlined at Investor Day. We're executing on that strategy and investing in the business to bring an optimal mix of inventory to the market. At the end of this investment cycle, we will have embedded significantly more value into the enterprise and permanently reset the business to a higher level of earnings of free cash flow production. And when we succeed in that, we will succeed in creating meaningful value for our team members, owners, and shareholders for many years to come.

I'll now turn things over to Dan to walk you through our financial results. Dan —

Dan Mathewes

Thank you, Mark, and good morning, everyone. Before getting into the numbers, just a quick reminder that last year's first quarter results reflect $37 million of net construction-related deferrals, $66 million in revenues, and $29 million in expenses and that, this year's first quarter results reflect no deferrals or recognition. You can see the details on Table T-1 in the earnings release.

Deferrals affect three line items in the real estate section of our P&L — sales of VOIs net, cost of VOIs sales, and sales and marketing expenses. Financing, resort, club, and rental are not affected by deferrals. Because deferrals create meaningful distortions to year-over-year comparisons, my comments today on net income, adjusted EBITDA, and real estate results will exclude the net impact of construction-related deferrals. This is the way we look at the business, and we believe it provides better perspective on period-over-period trends.

Taking this into consideration, the base for our comparisons to 2018 are as follows. Q1 2018 reported revenues were $367 million. Adding back the deferrals of $66 million results in a base for comparison of $433 million. On adjusted EBITDA, adding back the net deferrals of $37 million to reported adjusted EBITDA of $62 million results in $99 million. As previously mentioned, the net deferrals only impact our real estate results.

Now, let's get into the numbers. Total first quarter revenue increased 3.9 percent to $450 million, reflecting growth in the resort, club, rental, and finance areas, offset by a modest decline in real estate. The real estate and finance segment revenues were flat at $307 million, and segment-adjusted EBITDA decreased 1 percent to $80 million and segment margin declined 30 basis points to 26.1 percent.

Our recurring management and club fees helped drive a 12 percent increase in the resort and club segment revenues this quarter. Segment-adjusted EBITDA increased 10 percent to $65 million, and segment margin increased slightly to 59.1 percent. The strong performance in the resort and club segment offset a modest decline in the real estate and finance segment, resulting in adjusted EBITDA of $102 million, or an increase of 3 percent on revenue growth of 3.9 percent.

Net income was $55 million, and diluted earnings per share was 58 cents.

Now, let's go through the rest of the details on the quarter. First quarter real estate results reflect the challenging comparison against the Phase 1 launch of Ocean Tower last year. Given the extraordinary level of early demand for Ocean Tower, contract sales increased by 14.6 percent in Q1 last year. Despite solid customer traffic this year, limited inventory availability in key markets hurt our ability to maintain the record close rates we achieved last year. As a result, VPGs were down, and Q1 contract sales declined by 2.1 percent.

We saw strong performance from fee-for-service projects like Grand Island in Hawaii, Elara in Las Vegas, and our Myrtle Beach properties, resulting in fee-for-service contract sales increasing by 12 percent. This brought our fee-for-service mix to 59 percent for the quarter, up from 51 percent last year and above our 48-to-54 percent guidance range.

Typically, Q1 is our highest quarter for fee-for-service sales, so we expect the mix to tilt back toward owned as the year unfolds. It is also worth noting that last year was unusually low as Ocean Tower captured some of the demand that otherwise would have gone to fee projects.

In our real estate business line, Q1 revenues declined 2 and a half percent to $236 million. The mix of our sales helped drive commission revenues and mitigate the decrease in owned contract sales. We have some degree of variability in our real estate expense structure, which also helped mitigate lower contract sales.

Sales and marketing expense declined 2.2 percent, essentially keeping pace with contract sales. Product costs increased slightly as a percentage of owned sales. However, given the mix between owned and fee revenue, real estate expenses declined more than revenues, producing

$1 million of incremental real estate margin and modest expansion in our real estate margin percentage.

Turning to the finance business, Q1 margin increased $1 million to $28 million as the benefits of a larger receivables portfolio, higher average interest rates, and increased servicing revenue offset the incremental interest expense from our 2018 ABS deal. The higher interest expense did contribute to the 280 basis points of margin compression, but our financing margin percentage still stood at a healthy 68.3 percent.

Looking at the consumer portfolio at quarter end, gross financing receivables were down $12 million from year-end to $1.28 billion, as we continued to clear out foreclosure backlogs. Our average down payment has increased to 13 percent from 12.2 percent last quarter, as we continue to see the effects of requiring higher equity contributions on upgrade transactions.

Our average interest rate increased by 13 basis points to 12.31 percent as the rate increases we put in place last year continue to work their way through the broader portfolio. And, finally, our long-term allowance was 13.2 percent, down from 13.3 percent last quarter, reflecting a smaller foreclosure backlog.

Turning to resort and club business, NOG was 6.7 percent, which helped drive a 7.7 percent revenue increase in the quarter to $42 million. About three quarters of the growth was driven by new members and the rest was driven by pricing. Margin increased 10.7 percent to $31 million, and margin percentage expanded 200 basis points to 73.8 percent.

Q1 rental and ancillary revenues increased 16 percent to $59 million, and margin increased 4.3 percent to $24 million. Margin percentage contracted 440 basis points to 40.7 percent. Results reflect system growth and the mid-2018 addition of The Quin, which we are operating as a hotel until we convert it to timeshare use later this year. While The Quin did have a net positive impact, the first quarter is a shoulder season in New York, making The Quin less impactful to our results than it was in Q3 and Q4 of last year. As we start renovations, the impact from Quin will diminish in the back half of the year. Rental also picked up some additional developer subsidy expense as new properties opened. Over time, club sales and rental income will help offset these expenses.

Bridging the gap for Q1 between segment-adjusted EBITDA and total adjusted EBITDA, G&A increased $2 million; license fees were flat, and our JVs generated $2 million of adjusted EBITDA.

On to the balance sheet. As Mark touched on, we successfully completed the $200 million first phase of our share repurchase authorization last month, and yesterday we announced that the Board had approved an additional $200 million under the authorization. We continue to view return of capital as an important component of improving shareholder returns.

In Q1, a net draw of $175 million on the revolver funded buybacks and project spending. We purchased 3 million shares in Q1 for $97 million at an average price of $31.92 per share.

In April, we purchased an additional 925,000 shares for $30 million, at an average price of $32.55 to complete the initial authorization. We funded those repurchases with additional draws from the revolver.

In total, to complete the initial authorization, we've purchased approximately 6½ million shares since December for $199 million, at an average price of $30.73 per share. This represents about 6.4 percent of what our market cap was at the time that we announced the program back in November.

At the end of Q1, net leverage stood at 1.4 times. While this is close to our target range of 1½ to 2 times, given timing expectations for cash flows and anticipated liquidity events such as ABS transactions throughout the year, there is ample room for additional repurchases within our leverage guidelines.

In April, we amended our warehouse facility. We maintained its current size at $450 million, extended the maturity to 2021, and negotiated more favorable terms.

Looking at our liquidity positions, we ended the quarter with $158 million of unrestricted cash and capacity of $509 million on the revolver and $330 million on the warehouse. Corporate debt was $800 million, and our non-recourse debt balance was $720 million.

Adjusted Q1 free cash flow was a negative $36 million compared to negative $32 million in the prior year.

As Mark discussed, Q1 results, coupled with the shift in timing for Cabo, resulted in a reduction for our full-year contract sales growth target — the 5 percent to 8 percent from our previous guidance of 9 percent to 11 percent. The impact on adjusted EBITDA will be mitigated through continued strong performance from resort, club, and rental, cost controls and more favorable inventory product mix. Given this, we are taking our adjusted EBITDA guidance down by $5 million to $445 million to $465 million.

Walking through a few other line items in our guidance, we are increasing interest expense by $10 million to reflect incremental borrowing used to fund share repurchases, the Maui acquisition, and other projects. We are also increasing share-based compensation expense by $10 million. This change is driven by updated long-term performance tracking and the modification to our performance-based RSU awards that require the acceleration of expense recognition. For clarification, the modification does not impact the quantum of any awards or the timing of any vesting requirements.

The guidance reflects no additional share repurchases and is based on 92 million fully diluted shares outstanding. Taken together, our revised earnings-per-share guidance range is now $2.61 to $2.77 compared to our prior range of $2.74 to $2.89. We are maintaining our adjusted free cash flow guidance of $60 [million] to $120 million.

One other item that will help you as you update your models, our 2019 guidance does not assume any full-year deferrals or recognitions; however, on our February call, we discussed the possibility of inter-quarter deferrals. We have started selling some inventory that will be deferred until construction is complete and, in the case of just-in-time projects, until we take title, so we are expecting some deferrals in Q2 and Q3 that will be recognized in the fourth quarter.

Currently, we expect net deferrals to be between $25 [million] and $27 million in the second quarter, and $12 [million] and $13 million in the third quarter. Then the net recognition in Q4 would offset the cumulative deferrals from Q2 and Q3.

Finally, similar to what we discussed last quarter, we expect earnings to be back-end loaded with approximately 53 percent of our full-year adjusted EBITDA coming in the second half of the year, excluding the impact of deferrals. As always, feel free to give Bob a call to go through the details.

This completes our prepared remarks. We will now turn the call over to the Operator and look forward to your questions. Leann?

QUESTIONS AND ANSWERS

Operator

Thank you. If you would like to ask a question, please signal by pressing star, 1 on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, please press star, 1 to ask a question. And we'll take our first question from Brian Dobson with Nomura Instinet.

Brian Dobson

Hey, good morning. Thanks very much. So at this point, what gives you confidence in your revised outlook, given unexpected weakness in March, and can you walk us through the methodology you used in determining that outlook?

Mark Wang

Yeah, Brian, this is Mark. Anyways, thanks. First, I know you've heard me say this, and I know many on the call today have heard me talk about the high degree of confidence that we have in our business and, in particular, our outlook. And so why do we have this confidence? Well, first, when you think about our business, we've built it at minimum around a three- to five-year plan, which has allowed us to drive, you know, stable long-term value creation, and this was the case when we were under the Hilton umbrella and when we were sponsored by Blackstone, and as we've illustrated it the first couple years as a standalone company.

And one of the things we don't do is we don't manage the business to any particular quarter, and far more important, we don't panic or lose any focus when a quarter doesn't fall in line, and we don't, because we know our business. We adapt, we remain flexible, because we've been through this many times, and when I say we know our business, I'm referring to the decades we've been in the business, whether it's financial crisis or weather phenomena, we've seen it all.

So we don't get sidetracked, and we make the necessary adjustments that continue delivering the value, and this business is really about eight quarter cycles as I look at it, and a particular

quarter is not going to make or break us, so I'm confident that we're going to get the revised numbers we've put forth, and I'm confident we'll meet the longer-term goals that we laid out. I think there was a second part of that question. You were looking at —

Brian Dobson

Yeah, that's right. In addition to the methodology you may have used in determining that guidance, I was interested in how you felt the cadence of contract sales moving through the balance of the year, if there's some seasonal strength in particular quarters rather than others.

Mark Wang

Yeah, no, that's a fair question. I think, first, as far as sales guidance goes, the update really reflects the key factors. The first is, as we said in our prepared remarks, we were impacted on availability of inventory. But, again, we had plenty of inventory, and when you look at the actual absolute results of the quarter at $3,700 VPG, that's the fifth best VPG we've had in the last 12 quarters, so it wasn't like we had a major fall-off, and that VPG, you know, leads the industry. We don't see being able to recoup what we lost in Q1.

The second part of how we got to our forecast is we've adjusted our expectations based on what we know coming out of Q1, and that's mainly, again, due to the lack of upgradeable inventory.

And the third one is around timing of Cabo. We've moved Cabo, we've shifted that from late '19 to '20, so, as you know, these things can happen, especially when you're working across borders, and the delay there is really related to getting the condominimzation done on the property, so, again, the shift is timing, and we expect strong demand once it comes on line. So as far as how you break the impact up, it's roughly, you know, a third, a third, and a third, just to keep it at a high level.

And then as far as guidance on EBITDA for the quarter, when we look at EBITDA, the guidance — we moved it down $5 million. I think, this demonstrates the resiliency of our business model, that we're able to manage many of our costs, especially the costs that are aligned to contract sales, so, all-in-all, we're pretty confident that number is something we're going to be able to achieve.

Brian Dobson
Great. Thank you very much.

Mark Wang
Thank you.

Operator
And we'll take our next question from Stephen Grambling with Goldman Sachs.

Stephen Grambling
Hey, good morning. I guess with the volatility of inventory availability and contract sales, what can smooth that out? Is that scale that will help that over time, or do you need to have a more pure point system versus points overlay, or do you need to have a seasoning of your customer base?

Mark Wang
Yeah, Stephen, I think first, as far as moving it out, again, I think if you look at our performance for four to eight quarters, you're going to see that the performance is at the top in the sector. So it smooths itself out, because we're in a business, unlike many of our competitors today, we have this net owner growth, which is consuming inventory, so we're going to have to — and every day we're burning off inventory and we're constantly putting new inventory in, so there's no exact science on getting that exactly right.

As far as the product form goes, we like our product form. We know our customers like it. We think it provides the best of both worlds, and when I say that you get the security of the deed, which you'll also get in a pure points trust program, but, importantly, you get this priority reservation window. And then as far as utility of the product goes, we have a point-based system that's tied to each piece of inventory, so you get the same flexibility from a consumer standpoint, but you get more certainty on the reservation, and that's really critical in markets like New York and Hawaii. And we would be doing a disservice to our customers — for example, if we were selling the dream of Hawaii to our Japanese customers and then they were going to have to compete for a reservation with over 300,000 members, quite frankly, that just wouldn't work for our customers.

And there's other benefits too. I think, first, again, you know, I keep coming back to this point, if you normalize our VPGs, we're generating 20 to 80 percent higher VPGs across the sector, and so essentially our product form is working really well. We're yielding a lot from each customer we're talking to.

Other really important factors that play out here is that with the trust system, it would be almost impossible for us to utilize our fee-for-service program, because trust products, you're basically putting points in for one particular project at a time. It would also make it more difficult for us to do multiple just-in-time deals, and today, as you know, we've got over a dozen properties that sit on our third-party balance sheet, and we're selling those things simultaneously, so that's a big advantage for us.

I think affordability pretty much becomes a wash, so, look, at the end of the day, there are some benefits with the trust, and the trust product does leave some things out. There's less peaks and valleys, but I think we're willing to put in the extra work to achieve the higher absolute yields on both the real estate and higher returns.

And, importantly, I think the most important thing, our long-term expectations that we want to provide to our customers is really a priority here. So, all in all, it's not a perfect science, we're never going to get it smooth, we're going to have more peaks and valleys, but at the end of the day, when you add it all up, I think it shows that we've got the best product form for our particular company.

Stephen Grambling

That's helpful, but just to clarify, it sounds like there can be periods where demand for certain products is ahead of the supply, but I would think that as you gain scale and the customer base seasons — in other words, more inventory comes back to you — that lumpiness would theoretically even out over time.

Mark Wang

Yeah, you're right. That should even out over time, and we went into the spin, there was moderated investment coming into HGV, coming into the spin, we had our own dedicated balance sheets starting in January '17. It took us a while to put these projects together. So, I think once we get out toward the end of '19 and as we begin into '20 and then into '21, we're going to have

a lot more inventory available, and we're going to have a lot more variety of inventory, and the mix will better fit across the overall spectrum of customers that we're talking to.

We do risk, in some cases, with these peaks and valleys, some potential lost sales, but that's more with our first-time customers, because our owners are still there, and our owners will wait and they'll be patient.

Stephen Grambling
So one last one. Just given that, you know, the availability could be important, how can you get comfortable that the trend that you saw in March wasn't just because of the availability versus something going on in the macro? Do you see that in the conversion rates, or is there something else from a tour standpoint?

Mark Wang
Well, it's interesting, from a consumer standpoint, our consumers are behaving very good in markets where we have inventory. A great example, we just launched Central toward the middle of March. That's our new property in New York. Consumers are behaving really good. We're exceeding expectations there. Orlando, where we have ample inventory, again, another really strong market, and we're starting to see this pick up in Myrtle Beach as we will be opening the Enclave there, and so in markets where we have inventory, the consumer is behaving better. In markets where in APAC in particular, where we've exhausted most of Ocean Tower and we don't have that high-end upgrade inventory, that's a market that we're struggling with.

And so it's hard for me to really quantify and judge the consumer based on that, so I guess what I'm saying is where we have ample inventory, we're good. Where we don't, we're seeing lower commitment levels.

Stephen Grambling
Awesome. Thanks so much for all the answers.

Mark Wang
Thank you.

Operator

And our next question comes from Patrick Skolls [phonetic] with SunTrust.

Patrick Skolls

Hi. Good morning.

Mark Wang

Good morning.

Patrick Skolls

Good morning. It looks like in the quarter the fee-for-service contract sales mix jumped up quite a bit year over year. How would you see that fee-for-service mix, the trajectory of that throughout the year? Thank you.

Dan Mathewes

Sure, Hey, Patrick, it's Dan speaking. Fee-for-service was up year over year, quite substantially. One of those items driving that was Ocean Towers' success story last year at this time. It took a lot of the volume that you'd typically see go to fee-for-service projects, so last year was probably a little bit understated. And as we go out through the course of 2019, you'll see that coming down, one, just from seasonality, but, two, as more owned projects come online. And then as you look to the out years, we would look for that to drop below 50 percent in 2020 and then again below 40 percent in 2021.

Patrick Skolls

Okay, thank you. That's it.

Dan Mathewes

Thank you.

Operator

And our next question comes from Brant Montour with JP Morgan.

Brandt Montour

Hey, good morning, everyone. Thanks for taking my questions. So on the inventory availability topic, and I think we all have a pretty good handle of what's coming online in terms of new projects, but can you talk about which projects are rolling off soon, and, more importantly, you know, how much of these larger projects or how many large projects you have that you're in or near kind of in that danger zone in terms of low inventory availability? I guess what I'm asking, can this inventory availability issue become more of an issue before the new projects come on in a big way?

Mark Wang

Yeah, no, Brandt, it's Mark. No, I think we've adjusted our forward guidance, and you can only imagine we've looked very, very closely at our inventory. We feel comfortable that the inventory that we have on hand and that will be materializing this year will meet the guidance that we've put forth. So I don't think that this conversation that we're having this quarter will be the same going forward.

Dan Mathewes

And from a project perspective, I think when you look year over year, the only significant difference is really Ocean Tower Phase 1, where it's essentially sold out. We have multiple phases left to come online, and those will be coming online starting in 2020, so that's probably the main difference there.

Brandt Montour

Got it. Thank you. And then just a follow-up, Dan, on your comments. I think you were bridging us from the contract sales guidance lowering, but EBITDA, if it doesn't come down to the same extent, so I guess I think you mentioned the resorts, the other half of the house, the resort segment as well. Mark, you mentioned costs. Could you maybe just walk us through the different levers that you're going to be able to pull to ease the pain there and parse them out between and for us that would be helpful. Thank you.

Dan Mathewes

Sure, I'll give you a little extra color on that. I mean, I think when you take a step back and you look at the change in guidance for contract sales, looking at the midpoint, that's roughly a reduction of close to $50 million. So when you flow that through, using a real estate margin just

north of 20 percent, it gets you north about $10 [million] to $11 million, give or take, and we're obviously lowering EBITDA by $5 million. Where you see the bridge if you will, from that $10 [million] to $5 million gap, it's truly the outperformance that we've seen in the rental club and the resort business. We expect that to continue for the balance of the year, coupled with some cost controls that we have internally and to a certain extent, a mix in product sales and a lower cost of products. And it's probably in that order of magnitude.

Brandt Montour

Super helpful. Thanks, guys.

Operator

And we'll take our next question from Jared Shojaian with Wolfe Research.

Jared Shojaian

Hey, good morning, everyone. Thanks for taking my question. So can you tell us contract sales and VPG growth in April to give us some more confidence that March was more of an anomaly, especially now that the new Manhattan property is up and running? I realize it's a bit myopic, but anything quantitative you can really share to just help us get more comfort that March is really past us, and now you've got some inventory that's been coming online?

Mark Wang

Yeah, Jared, we can't provide anything specific on that, but I kind of go back to one thing I can say this, we think, is past us, because, the March phenomenon is one we think was really mainly driven by inventory. There's anecdotally a few other things that you could throw in there, but at the end of the day, I can tell you that I think we're past that, because our closing percentage for new buyers was actually up in April, so that is a turnaround for us, and so we're really pleased with that, so I think some of that new inventory is slightly bleeding into the system, in particular, the property in New York.

Jared Shojaian

Okay, got it. And then can you tell us how much of the full-year contract sales guidance reduction, that introduction was due to the first quarter miss as well as Cabo shifting forward into next year? It seems to me — correct me if I'm wrong — that you didn't meaningfully change your assumptions very much for the second and the third quarter. So I guess, first, is that true, and then can you

just help me get comfortable with the idea that contract sales are going to meaningfully ramp in the second and third quarter when, again, I think you're still up against some pretty tough comparisons, so maybe you can flush out some color there for me.

Mark Wang

Yeah, again, I think I said this earlier. It's roughly a third of our contract sales guidance is pulled down from Q1. So we don't see recapturing that. And then another third is based on what we've learned in Q1 around the inventory and the upgradeable inventory, and then another third is around Cabo being shifted. So, you know, again, I really feel like if we weren't comping against the best quarter we've had in 12 quarters, we had a very solid quarter with $3,700 VPG.

Now, that being said, you know, we've still got to put up some numbers for the rest of the year, and as we look at the rest of the year, it will shape up more or less opposite of how '18 came about, where we started off stronger with the launch of Ocean Tower. In this case, as the year goes on, Chicago sales center opens, Charleston comes into play, New York Central expands out and gets registered in additional states, and we have The Quin that we're going to be bringing on in Q4. So all of those things should help us and gives us confidence that demand will move up as we move through the year.

Jared Shojaian

Okay, thank you. And one more, if I may. You ramped up the prior $200 million buyback over the course of only a few months. Is that your expectation for the next round of the $200 million, and are there any restrictions and how soon can you start to deploy capital there?

Dan Mathewes

Hi, it's Dan. Just to give you a little color on that. I mean, I think stepping back to our conversation that we had on Investor Day, when it comes to capital allocation, our initial focus, obviously, was on investing in inventory, which we've obviously done. The second focus was deploying that capital in other ways, primarily through this share repurchase program and to lever up to our desired leverage range, which was at 1½ to 2 times.

So what you saw us do in December and obviously in Q1, and to a certain extent, in April, is really drive that, and we drove that through the $200 million share repurchase quite aggressively, and we did it through open market purchases under 10b -18 and 10b5 -1, which I think you can see

as we were buying in April close quarter end, which clearly indicates we were in a 10b5 -1 program. Going forward, we'll look to use those same options, and we will look to purchase stock as long as it makes financial sense to us. And when we look at our stock price, we compare it to our view of the intrinsic value, and if there's a return there, we will make that investment. At some level, it obviously behooves us to look at other options for that capital. Right now we've got a lot of inventory coming on the line in the next 24 (months) to 36 months. With that in mind, this is where we see the best use of capital at this particular time.

Jared Shojaian
Okay. Thank you very much.

Operator
And as a reminder, it is star, 1 if you would like to ask a question. Our next question comes from David Katz with Jefferies.

David Katz
Good morning, everyone. I know we've had a lot of discussion about the timing and placement of earnings and sort of getting our numbers lined up correctly, but what I wanted to do was just see if we can have a discussion about sort of a long-term, untimed opportunity or earnings power for the company, and, how you think about the white space that's available, and what could really be accomplished in the next three to five years in terms of capturing that? And we can figure out sort of the timing and the path there over time as we go.

Mark Wang
Yeah, look, I think — yeah, this is Mark — we are continuing with our strategy. We feel that there's tremendous opportunity for continued organic growth in our business, and I say that, because we're working closer than we ever have with Hilton, and Hilton is continuing to invest in their digital platform, and we're continuing to invest in our digital platform, and we're seeing some really good opportunities there. And I'm starting with that, because that's an opportunity that as we continue to build that platform, it will potentially allow us to move into some additional type of product forms.

And so those product forms that I'm not willing to discuss in more detail now, but I think what it does is it allows us some more flexibility to move in to not only some more geographic markets

here in the U.S. but also explore some opportunities for expansion internationally. So I don't know if that's answering your question. I don't have any specific timetable that I can attach to that.

Dan Mathewes

I mean, I think that the only thing I'd add to that, David, is when you think about a blank slate, I think that's what we were potentially faced with the last 24 months and where we pulled together our capital allocation strategy and decided to invest in this inventory, and that's what you see coming across over the next 24(months)to 36 months. And, as Mark said earlier in the call, we obviously are disappointed at having pulled that contract sales in 2019, but this in no way changes our view from those projections and expectations that we had on Investor Day. So looking out to 2021, we're focused on adjusted EBITDA north of $550 million. We are still in our mind, on track to get there, and we're very confident about that.

David Katz

Okay. Thank you very much. Appreciate it.

Operator

At this time we will conclude the question-and-answer session. I would now like to turn the call back over to Mr. Mark Wang for any additional comments and closing remarks.

CONCLUSION

Mark Wang

Well, thanks again, everyone, for dialing in this morning. We're moving forward into 2019 and remain confident in our business and our long-term strategy that we've laid out. And, as always, we appreciate your continued interest in HGV and look forward to speaking with everybody again next quarter. Thank you.

Operator

And this concludes today's call. Thank you for your participation. You may now disconnect.