Hilton Grand Vacations Inc.

Q1 2020 Earnings Conference Call

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CORPORATE PARTICIPANTS

Mark Melnyk – *Vice President of Investor Relations*

Mark Wang – *President & Chief Executive Officer*

Dan Mathewes – *Chief Financial Officer*

PRESENTATION

Operator
Good morning, and welcome to the Hilton Grand Vacations First Quarter 2020 Earnings Conference Call. A telephone replay will be available for 7 days following the call. The dial-in number is 844-512-2921 and enter pin number 13697041. 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 (*), one (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 (*), two (2). If you should require operator assistance, please press star (*), zero (0). If you are using a speakerphone, please lift your handset to allow the signal to reach our equipment. Please limit yourself to one question and one follow-up to allow the opportunity for everyone to ask questions. You may then reenter the queue to ask additional questions.

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

Mark Melnyk
Thank you, operator, and welcome to the Hilton Grand Vacations first quarter 2020 earnings call. Before we get started, please note that we have prepared slides that are available to download from a link on our webcast and also on the main page of our website at investors.hgv.com. We may refer to these slides during the course of our call or question-and-answer session.

As a reminder, our discussion this morning will include forward-looking statements. Actual results could differ materially from those indicated by these forward-looking statements and these statements 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 10-K, as well as similar sections of our 10-Q, which we expect to file soon after the conclusion of this call and in any other applicable SEC filings. We will also be referring to certain non-GAAP financial measures. 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 at investors.hgv.com.

As a reminder, our reported results for both periods in 2020 and 2019 reflect accounting rules under ASC 606, which we adopted in 2018. Under ASC 606, we are required to defer certain revenues and expenses related to sales made in the period when a project 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 T1 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 recognitions for all reporting periods. Finally, unless otherwise noted, results discussed today refer to first quarter 2020 and all comparisons are accordingly against the first quarter of 2019.

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. Mark and Dan will then make themselves available for your questions.

With that, let me turn the call over to our President and CEO, Mark Wang. Mark?

Mark Wang
Good morning, everyone. Earlier today, we released our first quarter results. I'd like to start by saying that this call is going to feel very different from the ones before and that's because we're in a very different environment. While I'll discuss the performance of the business, I believe it's also critical to address what we're facing today. It's clear that the impact of coronavirus has been sudden and significant and that this period of disruption remains uncertain.

While we saw minimal effects from the virus in January and February, it should come as no surprise that we saw a significant falloff in trends in March as the effects of the virus spread to the U.S. Health and travel advisories began to appear in late January and February in our major markets, which cascaded into a full lockdown and self-quarantine orders, as we moved through March in markets such as New York, California, Hawaii and Florida.

We took immediate action to ensure the safety of our team members, owners and guests by shutting all of our sales centers and suspending operations at most of our U.S. resorts. It was clearly an unprecedented decision that I never contemplated having to make particularly over the span of just a few short weeks.

Fortunately, we entered this period with a strong business model, engaged owner base and solid balance sheet and we took further steps to ensure those strengths will carry us through this time of uncertainty. Today, I'd like to talk to you about three things. First, I'll provide more context about, what we've done to address the urgent needs of the business and our people. Second, how we view the industry, its relative resilience during these times and our position within it, and last, I'll share four strategic priorities we are committed to and I believe will position us for success today and as we exit these restrictions and enter a new period of recovery.

First, let me walk you through some of the swift actions we've taken already. In mid-March, we paused our on-site sales operations to protect our staff and guests. We waived all cancellation penalties for our guests who plan to stay with us prior to the end of May and refunded all reservation fees associated with those days and we waived online transaction fees for owners, who book a stay by the end of May for travel in 2020 and 2021.

We've kept our customer service centers fully operational to answer questions, take future bookings and continue to provide our owners with a high level of service, and we made temporary changes to our booking rules and we will continue to evaluate and adjust them as necessary to ensure owners travel is protected.

At the same time, we took immediate steps to safeguard our future marketing pipeline post recovery. Our IT teams moved quickly to transition our call center staff to work-from-home and maintain continuity with our Hilton call transfer program along with the ability to service our customers booking future vacations. We also built out infrastructure to allow our top sales directors to work remotely, enabling them to begin sales to our top clients.

At the resort level, we worked with our HOAs to keep our properties in pristine condition during the pause. Prior to the shutdown, the rooms and common areas were deep cleaned, and many resorts took advantage of the slowdown to get ahead of planned maintenance projects that will allow us to have more rooms in service in the latter half of the year. We also acted quickly to protect the business with additional steps to defend our cash flow by adjusting our operating expenses and inventory spend.

Nearly 60% of our total operating costs are variable providing a natural hedge against periods of reduced business activity, and our Hilton license fee is almost entirely variable. To lower our fixed costs, we implemented cost controls including a pause in our discretionary spending, a hiring freeze and a temporary halt to our 401(k) match.

To adjust to the suspension of operations, we made the difficult decision to furlough approximately 6,100 of our valuable team members representing nearly 70% of our employee base and in addition, we reduced salaries for all team members and management across all levels of the organization.

On the inventory side, we identified over $200 million of budgeted spend for the year that can be deferred with minimal impact to the planned sales launch schedule for our new projects, representing over 50% of the previously budgeted spend over the next three quarters.

As the situation evolves, we'll continue to revisit our planned spend as we balance cash needs against the availability of new inventory. In addition, we also drew down our revolver and warehouse to strengthen our cash position - Dan will speak to those in more detail.

Collectively, these actions have significantly reduced our fixed cost burden, minimized our cash burn rate and strengthened our balance sheet to enable our business to weather an extended period of slowdown.

Next, I'd like to highlight the strength of our sector. The timeshare industry has both business model and product advantages not shared by other parts of the hospitality industry. Our business model is differentiated by a solid foundation of owners that provides a stable source of recurring EBITDA and protection from fluctuation in asset utilization.

For example, approximately 40% of our segment EBITDA last year was generated from financing and resort and club divisions and 90% of our member fees for this year have already been collected. Our business is fortunate in that these maintenance fees fund all the operational costs of our resorts. This reduces the fixed asset burden commonly seen in other areas of hospitality industry.

Further the timeshare product is better positioned to recover from a pandemic. Owners often return to familiar unit resort, which truly makes it feel like their home away from home. Because of this, they know the HGV staff and have a comfort level that is closer to a second home than a hotel. Additionally, our product is structured to allow us to reduce the reliance on communal features. For example, most units include in-room kitchens and laundry facilities. Rather than needing to dine at a common restaurant, our owners and guests can prepare meals for themselves in the comfort and safety of their accommodations.

Within the industry, we are starting from a strong position because of our NOG strategy, flexible inventory sourcing and the strength of our balance sheet. We entered the year with nearly $1 billion in liquidity and we've managed a conservative balance sheet with very low leverage and

significant cash on hand, which provides a staying power and the ability to protect our customers' interest.

While we can't be sure when the turn will come or what the path to normalcy will look like, one structural advantage that we've always enjoyed at HGV is the strength of our owners. Our 27 years of positive NOG has built a high-quality base of owners, who have an elevated level of connection to our brand. This provides us with historic levels of embedded, upgraded sales yet to be materialized, and 70% of our owners own their intervals outright and have made a material financial commitment to HGV. They're leisure travelers and they have both a desire to travel frequently and a prepaid vacation waiting for them when this disruption passes.

Our just-in-time and fee-for-service structure provides us with operational flexibility to tweak our pipeline for shifting needs and market conditions. We think it's important to not only consider the impact of the pandemic, but also the resulting recession. While we can't say what the shape or duration of the recovery will look like, we believe the best comparison we have is the past financial crisis. As we've discussed before HGV demonstrated the strength of our model during and after the last crisis and we feel we're even in better position to weather the storm and rebound now than we were in 2008.

To give a few data points, our owner base today is two times larger. The Hilton Honors loyalty program has grown its members by four times and we're entering with more liquidity. As we've done in the past, we'll continue to manage our business conservatively through this period of uncertainty and take steps to prepare for return to a new normal as travel restrictions lift and markets recover.

Finally, I'd like to briefly discuss our four strategic priorities. The first three are focused on winning the fight today, while the fourth is designed to position the business to win as we come out of these travel restrictions and enter a period of recovery. I will cover every initiative we have planned, but for your reference you can find them on page two of the materials we provided for this call.

The first priority is to safeguard, the safety and well-being of our team members, our owners and guests. When able we'll reopen our resorts and sales offices complying fully with local regulations and CDC guidance. To ensure the highest level of cleanliness, we created the HGV Clean initiative in alignment with Hilton which we will implement in our properties as we bring them back online.

The second priority is to streamline our spending to maintain our strong liquidity position and optimize our inventory assets. We'll continue to manage variable costs flexing them up and down to meet the demands of our business. We'll carefully monitor inventory demand and leverage our flexible inventory sourcing models to ensure appropriate supply, while minimizing the exposure of our balance sheet.

The third priority is to protect our recurring revenue streams and embedded value. We said before our owners are one of the foundational strengths of our business. To protect this foundation, we're ensuring owner points and vacations are not lost during these constrained travel periods. We're also planning to promote the return of travel to owners as restrictions allow through drive-to offers and other incentives.

The final priority is to grow demand and implement opportunities to create incremental value. The two key factors to create demand in our system are tour flow and inventory. To generate

tour flow and relaunch sales, we will focus on our owners and the over 400,000 new buyers we have in our package pipeline with enhanced promotions and marketing offers. Our new inventory investments should create incremental demand for both owners and upgrades and NOG sales as these audiences begin touring again.

We'll also continue to grow our new buyer package pipeline through direct marketing and digital channels with Hilton and other partners to ensure we have a robust pipeline of tours going forward, and we've developed a new prepaid term product that was originally scheduled to launch in April that we will now plan to pilot as soon as conditions allow. And finally, in 2008's financial crisis, we benefited from being opportunistic with distressed properties. We'll continue to monitor the market and work with our fee-for-service partners to do the same as opportunities present themselves.

To wrap up, clearly this is a time of unprecedented challenges. We acted quickly and decisively to secure our business and control the things that we can control. While this disruption is fundamentally different from others we've seen before, we're confident that leisure travel will recover and that timeshare owners will be at the leading edge of that recovery, and we're using this period of reduced business activity to position our business and lever our strategic drivers to ensure we emerge as a stronger business ready to engage our owners.

Before I turn it over to Dan, I want to say how proud I am of the efforts of our team who've been working around the clock to adapt to this situation in real-time and take the necessary steps for us to get ahead of it and I want to extend our best wishes to all of those affected either directly or indirectly by this pandemic and thank the frontline workers around the globe who are saving lives. Dan?

Dan Mathewes
Thank you, Mark, and good morning, everyone. We have a lot of ground to cover today and given the unique environment our format will be different from our prior calls. After a walk-through of our Q1 results, I will spend more time talking about our actions to preserve our cash flow during these unprecedented times followed by additional detail on our liquidity, credit position and covenants.

As Mark Melnyk mentioned in his introduction to our call, our Q1 results did include deferrals, specifically $47 million in revenue deferrals and net deferrals of $27 million impacting adjusted EBITDA and net income.

All references to net income adjusted EBITDA and real estate results on this call for current and prior periods will exclude the impact of deferrals and recognitions. A complete accounting for our historical deferral and recognition activity can be found on -- in Excel format on the Financial Reporting section of our Investor Relations site.

Let's turn to a quick review of the results for the quarter. Total first quarter revenue declined $52 million to $398 million reflecting declines in our real estate and rental and ancillary segments that more than offset the growth in our resort and club and finance businesses. This decline in revenue was primarily the result of COVID-19 and its global impact on consumer activity.

Q1 adjusted EBITDA came in at $60 million versus $102 million last year. In addition to lost sales and rentals during the month of March, Q1 2020 was impacted by incremental bad debt accrual of $23 million, which I will discuss in a few minutes, as well as $11 million in one-time

payroll-related expenses incurred in connection with operational closures and a refund of $2.2 million in reservation fees for those impacted by our resort closures.

Net income was $35 million and diluted earnings per share was $0.40 compared to net income of $55 million and diluted earnings per share of $0.58 in the first quarter of 2019.

With real estate, Q1 contract sales declined 24.2%, driven by a reduction in both tours and VPG. Through the first two months of the quarter, tour growth of 6% was tracking in line with our expectations, reflecting gains from both owners and new buyers. However, as we moved through March, the impact of COVID-19-related disruptions resulted in tours declining 19% for the quarter. Close rate was up three basis points in the quarter as gains in January and February were partially offset by a decline in March.

A highlight I'd like to note is that our owner close rate was up every single month of the quarter underscoring both the strength of our owner base and the connection that we have -- that they have with HGV. Our fee-for-service mix for the quarter was 53.3%.

On the consumer lending side, our provision for bad debt was $37 million. I'd like to pause here to talk through the increase in our provision this quarter. The charge of $37 million can be broken down into effectively two parts. First, an ordinary course of business bad debt expense of $14 million which is similar in magnitude to the one that we made in the first quarter of last year.

Second, we recorded a charge of an incremental $23 million associated with the potential impact that coronavirus could have on our portfolio. This has increased our overall allowance on the balance sheet to $212 million or 15.9% of the gross financing receivables.

I say potential impact because our static pool models require us to make an estimate about the expected performance of our portfolio and recognize any potential future defaults in the current period. So, as a reminder, our provision is based on credit modeling and future expectations of losses. It is not on a loss-as-incurred basis.

As of today, we have less than 60 days of data indicating how COVID-19 will impact our portfolio. With such limited data, we have not seen an increase in our default rates to date. However, we have seen an increase in delinquency rates over the past quarter from 2.5% at the end of Q4 to 3.2% at the end of Q1 and 3.5% through the end of April.

Turning back to real estate expenses. Product costs were 23.7% of our owned contract sales. SMG&A was 54.1% of contract sales as a result of deleverage associated with the decline in revenues. Real estate margin was $25 million down 63.8% versus last year driven by the $23 million accrual as well as payroll costs associated with operational closures. Margin percentage was 14%.
In our financing business first quarter margin was $31 million with a margin percentage of 70.5% versus a margin of $28 million and a margin percentage of 68.3% last year.

As I mentioned, our credit trends were stable through the end of the quarter aided by recent improvements to our collection standards. We have seen an uptick in delinquencies in April and anticipate them to increase in the coming months as a result of the elevated levels of unemployment owing to COVID-19 endemic.

Looking at the portfolio balance gross receivables stood at just over $1.3 billion. Our average down payment year-to-date is 12.4%. Our average interest income rate increased to 12.5% from 12.3% last year.

Turning to our resort and club business, NOG was 5.3% for the quarter which drove a 4.8% increase in revenue to $44 million. EBITDA for Q1 was $32 million with margins of 72.7%, down 108 basis points versus last year. The decrease in margin percentage was driven by the refund of reservation fees during the quarter.

Rental and ancillary revenues were $52 million versus $59 million last year due to a combination of lower supply of rooms at the Quin and lower occupancy levels as the pandemic progressed through the quarter.

Expenses were $2 million higher at $37 million owing to larger subsidy requirements for newly opened properties. Our EBITDA was $15 million with margins of 28.8% and impacted by deleverage over a relatively fixed cost base.

Bridging the gap between segment adjusted EBITDA and total adjusted EBITDA, first quarter G&A decreased $3 million, license fees were down $1 million, and EBITDA from JVs was up $2 million.

Now I want to spend a few minutes talking through our operations and some of the adjustments that we've made due to the impact of COVID-19. During the course of the last 45 days, we have significantly changed our expense structure to adapt to a reduced level of business with a focus on preserving our cash flow.

We expect that these cost-saving measures which include furlough in close to 70% of our employees, salary reductions for the remaining active employees, elimination of all discretionary spend and a hiring freeze among others further reduced our cost base by over $100 million. As business returns, we have the ability to add back costs in a methodical manner to maintain our flexibility in what we anticipate will be an uneven recovery path.

Regarding inventory, prior to coronavirus outbreak we planned to spend just under $400 million this year with the largest spend associated with our new projects; Maui, Ka Haku and The Central.

Given the impact that COVID-19 has on construction in New York, The Central will be further delayed and our initial contractual payment will be shifted to 2021. We have slowed our spend in Maui, completely paused our development activity at Ka Haku as well as Cabo, and adjusted the amount of inventory repurchases we will make this year. These actions will result in us reducing inventory investment by just under $200 million without having a material impact to our prior planned sales launches. That said, Ka Haku will now begin sales in first quarter of 2021 rather than the back half of 2020 as previously expected.

In the first quarter, we spent $30 million on inventory which indicates that we've cut over half of our previously planned inventory spend for the balance of the year. It is important to note that the vast majority of our planned inventory spend pertains to own projects.

The contractual level of inventory spend for the balance of the year is limited to $26 million. So, we have additional flexibility to further adjust our spending as we progress through this year and balance our cash needs against our planned sales launches.

We also took several proactive steps during the quarter to ensure the strength of our balance sheet. We substantially drew down the remainder of our revolving credit facility and raised additional cash by borrowing against receivables collateralized through our warehouse facility.

In 2018, we amended our credit facility and were able to increase our revolver from $200 million to $800 million. This amendment combined with the focus on maintaining relatively low leverage levels have allowed us to be in a strong financial position as the COVID-19 crisis unfolded.

As of March 31st, our liquidity position consisted of $670 million of unrestricted cash, $39 million of availability under revolving credit facility and $255 million of capacity in the warehouse. With regards to our warehouse facility, our existing timeshare receivable collateral would allow for $120 million draw on the remaining capacity of $255 million. On the debt front, we had a corporate debt of $1.3 billion and nonrecourse debt of $885 million.

Turning to our credit metrics. At the end of Q1 our net leverage stood at 1.45 times. Our interest coverage at the end of the quarter was 9.56 times. Our nearest debt maturities are the warehouse facility in 2022, the credit facility in November of 2023 and our senior notes in December of 2024.

Our warehouse facility is a key funding advantage for us providing a cash advance against our pledged collateral at attractive rates. The facility was set up in the wake of the global financial crisis to insulate us from disruptions to the term securitization markets. Necessary, we're in a position to borrow another $120 million or $315 million in total on the warehouse facility.

Currently our cash position combined with the availability on our revolver as well as the warehouse facility provides us with ample liquidity. We have sufficient liquidity even in the event that business remains paused for the next 22 months. While, we maintain low leverage ratios and have great access to capital via our warehouse facility and the ABS markets, our covenant thresholds are nevertheless at levels that are lower than those of our peers.

With the advent of COVID-19, we have been in active negotiation with our lenders to amend our covenant thresholds to provide more flexibility as we navigate through the crisis. We feel good about the progress we've made in our request and remain very comfortable with our strong liquidity and deliberately conservative leverage positions.

We will now turn the call over to the operator for your questions. Operator?

QUESTIONS AND ANSWERS

Operator
Thank you. We will now begin conducting a question-and-answer session. We ask that all callers limit themselves to one question and one follow-up. If you have additional questions, you may re-queue and those questions will be addressed time permitting. If you would like to ask a question, please press star (*), one (1) on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star (*), two (2) if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star (*) keys. One moment please while we poll for questions.

Thank you. Our first question comes from the line of Jared Shojaian with Wolfe Research. Please proceed with your question.

Jared Shojaian
Hi, good morning everyone. Thanks for taking my question and I appreciate all the color and commentary here today. Could you just talk about how you decided the new 15.9% allowance rate is the right number? And what's your level of confidence there? And then I appreciate the commentary on the delinquencies. It doesn't seem like much of an increase so far, but it's also only been 45 days since the shutdown. So, if you have it, maybe a better stat would be what percentage of people are late on their monthly loan payments right now versus what you might normally see?

Dan Mathewes
Hey Jared, it's Dan. Good morning and thanks for the question. With regards to the additional bad debt expense that we accrued getting to that allowance of 15.9%, it's a really tough estimate to make, because to your point very limited data, it's been less than 60 days, so what we did was we looked back to the last shop that we sell to the portfolio and that dates back to the Great Recession.

We're very cognizant that this crisis is going to be different than -- potentially different than that crisis, but that's the best thing that we had to look to. So, what we did was we looked at the increase in defaults during that period applied that same increase in default to every single bucket in our static pool and assumed that the -- that impact negatively impacted us for about 15 months. So effectively rolling out until August of 2021 and then it starts to more normalize, and once you do that it -- the additional reserve you would need is roughly $23 million.

Now the level of delinquencies that we see today at just north of 3% are also below the level of delinquencies that we saw during the Great Recession if you will, and they were more at the level of 4.2%, which is more in line with what that bad debt expense expects over the course of this period.

Now how comfortable are we with that? We have a limited set of data points. It could clearly extend longer than that and it could clearly extend less than that. This is going to be a bit of an evolution process, but given the fact that we have to date, you can see that we've assumed a higher delinquency rate than we're currently seeing, and we're also tying it back to the last major shop that we sell to our portfolio. Hopefully that's helpful?

Mark Wang
Yes. Jared this is Mark, and I'll just add to that. As Dan alluded to, it's just too early still to really get your arms around this one, but we have been as you know over the last decade since the financial crisis -- we've been originating our loans at around 740 FICO score. In a pre-financial crisis, we originated around 700. So hopefully the quality -- well, obviously the quality has improved but hopefully that quality will hold up.

Dan Mathewes
Just another point to add on the quality standpoint that we did not take into consideration. During the Great Recession, the credit process here has improved materially not only from a FICO score perspective, but back in 2008, 2009, we actually did not do credit reporting either. That is in place today, so that should help mitigate that to some extent, but that was not taken into consideration when we came up with our accruals.

Jared Shojaian
Thank you. That's really helpful and I guess just the second part of that question. I mean have you seen anything unusual in terms of people that are not necessarily delinquent because they're not in that 60-day window but maybe they missed a payment? I mean have you seen anything unusual there?

Dan Mathewes
Well, I think the best stat to tell you -- and this is a bit anecdotal, but when we talk to the portfolio team and we analyze the calls that are coming through the doors, the number of individuals who are calling to cancel something and just completely default and they just want to get out has not increased from Q3 last year to Q4 last year till today, so that's been a very static number.

What we have seen is an increase in the number of calls of individuals asking for some level of deferment, and to date we're just over 1000 individuals in aggregate who have reached out to ask for some level of deferment. So out of the people that have loans with us that's just under 2% of the portfolio, and some of these callers are individuals who -- obviously, some of the larger banks are allowing deferments on mortgages, so they're just looking to say "Hey look they're doing it you should be doing it too" and then there's other individuals who obviously have been directly impacted by COVID-19. These are all being handled on a one-off basis, but again it's less than 2% of our portfolio to date.

Jared Shojaian
Okay. That's really helpful. I appreciate that, and then just for my second question. What do you think that -- if I look back to slide 5, which is really helpful on the liquidity and the cash burn, what do you think that $38 million monthly burn looks like when you start to reopen? Assuming you're at very low volume levels initially and you start to bring back those costs, do you think you're still burning cash initially? And if so, should we assume that any burn is definitely going to be less than the $38 million?

Dan Mathewes
Look I think it's a great question. It's all how we bring things back. We've done -- we've obviously readjusted the business as something that you've never ever planned for, right? So, we've really pulled back that expense quite dramatically, and it's all how we come back. I mean there's a scenario where you bring individuals back who are selling packages sooner than you actually open up sales centers. So, while you would have a cash, hopefully neutral standpoint, you would have compression on your margins, but I don't want to get into a level of prediction at this point just -- since we're so early into this. We -- the $38 million is really trying to be just an example of if we're where we are today for the balance of this crisis how long can we last. I just don't want to get into anything predictive at this point.

Jared Shojaian
Okay. That's helpful. Thank you very much. I appreciate it.

Operator
Our next question comes from the line of Stephen Grambling with Goldman Sachs. Please proceed with your question.

Stephen Grambling
Hey, good morning. Thanks for taking the questions and all the details as well. As a follow-up to Jared's last question I know you don't want to be predictive, but is there any additional detail

you can provide on how you generally are thinking about or evaluating reopening of the sales centers? How you may be shifting to target existing owners differently? And is there a level of contract sales that you would need to get to free cash flow positive?

Mark Wang
Yes. Stephen this is Mark. Good morning. Look, sales centers where we've -- I can say that for the first two, three weeks 100% of our focus was how to resize the business and recalibrate the business, and since then it's all been about getting prepared and getting ready to reopen. We expect our sales centers will open in close alignment with our resort openings, and the two main factors there really is really around the timing of the government mandates and also how people feel around traveling, and so -- and at this point we can't predict the restrictions -- when those restrictions are going to be lifted, but as of today, we expect probably a number of our markets will reopen here toward the latter part of this quarter and rolling into summer.

So, that's what we're predicting on that at this point, but again, that's a moving target, and it could shift any time. So, that's what we're seeing. As far as which markets, I think, we start off in a really good position. Our top eight markets last year saw over 300 million visitors. So, there's strong inherent demand, and 70% of our markets are drive-to markets, which I think approximately 60% of the U.S. population, can reach within a 300-mile drive.

So, we see each market really recovering on its own timeline, and it's going to be based on the demand, and also the shelter-in-place will supersede all of those conditions. When you look at our portfolio, we -- you kind of categorize it really as urban, and then resort theme and resort feature or mountain, and our expectation is that, urban will take longer to recover due really to the density and nature of the urban markets in particular New York, which has been so heavily impacted. Orlando and Vegas, it's -- I think, the demand is -- the pent-up demand will be there, but it's all driven by, how we see the theme parks and casinos opening, and I can't speak for those companies, but we're following their progress very closely, and we know that they're working to get reopened, and again, we think strong pent-up demand.

We think that our beach locations Myrtle Beach, Hilton Head, Southern California. Our mountain locations in Colorado and Utah will be the quickest to return to a more normal state. With -- I think beach is going to be in high demand for the summer and the low density of these markets, and then, as we look at our fly-to markets, Hawaii and Barbados. We're showing really good demand, and again, there's less density and an abundance of sunshine in those markets. As it relates to Hawaii, as you know we have a -- we have about 18% of our product sits in Hawaii.

Again, showing very strong demand on our books right now, both from our U.S. and Japanese customer, Hawaii is perceived as very safe. I think it has the lowest infection rate per capita in U.S. but it's very early. We still don't understand how the state of Hawaii is going to manage the inbounds of both domestic and international, and how well the airlines are going to do, but I think the airlines are working very hard at getting people back on planes. So again, probably a long-winded answer, but it's a very dynamic situation. It's going to remain very fluid for some time, but we're building plans around all of these, and we'll be able to reopen in fairly short order once we get the word.

Stephen Grambling
Thanks, and I guess as a follow-up on the demand side. I'm sorry I guess maybe I cut you off there, but just I'll sneak it in real quick, if you want to address it afterwards. On slide nine you have some good statistics on owner arrivals, rental arrivals, marketing sampler package

arrivals, year-over-year. Is there any color you can give on postponements deferrals or cancellations on those? Thanks.

Mark Wang
Yeah. So, look, again, when we look at the data we're really pleased with the trends. I think we're about 80% of the levels we saw at the same time last year, and our owners are sitting at about 90%. If you kind of take a snapshot, I think, it was done on April 28, this has been really, really consistent with what we've seen in previous slowdowns, and I think again, indicative and we've talked about this before and our competitors have said the same.

The ownership position really -- the prepaid ownership nature of the business really drives that demand. However, I think the important thing is as I alluded to a minute ago there's still a lot of uncertainty around markets opening, airlift and all of that, but I think, as we look at the data the important thing is the behavior. It's very consistent with what we've seen in the past, and that consistency gives me a lot of confidence that next year, we'll see a good return of our owners as we get farther along in the recovery.

Then, from a cancellation standpoint, from a package standpoint, we've only -- let's see 92% of our -- those who have cancelled in our package pipeline have rebooked for a date later out. So, we've had a relatively small percentage of those cancelling.

Dan Mathewes
Stephen just the second question with regard to adjusted free cash flow. I mean I guess the best way to look at it is I'll just tell you something similar that some of our peers have said. If you assume this paused state for the remainder of the year us getting to an adjusted free cash flow neutral basis is really dependent on the level of inventory spend right? If you -- if we stick to the contractual level which I mentioned earlier was $25 million $26 million that coupled with what we've already spent to date, we can easily get to adjusted free cash flow neutral, and even if we spend closer to what we've indicated just under $200 million it would be neutral-ish, so to speak. So, we're in that ballpark. Hopefully, that's helpful, just from a prospective basis.

Stephen Grambling
Okay. That's great. Thanks so much.

Dan Mathewes
There's one other thing to add to that. The level of inventory spend -- we're very cognizant of this, we're managing this, obviously, as everybody else is day-to-day, and if we are shuttered for the balance of the year, we're clearly going to make a material decrease in that spend. The reason we're so focused and so cognizant about not just cutting the spend right now is we have several large projects that we're currently invested in Maui, Ka Haku, Quin, Ocean Tower, and those projects as we continue to invest, it's important to keep in mind, it's north of $5.5 billion in future sales value. So that's the reason where -- why we just don't automatically shut everything off. Now if we need to, we can, and we will manage that very prudently.

Stephen Grambling
Great. Thanks, again.

Operator
Our next question comes from the line of Brandt Montour with JP Morgan. Please proceed with your question.

Brandt Montour
Hey, good morning, everyone. Thanks for taking my questions and I appreciate all the details today. Quick question on slide 5 on the cash burn analysis, I just want to -- just curious. What, if any, assumptions are baked into that with regards to sort of recapture of defaulted inventory?

Dan Mathewes
This, from a cash burn perspective, this assumes a very minimal repurchase of defaulted inventory.

Brandt Montour
Could you – sorry, and then could you just sort of, I guess, just re-explain to us sort of what you would be viable for? I know this is nonrecourse debt, but is there a sense that you would be potentially in the market since it is obviously a good business, a lot of the time to do so? And sort of what that could look like in the -- as part of your forward modeling that you talked about with loan loss provisions?

Dan Mathewes
Yes. No, sure. So, the financing cash inflow that you see here takes into consideration the level of defaults that we've discussed earlier. It also, from a liquidity perspective, when you look at the warehouse availability, clearly, we already mentioned that the remaining capacity is at $255 million. What you see here is $120 million. What's driving a large part of the delta is us holding back loans for substitutions if we were to remain shuttered, so we've tried to capture those elements in this cash burn analysis.

Brandt Montour
Got it. That's super helpful, thank you and then just on the drive-to versus fly-to stats, which were really helpful. I was just curious, which I think might be a different way to look at it, but how do you -- how would you sort of quantify how much of your sales mix is drive-to? And what I'm trying to get at is I think we all kind of maybe agree that the first segment to come back would be your existing owners that can drive to their market that you could potentially sell upgrades to, and so I'm just curious what percentage of your current mix is that sort of business? And then just a quick second parter of that is, do you think you might see a shift toward repeat business as a percentage of your mix?

Mark Wang
Brandt, this is Mark. Yes. Our drive-to market is about 65% of our overall real estate revenue, and I'm sorry, the second part of that question?

Brandt Montour
Well, I was just curious because if you do see a shift to repeat business, which is arguable that it will be easier to get repeat customers in for tours versus new customers, that obviously comes with a higher VPG, a higher close rate. So that would be something for us to consider when we're looking to model forward. So just curious if you think that, that mix will shift towards repeat customers.

Mark Wang
Yes, right. Okay. Yes, we're definitely going to lean on our owners coming out of this, and historically, we run at about a 50-50 mix, and -- but we're going to leverage our owners coming out of this. As you can see, there's a fairly strong demand, as I talked about a few minutes ago, and in the back half of this year from a bookings standpoint, but more importantly, we think that's going to continue into next year, that behavior. Fact that we've been able to double our

owner base in the last 10 years and the fact that we've been driving positive NOG, we've got a lot of pent-up, unmaterialized embedded value in sales for our owners. So, you should expect that that mix is going to shift. I can't give you an exact number, but 60-40 for the next 12 months wouldn't surprise me, as I think our owners will be more confident to travel and, again, the prepaid nature of it, but yes, so we will definitely lean heavier on our owners, and as you know, that's a much more efficient sale.

Brandt Montour
Excellent, thanks guys. Good luck.

Mark Wang
Thank you.

Operator
Our next question comes from the line of David Katz with Jefferies. Please proceed with your question.

David Katz
Hi. Morning, everyone. You've covered a lot and all the questions and so forth. I appreciate that, so thank you. With respect to the construction of inventory, I think, Dan, you said you're sort of cutting that back by half. Just to follow up on that point. When it comes time to ramp that back up again, what kind of trajectory should we expect? I mean, is there kind of a several month ramp-up period to it, or can you turn it back on with the same speed you shut it off?

Mark Wang
Yes. So, it's Mark. Just -- so what we've done is we've -- with Maui, for instance, we've just slowed it down, and Maui is a horizontal project. What I mean by that? It's low density. It's multiple smaller buildings, and so what we've done is we've slowed that down. So that will continue moving along.

As it relates to Ka Haku, we have been able to get all the necessary permits to improve the land. So, we've stopped that project in its entirety, but we will be able to turn it on in a relatively short period of time to -- they have to remobilize, because they moved all the equipment off-site, so that could take 60, 90 days to remobilize. With Ocean Tower, again, because it's a phased project, where we're converting hotel rooms, we've just slowed that down and it will -- we can ramp that up relatively fast, so I think we have a lot of flexibility. There's nothing here that we're talking about. Cabo, for instance, actually most of the renovation has been completed. We just decided, let's just pause and preserve that cash and push it into early next year.

So, we have a lot of flexibility and there's nothing that's going to take a long time to get back and going, but as you know, these projects take a long time to develop, and so even when we do restart Ka Haku, it's going to take a good couple of years to finish it, so it's going to push back our sales -- original sales date, which was originally set to be the back half of this year and we're going to have to push that sales start date to the latter part of 2021.

David Katz
Got it. Thank you, very much and good luck.

Mark Wang
Thank you.

Operator
As a reminder, if you would like to ask a question, press star (*), one (1) on your telephone keypad. Our next question comes from the line of Patrick Scholes with SunTrust. Please proceed with your question.

Patrick Scholes
Hi. Good morning everyone.

Mark Wang
Good morning, Patrick.

Patrick Scholes
Good morning. You folks are quite possibly the best capitalized timeshare company out there both public and private, and I'm wondering, how are you thinking down the road here opportunities for distressed acquisitions. I think back the Elara was one. I don't know if it might have been Centerbridge who did that, but certainly you own it now. What are your preliminary thoughts in that regard?

Mark Wang
Yes. Great question, and as we've been talking about really over the last couple of years, we have a very robust pipeline of inventory. So, we're not at this point looking to put any of our capital to work today, but as you pointed out the last crisis really put us in a position where we had to go out and seek third-party capital, and we were very successful propping up and developing this fee-for-service model, and in fact we've done 10 deals to date with really good partners. You mentioned one Centerbridge. We've done a number with Goldman and Strand and Blackstone, and so we think there's going to be a good amount of dislocation in the market, and I think we also believe that the highest and best use for a number of these assets will be timeshare. So, we definitely are going to keep our eyes and ears open, and importantly, we've got great partners and we've been fielding some inbound calls already. It's still a bit early, but we think there'll be some opportunities and we just want to -- like we did out of the last crisis, we want to be really smart on making sure they're good assets that fit well into our -- in our brand standards and our portfolio and we have a really good partner that's working beside us.

Patrick Scholes
Okay. Sounds good. To be clear in addition to possible existing timeshare location acquisitions, it could be conversions of hotel -- existing hotels or hotels that are in development as well that you might be interested in. Is that correct?

Mark Wang
Absolutely. I think it could be hotel. We've recently been doing a number of hotel conversions. We did the units in Chicago with the DoubleTree. We did the number of floors in the Embassy Suites in Washington, D.C. We've done floors in Hawaii and New York, and so we think it's a really efficient model, and in some cases, it improves the hotel asset in that it reduces the overall size, so the overall yield and performance of hotel improves, and in some cases, just converting the entire hotel over is an opportunity for us too.

Operator
Our next question comes from line of Jared Shojaian with Wolfe Research. Please proceed with your question.

Jared Shojaian

Hi. Thanks again for taking my follow-up here. So just to tag on a little bit to that comment. You are pretty well capitalized here, but do you have any desire to raise unsecured debt right now? I know we've seen a lot of other companies who don't really need capital, just go out and raise capital just because the credit markets have reopened, and then I guess along those lines too, can you talk about what you're seeing in the securitization market right now both public and private? Judging by Wyndham's terms this morning, it would seem that the private market is still quite good, but can you just help us think about that and maybe the timing on when you guys would do a transaction?

Dan Mathewes
Hi, Jared it's Dan, and thanks for the follow-up. I'll answer your second question first. With the -- with terms -- with consideration in the ABS market, we still believe, and we have a number of incoming calls showing a lot of support for our ABS-backed paper, both private and public. Obviously, I think everybody knows that S&P in particular paused on ratings over the last 30 or 45 days. We've had discussions with them where they are going to be getting back in. They may be adjusting their loss factors for obvious reasons just like we have adjusted our loss factors as well. So, we are confident that we will be able to get a deal done in one way or another.

Currently we clearly have enough availability under our warehouse facility to do the same kind of order of magnitude that we have done historically. We've also had a number of incoming calls from private institutions with regards to doing a deal similar to what you saw Wyndham announced today. So, we're actually going down a dual path looking at both public and private as we speak today and we're very confident we'll get that done, but timing is probably late Q2, maybe early Q3. We're going to see how that actually unfolds.

With regards to raising either senior unsecured or senior secured debt, look we talk to a number of advisers. We, obviously, listen to the opportunities that are out there, and when we sit here and we look at 22 months of liquidity, it's not the top order of our list right now. That's not to -- that does not mean that we do not look at this and analyze it on a routine basis, but I'll just leave it -- leave at that for now.

Jared Shojaian
Okay. Thank you. That’s really helpful.

Operator
Thank you. Before we end, I will turn the call back over to Mark Wang for any closing remarks. Mr. Wang?

CONCLUSION

Mark Wang
Well, thanks everyone for joining us this morning. Stay safe and we look forward to speaking with you over the coming weeks and updating you on our next call.

Operator
Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.