Hilton Grand Vacations

Q3 2020 Earnings Conference Call

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CORPORATE PARTICIPANTS

Mark Melnyk – *Vice President of Investor Relations*

Mark Wang – *President and Chief Executive Officer*

Daniel Mathewes – *Chief Financial Officer*

PRESENTATION

Operator
Good morning and welcome to Hilton Grand Vacations Third Quarter 2020 Earnings conference call. A telephone replay will be available for seven days following the call. The dial-in number is 844-512-2921 and enter the pin number 13697043.

At this time, all participants have been placed in a listen-only mode. The floor will be open for your questions following the presentation. If you would like to ask a question, please press star-one 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. If you require operator assistance, please press star-zero. If you're 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 question 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 third 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. You may refer to these slides during the course of our call for our 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 in our 10-Q, which we expect to file after the conclusion of this call and in any other applicable SEC filings.

We'll 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've adopted in 2018. Under ASC 606 we're 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 these revenues and expenses until the period when construction is completed.

To help you make more meaningful peer-to-peer comparisons, you can find details of our current and historical deferrals and recognitions in table T1 of our earnings release. For ease of comparability and to simplify our discussion today, our comments on adjusted EBITDA and our real estates will refer to results excluding the net impact of construction-related deferrals and recognition for all reporting periods.

Finally, unless otherwise noted, results discussed today refer to third quarter 2020 and all comparisons are accordingly against the third 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
Morning everyone. The results we released today improved substantially as we return to a full quarter of operations at the majority of our resorts. As we sit here today, we're optimistic about the future while being realistic about the present. Our optimism stems from the fact that we continue to see improvements in demand for our owners' reservations and pre-paid vacation packages, which is an indication of pent up desire to travel. Additionally, in markets that are unconstrained, the consumer demand is driving a strong resurgence in occupancy in contract sales.

I'm also encouraged that Hawaii, a key market for us, has just restarted to reopen; and we continue to see resilience from our owners who remain committed to HGV and are predisposed to travel. However, this must be balanced with the near-term realities. The path of improvement will depend on local markets where we operate and many of our markets today remain closed or constrained.

For example, Las Vegas and Orlando, our largest markets that represent nearly 40% of our contract sales last year, still have capacity restrictions at their important tourist attractions coupled with reduced air travel. And compared to our owners, new buyers will likely take longer to recover as consumers continue to divide their level of comfort with travel. Most importantly though, we've adjusted as a company and have the financial flexibility to manage through the near-term environment and ultimately capitalize on the long-term opportunities that will return over time.

Now let me take a few minutes to talk to you about what we're seeing in our different markets in consumer segments. Since we restarted operations in late May, we've seen monthly sequential improvements in our key operating metrics. In the markets where we're open, our contract sales have recovered to nearly half of the levels that we produced at those properties last year.

VPGs in open markets improved substantially – up over 80% versus prior year to about $4,200 – and our consolidated six-month forward bookings are tracking at over 60% of prior year levels. While this data is somewhat volatile as our booking and cancellation windows remain shorter than normal, it indicates to us that there's a desire to travel. And cancellation rates, which peaked in the mid-30% range this summer have now fallen to under 10%.

Digging deeper into the trends at our open properties shows that these improvements have varied from market-to-market. Our regional resorts, particularly outdoor oriented locations like South Carolina, California, and Utah have seen a rapid recovery. South Carolina, for example, is trending 95% of contract sales pace they did in the prior year owing to strong closed rate gains and occupancy rates into the 90% range. As a whole, our regional markets have seen similar improvements surpassing last year's contract sales levels in the month of September with strong occupancy rates.

On the other hand, our largest resorts in destination markets associated with local attractions that have capacity restrictions, such as Orlando and Las Vegas, have seen more measured progress. Occupancy levels have improved to roughly 50% in Orlando versus 30% to 40% at opening, and Las Vegas has moved to the range of 40% from 30%. But while they've improved at a slower pace, the appeal of these markets is time tested and we're confident that they will ultimately come back as the local attractions return and air travel normalizes.

One market we're excited to bring back is Hawaii and we think we'll see great demand there. It's an important market for us. In 2019, it represented 22% of our total contract sales. We have nine high-quality resorts in prime locations on Oahu and The Big Island and our tenth resort in Maui is currently under construction and in presales. On October 15th the State of Hawaii officially moved forward with its reopening plan. It was met with a release of pent-up demand from over 10,000 travelers returning on the first day, or about one-third of the normal daily pace in inbound traffic.

We also continue to see notable enthusiasm for Hawaii product from our members as well. In fact, despite having no operating sales centers, Hawaii inventory made up 34% of our inventory mix this quarter versus 37% last year. And a big driver of that stability was our Japanese business, which again, proved to be a key advantage to us this quarter. Our network of regional off-site sales centers in Japan remained operational through the pandemic and has recovered to over 60% of last year's contract sales levels – the majority of it which was Hawaii product.

We'll be reopening our resorts and sales centers as we progress through the quarter and, as a result they're unlikely to contribute to our consolidated results this year. However, we hope to be back to full operating capacity in Hawaii in the first quarter and expect our properties to ramp through the first half of next year and be meaningful contributors again in 2021.

Finally, our urban sales centers remain closed in New York, Chicago, and Washington, DC. These markets accounted for just over 11% of our contract sales last year and we expect they will be the last to recover.

Turning to our customer segments, we had another quarter of strong execution. Our VPGs benefitted from two factors: higher owner mix and improvements in both our owner and new buyer close rates. We expect the segment close rates will trend towards historical levels and drive a moderation in our VPG growth, but we'll continue to see a benefit from a higher mix of owner sales in the quarters ahead. Owner sales were 67% this quarter versus 50% historically and that outperformance will likely continue as new buyer traffic takes longer to recover.

Our financing and club & resort segments continued to provide an important source of stability to the company by generating solid results and cash flow, although we did see a slight decline in our club & resort business due to lower activation fees and member usage fees. Importantly, NOG was 1.9% as we continued to see growth in new buyers that will add to the embedded value of our business for years to come.

As we mentioned before, we revisited our strategic priorities at the onset of the pandemic and we've kept making progress here. We now have a full quarter with implementation of the HGV Enhanced Care initiative and have received great feedback from our guests on the program. Importantly, we haven't noticed any adverse effect from the initiatives on either our sales process or our resort operations, as masks and social distancing have become a commonplace across the globe.

Maintaining our financial health has remained a critical focus throughout the pandemic and we've continued our efforts to fortify our balance sheet and optimize our cash flow. We've found cost savings across all levels of our organization. Some of those have unfortunately required us to make tough decisions around our staffing levels as you likely saw in our recent filing. As a result, we believe we found sustainable cost savings and reset our cost structures to allow us to get back to our pre-COVID levels of EBITDA at a lower level of contract sales.

We've also reexamined our inventory in project spending in light of the new environment, but we're well-positioned through the pandemic and beyond due to the inventory investments we've made over

the past few years in the projects like Ocean Tower and Maui. Due to these efforts, we now believe our adjusted free cash flow will be comfortably positive for the year, which has extended our cushion of available liquidity to 31 months, assuming no further improvements from September trends.

Throughout the pandemic, we kept sight of what's most important, our commitment to our owners and our team members. Our teams have done a great job restarting our operations smoothly both at the resort level and at our member service centers and I want to take a moment to recognize them for their efforts. And we've provided our members with additional flexibility to roll their unused points in 2021 to preserve their value of their membership with HGV.

Our marketing teams have been successful engaging potential new buyers, driving sequential package growth trending at nearly 75% of last year's levels versus only 10% of the prior year back in April. So, it's clear to us that people have the desire to travel, but it's also clear to us that you can't force people to travel until they're comfortable doing so. However, the demand for prepaid vacation experiences gives us confidence that those travelers will ultimately choose to vacation and tour with us.

Looking ahead, our outlook reflects an acceptance that we're going to have to continue to contend with the impact of the virus as consumers define their individual level of comfort with travel. While we're seeing moderate week-over-week and month-over-month improvements, we expect the pace of recovery to vary across different markets. But I'm confident in the long-term strength of our business model and our plan and I remain optimistic about our future.

With that, I'll turn it over to Dan to walk you through the financial results. Dan?

Dan Mathewes
Thank you, Mark and good morning everyone. As Melnyk mentioned in his introduction to our call, our results for the quarter included $13 million in sales deferrals and backing imported revenue and net deferrals of $8 million impacting both adjusted EBITDA and net income. All references to consolidated net income, adjusted EBITDA and real estate segment results on this call for the current and prior periods will exclude the impact of deferrals and recognitions. A complete accounting of our historical deferral and recognition activity can be found in Excel format on the financial reporting section of our Investor Relations' website.

Let's review the results for the quarter. Total third quarter revenue was $221 million, reflecting the clients across our business segments, due to the ongoing impact on global travel from COVID-19 pandemic along with the absence of resorts in several major markets where we haven't yet resumed sales operations. Q3 adjusted EBITDA was $27 million, as our financing resort and club segments generated positive EBITDA, with flat EBITDA at our rental segment and a slight decline in real estate.

Our EBITDA was also impacted by $3.8 million of one-time charges primarily due to restructuring and COVID-related expenses during the period. In addition, as we laid out in our press release, there were another of $6 million of COVID-related items that were not adjusted from our EBITDA, including a $7 million benefit from employee-related credits offset by a $1 million loss of current transaction fees that were refunded during the quarter for reservation charges such as with property closures.

Net income was $1 million and diluted earnings per share was $0.02 compared to net income of $58 million in diluted earnings per share of $0.67 in the third quarter of 2019. Within real estate, Q3 contract sales were $117 million, or one-third of the prior year reflecting operations resuming at roughly three quarters of our resorts. For the quarter, tours were down 75% and VPGs grew by 25%. Our mix of owner contract sales remained elevated this quarter at over two-thirds of the total.

Our recovery was steady over the course of the quarter with absolute number and year-over-year growth rate of our tour flow improving sequentially each month. Close rates were once again up in each of the months for the quarter for both owners and new buyers, reflecting solid execution in driving our strong VPG. As we progressed through the quarter we saw an expected normalization of close rates from the elevated levels seen in Q2. We expect that trend to continue, although we anticipate VPG will settle at a higher level than pre-COVID in the short-term, owing to a shift towards higher VPG owner sales.

Our fee-for-service mix for the quarter was 57%. On the consumer lending side, our provision for bad debt was $12 million and our overall allowance on the balance sheet was $217 million, or 17.7% of gross financing receivables.

SG&A was $67 million, reflecting both fixed expenses as well as a full quarter of variable expenses as we resumed sales operations. Real estate margin was a loss of $1 million. In our financing business, third quarter margin was $27 million with a margin percentage of 67.5% versus a margin of $29 million and a margin percentage of 67.4% last year. Margin was lower based on the declining receivables balance versus last year limiting portfolio income, along with higher interest expense associated with the securitization completed in Q2. Our gross receivable balance decreased to $1.2 billion. Our average down payment year-to-date is 11.8% and our portfolio average interest rate increased to 12.6% from 12.4% last year.

Over the past three months, we've seen an improvement in our delinquency rate to 3.35% of our receivables portfolio versus 3.5% at the end of the second quarter, but it is up from 2.5% at the end of 2019. Our annualized default rate has increased to 5.96% versus 5.48% at the end of the second quarter and 5.14% at the end of 2019. The increase remains consistent with our expectations of seeing upward pressure on both our delinquencies and defaults over the near-term as we continue to cycle through the pandemic. Though we still believe we are adequately reserved at this time, we will continue to monitor our portfolio trends closely. The performance of our loans on a payment deferral has been strong. Of the owners who utilized a deferment across our entire platform, which accounts for $27 million in loan balance, or 2% of our portfolio, just under 80% are current today.

Turning to our resort and club business, NOG for the 12 trailing months was 1.9% and we grew our member base to over 327,000. Revenue of $39 million was down 13.3% from the prior year, driven by lower transaction fees from reduced member activity as well as additional one-time fee waivers and refunds related to COVID-19. Margin for Q3 was $30 million with a margin percentage of 76.9% versus a margin of $34 million and a margin of 75.6% last year.

Rental revenues were $20 million for the quarter reflecting a resumption of operations and the realities of the global travel that is still feeling the impact of the COVID pandemic. Expenses in the quarter were $24 million and were driven by expenses associated with Hilton Honors point conversion activity and developer maintenance fees. Bridging the gap between segment-adjusted EBITDA and total adjusted EBITDA, third quarter corporate G&A was $15 million, down $5 million, or 25% versus the prior year, reflecting the benefits of our cost savings program, and license fees were $11 million.

Regarding our cost savings, in the first quarter we moved quickly to examine our cost structure and adapt to a rapidly changing business environment, including process improvements, spending cuts, temporary furloughs, and unfortunately permanent headcount reduction. The net result is that we believe we've identified $20 million to $25 million in savings across the organization that are recurring in nature.

As Mark mentioned earlier, Hawaii recently reached a major milestone in their reopening progress by

removing the quarantine requirement for COVID-negative travelers. While we are excited to be reopening one of our largest and most important markets, in light of the staggered progression of the openings and the associated ramp period, it is important to note that we do not anticipate Hawaii distribution centers to be meaningful contributors to our contract sales in Q4. Thus, our fourth quarter is expected to show only continued modest sequential growth in our operating metrics.

Our adjusted free cash flow in the quarter was a net use of $99 million which included inventory spend of $39 million and cash use from non-recourse debt pay down of $90 million owing to the shift in timing of our strict securitization into Q2 from our typical third quarter timing. For the year-to-date, our adjusted free cash flow was $156 million after inventory spend of $108 million. As a reminder, our inventory budget for this year was approximately $400 million and we now expect to spend slightly less than $200 million.

Given this level of inventory spend and the expectations that Q4 will show modest sequential growth in operations, we now anticipate that we will have positive adjusted free cash flow for the full year of $40 million to $50 million, which compared to our prior expectation of achieving roughly breakeven for the year.

We continue to maintain a strong balance sheet with low leverage and ample liquidity. Assuming that we saw no further improvement in real estate or rental business from September levels, we estimate that we would have 31 months of available liquidity. As of September 30th our liquidity position consisted of $625 million of unrestricted cash, $39 million of availability under a revolving credit facility, and $450 million of capacity in the warehouse. We currently have $100 million in timeshare receivables available for collateralization.

On the debt front, we had roughly $1.3 billion in corporate debt and non-recourse debt balance of $837 million.

Turning to our credit metrics, at the end of Q3 our net leverage and first lien net leverage with covenant compliance purposes stood at 2.14 times and 1.11 times respectively. Our interest coverage ratio for the covenant compliance purposes at the end of the quarter was 7.17 times.

We will now turn the call over to the operator and look forward to your questions. Operator?

QUESTIONS AND ANSWERS

Operator
Thank you. Again, if you would like to ask a question, please press star-one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star-two if you would like to remove your question from the queue. And for participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys.

Our first question is from Jared Shojaian with Wolfe Research. Please proceed.

Jared Shojaian
Hi everybody. Thanks for taking my question. On Hawaii, Dan, I appreciate your commentary that you're not expecting a meaningful contribution in the fourth quarter from Hawaii sales centers. But can you just talk about what you've seen since the quarantine was removed? What have you seen with arrivals? What do you have on the books today versus this time last year?

And then, I know you've still been selling Hawaii at other locations and you've had some success with

that. Can you give us a sense for what Hawaii contract sales are currently run rating at right now on a year-over-year basis with obviously not being able to go to Hawaii in the third quarter?

Mark Wang
Yes. Jared, this is Mark. I'll take part of that and I'll let Dan take part of that question. You had a few questions in that question, so we'll try to connect on everything. But I think, when you think about Hawaii, first of all, excited that the quarantine enforcement has finally been lifted and that the state reopened on the 15th for domestic travel. We're still waiting to hear on Japan inbounds, but recent indications suggests that the state is probably going to be opening up for Japan visitors sometime in November, so, happy about that.

We also think Hawaii's going to be our next catalyst for the recovery as we enter '21. We've talked about it numerous times, but we have amazing assets in prime locations there. And historically Hawaii's been one of our highest demand markets for both our U.S. and Japanese members. So, as far as what we have going on there right now, we have a few very small properties that are open but really no sales going on in Hawaii right now. The plan is that we plan to open up our sales centers on The Big Island by mid-November and that we're going to open all of our properties and sales centers in mid-December in Oahu.

So, I think you mentioned Japan and Hawaii inventory. We are having great success and had great success in Japan during this crisis; they never really closed down, though the business did drop back considerably early on when the pandemic first started. But we mentioned, I think, in our prepared remarks 34% of our sales for the quarter were Hawaii compared to 37% last year. And that really has a lot do with the work that our Japanese teams are doing. This month in October we're trending at about 75% prior year's levels. So, that's looking really good.

As far as forward-looking bookings, for next year we're showing about 70% on the books this same time last year, and I know we've had about a 15% pick up over the last four weeks as people have gotten a better line of sight of when we think we're going to be opening. I don't know. Are there anything else, Dan, that you want…

Dan Mathewes
Yes. I think just to quantify part of your question on Hawaii, Jared, if you look back to Q2 obviously as we were coming out of a shutdown scenario we did total contract sales of $35 million. Just over $10 million of that was associated with Hawaii. If you look at Q3, that number has jumped to just south of $40 million, and we would anticipate that to be probably a hair better because we do believe operations will be open to some extent in Q4. So we believe they will be slightly better than that in Q4. But compared to run rate historically prior year, you're looking at Q2 and Q3 being close to $130 million. So, still substantially down but obviously making traction in going in the right direction.

Mark Wang
Yes. And then I'd just add one more thing. I think when you think about Hawaii, obviously, airlift is really important and from what we're seeing, the airlines are starting to get their airlift back in place. And so there's a lot of choreographing that goes on when you open up Hawaii versus other markets for us because of this flying component that you have to deal with.

The other thing you have to think about is a number of our biggest resorts and our properties coexist on campuses that also have major hotel assets that Park Resorts owns. So, we have to working conjunction and get aligned with them around staffing and the such. So, generally we think Hawaii is going to—we're happy it's finally going to reopen. We thought it was going to be reopened late in Q3, so it would benefit us in Q4. It got pushed back but at the end of the day, we're just pleased that it's

going to reopen and hopefully, the process they've put in place is going to endure and create a very safe environment for visitors that are going to Hawaii and we're very optimistic that our business is going to bounce back strong there.

Jared Shojaian
Okay. Thank you. That's very helpful. I think you got all that from my convoluted question. Just to switch gears here, can you talk about how you're thinking about inventory spend for next year? And I know a lot depends on the demand environment, but is it fair to think that next year is not going to be a free cash flow year and then, by 2022 you're starting to just meaningfully ramp on free cash flow? Is that the right way to think about it? Anything you can share there?

Dan Mathewes
Hi, Jared. It's Dan. It's a great question and I think we've talked about this all year. I mean, just to take a step back as you know you've heard us say it on two calls now. The original amount that we expected to spend in 2020 was north of $400 million. We've contracted that below $200 million. What I want to emphasize is that contraction is not just moving it from 2020 to 2021. That contraction is really putting things to the side and allowing us to analyze and make the best choice when it comes to the course of action on that inventory spend. The most notable example of that is Ka-Haku, right? We've had a contraction in Hawaii in particular on sales and now the question is when do you need Ka-Haku which is a Waikiki sequel to actually come online? And we'll continue to analyze that.

When you fast-forward to 2021, the flexibility that we saw in 2020 is not the same in 2021. In 2020 our contractual obligations, i.e., the just-in-time projects that we had, were roughly $25 million. When you look at 2021 those contractual obligations are over $200 million. Now, the thing to emphasize here is they are just-in-time projects. So, from a capital efficiency standpoint they have proved out to be very good for us. In particular, as you can imagine, right now we have developers spending money on projects, most notably The Central in New York and Sesoko in Japan that otherwise would be on our balance sheet. So, we have had the benefit of that, but what you will see in 2021 is those obligations will start to kick in. So, that flexibility and contracting inventory spend does come down. And like I said, it's roughly $200 million in contractual obligations in 2021.

When it comes to free cash flow, it's all about the recovery. How does 2021 recover versus where we are in 2020? We see some nice trends now. Some of our larger markets are on a steady march, although albeit it slower than we would like, but on a steady march to recovery. Hawaii is just about to open up so it's really going to be dictated around the recovery itself on what 2021 shows.

I think I'm trying to give you a lot of color. We're not trying to give specific guidance on 2021, but hopefully that context is helpful.

Jared Shojaian
Yes. No, that's helpful. I appreciate it. Maybe just to quickly follow up on that. I mean, if we assume this recovery that we're seeing here continues and you extrapolate that out through all of 2021, so that 2021 is kind of a transition year, you're still far below peak levels but we're moving in the right direction. We're improving.

Under that scenario, should we be assuming that next year is not a free cash flow year? I guess I'm really just trying to help set that expectation on how you're thinking about it and then by 2022, assuming this recovery is just continuing, that you start to see that meaningfully build again. Under that context is that how we should be thinking about it?

Dan Mathewes
Yes. So to say it a different way, if you were to look at what a lot of analysts are saying about the recovery in 2021 and build in that contractual and the not only contractual because keep in mind, there's contractual inventory payments and then there's also other projects that are under our control admittedly, but they are also further inventory spend--projects like Maui and Ocean Tower phase 2. There's flexibility there if the recovery then plays out as we expect, but if you go with analyst consensuses so to speak, and you build in that kind of inventory spend, you are looking at an adjusted free cash flow of neutral to down year with the path really building in 2022.

Jared Shojaian
Okay. Super helpful. Thank you very much.

Operator
Our next question is from Stephen Grambling with Goldman Sachs. Please proceed.

Stephen Grambling
Hi. Thanks for taking the questions. Two quick ones. First, I know you referenced that with the cost cuts that you've announced you feel like you can get back to call it prior levels of EBITDA without getting to prior levels of contract sales. Is there any more that you can provide in terms of quantifying that and perhaps I missed it earlier?

And then, the second question which is unrelated is just if you can give any more details on what you're seeing in terms of the demographic of new owners arriving. Is that similar or different to what you saw pre-COVID or are you seeing truly a different type of customer base, younger, maybe coming in?

Dan Mathewes
Great questions. I will take the first ones and then I'll turn it over to Mark on some of the demographic information. So, we did say in our prepared remarks that we have done a lot. We have taken out various layers. As we sit here today and you saw last week it might have been the week before where we filed an 8-K disclosing that we did do a reduction in force, but over the course of 2020 we took out a significant amount of costs. Initially it was temporary furloughs. Now we've gone to a reduction in force. We also still have an excess of 2,000 individuals furloughed today, but based on what we've seen today and the course of the recovery we see now, out of all the actions we've taken, we believe that there's between 20 and 25 in recurring cost savings associated with that reduction in force and other ancillary expense items.

Mark Wang
Yes, Stephen, Mark. On the demographic side, if you look at Q3, Millennials made up 26% of our new buyers, Gen-X 38%. So it's approximately 65% of our new domestic buyers in Q3 fit in that Gen X/Millennial age group.

Stephen Grambling
And did that move materially year-over-year? And also, I guess with the restraints on the sales centers, are you seeing any changes or making any changes in terms of thinking through digital sales?

Dan Mathewes
Yes. No, good question. Well as far as the year-over-year PTL, the Millennials continue to grow as Gen Xs do and boomers are basically falling off. And we're seeing that sequentially really over the last three or four years. And so Millennials are building and Gen Xs are building.

As far as digital sales go, the teams have done a lot of good work around innovating on the digital side.

I just got a report in this morning that we've done over $1 million in the last couple months in Japan on a peer virtual platform that we've put in place. We're also using a lot more technology and our club direct capabilities are improving. We started seeing the benefit of selling Maui that way.

Direct sales represented about $60 million of our sales last year. We have now recovered to approximately about 70% of what we were doing last year. So, that part of the business is recovering well. And while it's still a minor piece of our business, our capabilities are growing, and we're excited about what that will mean for us in the future.

Stephen Grambling
Great. Thanks so much.

Operator
Okay. Our next question is from Patrick Scholes with Truist Securities. Please proceed.

Patrick Scholes
Hi, yes. Good morning everyone. My first question concerns Orlando, so one of your larger markets. We heard yesterday from a competitor how Orlando pre-bookings for next year are really coming on very strong. Curious what you folks are seeing in that regard. Thank you.

Mark Wang
Yes, Patrick. We're seeing the same thing, and in fact just looking at the numbers this morning we have nine steady weeks of improved pace in Orlando and in Vegas. So, we're seeing improved pace in those markets and we expect as the capacity restrictions diminish in this market, we'll see more and more visitors come here. So, Orlando's our tried and true market. It's going to come back. It's just a matter of time, but we're seeing some very positive trends of late.

Patrick Scholes
Okay. Good to hear. And then my next question hopefully you can answer this. Again, it's a bit of a follow up to the first question that was asked today. On your earnings release you noted that owned inventory represents 80% of your total pipeline while only 32% of that owned inventory pipeline is currently available for sale. Where would you expect that percentage by the end of the year to be, that 32%, and how would that trend into 1Q?

Mark Wang
From a pipeline perspective I wouldn't see significant movement there, Patrick. From a sales mix perspective as the owned inventory comes online, you'll naturally see that compress. So that 57% should naturally come down as you roll into 2021. Depending on the pace of recovery, we would also see it fall and I would imagine or we would expect it to fall below 50% in 2021, depending on what the recovery plays out.

I think what you see here today where we are still in the high 50s on a fee-for-service mix is really speaking to some of the locations that have performed really well in a COVID environment, such as Myrtle Beach, which is a fee-for-service center if you will, but hopefully that lays that out for you pretty well.

Stephen Grambling
Okay. Thank you. That's it for me.

Operator
Our next question is from Brandt Montour with J.P. Morgan. Please proceed.

Brandt Montour
Good morning everyone. Thanks for taking my question. I was wondering if you could maybe give us the year-over-year contract sales growth by month in the third quarter.

Mark Wang
Yes. So hi, Brandt. This is Mark. What we saw, sales growth of though we didn't have sales growth, but if you look at the performance on a sequential basis, in markets that we were open we were down 59% in July, down 58% in August, and down 47% in September. So, that's based on the markets that we were open in.

Brandt Montour
Great. Thanks. And then just, you gave us a great snapshot on your cancellation rates now versus cancellation rates in the spring. And I was just curious and I hate to split hairs and ask a really short-term question, but just because we're sort of in the first or second stages of this broader uptick in infection rates and potentially the mobility slowing down, has it gotten worse in the very near-term I guess is that I'm asking?

Mark Wang
Yes. No, great question. I can tell you that we're just not seeing the same correlation between cancellation and spikes in COVID that we did over the summer. When we look at our own arrivals on the books, they remain strong indicating that there continues to be strong demand. I think, when you look at our marketing package and our new buyer pipeline, the majority of the consumers who are making changes or travel dates with us are rebooking for a later period of time. So right now, again, obviously there's a lot of activity.

There's a lot of uncertainty out there around the infection rates, but we're not seeing the same type of spikes in activity that we have in the past. And I think part of it is just people are adapting to this situation and I look at it either people are looking to travel or they're not looking to travel right now. And those that are looking to travel are adapting to ways to travel safely.

When you look at the entire sector, the travel sector, I think the entire travel sector is doing a really good job from the airlines to…I know our properties in the Hilton brands of collectively working together. And I think that is making a difference in the consumer confidence to travel. But I think in the near-term absent containment the virus, I think the pretesting requirements like we're seeing in Hawaii could also encourage a lot of people to start flying.

So, there's a lot going on. Everybody's working together collectively to make travel, especially leisure travel open up again. And so, we're going to have to watch it closely. You know, the reality is this is a dynamic situation, but right now I can't say that we're seeing any spikes right now. Sorry for the longwinded answer but a lot to think about there.

Brandt Montour
Yes, very helpful. Thanks a lot everyone and good luck.

Mark Wang
Thank you.

Operator
Our next question is from David Katz with Jeffries. Please proceed.

David Katz
Hi. Morning and thanks for including my question. Number one I just wanted—and I apologize if you've touched on this a bit—but I wanted to get just a clear update on your capital allocation philosophies.
There's always discussion around the company in terms of returning capital versus not. And then I have one quick follow-up.

Dan Mathewes
Hi, David. It's Dan. Look, from a capital allocations strategy, we've been fairly consistent on this. We've talked about investing in inventory. We've clearly done that. We're in the process of that and you can see us further taking—we took a pause in 2020 and reanalyzing what the best way to use that inventory spend is. The second would be return the capital to shareholders, and obviously, M&A is always on the books. It's always interesting to me when we report a quarter where contract sales are down quite dramatically and people want to talk about capital allocations. So, we're focused on it. I wouldn't look for us to be in the market repurchasing shares in the immediate future, but I think that lays out our plans. Very consistent.

David Katz
Thank you for that. Go ahead. Sorry.

Dan Mathewes
No, sorry. I just wanted to say very consistent with how we've always spoken about it.

David Katz
That's correct and I was not trying to imply that you should be in the market buying back your stock as necessarily as a choice avenue. From a much longer-term perspective, as so much of our coverage is focused on attracting younger and younger consumers, do you have any updated thoughts on shorter duration product offerings or any alternative structures that might attract that group in a more fulsome way?

Mark Wang
Yes. No, but great question. I think we've mentioned it in the past that we are experimenting with some shorter-term product and, as you can imagine we're very focused on getting the business back in order and getting the trajectory back in order so that the focus has really been around our core business. But we believe that there's a great opportunity to expand our offerings and introduce term product and some of that's being tested right now as we speak, but it's really too early to provide any guidance especially in this reduced volume environment. But we will make sure to keep you posted as we move forward.

David Katz
Appreciate that. Thank you very much.

CONCLUSION

Operator
We have reached the end of our question-and-answer session, but before we end, I would like to turn the call back over to Mark Wang for closing remarks.

Mark Wang
Well, thanks everyone for joining us this morning and I know I mentioned it my prepared remarks, but I

want to give another special thanks to all of our team members for their hard work and dedication to providing our guests with a safe and memorable experiences when traveling with us. We look forward to speaking with you over the coming weeks and updating you on our next call. Have a great day. Thanks.

Operator
Thank you. This does conclude today's conference. You may disconnect your lines at this time.