DEPARTMENT OF BUSINESS AND MANAGEMENT

Chair of Structured Finance

Leveraged Buyout in the Hotel Sector: the analysis of the Hilton Hotels Acquisition Made by The Blackstone Group

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Introduction

The financial markets are continuously changing, characterized by volatility, uncertainty and, due to the 2008 crisis, one of the less reliable sectors to operate in has become the *real estate market*. For that reason, the aim of this work is to analyze and to better understand how The Blackstone Group acquired Hilton Hotels in 2007. We will take a deeper look at the operation and its characteristics, at the operational improvements, at the financial statements, as well as the exit strategy. In order to do so, we have to comprehend the environment in which the operation has taken place, the core values and the history of the firms involved in the process and the main characteristics of the *Leveraged Buyout*. Another aspect we have to take into consideration is the Hotels' Industry and the Hilton's competitors.

So, this work will be split into three main sections: the first one will be about the description of the companies taking parts in the operation, the sector analysis, the competitors' identification and the use of the leveraged buyout in the North-American market.

The second section will deal with the operation, the analysis of the financial statements, the composition of the offer, the price paid for the acquisition, the evolution of the companies works and the sources of financing.

The last part of this work will be focused on the exit strategies and the future scenarios. Furthermore, it will include a judgement on the operation, covering all its shades and its final outcome.

The whole work is developed accurately, after the collection of all the necessary information, in order to be able to discuss this subject: the goal is to make it *comprehensible, well-defined, logical* and *complete*.

First Section: Actors and Environment

Corporates don't act alone, the environment in which they exist makes the difference and, sometimes, it assumes more importance than the operating activity belonging to the business itself.

For this reason, in order to understand the context in which this renowned buy-out has taken place, we have to take a deeper look at the history and the values of the actors.

Hilton Hotels: History

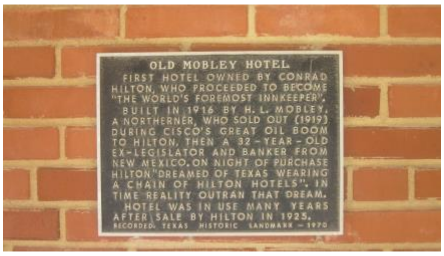

Figure 1: Mobley Hotel Plaque, Wikimedia Commons

The *Hilton Worldwide* was founded in 1919 in the USA. The first hotel had been bought by Conrad Hilton and it was called "The Mobley". It was located in Cisco, Texas and the price paid for the entire building was of about 40.000$. In 1925 Conrad Hilton decided to give its last name to the hotels he owned, and its aim was to create a hotel franchising that had to be the best in the North American state of Texas.

Figure 2: Old Mobley Hotel, Twitter, Hilton Foundation

After that, the decade of the *forties* was noteworthy for the Hilton Worldwide Company. Other than listing in the New York Stock Exchange in 1946, in 1943 the HW turned into the first American Firm to operate in the hotel sector and it already had several hotels in New York, some of them very known such as the *Roosevelt* and the *Plaza.* At the end of that decade, Hilton was the first hotel corporation to have accommodations in *Porto Rico* and, moreover, in 1949 the firm acquired one of the most popular hotels in New York, the *Waldorf Astoria*.

For these reasons Hilton is considered the pioneer of the hotel business among USA and so, the world. In the 50ies, Conrad Hilton introduced the air conditioner in its rooms and developed, alongside with the management of the firm, a centralized reservation system. Together with these innovations, the Hilton hotel chain was enriched by the acquisition of other properties in Europe and San Francisco.

In 1964, while the hotels portfolio was continuously enlarging, the firm was split into two main divisions: *Hilton International* and *Hilton Hotels Corporation.*

The first one was created in order to manage the properties that were outside the US efficiently, while the latter detained the ownership of all the ones in the US soil. In 1967 Hilton International was sold to *TransWorldAirlines*, a company that was seeking synergies from the interconnections between the hotel and the air transport sector.

In the 70ies Conrad Hilton passed away and, in the same years, Hilton bought the *Casino Hotel Flamingo*, diversifying the business by adding the *casino sector* to the *hospitality* one.

The eighties were characterized by the transfer of the ownership of Hilton International from *TransWorldAirlines* to the holding *United AirLines* as a first stage and subsequently to *LadBrokes PLC*[1].

In 1982 the *Conrad Hotels* was founded, a new company in the group created in order to offer a network of luxury hotels in the main destinations all around the world. The evolution of the company never stopped during these years: in 1987, the still functioning fidelity program *HHonors* was introduced, granting rewards to clients based on miles and bookings made with Hilton.

In 1990 the *Hilton Garden Inn* was founded, starting with 4 new hotels. Nowadays it counts almost 500 inns. Moreover, the development of the world wide web lead the management to open their first website in 1995. In 1996 Stephen Bollenbach was nominated CEO[2]: he had several experiences in big companies, such as Disney, where he worked as CFO, and Trump Organization, where he was responsible for the casino sector.

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[1] *Ladbrokes PLC in 1987 changed the name of Hilton International into Hilton Group after a litigation with United AirLines.*

[2] *For the first time in Hilton history, the CEO does not belong to the Hilton family but he acted alongside with Barron Hilton, a member of the family.*

This nominee led the *Hilton Hotel Corporation* to achieve great results in the first years. The company was recovering the prestige it had gained under the *Conrad Hilton* administration and the financial ratios were florid. The revenues increased by 2,3x and EBITDA by 3,5x: these improvements, in terms of financial indicators, made the company noticeable and people started booking at Hilton again, since it was considered the best hospitality company in the whole world. The room offer registered an increase of 238%, corresponding to 350.000 units. Despite that, after 09/11 the whole hotel sector took a bad hit, losing almost 50% immediately. Hilton's EBITDA fell down by 20% at the end of the year 2001 and the stabilization phase continued until 2003. In any case, in the first years of the new millennium, Hilton expanded its business again by creating the *Hilton Worldwide Resort,* a branch offering luxury properties in exotic locations. It was in 2006 that *Hilton Hotels Corporations* bought back *Hilton International*: the firm was reunited again for the first time since 1967. The price paid for the operation from *Hilton Hotel International* to the English counterpart *Ladbrokes PLC* was 3,3 billion pounds.

2007 is the crucial year during which the subject of this thesis takes place. *Hilton Hotels Corporation* is acquired by the American Private Equity Group *Blackstone.* Cristopher Nassetta is nominated new CEO in the same year and he is the maker of the expansion process, in which Hilton is still involved. The company became private with the 2007 acquisition, but in 2013, six years later, it had its second IPO at the New York Stock Exchange (NYSE) with the name of Hilton *Worldwide Holdings Inc.*

Hilton Hotels & the Hotel Industry

At present, Hilton is world leader of the sector. It owns 14 brands, more than 5000 properties with 848.000 rooms in 105 countries, it welcomed 160 million guests and in 2017 it made revenues for more than 9 billion dollars.

As we can see from *Figure 3,* the 14 brands owned by Hilton are diversified across chain scale, it is largely internationalized and for these reasons it has different competitors for each branch of the company. We can observe that, while at the beginning Hilton was focused on the luxury market, as the years go by, the firm has diversified its business by including in its portfolio brands such as the *Hampton Inns* that serves the *Upper Midscale*[3]and that counts the highest number of room in the entire conglomerate.

Our Brand Portfolio

The goal of each of our brands is to deliver exceptional customer experiences and superior operating performance.

		December 31, 2017				
Brand[(1)]	Chain Scale	Countries/ Territories	Properties	Rooms	Percentage of Total Rooms	Selected Competitors[(2)]
Waldorf Astoria Hotels & Resorts	Luxury	12	27	9,579	1.1%	Four Seasons, Mandarin Oriental, Peninsula, Ritz Carlton, St. Regis
Conrad Hotels & Resorts	Luxury	24	34	10,709	1.3%	Fairmont, Intercontinental, JW Marriott, Park Hyatt, Sofitel
Canopy by Hilton	Upper Upscale	2	2	287	—%	Hyatt Centric, Joie De Vivre, Kimpton, Le Méridien
Hilton Hotels & Resorts	Upper Upscale	88	578	211,423	24.7%	Hyatt Regency, Marriott, Renaissance, Sheraton, Sofitel, Westin
Curio A Collection by Hilton	Upper Upscale	15	48	10,548	1.2%	Autograph Collection, The Unbound Collection
DoubleTree by Hilton	Upscale	41	520	123,773	14.5%	Crowne Plaza, Delta, Holiday Inn, Hyatt, Radisson, Renaissance, Sheraton
Tapestry Collection by Hilton	Upscale	1	4	467	0.1%	Ascend Collection, Tribute Portfolio
Embassy Suites by Hilton	Upper Upscale	6	245	57,216	6.7%	Courtyard, Hyatt Regency, Marriott, Renaissance, Sheraton
Hilton Garden Inn	Upscale	37	771	111,438	13.0%	Aloft, Courtyard, Four Points, Holiday Inn, Hyatt Place, Springhill Suites
Hampton by Hilton	Upper Midscale	21	2,338	237,334	27.7%	Comfort Suites, Courtyard, Fairfield Inn, Holiday Inn Express, Springhill Suites
tru by Hilton	Midscale	1	9	911	0.1%	Best Western, Comfort Inn & Suites, La Quinta, Quality Inn, Sleep Inn
Homewood Suites by Hilton	Upscale	3	451	51,305	6.0%	Element, Hyatt House, Residence Inn, Staybridge Suites
Home2 Suites by Hilton	Upper Midscale	2	204	21,015	2.5%	Candlewood Suites, Hawthorn Suites, TownePlace Suites, WoodSpring Suites
Hilton Grand Vacations	Timeshare	3	48	8,101	0.9%	Hyatt Residence, Marriott Vacation Club, Vistana Signature Experiences, Wyndham Vacations Resorts

(1) The table above excludes five unbranded properties with 2,009 rooms, representing approximately 0.2 percent of total rooms. HGV has the exclusive right to use our Hilton Grand Vacations brand, subject to the terms of a license agreement with us.

(2) The table excludes lesser known regional competitors.

Figure 3: Hilton Hotel's Brands, Hilton 10-K report, 2018

[3] *A definition of this chain scale will be provided in the next paragraph.*

The Hotel Industry

The Hotel Industry is characterized by its cyclical nature and this business is categorized as one of the most influenced by regulations. Today 78% of Hilton Worldwide's properties are on the American soil, so we will focus on the North-American region. Hotels, generally, compete for customers basing their competitiveness on the facilities provided, the service level, the location of the properties, on the brand reputation and ultimately on loyalty programs.

The main competitors for Hilton are: *Accor SA, Hyatt Hotel Corporation, Marriott International* and *Intercontinental Hotels Group (Bloomberg, 2018).* On the table below, we have an overview of some central figures of Hilton's key rivals.

Table 1: Competitors Performances, Hoovers 2017

	Revenues	Gross Profit	EBIT	Net Income	Diluted EPS
Hilton Worldwide	$9,140	$7,854	$1,372	$1,259	$3.85
Accor SA	$2,320	$1,269	$585	$528	$1.68
Hyatt Hotels Corporation	$4,685	$681	$302	$249	$1.97
Marriott International	$22,894	$3,702	$2,518	$1,372	$3,61
Intercontinental Hotels Group	$1,784	$1,176	$829	$592	$3.05

As we can see from the table, Hilton, together with Marriott, dominates the *Hotel Industry* in terms of revenues. Moreover, it is visible that Hilton has a balanced control over expenses since the Revenues are eroded by expenses only for approximately 10% compared to the competitors that register costs for at least 32%. The Gross Profit, the Operating Income and the Net Income generated are remarkable accordingly.

The Hotel Industry is to be considered peculiar also for the metrics used in order to calculate the value and the potentiality of a firm. The *Key Performance Indicators (KPI)* more common in this field are: The *Occupancy*, the *Average Daily Rate* and the *Revenue per Available Room.*

Occupancy: represents the number of rooms sold over the total of room available for an hotel or for the group of hotel owned by a company. Hilton, such as other big companies, uses this metric in order to measure the demand for the rooms in certain periods.
It is also used as an auxiliary KPI in the calculation of the Average Daily Rate.
Average Daily Rate (ADR): represents the revenues given by room sold over the total number of room sold in a certain period. This metric is useful in order to understand the average income for room in the big companies such as Hilton. Moreover, ADR provides valuable information on the pricing environment, on the competitors and on the nature of the customer base.
Another important feature belonging to the ADR is the capacity to grant information about the income generation related to different types of clients[4].
Revenue Per Available Rooms (RevPAR): This is the most common KPI in the Hotel Industry and it is obtained by multiplying Occupancy and ADR or dividing Total Hotel Room Revenue by total number of rooms available. It is a major indicator for performance and it is useful for comparing the results of a company with the one of a competitor or to compare revenue on different periods for the same hotels.

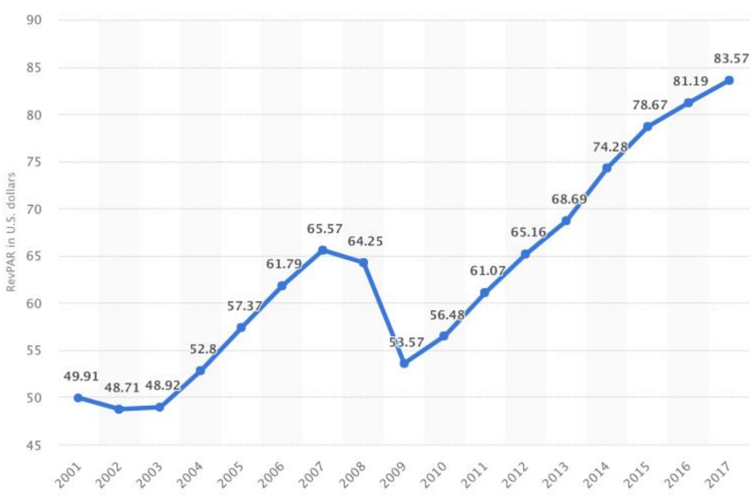


Figure 4: Average RevPAR Trend in the US, www.statista.com, 2018

[4] *NB: Changes in prices and so, on ADR, have a deeper impact on revenues compared to changes in the levels of occupancy.*

The RevPAR alongside with the ADR had risen from 2001 until 2007, year during which the crisis has verified. In the two following years, the Hotel Industry has registered a decrease in these KPIs and it took 5 years to get back to the values of 2007. By the way, after 2012, the industry shows a very positive trend. These have made Hilton profitable and the investors attracted to the sector.

Another important subject regarding the Hotel Industry is the *chain scale*, since it represents the client basin for the specific properties or hotel franchising.

There are mainly 6 categories of chain scale:
Luxury: The rooms are comfortable and large, the hotels offer several services such as SPA, conference centers, concierges and shuttles. The prices, and so, the ADR are over 190 USD per night.
Upper Scale: The rooms are similar to the luxury ones, but the ADR is in the range of 130 to 190 USD.
Upscale: Same kind of rooms as before, but less services and the ADR is between 105 and 130 USD per night.
Upper Middle Scale: Other than the rooms, other services are offered such as swimming pools, restaurants and 24/7 vending machine. ADR is in the range of 85 to 105 USD per night.
Midscale: It consists in minor and less pretentious rooms; few services are offered (e.g. external swimming pool) and the ADR is between 60 and 80 USD per night.
Economy: Simple rooms, almost no services offered, ADR is lower than 60 USD per night.

Hilton’s Business Units

Owned and Leased Hotels: 61170 rooms are distributed by hotels owned directly by HW or managed through leasing agreements, generating revenues from lodging, meals, SPA and recreation as well as conference activities and others. This portfolio of hotels has the potential to be sold with added value, in line with what management is doing with the sale of iconic properties such as the *Waldorf Astoria* in NY for 1.95 million Dollars in October 2014.

Thus, prior to selling Waldorf NY to HW's HW portfolio, it had 10 properties that accounted for 56% of the total EBITDA of owned hotels associated with hotels owned by the company in locations such as New York, London, Chicago, Sao Paulo, Sydney or Hawaii. The sale of these assets and the reinvestment in other properties with the amounts coming from the sales that generate more cash flow than the previous situation was one of the objectives initially detected by Jonathan Gray, responsible for the Real Estate segment of Blackstone, when buying the Hilton Hotels Corporation as a value-enhancing factor.

HW Holdings owns 73 hotels and resorts in almost 30 different countries and grants 22,000 rooms in which it has invested more than 2000 million dollars since the management of the Blackstone Group bought the firm in 2007. At the time of the SIPO, EBITDA in this segment had grown 10% per year since the problematic phase that had its peak in 2009.

Managed hotels: The 208,235 rooms and 656 properties under this format are managed by HW and that generates base fees resulting from the total sales of hotel units in the segment. Moreover, there is a variable component associated with the performance of these establishments. These agreements have a larger variable component outside the US, with costs reimbursed by hotel owners. The hotels under the managed scheme normally generate for the brand fixed fee called base fee, which in the case of HW was 3% of the total revenues generated in hotels under this scheme in 2013, and there is also a variable remuneration called incentive fee, which is about 10% of the incentive income. These contracts usually have a validity period of 20 to 40 years.

Franchising: 625,674 rooms covered by the franchise agreements: after an initial payment to HW for the entry of the hotels into the company's portfolio, it follows a base compensation as a percentage of sales of the units under this scheme, hotels with insignia with a value proposition return to HW a percentage of other revenues such as recreation and catering sales, as well as a general expenses such as IT, promotion or reservations. This type of agreement has a standard duration of 20 years for new hotels, which can be reduced to 10 years in case of brand changes, with the fee being charged an average of 5.4% of RevPAR's housing.

At the time of SIPO, these two business segments were worth 52% of HW's EBITDA combined, compared to 47% in 2007 and 27% in 2000. It was through recourse to this type of contract that HW increased between 2007 and 2013 the number of rooms in international properties from 101000 to 148900, that is, 47% more than the date of SIPO, and as of the date of SIPO 80% of the rooms under construction were located outside the US.

Timeshare: Represents the sale and financing of 7,592 rooms on HW's 46 resort properties under the Hilton Grand Vacations brand, and the amounts associated with them represent the bulk of the revenue for this segment, as well as meals or other services provided at resorts within this segment model. Recently and within the deleveraging policy of the company, a new model was adopted, with a greater focus on the management and commercialization of units developed by third parties. Thus, within this new model, the company obtains revenues related to the commercialization and promotion of fractions, as well as revenues from operating the resorts. In 2016 Hilton realized a spin-off of this portion of properties in order to split the revenues coming from Managed and Franchised on one hand and Timeshare (Grand Vacation brand) on the other. Moreover, the spin-off involved Hilton Park Hotels & Resort.

The Blackstone Group: History

The Blackstone Group was founded in 1985 by Stephen Allen Schwarzman and Peter George Peterson in New York starting with just 400.000$ in seed capital. The name of the firm comes from the names of the founders: *Schwarz* means *black* in German and *Peter* means *stone* in Greek.

Mr. Schwarzman is at #42 in the *Forbes* chart for powerful people and #117 in the 2018 millionaires chart, he worked alongside with Trump as chair of strategic and policy forum, in 2017, while is salary amounted to *only* 350.000$, he received a dividend payout of 786 million dollars for the year. Mr. Peterson, on the other hand, was son of poor Greek immigrants and started at the age of 8 working the cash register during the *Great Depression.* He started the new company alongside with the fellow billionaire in 1985 after the experience as secretary of commerce with Richard Nixon, but he left the company in 2007 after *the Blackstone Group* IPO. He passed away the 03/20/18 by leaving a heritage of approximately 2 billion dollars (*Forbes, 2018).*

The group formed the Real Estate Department in 1992 and, the following year, it is already the largest independent asset manager in the world. After several years of operations and subsequently to the opening of other firm 's groups, such as the corporate debt one, the *Blackstone Group* completes the IPO worth 4,13 billions dollar, listing in the NYSE with the ticker BX in 2007[5]. It's the same year during which *Peterson* leaves the firm and the LBO to acquire Hilton takes place. This operation is still considered one of the biggest ever made in the whole world with a price paid of 26,3 billion dollar[6].

After that year the firm has continued operating in the management of the corporate private equity funds, hedge funds solutions, closed-end mutual funds, credit oriented mutual funds and real estate funds. The Group, moreover, owns interest in the hospitality sector by *Extended Stay America* and *La Quinta Hotels*. In 2013, 6 years after the

[5] *It was the biggest IPO in the US since 2002.*

[6] *The LBO was completed through two funds belonging to the firm: the blackstone real estate properties fund (BREP VI) and the blackstone capital partner (BCP V) one.*

acquisition of the Hilton Group, Blackstone has become the *principal global private equity real estate manager with 64 billion $ of assets under management.*

The Leveraged Buyout

Definition

When a firm is funded or, like in the Blackstone-Hilton case, acquired with more debt than equity we are facing a case of leverage finance or, respectively, a leveraged buy-out. The leverage finance is used to achieve a specific objective such as acquisition funded by debt, share repurchase, payment of extraordinary dividends or *to buy-out a company*. We will focus specifically on the latter.

The **LBO** is the acquisition of a company or a division using a significant portion of debt. Usually, the investment is a high cash generating asset and, in the majority of cases, the cash flow generated from the latter is used to repay the principal and the interest linked to the financing used in order to fund the operation.
Technically, the *LBO Sponsor* is the main actor of this operation and its aim is to first acquire the target company, and then re-selling it within (typically) 5 years in order to monetize the investment. The LBO is financed by recurring to debt for a major portion

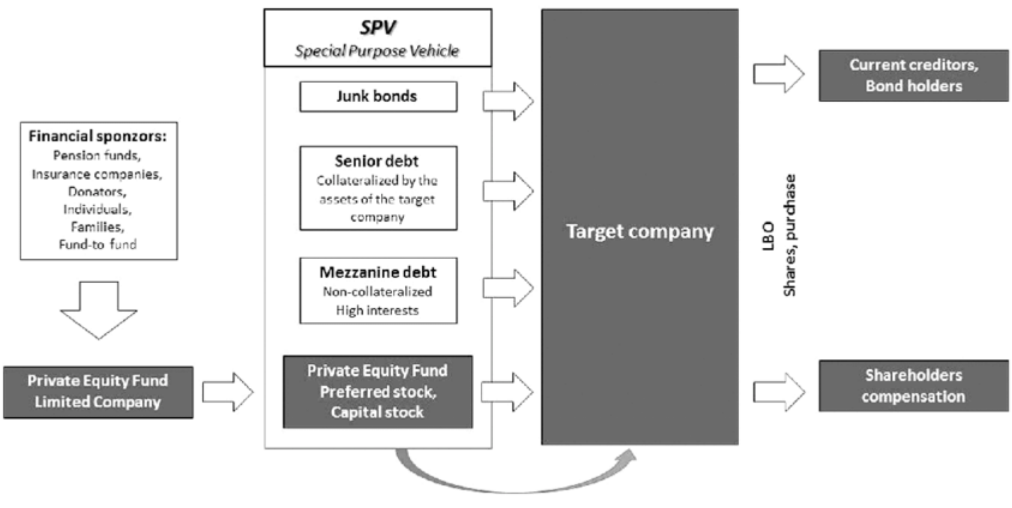


Figure 5: The Leveraged Buyout Process, Illustration, Research Gate, Miroslav Spacek, 2018

and equity in a small quota. The equity sponsor's aim is to increase the value of the firm through internal growth or through the repayment of debt or other acquisition.
The equity, before the acquisition, is injected into a shell company that issues debt and uses the aggregate value of debt and equity to pay for the target company.

Later, we will see the characteristics of the LBO made by The Blackstone Group to acquire Hilton Hotels. Now we will take a look at the forms of financing used in the Leveraged buyout and at the LBO market in North America.

Financing Sources

One of the biggest challenges in acquiring a company through the recourse to leverage finance is to identify the optimal capital structure in light of the projected cash flow of the *target company.* The financing sources that can be used in a Leveraged Buy-Out are divided into four main categories: The *Bank Debt*, the *High Yield and Subordinated Bonds*, the *Hybrid Debt* and the *Equity*.

The **Bank Debt** is typically the 30%-50% of capital structure, it is based on asset value or cash flow and it is a LIBOR based, floating rate, term loan. The rate is also influenced by the characteristics of the borrower that may obtain a discount or a premium based on the ability to repay the previous debts or the financial statements analysis. It is characterized by a 5-8-year maturity and it is amortized annually in excess, the duration of the amortization is completed in 4-5 years. Usually it is secured by the asset of the company and stocks and it has maintenance and incurrence covenants. The latter usually restrict the company's possibilities to make further acquisitions, to increase the level of indebtness and pay dividends to shareholders. Moreover, when maintenance covenants are included in the loans, the company is obliged to make quarterly performance tests.
The *Bank Debt* may include a portion of an unfunded revolving credit facility in order to fund working capital needs. Commonly, no minimum size is required and it can be split into Term A Loan and Term B Loan. In the first case we have shorter terms and higher

amortizations, in the second we have longer term, nominal amortization and bullet payments (large payment in the last year).

The **High Yield and Subordinated Bonds** are generally the 20%-30% of the capital structure and are generally unsecured. They are re-paid with fixed coupon and have higher maturity than the Bank Debt (7-10 years). No amortization is expected, and, like the Bank Debts, they have incurrence covenants. These kinds of bonds may be classified as Senior, Senior Subordinated or Junior Subordinated. For the Senior and the Senior Subordinated offerings are cash paid, while the Junior Subordinated may be zero coupon and issued at a holding company. Furthermore, the latter are usually issued together with Senior bonds. High Yield offerings are generally issued for 150 million dollars or more and usually are accompanied by warrants granting an IRR of 17%-19% to bondholder.

The **Hybrid Debt** can vary from 0% to a 30% of the operation capital structure. it may be composed by: *the mezzanine debt, convertible subordinated notes, preferred stocks, PIK preferred stocks and warrants.* The main characteristics of the Hybrid debt is that it embeds the benefits of the equity alongside the ones coming from the debt. Indeed, this kind of debt is convertible into equity and the IRR for the investor is in the range of 17% to 23% on a 3 to 5 years holding. This kind of debt is occasionally used in place of High Yield Debt, it is a mix of payments in cash and in kind, can be both or change over time and usually it has *warrants* in order to make the IRR higher (than the coupon rate) for the investors. The typical terms for this kind of financing are from 7 to 10 years and it is similar to a junior subordinated debt. In fact, it is structurally subordinate in priority of payment and claim on collateral respect to other forms of debt.

The **Equity** is usually injected by the private equity fund that raises capital from a basin of investors that belong to pension funds, endowments, insurance companies, investment banks and *high net worth individuals.* It is typically the 20-35% of the capital structure and it usually yields a 20-30% IRR on a about 5 years holding period[7].

[7] *When the transactions are not that risky, the IRR can be lower.*

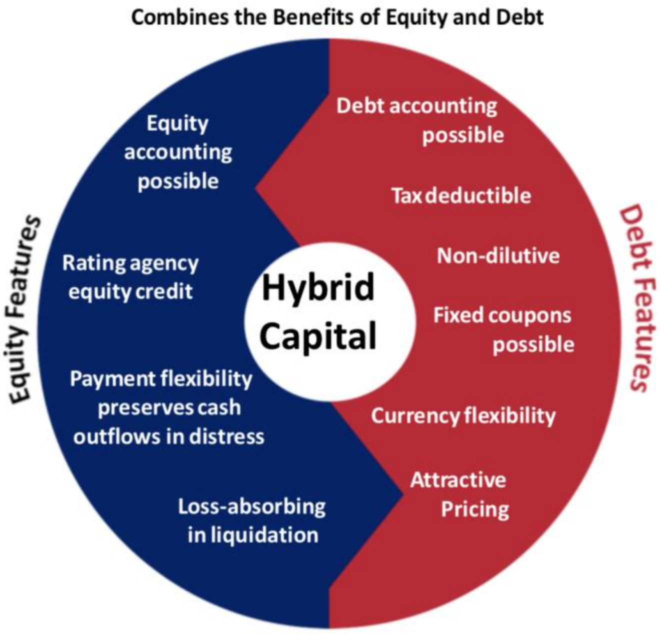


Figure 6: Features of a Hybrid Instrument, M. Comana, Corporate & Investment Banking, 2018

The LBO in the North American Market

In 2006 the PE sector registered a record in terms of capital invested with $874 billions of invested capital, beating the record set in the 2000s with the *high-tech bubble* that reached the peak of $515 bio of invested capital (Warner and Weisser, 2007). The LBOs were giving high returns at the time and so, the environment was very favorable for investors willing to pay for the benefits coming from this type of investment. Furthermore, debt markets were characterized by their extreme liquidity. The market seemed florid due to the consistent availability of covenant-lite loans, payment-in-kind (PIK) notes followed the same trend and, ultimately, the issuance of C-Rated debt skyrocketed compared to the previous year passing from 13.8 billion $ in 2015 to 26 billion $ in 2016. Another important feature of this period was the large availability of syndicated bank debt[8] that fueled the LBO granting huge amounts of money thanks to the participation of groups of banks that gave credit to single investors. Last but not least, the

[8] *Allows firms to fund their operations with larger amounts of money without exposing the banks to high credit risks*

privatization events dominated the American industry. This growth is strictly related to the PE's ability to obtain funding for enormous individual transactions.

The going-private activities increased as well in 2006 with an overall of 1,088 announced LBO transactions amounting to an astounding $397 bio in deal value. This condition was common in the USA. In fact, due to the high concentration of regulation, the managers of the firms had to find plans in order to escape from them. The shareholder community became active in that year and The Blackstone Group made the acquisition of Hilton with this climate of excitement taking the upper hand on the market.

After this huge increase in the LBO sector, with the 2007 bubble, the market changed and as we can see from the graph *(Statista, 2018)*, the statistics regarding the value of private equity-backed buyout deals plunged until 2009. After 2010 the trend changed and started becoming positive again. In the last two years it has decreased, following to a very high peak occurred in 2015.

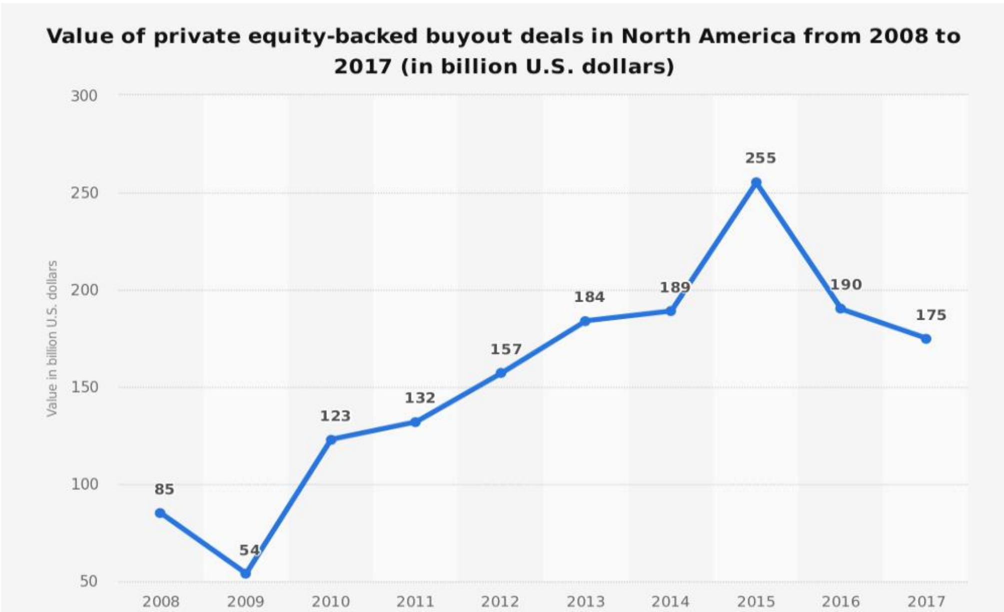


Figure 7: Value of private equity-backed buyout deals in North America from 2008 to 2017, www.statista.com , 2018

Second Section: The Case Study

In this section we will analyze the three main phases of the acquisition. We will start examining the financial statements of the two firms and the conditions that pushed the managers to start the operation. Secondly, we will see the main characteristics of the operation and what changed with the acquisition: strategies, board of directors etc.…
Moreover, we will focus on the financing sources and on the banks that took part in the process. The last paragraph will treat the overall outcome of the acquisition and the exit strategies.

Pre-LBO Phase

2007 saw the third consecutive profitable year for overall lodging industry and hotels proved quite appealing targets for private equity investors (*Guinn, 2007*). Between 2000 and 2006, in fact, Hilton was offering high returns to investors, with an average of 20.3%. The American hotels chain registered remarkable performances in terms of operational performance and sales growth, but this notwithstanding, these extraordinary returns for investors and the international expansion lead Hilton to search for a partner in order to support their ambitions and activities. The debt levels, in fact, increased due to the expansion strategy and Hilton's cash flow was not sufficient for covering the expenditures of the internationalization.
As of 2007, therefore, Hilton was investing intensively outside the US in order not to make big piles of money generated from franchising: repatriation of gains was hostile due to tax implications. The investments abroad meant deployment of huge cash flow percentages and so, the search for a partner became a primary goal for the American company. The private equity market was booming and the necessity of a partnership with a firm characterized by strong expertise in the *real estate* sector was crucial.
Blackstone, on the other hand, came from several acquisition in the hospitality sector. In fact, between 2004, 2005 and 2006, the private equity group incorporated as many as 5

hotel companies: *La Quinta Corporation, Wyndham International, Boca Resorts, Extended Stay America* and *MeriStar REIT*. The acquisition of Hilton Worldwide would have meant becoming the first private equity group in the world operating in the real estate sector. *Jonathan Gray*, responsible of the housing market for the Blackstone Group, had the feeling that there was a fast-growing interest among investors in the real estate sector. Moreover, he understood that the market was underestimating *Hilton*'s hotels by devaluing the market price of the properties.

The willingness to make the operation became concrete in 2006, when the negotiation between Gray and Matthew J. Hart[9] started. At the beginning the deal was questioned by the press and the CEOs themselves because of the discrepancies that were emerging regarding the price that should have been paid.

The conditions for the LBO were favorable anyway: The industry and the company were mature, granting an acquisition that could have increased its value, moreover there were feasible exit options, since making Hilton private again would have led to another IPO once the value had grown over time. Another important feature of the operation would have been the exploitation of the competitive advantage that Hilton had reached over the years. The synergies due to the expertise of the two firms and the possibility to invest granted by Blackstone would have made the difference once the deal would have been completed and there was room for expense reduction since 6316 million dollars of expenses reduced the 7438 million dollars of revenues (*Hilton Hotel Corporation Financial Report, 2006*). Furthermore, Blackstone could have sold the Hilton properties in case there was the necessity to cover the debt issued for the acquisition and the asset could have been used as collaterals to secure the debt too. Even though the Hilton's balance sheet was not clean with 6556 million dollars of debt, the LBO was under a traditional proposal.

[9] *President and COO of Hilton Hotels Corporation from May 2004 until October 2007.*

Hilton Hotels Corporation Financial Statements

One of the most important factors to evaluate the company is the analysis of the composition of its activity. Below we can take a look at the table representing the financial statements for Hilton Hotel Corporation before (2006) and after (2007) the completion of the LBO.

Assets	2006	2007
Current Assets		
Cash and Equivalents	107	341
Restricted Cash	293	1318
Accounts Receivable	618	681
Inventories	425	666
Deferred Income Tax	95	93
Current Portfolio of Notes Receivable	55	67
Income Tax Receivable	52	314
Prepaid Expenses and Other	155	291
Discontinued Operations	1426	
Total Current Assets	3226	3771
Investments, Property and Other Assets		
Investments and Notes Receivable	759	1362
Property and Equipment	4818	9914
Management and Franchise Contracts	1174	2425
Leases	310	448
Other Identified Amortizable Assets		388
Brands	2486	6474
Goodwill	2948	12233
Deferred Income Taxes	76	53
Other Assets	684	800
Total Investments, Property and Other Assets	13255	34097
Total Assets	16481	37868

Table 2: Hilton Hotels Corporation assets before and after the LBO, Hilton Hotel Corporation Annual Report, 2007

Liabilities and Stockholders Equity	2006	2007
Current Liabilities	1705	2576
Accounts Payable and Acurred Expensed	412	61
Current Maturities of Long Term Debt		
Current Maturities of Non-recourse Debt and Capital Leases	110	112
Income Taxes Payable	40	88
Liabilities Associated with Discontinued Operations	331	
Total Current Liabilities	2598	2837
Long Term Debt	6556	21177
Non-recourse Debt and Capital Leases	390	390
Deferred Income Taxes	1950	7445
Insurance Reserves and Other	1260	821
Total Liabilities	12754	32670
Common Stock $0,01 par Value , 121 Million Shares Outstanding		-1
Predecessor Common Stock $2,50 par Value, 387 Million Shares Outstanding	1023	
Additional Paid-in Capital	1248	5409
Retained Earnings (Accumulated Deficit)	1663	-125
Accumulated Other Comprehensive Income (Loss)	262	-87
	4196	5196
Less Treasury Stock, at Cost	-469	
Total Stockholders Equity	3727	5196
Total Liabilities and Stockholder's Equity	16481	37866

Table 3: Hilton Hotels Corporation liabilities and equity before and after the LBO, Hilton Hotel Corporation Annual Report, 2007

The financial reports show the consequences of the LBO. We can notice the growth of the financial leverage due to the operation and so, we can consider the revaluation of the assets, such as the *Goodwill,* strictly related to this increase. In fact, it grew from 2.948 to 12.233 million dollars. This change is due to the rise of the value of the portfolio of brands owned by Hilton. For what concerns the liabilities, examining the statements we can observe that the financial leverage strongly influenced the net debt. This *item* registered an increase of almost 20 billion dollars and it was composed mainly by secured debt and mezzanine debt with maturity in 2010 and the possibility to extend the terms for other 3 years. Moreover, there was an increase in the non-recourse debt. The ratios comparing the Operating Income to the Net Debt changed reaching 13,1x.

Revenue	2006	23/10/2007
Owned Hotels	2506	1937
Leased Hotels	1641	1645
Management and Franchise Fees	681	632
Timeshare and Other Income	767	592
Other Revenue From Managed and Franchised Properties	1843	1748
Total	7438	6554
Expenses		
Owned Hotels	1771	1369
Leased Hotels	1410	1440
Timeshare and Other Operating Expenses	546	431
Depreciations and Amortizations	426	349
Imparment Loss and Related Costs		27
General and Administrative Expenses	331	292
Merger Expenses		295
Other Expenses From Managed and Franchised Properties	1832	1739
Total	6316	5942
Operating Income from Unconsolidated Affiliates	57	45
Operating Income	1179	657
Intrest and Dividend Income	27	19
Intrest Expense	-498	-325
Net Intrest from Unconsolidated Affiliates and Non-controled	-45	-40
Net Gain (Loss) on Forgein Exchange Transactions	34	-18
Loss from Extinguishment of Debt	72	-12
Loss from Non-Operating Affiliates		-71
Loss from Non-Operating Affiliates	-16	-12
Income (Loss) Before Minorities and Non Controled Intrests	753	198
Income Tax (Provision) Benefits	-245	-9
Minority and Non Controled Intrests Net	-7	-7
Profit from Continued Operations	501	182

Table 4:Hilton Hotel Corporation Income Statement before and after the LBO, Hilton Hotel Corporation Annual Report, 2007

The Negotiation

Jonathan Gray and Matthew J. Hart together with Stephen Bollenbach[10] started negotiating again at the end of 2006 riding the wave to privatization that was hitting the whole continent. Notwithstanding the divergences that occurred during the first meetings, the CEOs decided to meet again because the conditions, adjusted to the constraints imposed by Hilton, could have brought benefits to Blackstone, anyway. The previous offer, made in August 2006, was of about 30$ for a spot price of the action that was around 20$. After September 2006 the price of the stocks skyrocketed from a maximum of 28,53$ registered during the Q3 of 2006 to a maximum of 35,79$. The market in fact relied on the private equity operation and, moreover, Blackstone was used to invest in that kind of firms. The news about the possibility for the Private Equity group to buy the hotel chain made the public hopeful and ready to invest on the operation.

After the second meetings, Hilton decided to ask UBS an opinion about the deal and the Swiss firm advised the American company underlining the fact that the market was underestimating the value of the stocks. Hilton wasn't supposed to accept an offer below 42$.

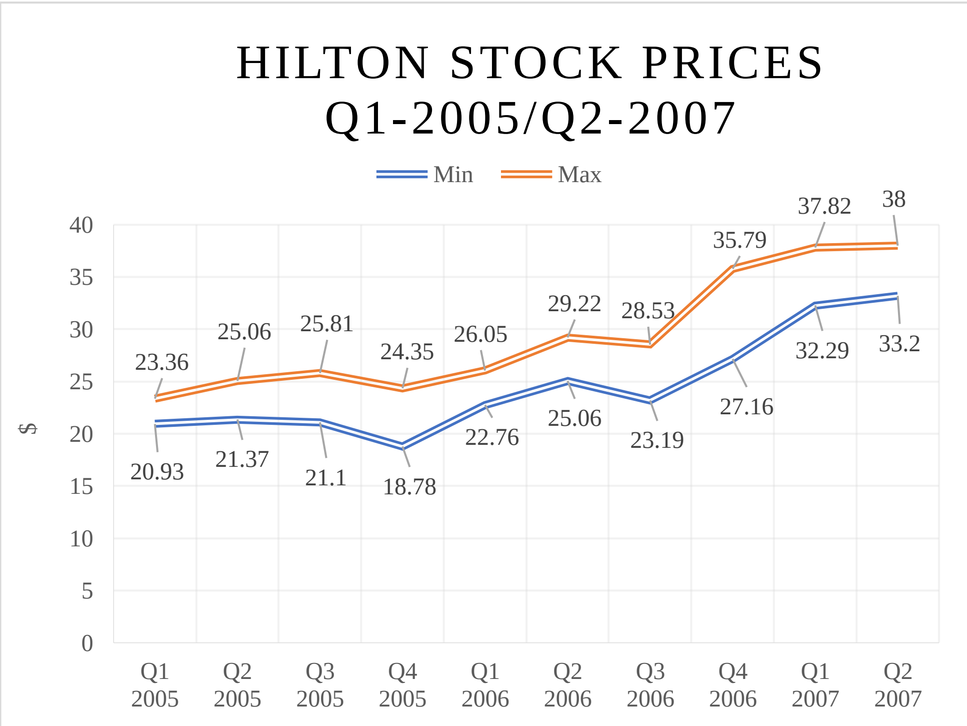


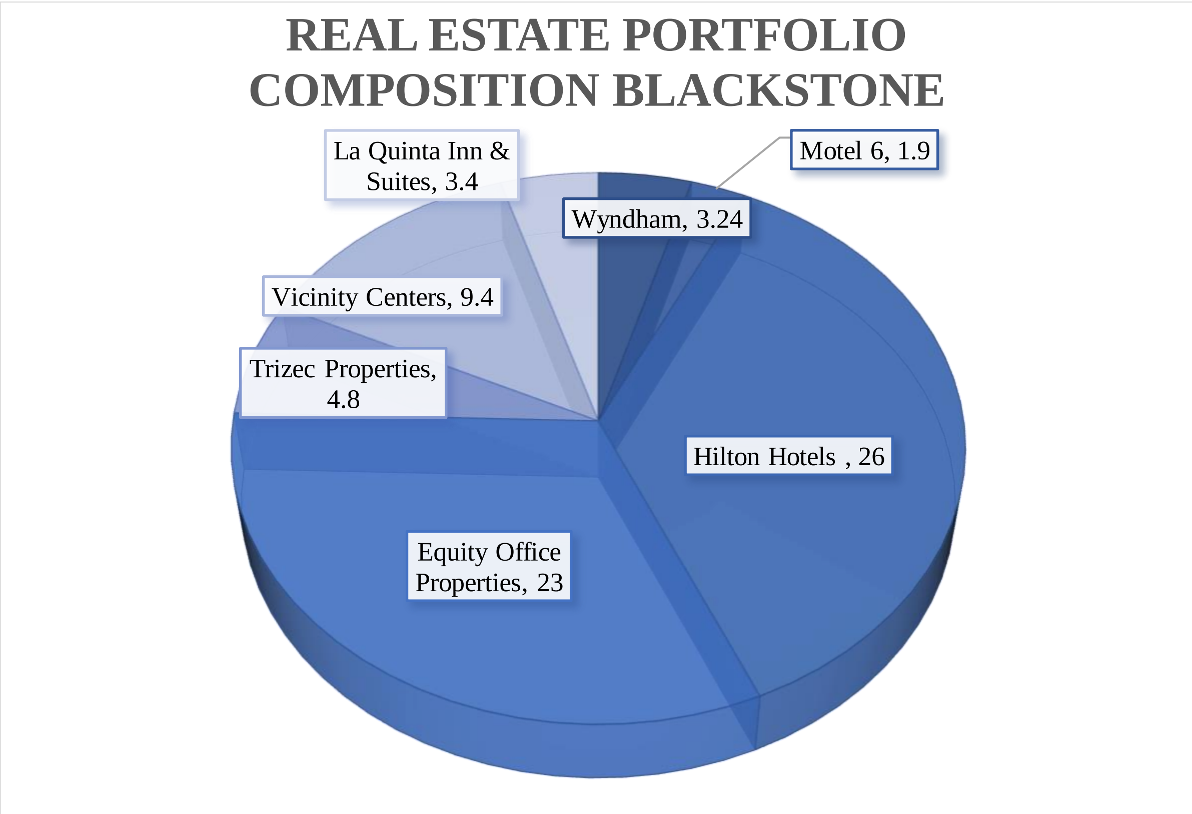
Table 5: Hilton Stock prices Q1-2005/ Q2-2007, source: MarketWatch, 2018

[10] Hilton CEO, 2007

Ultimately, The Blackstone Group and Hilton Hotel Corporation entered into an exclusive negotiation with requested due diligence for both counterparts. During May 2007 the offer was completed, and Blackstone engaged to guarantee a 40% premium over the closing day price of the stock.

The operation was closed on June 29th, Hilton stated that the closing would have brought large benefits to the shareholders and so, the price of the stock rose by 6.4% reaching 36,05$ per share. The final price paid by Blackstone was 47,5$ per share generating an effective premium of about 42%. The Private Equity Group became the largest hotel equity manager and added to its portfolio of 5 hospitality company, the most important one.

Table 6: Blackstone Real Estate Portfolio Composition, in billion dollars, source: Blackstone 2017



The Price paid for the entire acquisition by Blackstone amounted to 26 billion dollars and evaluating the firm 12.2x the EBITDA registered during the 12 months before the operation.

The 3rd of July the LBO was concluded between Gray and Bollenbach and Blackstone bought Hilton Hotels out. The firm paid the total amount using 20,6 billion dollars using

financing sources and the remaining 5,4 billion dollars with equity coming from its funds BREP VI and BCP V. The Hilton debt was transferred to the American PE group and the proceeds of the operation were divided between AXA Financial[11], Barron Hilton[12], the *charitable trust* of the family[13] and the other shareholders.
In that years, the LBO was ranked 10th among the greatest acquisition of all time and the first for Blackstone. The premium paid for the purchase was one of the higher paid in the history and exceeded hugely the premiums paid previously by the Blackstone Group for Wyndham (19% premium) and Fairmont (28%). The premium was above the average of the north American LBO market and of the M&A too, respectively 25,62% and 30,55%.

Below are reported the statements collected on July the 3rd :

Stephen F. Bollenbach, Hilton's co-chairman and chief executive officer: *"Our priority has always been to maximize shareholder value. Our Board of Directors concluded that this transaction provides compelling value for our shareholders with a significant premium. We are delighted that a company with the resources and reputation of Blackstone fully appreciates the value inherent in our global presence, strong brands, industry leading marketing and technology programs, and unique portfolio of hotel properties." (Blackstone Press Release, 3rd July 2007)*

Jonathan Gray, Senior Managing Director, Blackstone: *"It is hard to imagine a better strategic investment for us than Hilton with its world-class people, brands and network of hotels. This transaction is about building the premier global hospitality business. We are committed to investing in the company and working with Hilton's outstanding owners and franchisees to continue to grow and enhance the business." (Blackstone Press Release, 3rd July 2007)*

[11] Holding 7,9% of Hilton
[12] Conrad Hilton son, Holding 5,3% of Hilton
[13] Holding 5% of Hilton

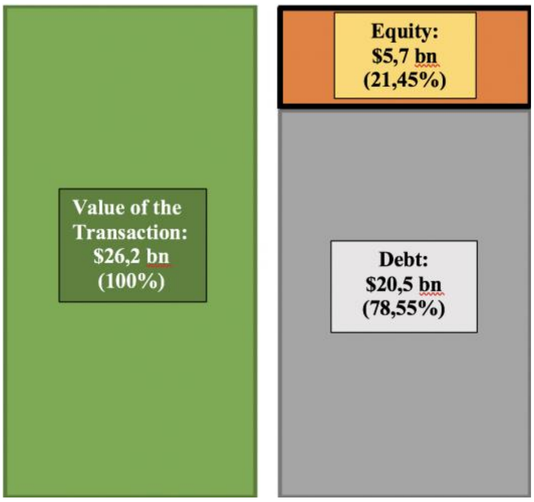
Michael Chae, Senior Managing Director, Blackstone: *"Blackstone's real estate and corporate private equity funds collaborated on the acquisition of Hilton, demonstrating Blackstone's unique ability to undertake such a transaction. We look forward to working with Hilton's management team and employees to enhance the value of the company." (Blackstone Press Release, 3rd July 2007)*

The Buyout

Thanks to the following paragraphs we will go deeper into the details of the operation and the crucial phases of the acquisition. We will understand the way the LBO was financed and how the management has changed after the Blackstone settlement. We will look at how the Private Equity group faced the doubts about the good outcome of the operation and the trends of the sectors for the years before the second Hilton's IPO.

Details of the LBO

As we saw on the previous paragraph, Blackstone borrowed a massive portion of debt



corresponding to 20,6 billion dollars and injected 5,4 billion dollars of equity in order to complete the acquisition.

The debt quota was furnished by a syndication of banks composed by seven[14] high reputable financial institution that participate to the funding for the 80%: Bear Stearns (whose USD 4 billion securities were transferred after the acquisition of the latter by JPMorgan),

[14] *The total number of financial institutions participating in the syndication was 26.*

Bank of America, Deutsche Bank, Goldman Sachs, Lehman Brothers, Merrill Lynch and Morgan Stanley. These institutes not only provide the loans to the private equity group but acted also as financial advisors. Hilton on the other hand, hired UBS and Moelis Advisors for helping them in making the operation work out.

Thus, this transaction is one of the 10 largest to that date, given the fact that the company had a net debt of more than USD 6.5 billion dollars and the advising companies valued the enterprise 26.3 billion dollars. For what concerns the financing of this operation, the BCP V and BREP VI funds only placed USD 5.7 billion in the form of equity and the rest of the enterprise value was financed from outside capital under the Leveraged Buy-Out process.

Fund	Vintage	Fund Size (Million $)
Blackstone Capital Partners I	1987	800
Blackstone Capital Partners II	1994	1,271
Blackstone Capital Partners III	1997	3,750
Blackstone Capital Partners IV	2003	6,450
Blackstone Capital Partners V	2006	21,700
Blackstone Real Estate Partners I	1994	485
Blackstone Real Estate Partners II	1996	1,300
Blackstone Real Estate Partners III	1999	1,500
Blackstone Real Estate Partners IV	2003	2,500
Blackstone Real Estate Partners V	2006	5,250
Blackstone Real Estate Partners VI	2007	10,900
Blackstone Real Estate Partners International I	2001	800
Blackstone Real Estate Partners International II	2006	1,550

Table 7:Blackstone's Private Equity and Real Estate Funds Raised (As of 2007), Source: Preqin

Estimates at the time of the transaction based on UBS projections indicated that in 2013 the equity in the company could be worth 29,555 million USD, for that, there was a room for maneuver of almost 24 billion USD, in case something was not going as forecasted.

However, after the issuance was structured and the necessary approvals were obtained, the market collapsed in 2008 following the sub-prime crisis.

The company's real estate assets then had a concentrated pattern, as 80% of the cash flows associated with real estate came from only 10 hotels including the iconic Waldorf Astoria NY[15] .

One of the peculiar characteristics of the debt associated with Hilton's LBO was that it was cov-lite, with few covenants and reduced limitations. Thus, instead of what would be expected in a leveraged operation of this kind, in which creditors would place restrictions and seek guarantees of prudent management, this operation had few associated safeguards that allowed Blackstone to cope with the downturn in the sector to come to be verified in the aftermath of the sub-prime crisis in a quieter way, with debt restrictions on company value, EBITDA ratios and leverage constraint being removed.

In 2007 the interest burden was already high, and their coverage deteriorated significantly after 2008, and by Leveraged Buy-Out, they already accounted for 65% of the gross cash flow of 2,000 million Dollars, or EUR 1300 million. This became more problematic following the sector's fall in profitability in 2009 as a result of a 6% drop in demand and a 16.69% RevPAR decline in 2009. As a result, at the end of 2009, competitors like *Starwood*, which recorded a 35% drop in EBITDA compared to the same quarter of the previous year, began to discuss the need for a debt restructuring. Having Starwood itself raised its debt limit in 2009 from 4.5 to 5.5x EBITDA and issued 500 million Dollars in new obligations with a fixed coupon of 7.875% and maturity in 2014 (Bloomberg, 2018). Considering this scenario of decline in the sector, Blackstone had to establish provisions in its funds up to 70% of the initial investment in terms of equity. Thus, the period immediately following the Management-Buy-In[16] coincided with the fall of the American and world economy, so, with the economic crisis, total revenues and RevPAR fell consistently and hugely. This led to a deterioration of performance operating in the industry, to which Hilton Worldwide was not immune.

[15] *The hotel was sold in October 2014 to Chinese insurer Anbang Insurance Group Co. for 1 ,95 billion Dollars.*

[16] *MBO*

Thus, between 2008 and 2009, Hilton's revenues fell from 8,875 million Dollars to 7576 million euros, decreasing by 15%. The same occurred in terms of adjusted: a decrease of 28.89% was registered, from 1,703 million euros to 1,211 million euros, with cash-flow declines at the start of LBO of 30%. Thus, the complicated situation of this LBO with EBITDA of 1,211 million Dollars in 2009 and a long-term debt of 21,157 million Dollars plus 574 million Dollars in non-recourse debt with only 1,134 million Dollars in cash and cash equivalents: difficulties became evident. Net Debt / EBITDA ratio was 17X, this made the financial sustainability of the company concerned, especially if the downturn in the hotel industry cycle became persistent. Given these factors, Blackstone recorded an impairment loss of 5,611 million Dollars in Hilton assets.

Unlike most companies that only renegotiate with creditors in situations of insolvency or when covenants that cannot be respected, Blackstone informed investors of its funds that 3,9 billion Dollars of Hilton's value would probably be lost, with a write-off of goodwill amounting to 5,6 billion Dollars in HW's balance sheet in 2008. Thus, The Blackstone Group entered into negotiations with Hilton's investors in 2009 ending the latter in 2010. This renegotiation was made possible by the bad timing of several Leveraged Buy-Outs in the hospitality sector: only Hilton and La Quinta Inns survived, both owned by The Blackstone Group.

Blackstone took time since the market condition were twisting the true potentiality of the operation. Indeed, the press and the investors were really concerned about the soundness of the operation but the new management (Nassetta and Gray) asked for more time in order to implement the necessary transformations at Hilton, knowing that the hotel industry has a strong cyclical nature. Thus, the situation could have changed by renegotiating debt, increasing capital by credit conversion, reducing the interest burden and the net debt of the company, improving the financial profile of the company, but mainly they needed time to wait for a change in the economic cycle that allowed the management to make assets recover their pre-crisis value, increasing exponentially the worthiness of Hilton Worldwide.

Composition of the funding

As we can see in the paragraph above, the offer was split into equity and debt. For what concerns the latter, different kind of debt were issued. First of all, we have to underline the efficiency granted by the syndication of banks that participated in the transaction. It made the cost of debt lower due to the lower risk assumed by each bank. Moreover, the 20,6 billion debt was composed from different sources, each one with a specific maturity and terms. In the table below, we can observe the sources of the funding:

Sources	Billion $
Senior Mortgage Loan due 2010	11,345$
Secured Mezzanine Loans due 2010	8,000$
Unsecured Notes, 9,55% due 2010	500$
Mortgage Notes, 5,05% to 8,65 due 2008 to 2016	280$
Notes, with average rate 7,65% due 2008 to 2031	270$
Capital Lease Obligations, 7,01% due 2008 to 2097	90$
3,375% Contingent Liability Notes due 2023	15$
Total	20,500$

The secure mezzanine debt was divided into 11 tranches and the largest financing holder was The Maiden Lane Grantor Trust since it had interests in mortgage loans and nine out of the eleven mezzanine tranches. To these items we have to add the part payed in Equity that amounted to 5,660 billion dollars for a total amount of approximately 26,6 billion dollars. The table below, show how these funds were invested:

Uses	Billion $
Purchase of Common Stocks	19,247$
Purchase of Options and restricted Stocks	894$
Debt Retired	3,900$
Stock Based Rewards	695$
Transaction Costs	470$
Other Merger Related Transaction	299$
Total	25,386$

As we can see from the table, the funds (Debt + Equity) were not used entirely. The Private Equity group retired immediately 3,9 billion dollars of debt and added the other debt, due to the transaction, to the liabilities of the company. Indeed, as we saw in the financial statements (*Hilton Hotel Financial Statements*) the Long-Term Debt amounted to 21,177 billion dollars in 2007.

At the time of the acquisition, bearing an average *all-inclusive* interest rate of around 5.7%, Blackstone had to pay an annual interest cost of 1.14 billion dollars per year. From the analysis conducted before the acquisition, projections called for earnings before interest, tax, amortization and depreciation of around 2 billion dollars in 2008. Moreover, capital expenditures for such a business amounted to 500 million dollars a year leaving room for contingencies. In this way, adding the 500 millions of projected capital expenditures to the 1,14 billions of interest costs, there was adequate cash flow to cover interest burden and maintenance. Banks were earning good interest rates and Hilton's old owners had obtained more than expected from the acquisition: it seemed a win-win-win scenario. After the recession, however, the swap protection on Hilton almost doubled, hitting 735 basis points from June to October. By the way, the acquisition could have led to a good outcome in any case since Blackstone specified on the contracts the possibility to defer almost 400 millions of interests each year. Furthermore, in 2010 the management decided to renegotiate the terms of the debts by restructuring a big portion of the latter.

The Management

After the completion of the Leveraged Buy-Out the management of Hilton was almost completely replaced by Blackstone, introducing in the Hotel firm new people that, as we will see later, will result of key importance to the good outcome of the acquisition.
The new board, in 2007, was composed by the following people:

Name	Position
Cristopher J. Nassetta	President, CEO and Director
Johnathan D. Gray	Chairman of the Board of Directors
Michael Chae	Director
John G. Schreiber	Director
William J. Stein	Director
Simon Vincent	Executive Vice President and President Europe, Middle East and Africa

The team, chosen by Nassetta, was charged with implementing an internationalization strategy: the neo-CEO understood that there were many possibilities for the Hilton *resurrection* after the 2008 crisis, thanks to the fact that the company's core business was focused on providing the hotel services in the North American soil more than making it stronger abroad too. The manager, thanks to its ambitions, wanted to develop the business in the emerging market such as Asia and Middle east. Indeed, Simon Vincent was responsible for the opening of 100 out of the 300 hotels opened during its direction. Johnathan D. Gray, that in 2012 was nominated director of the Blackstone's Real Estate sector, worked alongside with Nassetta working on the department that resulted sleepy during the pre-acquisition analysis. Hilton, in fact, seemed a very good company, but the reality was that the company, in the moment of the acquisition, was a shadow of what it had been during the roaring first years when it was compared to giants such as Coca Cola. Indeed, he pushed Blackstone management to make an effort in order to offer 5,7 billion dollars in equity when Hilton refused the first offer. He understood that there were room for improvements for the hotel company since the other part of the world were getting richer and the demand for the hospitality sector was rising hugely.

Gray said in an interview published the July 6th, 2014 on *The Washington Post*: "There was enormous growth potential out there. We thought, 'Wouldn't it be great if we could give them a passport to travel around the globe.'"

Hilton competitors, such as Starwood or Marriot International, in fact, were benefitting by their internationalization strategy: it wasn't about owning hotels anymore, the hotel companies should have managed the hotels from that moment on.

Based on the analysis they carried out prior to the acquisition, it had emerged that another bias caused by the old management was given by the absence of quality standards that were triggering bad experiences for the customers. For these reasons, the 5,5 billion dollars check[17], seemed high, but not disproportional to the target they were acquiring. By the way, in 2007, after the 4th of July, the economy began to collapse, and the Blackstone management understood that there was the need to sign a superstar to head Hilton Worldwide. Nassetta was almost immediately contacted because of its experience in the sector: he was president of Host Hotels and Resort from 2000 to 2007, he worked at The Oliver Carr Company and, before joining Hilton, he co-founded Bailey Capital Corporation. The latter was an advising company for investment on the real estate sector.

One of the first thing Nassetta wanted to change in Hilton culture was to avoid people that were heading to make changes with superficiality, namely, he introduced the "immersion": every corporate manager should have spent at least three days in the front lines, cooking, housekeeping, and working in the front desk. They needed contact with the customers in order to make profitable changes. Furthermore, a system for employees' performances evaluation was implemented, stimulating competition and efficiency

[17] *Biggest check ever signed.*

between workers. These kinds of strategies lead to cutting high percentages of costs in the long term thanks to the being thorough in deciding what to change in the hotels and in the headquarters as well. Indeed, the most successful battles carried out by Nassetta were meant for changing the systemic inefficiency that pervaded the Californian HQs. The CEO believed that one of the most important problems in the administration was the location of the Hilton's offices: they were situated in Beverly Hills, few blocks off Rodeo Drive. There, the vibe was about spending money more than working hard in order to earn them. Moreover, the airport was pretty distant, and the traffic jams could have provoked delays and postponed business meetings. Furthermore, Southern California had the highest housing and renting costs: Hilton was a big firm, needed huge spaces and changing the location of those Headquarters could have generated massive cost cuttings. So, the HQs were moved on Washington DC, there, other competitors such as Marriot, Host and Choice had located their offices and these moves attracted different types of investors. Another factor that was creating added value at that time was the emerging World Wide Web reality: Nassetta thought firmly that having a competitive advantage in providing services to the clients through the internet would have made Hilton great again. The first changes were made on the HHonors side: the digitalization of this service made it easier for customer to get the rewards and to be in contact with the Hilton company. In addition, the integration of the timeshare unit (considered an exclusive and independent department until the acquisition) into the company generated a 44% leap of revenues and most of the economic benefits that involved the Nassetta era were due to the employment of Jacobs as CFO. In 2009 the employees were summoned to be informed that the firm has changed its seat to Washington and that only 100 out of the 500 that were at the meeting would have continued working for Hilton: *"I was committed to look them in the eye, tell them what I'm doing, give them the reasons why and answer questions for as long as they wanted."* (*The Washington Post, 2014*) Nassetta said.

In the first years, the new management made Hilton Worldwide more attractive by making many accomplishments:

Added 302 new hotels in 2009, the second most in the company's 91-year history. Became the leading hotel company in the U.S. by number of open and operating rooms.

Has more rooms under construction outside the U.S. than within the U.S. for the first time in the company's history.

Maintained a robust development pipeline that includes more than 900 hotels in 57 countries. Surpassed a record 25 million members for Hilton HHonors, the loyalty program for Hilton Worldwide's portfolio of hotel brands, after the largest enrollment year in the program's history in 2009.

Received the People's Choice Stevie® Award for "Sales & Customer Service – Favorite Customer Service in Leisure and Tourism" in this international competition that recognizes excellence in disciplines crucial to business success. Ranked the highest in brand equity with its Hilton brand compared to all the other major hotel brands in the industry in the 2010 EquiTrend® study conducted by Harris Interactive, a leading global market research rm.

Opened the 500th hotel for its Hilton Garden Inn brand – a number that was achieved in just 14 years and that is still rapidly growing with hotels either opened or soon to open in 11 countries around the world.

Was honored by the Business Travel News 2010 U.S. Hotel Chain Survey for several of its brands across multiple categories, including Hampton Hotels which was named the best hotel brand in the Mid-price Tier.

Enabled Home2 Suites by Hilton to become the fastest growing brand in Hilton Worldwide's history with 100 properties scheduled to open by the end of 2013 in the U.S., Canada and Mexico. (Blackstone Press release, April 8th, 2010)

The Crisis

After the acquisition, the main goal for Hilton was to catch the competitors that were gaining a competitive advantage respect to the firm founded in 1919 by Conrad Hilton. The company started opening hotels outside the US in order to catch potential customers belonging to almost all the social classes. Indeed, other than the core three: Hilton, Conrad and Hilton Grand Vacation, Nassetta pushed to provide hotels for middle-class and business travelers in Europe and especially Asia. Hilton Garden Inn and Hampton Inn were introduced in the two continents with the company investing huge amounts of money in the internationalization strategy. Yet, despite that, Jacobs, Nassetta and Gray always made attention to keep the cash flow deriving from the operating activities positive. In 2008, however, economy started to collapse alongside with the hotel industry. After the demise of Lehmann Brothers, the hospitality sector started to decline with hotel sales going down by almost 20% and profits falling by 40%.

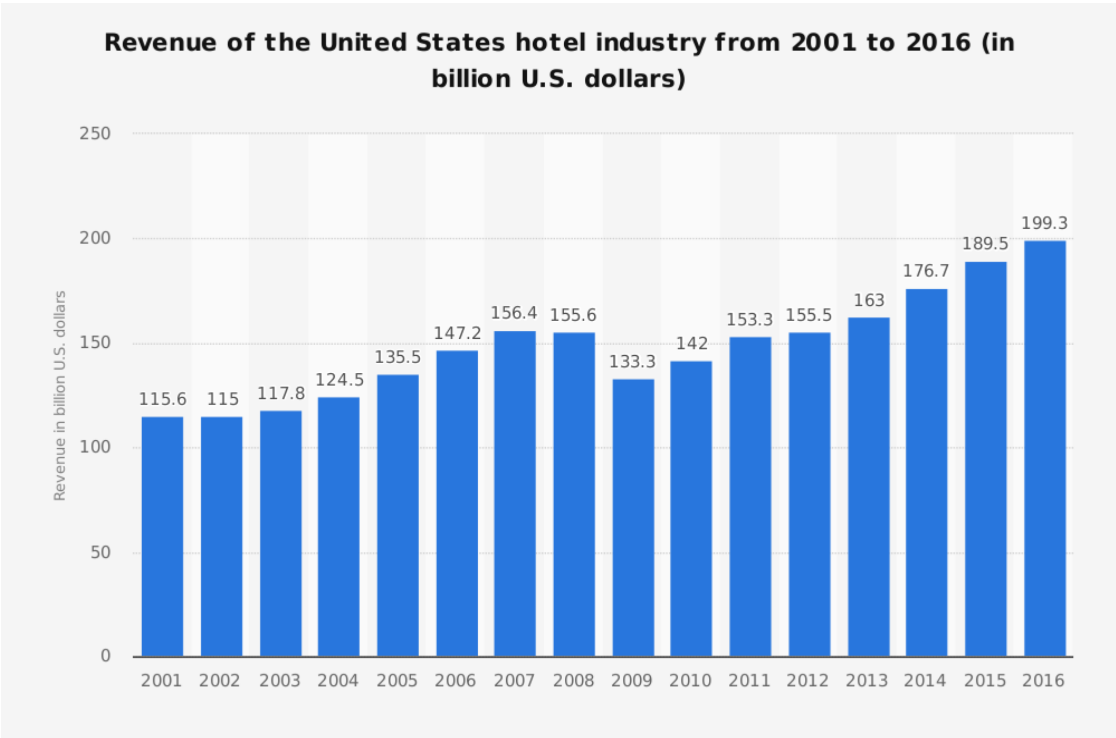


Table 8: Revenue of the United States hotel industry from 2001 to 2016, source: Statista.com

The managers didn't want to sell Hilton's fixed assets in order to repay their debts with banks: Gray and Nassetta started thinking about the possibility to ask to the syndication of banks to review the terms of the debts together. In the meanwhile Starwood sued Hilton for stealing corporate secrets: 2 out of the 10 new Hilton's managers that worked for Starwood before the acquisition, revealed some confidential material like presentations and market research studies that costed around d 1 million dollars to Hilton's managers in order to predict the moves on the market. In fact, Hilton wanted to launch a new brand called Denizen that consisted in 13 hotels in locations such as Las Vegas, London, Miami and so on. It was marketed as an "eclectic, global lifestyle destination". Starwood, on the other hand, was launching its own brand called *W*, a concept that foresaw the creation of *resto-lounge* that provided food service in a living room setting. Kenneth Siegel, Starwood's general counsel said about the fact: "We expect and welcome fair competition. This, however, is a blatant case of trade secrets, computer fraud and unfair competition."(*The Guardian, 2009)*
The conflict was settled in 2010 when Hilton accepted the ban on the development of the Denizen project.

No doubts, the competition was becoming fierce because of the hard times for the hospitality sector, especially for Hilton that was trying to pay its debt while facing the deep crisis. In 2009 after the first trial and the economic downturn, Hilton had lost 70% of its value. Gray and Nassetta started contacting the banks in order to prepare a debt restructuring.

Revenues, however, continued increasing despite the critical situation passing from 7,58 in 2009 to 9,75 billion dollars in 2013(year of the second IPO in Hilton's history). This trend regarding the sales played a crucial role in restoring the investors' confidence of the American firms and in the negotiation with banks for the renegotiation of the debt that will start at the end of 2009.

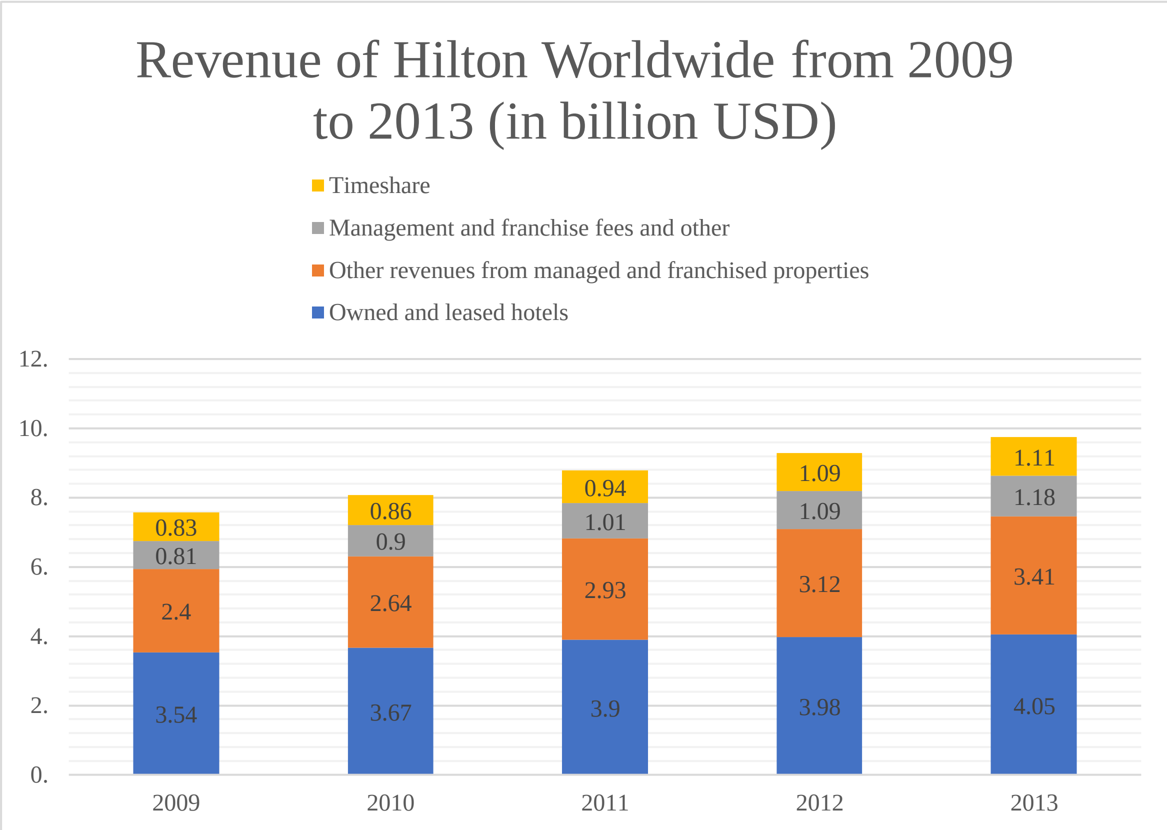


Table 9: Hilton Worldwide Revenue 2009-2013 by sector, Source: Statista.com

The Debt Restructuring

In 2009 Hilton started meeting each bank and participating to the syndication. After several months of negotiation, the banks, that were losing around 5,1 billion dollars from the operation started two years before with the private equity group, decided to concede to the American firm several changes to the terms of the loans.

As a result, in 2010 the company completed the restructuring of the remunerated debt in order to bring financial costs to an operating result level of about half compared to the one obtained during the LBO in October 2007. It was therefore necessary to call on creditors to share the 5,1 billion dollars losses attributable to Blackstone, the recovering of the losses was carried out between 2008 and the end of 2012.

In 2010, was implemented a debt restructuring which consisted in repurchase of the outstanding debt for 1,8 billion dollars Blackstone. In addition to this operation, a second capital increase was made through the conversion of junior mezzanine debt to preferred equity amounting to 2,1 billion dollars. In addition to the 18.9% reduction in Hilton Worldwide's net debt, the maturity of the remaining debt was extended to November 2015, removing pressure on the team led by the CEO Nassetta and Blackstone. Thanks to that the exit strategy that Blackstone could have implemented were postponed given the fact that the debt maturity was risen by 2 years[18]. This favorable restructuring for Blackstone's funds was also possible because the FED reduced the lead rate to 25 basis points, reducing LIBOR to 0.3% on the date of the renegotiation of debts, with fixed premiums for Junior and Senior Debt.

The consortium of financial institutions accepted this proposal after 10 months of negotiations, as it allowed it to recover the value of the remaining debt, and to gain potential appreciation by converting credits into capital, as, in fact, it verified. This restructuring, in which the most difficult partner to convince was the New York Federal Reserve[19], was only realized due to the quality of the tangible and intangible assets of Hilton Worldwide and the management team.

One of the shareholders who chose to convert its Junior Mezzanine Debt into Hilton's preferred stocks was Singapore's GIC Private equity fund, which converted the 4.8% shares it owned after public offering of the company.

Following these capital increase and renegotiation operations with creditors, HW had a ratio of adjusted net debt to EBITDA in 2010 of 10.5X, this reduction was accomplished as a logical consequence of the cyclical nature of the Hospitality sector together with the measures implemented by the management of the company that allowed to generate a better operational result.

"*This debt restructuring is another important step forward for the company, and I would like to thank all of our lenders as well as our investors, led by Blackstone, for their tremendous efforts in completing this transaction*," said Christopher J. Nassetta, President & Chief Executive Officer, Hilton Worldwide. "*Together with several recent*

[18] *Previous maturity was in 2013.*
[19] *Public Institution and so, under the eye of press and public scrutiny.*

achievements, Hilton Worldwide is positioned very well to capitalize on the recovery in the hospitality industry."

Given that the New York federal reserve held Bear Sterns' toxic assets, it had to take a 56% or 320 million dollars loss on a debt tranche given to Blackstone, having sold in relative terms less debt than some banks and hedge funds involved in the restructuring did. In terms of accounting, the recording of this operation was different since, with the restructuring, Hilton's debt became more liquid and safer, but on the other hand the remaining debt increased because of the longer maturities: this offset the loss incurred in the restructuring for the financial institution. Following the restructuring in June 2010, Goldman Sachs and Bank of America sold respectively 600 and 1,700 million dollars of mezzanine debt from Hilton Worldwide distributing them to 150 institutional investors in 7 tranches; everyone subscribed to the offer. In addition, in November 2010, in a context where the delinquency rate associated with loans to the hotel sector was 15.94%, there were negotiations between these two entities to place 2.66 billion dollars of Commercial Mortgage Backed Securities, and the operation failed.

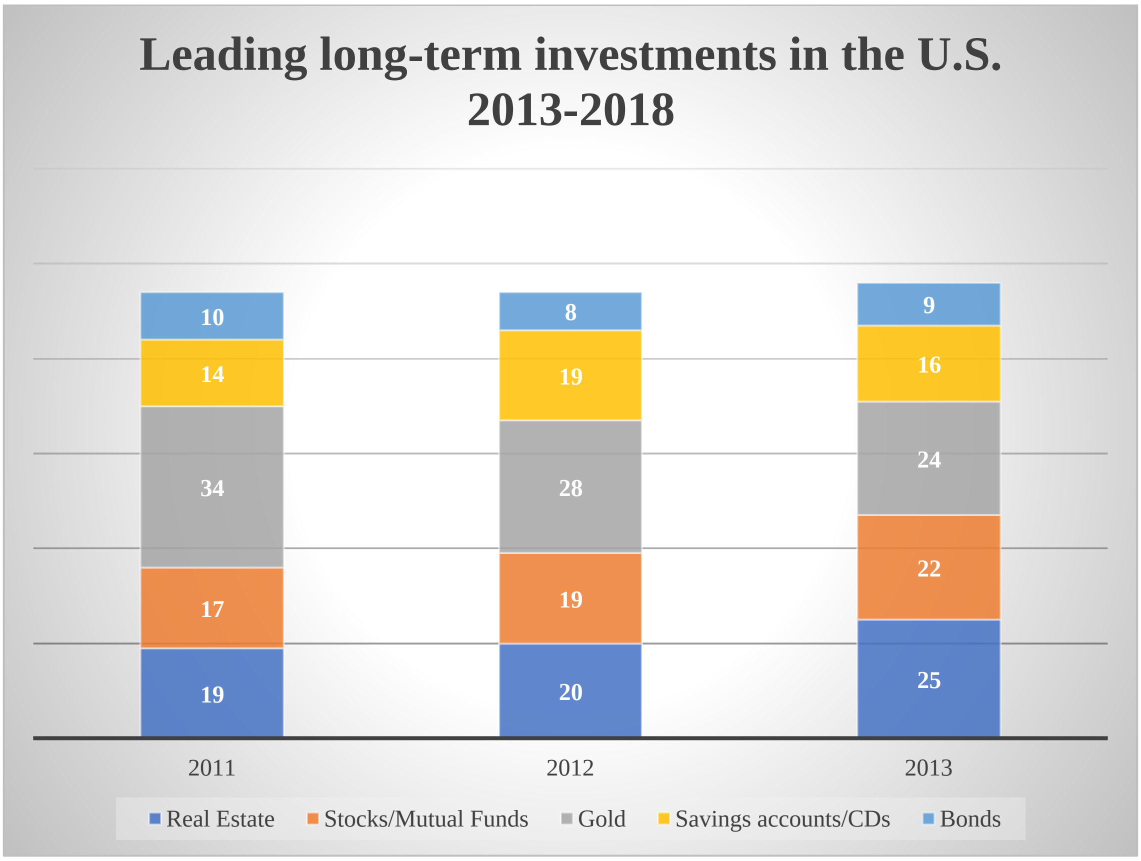
Post-Buyout

As we saw in the paragraph above, after the crisis, Hilton had to face several problems related to the collapse of the entire economy. The real estate sector was hit badly by the events of 2008 and the prices of the properties was declining rapidly. Pessimism about the American hotel chain giant and it was reflected to the Blackstone Group too. The management of Hilton Worldwide, however, continued on believing that, the mix of hard work and capabilities could have led the company out of the troubled waters. Furthermore, in 2011, the hotel industry's performances started rebounding sharply and Blackstone's Mr. Studzinski[20], that was engaged on renegotiate the debt with investors

[20] *Head of Corporate Advisory and restructuring practices*

and banks, understood that it was time to stop buying debt back and start selling it to investors.

Table 10: Leading Form of Investment in the US 2011-2013, Source: Gallup



As we can see from the table above, in 2 years, investments in the real estate sector rose from 19 to 25 billion dollars. This meant that it was the right timing for starting to sell instead of continuing buying.

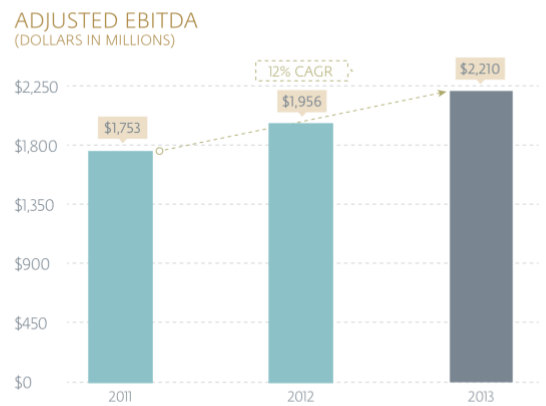


Table 11:Hilton Adjusted EBITDA from 2011 to 2013, source: Hilton Annual Report 2013

The first things a firm that wants to go public has to look at four main factors: the first is the EBITDA the second is the timing, the third is the location of the offer and the fourth is the amount to sell. For what concerns the first item to look at, EBITDA was registering an YoY[21] growth of around 13,3% passing from

[21] *Year over Year*

1,753 million dollars in 2011 to 2,210 million USD in 2013. This was also due also to the renegotiation of the debt: indeed, by rebuying and converting into equity almost the 20% of the debt, Hilton found huge benefits from the perspective of the Net Debt/EBITDA ratio. Going into the details that make an IPO successful we find the timing in the second place.

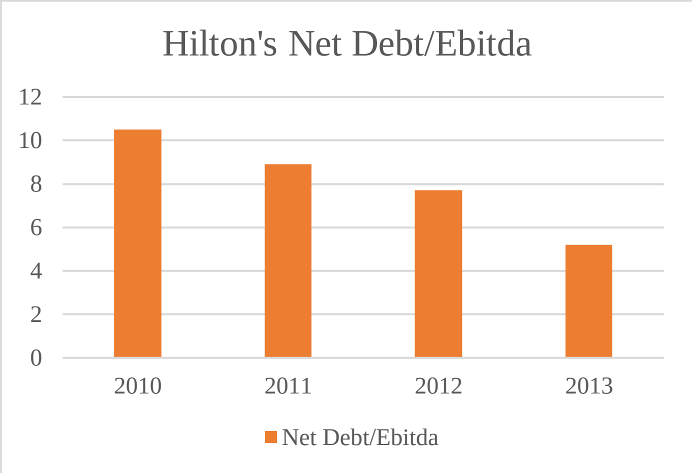


Table 12: Hilton's Net Debt/EBITDA 2010-2013, Source: Hilton Investors Relation 2013

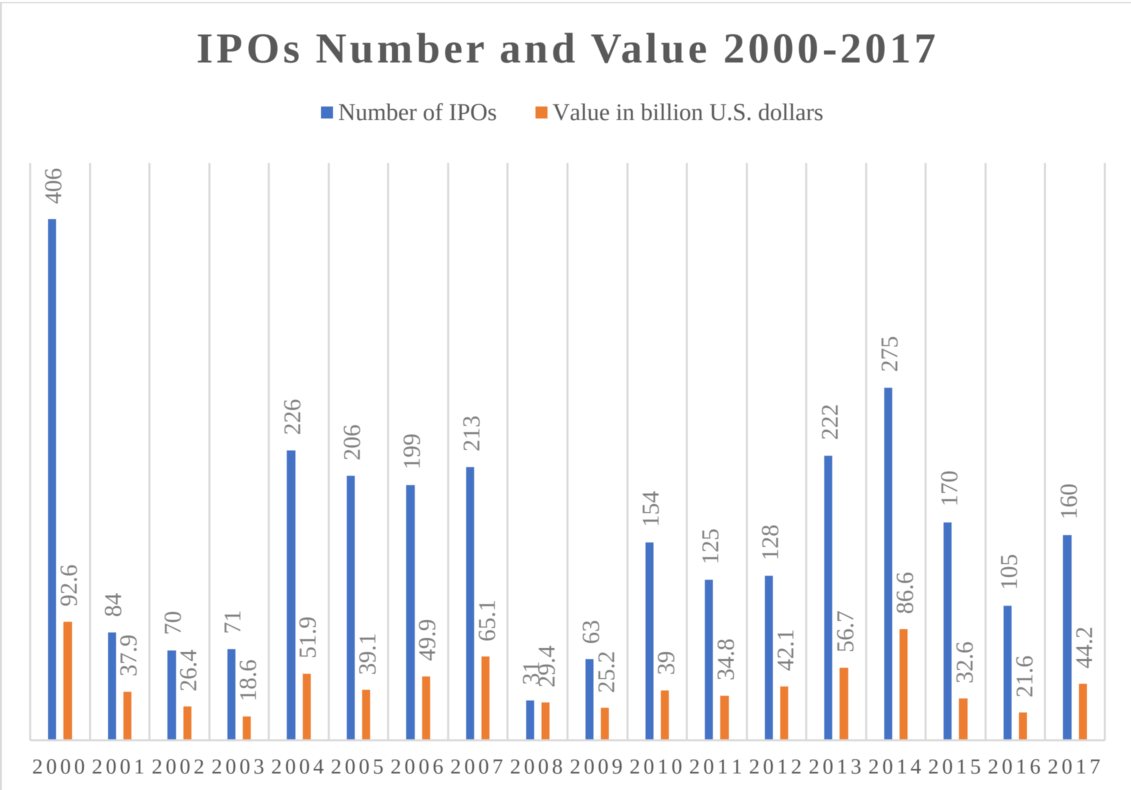
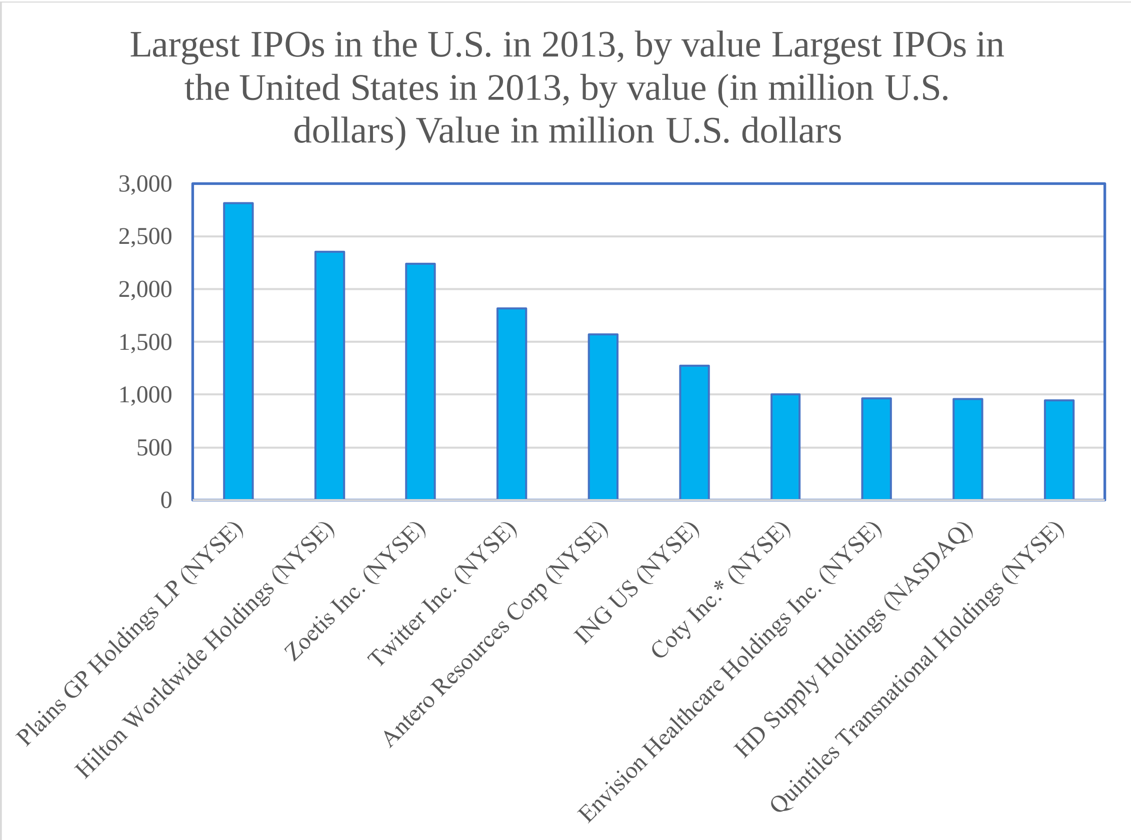


Table 13: IPOs Number and Value 2000-2017, source: Statista.com

This kind of sector, in fact, is characterized by two main types of moment: *hot* and *cold*. We call *cold* the moments during which the number of transactions is stable and doesn't seem to increase along time: the market is usually called *a bear* during these time spans. On the other hand, we call *hot* the moments when the markets seem buoyant. As we can easily deduct from the *table n. 12*, 2013 was a *hot* year for IPO: the sector registered a rise in the number of money invested and, in addition, in the number of transactions made. This meant that 2013 could have been a good year for such a transaction.

The third aspect that Hilton took into consideration was where to place the offer. Choosing the right stock exchange was vital in order not to incur in losses due to the high regulation but at the same time a company prefers to be visible and to enjoy legal protection. Last but not least is the amount to sell and as we can see in *table 14* the Hilton Worldwide Holdings IPO was one of the biggest recorded in the year 2013. Given these premises, we will take a deeper look at the operation and its features.

Table 14: Largest IPOs in the US in 2013, Source: Bloomberg



Management Compensations

Before going into the details of the IPO, we have to underline the fact that the decision of implementing the public offering was a consequence of the excellent management measures implemented by Christopher Nassetta. For that, we have to include a special mention about the way the management was remunerated under this operation.

Other than salaries, the management was entitled of cash awards and generous long-term incentive awards, with a package of shares in the maximum amount of 230 million dollars or a 2.75% portion of the company as a class A or Tier I premium. In addition, there were still Tier II or Class B premiums available from the moment when the company would have been out of the stock market: it shad to be activated by April 2015 and its value and its consequent activation depended on the creation and increase of the value of the HW, being that, in the sequence of the secondary IPO, the class B units were converted into actions that could be transacted freely for the 40 %. Different rules for the remaining portion that could have been converted from the moment when the IPO was converted on December 11, 2014 that is, in other words, when Blackstone had no longer the majority in the company. At SIPO, the remaining units were converted into stock options and were thus paid at the end of 2013 in addition to the shares already delivered. Only 1,3% of the total shares (2.75%) available for distribution to the management of the company, in the form of equity awards, were activated.

Regarding the remuneration of the company's management, it contains, in addition to the long term incentive awards described above, a basic component and another variable, establishing a target for the company and the remuneration for the achievement, comparing the performances of the management and the compensation policy to the peers in terms of EBITDA growth and total shareholder return in accordance with the peer pay structure (e.g. Nike, Starwood Hotels & Resorts Worldwide, Choice Hotels, Wyndham Worldwide Corporation).

Looking at *Figure 8*, it appears that the CEO of HW obtained both base and total compensation below peers from direct competitors, possibly deriving from the high share premiums Nassetta and the remaining management of the company obtained, with the base component of the remuneration being lower, a usual feature for Private Equity companies (Leslie & Oyer, 2009). In this way, the management of HW in 2014 was remunerated through a strong preponderance of forms of variable remuneration, namely through performance shares, annual incentive or stock options.

So, in the case of the Hilton's CEO, the fixed remuneration was only 12% of its total remuneration of USD 9.9 million, an amount that in the rest of the management team amounted to 20%. The low weight of the base compensation contrasts with the weight of the remuneration through performance shares that was the main mean of remuneration: 38% in the case of the CEO and 34% in the rest of the management team. This was a clear indicator of the Nassetta's policy regarding compensation related to the strong hard work culture he always wanted to introduce in the firm.Thus, after 2013, the company's executive compensation plan became more modest, with an expense of USD 32 million in 2014 compared to EUR 313 million in 2013, thanks to the allocation of 5.6 million restricted stock units with conversion date in 2016, 520,000 performance shares with an average price of 23.56 USD obtained through Monte Carlo simulation, 986.000 Stock Options individually evaluated by the Black-Scholes model at 7.58 dollars each, USD 98 millions of deferred expenses. In addition, HW's salary system provides special compensation for the management team, in the event of a change of control, death or incapacitating illness or termination of the contract.

Top 10 Hotel CEO Pay Packages of 2013

Hotel Brand	CEO	Salary	Stocks, Options, Incentives, Bonus, Pension Change	All Other Compensation	Total
1. Wynn Resorts	Steve Wynn*	$4,000,000	$14,000,000	$1,601,381	$19,601,381
2. Las Vegas Sands	Sheldon Adelson**	$1,000,000	$9,426,241	$3,577,640	$14,003,881
3. Wyndham	Stephen Holmes*	$1,451,932	$11,268,679	$818,321	$13,538,932
4. MGM Resorts	James Murren*	$2,000,000	$8,427,683	$563,743	$10,991,426
5. Starwood Hotels	Frits van Paasschen	$1,250,000	$9,584,950	$78,744	$10,913,694
6. Marriott	Arne Sorenson	$1,200,000	$7,825,959	$132,661	$9,158,620
7. Hyatt Hotels	Mark S. Hoplamazian	$1,015,000	$5,805,458	$37,929	$6,858,387
8. InterContinental	Richard Solomons	$1,236,784	$413,944	$3,648,094	$5,298,822
9. Choice Hotels	Stephen Joyce	$928,846	$3,536,658	$201,881	$4,667,385
10. Hilton Worldwide	Christopher Nassetta	$850,000	1,290,420	$121,622	$2,262,042

Source: Securities and Exchange Commission filings
** Chairman and CEO*
*** Sheldon Adelson is Las Vegas Sands' chairman, CEO and treasurer*
Note: All of the other CEOs listed are president and CEO of their companies

Figure 8: 2013 Hotels CEO compensation, Source: Skits.com

The Initial Public Offering

"Hilton Worldwide Holdings Inc. ("Hilton Worldwide") announced today the pricing of its initial public offering of 117,640,624 shares of common stock at a price to the public of $20.00 per share. Hilton Worldwide is offering 64,102,564 of such shares and a selling stockholder is offering 53,538,060 of such shares. The selling stockholder has granted the underwriters an option to purchase up to an additional 17,646,093 shares at the initial public offering price less the underwriting discount. The shares are expected to begin trading on the New York Stock Exchange on December 12, 2013 under the ticker symbol "HLT." The offering is expected to close on December 17, 2013, subject to customary closing conditions." (Hilton Newsroom, December the 11th, 2013)

On December 2013 this announcement specified the number of shares, the total amount, the stock exchange and the date of the Secondary IPO made by Hilton through Blackstone. As we analyzed before in this case study, 2013 resulted one of the best years for the Real Estate sector since 2004 in terms of IPO. For that, Blackstone, after having done the same things few months before with *Extended Stay America*, understood that it was the right time to offer Hilton Worldwide Holding's stocks to the public. The Private Equity Group directed the operation by offering 11,5% of Hilton's shares in the proposal.

After the debt restructuring, Blackstone had invested a total of around 6,8 billion dollars on the hotel company: with the IPO, it wasn't selling any of its stocks, though. It maintained its 76% of the company. That meant that it was raising up to 2,37 billion dollars from the offer and that the initial investment was becoming successful. In fact, in 2007, Hilton was valued 26,7 billion dollars debt included: in 2013 the IPO was made for a total value of 32,5 billion dollars. This meant that the American private equity group was earning huge amounts of money from the operation that almost everybody was disapproving at the beginning. The use of proceeds of the offer is identified by the repayment of 1,25 billion dollars of debt. The occupancy rate was raising rapidly in that year and other hotel firms were attempting to make an IPO. Despite that it resulted as the second biggest IPO in 2013 overcoming the results of highly marketed offers such as

Figure 9: Cristopher J. Nassetta during the IPO at Wall Street, source: NYTimes, 2013

Twitter. "Blackstone has timed the Hilton IPO at the perfect market inflection points of increasing global consumer travel demand, daily room rates and occupancy," (Telegraph, December the 2nd, 2013) said Christopher Muller, a professor at Boston University's School of Hospitality Administration. Indeed, the US hotel index increased by 30% in 2014. The biggest hotel IPO was Hyatt Hotels, but, from that moment, the Hilton one became the leading Initial Public Offering in the sector.

In the announcement there are the names of the bank that acted as Joint Bookrunners for the offer and the co- managers: "*Deutsche Bank Securities, Goldman, Sachs & Co., Bank of America Merrill Lynch, Morgan Stanley, J.P. Morgan and Wells Fargo Securities are acting as joint bookrunners. Blackstone Capital Markets, Macquarie Capital, Barclays, Mitsubishi UFJ Securities, Citigroup, Credit Suisse, HSBC, RBS, Baird, Credit Agricole CIB, Nomura, Raymond James, RBC Capital Markets, UBS Investment Bank, CastleOak Securities, L.P., Drexel Hamilton, Telsey Advisory Group and Ramirez and Co., Inc. are acting as co-managers." (Hilton Newsroom, December the 11th, 2013)*

Underwriter	Number of Shares
Deutsche Bank Securities Inc.	25,880,937
Goldman, Sachs & Co.	25,880,937
Merrill Lynch, Pierce, Fenner & Smith Incorporated	18,822,500
Morgan Stanley & Co. LLC	16,469,687
J.P. Morgan Securities LLC	4,705,625
Wells Fargo Securities, LLC	2,646,914
Blackstone Advisory Partners L.P.	5,882,031
Macquarie Capital (USA) Inc.	2,058,711
Barclays Capital Inc.	1,470,508
Citigroup Global Markets Inc.	1,470,508
Credit Suisse Securities (USA) LLC	1,470,508
HSBC Securities (USA) Inc.	1,470,508
Mitsubishi UFJ Securities (USA), Inc.	1,470,508
RBS Securities Inc.	1,470,508
Robert W. Baird & Co. Incorporated	882,305
Credit Agricole Securities (USA) Inc.	882,305
Nomura Securities International, Inc.	882,305
Raymond James & Associates, Inc.	882,305
RBC Capital Markets, LLC	882,305
UBS Securities LLC	882,305
CastleOak Securities, L.P.	294,101
Drexel Hamilton, LLC	294,101
Samuel A. Ramirez & Company, Inc.	294,101
Telsey Advisory Group LLC	294,101
Total	117,640,624

Figure 10: Underwriters of the IPO, source: SEC filing S-1

The IPO was immediately considered a great success, not only for the amount *issued*: some sources claim the IPO was oversubscribed by a factor 9 *(Yu et al., 2013)*. Moreover, on the first day, the price of the shares reached 21,5$ at closing. For what concerns

Blackstone, it seemed that it was the first step to exit the 2007 LBO. On the other hand, Blackstone's CEO, Mr. Schwarzmann stated that he was intentioned to remain the owner of the firm for a long lapse of time. In fact, Blackstone, in the first days after the launch of the IPO, started realizing that, by maintaining the 76,4% of the company and calculating the Enterprise Value as 20$ per the number of shares issued, it owned 15 billion dollars by having invested roughly 6,5 billion dollars in 2007 registering an almost 3x for invested capital on enterprise value.

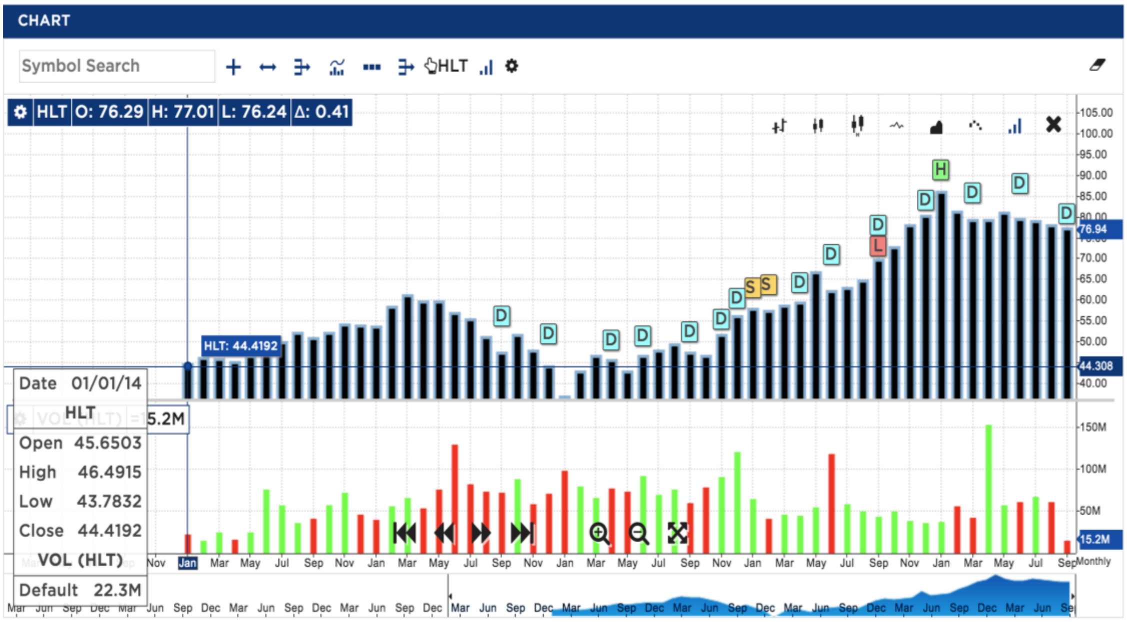


Figure 11:NYSE chart of the prices of the Hilton's stock publicly traded during the first two years, source: NYSE.com

As we can observe from the figure above, the listing on the NYSE registered a good result. The trend is ascending and, generally, the Hilton IPO is taken into consideration as an example useful to show how the real estate sector started growing again from 2013 on. The price on the NYSE, on the first day, was 45,65 USD per share: a huge profit for the underwriters that subscribed the whole amount of shares. One of the main features of this offer, as we said previously, was the commitment of Blackstone in remaining the owner of the company with a 76,4% stake.

On the prospectus published prior to the offer we can also read about the risk considered in issuing the offer:

Our business is subject to a number of business, financial and operating risks inherent to the hospitality industry, including:

- *significant competition from multiple hospitality providers in all parts of the world;*
- *changes in operating costs, including energy, food, compensation, benefits and insurance;*
- *increases in costs due to inflation that may not be fully offset by price and fee increases in our business;*
- *changes in tax and governmental regulations that influence or set wages, prices, interest rates or construction and maintenance procedures and costs;*
- *the costs and administrative burdens associated with complying with applicable laws and regulations;*
- *the costs or desirability of complying with local practices and customs;*
- *significant increases in cost for health care coverage for employees and potential government regulation with respect to health care coverage;*
- *shortages of labor or labor disruptions;*
- *the availability and cost of capital necessary for us and third-party hotel owners to fund investments, capital expenditures and service debt obligations;*
- *delays in or cancellations of planned or future development or refurbishment projects, which in the case of our managed and franchised hotels and timeshare properties controlled by homeowner associations are generally not within our control;*

- *the quality of services provided by franchisees;*

- *the financial condition of third-party property owners, developers and joint venture partners;*

- *relationships with third-party property owners, developers and joint venture partners, including the risk that owners may terminate our management, franchise or joint venture agreements;*

- *changes in desirability of geographic regions of the hotels or timeshare resorts in our business, geographic concentration of our operations and customers, and shortages of desirable locations for development;*

- *changes in the supply and demand for hotel services (including rooms, food and beverage, and other products and services) and vacation ownership services and products;*

- *the ability of third-party internet and other travel intermediaries to attract and retain customers; and*

- *decreases that may result in the frequency of business travel as a result of alternatives to in person meetings, including virtual meetings hosted on-line or over private teleconferencing networks.*

Any of these factors could increase our costs or limit or reduce the prices we are able to charge for hospitality services and timeshare products, or otherwise affect our ability to maintain existing properties or develop new properties. As a result, any of these factors can reduce our revenues and limit opportunities for growth.

(Hilton S-1, IPOs Filing, 12/2013)

Obviously, investing in such an activity with a high level of indebtness, may have granted high returns to investors. Reading the prospectus of the offer, it is clear that the high level of risk related to the acquisition of Hilton's stocks had to be specified in order not to incur in litigations.

In order to protect investor from those risks, the offer was pondered by including several restrictions such as the lock-up agreement of 180 days or the promise not to pay dividends for several years: *"We have no current plans to pay any cash dividends" (Hilton S-1, IPOs Filing, 12/2013).*

The latter was intended to preserve the availability of cash flow to cover the interest burden related to the high levels of debt. As of September 30, 2013, this amounted to approximately 13 billion dollars including 1,006 million dollars of non-recourse debt.

Another important feature of this offer was the possibility, for the underwriters, to exercise the green shoe option, namely the chance to buy other 17 million shares making the total offer reach the number of 135,286,717 shares. The exceeding portion would be provided by Blackstone that would have maintained 765,932,085 shares even in the case the overallotment option was exercised.

"We, our officers, directors and holders of certain of our outstanding shares of common stock immediately prior to this offering, including our Sponsor, that collectively will own 783,578,178 shares following this offering (or 765,932,085 shares if the underwriters exercise their option to purchase additional shares in full), will sign lockup agreements with the underwriters that will, subject to certain customary exceptions, restrict the sale of the shares of our common stock held by them for 180 days following the date of this prospectus." (Hilton S-1, IPOs Filing, 12/2013).

Post-IPO Financials

After the issuance of the public offer, Hilton became public again with all the pros and cons that this kind of event creates. Some, like Professor Kaplan of the University of Chicago, said that compared to an investment in the public markets, Blackstone's investment in Hilton has been good but not great. Since the start of 2007, the Standard & Poor's 500 stock index is up 25 percent. Blackstone more than doubled its money. "This is a good deal if you're measuring it relative to the public market," Mr. Kaplan said. *"But it's not a home run."* Other alternative investments and asset classes have performed better over the last six years.

Even against Blackstone's internal expectations, the Hilton deal, while an enormous winner, may not tick every box. Most private equity firms aim for an annual internal rate of return of about 18 to 20 percent. Spread over six years, the investment in Hilton looks to have yielded about 16 percent for Blackstone. *"If you look at it against target returns, it's not amazing"* Mr. Kaplan said. *(The New York Times, December 2013)*

With the help of Hilton's financial statements, we will see the consequences of such an operation considering the amount of debt they had registered in their balance sheet and that they promised to repay partially by using 1250 million dollars coming from the IPO.

HILTON WORLDWIDE HOLDINGS INC.
CONSOLIDATED BALANCE SHEETS

(in millions, except share data)	December 31, 2014	December 31, 2013
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 566	$ 594
Restricted cash and cash equivalents	202	266
Accounts receivable, net of allowance for doubtful accounts of $29 and $32	844	731
Inventories	404	396
Deferred income tax assets	20	23
Current portion of financing receivables, net	66	94
Current portion of securitized financing receivables, net	62	27
Prepaid expenses	133	148
Income taxes receivable	132	75
Other	70	29
Total current assets (variable interest entities—$136 and $97)	2,499	2,383
Property, Investments and Other Assets:		
Property and equipment, net	7,483	9,058
Property and equipment, net held for sale	1,543	—
Financing receivables, net	416	635
Securitized financing receivables, net	406	194
Investments in affiliates	170	260
Goodwill	6,154	6,220
Brands	4,963	5,013
Management and franchise contracts, net	1,306	1,452
Other intangible assets, net	674	751
Deferred income tax assets	155	193
Other	356	403
Total property, investments and other assets (variable interest entities—$613 and $408)	23,626	24,179
TOTAL ASSETS	$26,125	$26,562

Figure 12: Hilton Worldwide Holding INC. Consolidated Balance Sheets: Assets, Source: Hilton Annual Report 2014

By looking at the consolidated balance sheets we can easily notice how the long term debt was reduced from 11,750 million dollars in 2013 to 10,803 million dollars in 2014. This information lead to a general decrease in total Liabilities but an increase in the current ones.

Moreover, looking at the assets, we can see that 1,543 million dollars are Property & Equipment held for sale. On the description of the item in the Annual Report, it is specified that the property that are intended to be sold within a year will be embedded in that item.

HILTON WORLDWIDE HOLDINGS INC.
CONSOLIDATED BALANCE SHEETS

(in millions, except share data)	December 31, 2014	December 31, 2013
LIABILITIES AND EQUITY		
Current Liabilities:		
Accounts payable, accrued expenses and other	$ 2,099	$ 2,079
Current maturities of long-term debt	10	4
Current maturities of non-recourse debt	127	48
Income taxes payable	21	11
Total current liabilities (variable interest entities—$162 and $86)	2,257	2,142
Long-term debt	10,803	11,751
Non-recourse debt	752	920
Deferred revenues	495	674
Deferred income tax liabilities	5,216	5,053
Liability for guest loyalty program	720	597
Other	1,168	1,149
Total liabilities (variable interest entities—$788 and $583)	21,411	22,286
Commitments and contingencies—see Note 25		
Equity:		
Preferred stock, $0.01 par value; 3,000,000,000 authorized shares, none issued or outstanding as of December 31, 2014 and 2013	—	—
Common stock, $0.01 par value; 30,000,000,000 authorized shares and 984,623,863 and 984,615,364 issued and outstanding as of December 31, 2014 and 2013, respectively	10	10
Additional paid-in capital	10,028	9,948
Accumulated deficit	(4,658)	(5,331)
Accumulated other comprehensive loss	(628)	(264)
Total Hilton stockholders' equity	4,752	4,363
Noncontrolling interests	(38)	(87)
Total equity	4,714	4,276
TOTAL LIABILITIES AND EQUITY	$26,125	$26,562

Figure 13: Hilton Worldwide Holding INC. Consolidated Balance Sheets: Liabilities and Equity, Source: Hilton Annual Report 2014

The property will stop depreciating and any gain or loss from disposal will be registered in the following year. The 1,543 million are surely referred to the **Waldorf Astoria** in New York: indeed, in 2014 the most famous hotel in New York, was sold to the Chinese Insurance company called Anbang for 1,95 billion dollars. Nassetta said after the disposal: "*This relationship represents a unique opportunity for our organizations to work together to finally maximize the full value of this iconic asset on a full city block in Midtown Manhattan*" (*New York Times, October 6, 2014)*

Figure 14: The Waldorf Astoria in New York, Source: TripAdvisor.com

For what concerns the other items, they are stable changing by few percentage points over the year.

On the other hand, the statements of operations give us the perception that Hilton was working really well, and that Cristopher Nassetta had its reasons thinking about the internationalization, the digitalization and the restructuring of the HHonors as necessary things. Indeed, the first thing that our eyes go to is the steady and significant increase of the Revenues generated followed by a lower increase in the expenses. This led to a high growth of EBITDA and Operating Income as well that passed respectively from 1,705 (Operating Income plus Depreciation and Amortization) and 1,102 to 2,301 and 1,673 million dollars. This meant an increase in EBITDA of 35% and a 52% growth in Operating income in the year following the offer. Net Income increased hugely as well

HILTON WORLDWIDE HOLDINGS INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in millions)	Year Ended December 31, 2014	2013	2012
Net income	$ 682	$460	$359
Other comprehensive income (loss), net of tax benefit (expense):			
Currency translation adjustment, net of tax of $(73), $39, and $102	(299)	94	138
Pension liability adjustment, net of tax of $27, $(37), and $23	(45)	60	(41)
Cash flow hedge adjustment, net of tax of $5, $(4), and $—	(9)	6	—
Total other comprehensive income (loss)	(353)	160	97
Comprehensive income	329	620	456
Comprehensive income attributable to noncontrolling interests	(14)	(63)	(21)
Comprehensive income attributable to Hilton stockholders	$ 315	$557	$435

Figure 15: Hilton Worldwide Holdings Inc. Consolidated Statement of Comprehensive Income, Source: Hilton Annual Report 2014

changing from 460 to 673 and so recording a 46,3% increase: great statistics that will take the American hotel firm at the top again. For what concerns the most important ratios, we

HILTON WORLDWIDE HOLDINGS INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31,		
(in millions, except per share data)	2014	2013	2012
Revenues			
Owned and leased hotels	$ 4,239	$4,046	$3,979
Management and franchise fees and other	1,401	1,175	1,088
Timeshare	1,171	1,109	1,085
	6,811	6,330	6,152
Other revenues from managed and franchised properties	3,691	3,405	3,124
Total revenues	10,502	9,735	9,276
Expenses			
Owned and leased hotels	3,252	3,147	3,230
Timeshare	767	730	758
Depreciation and amortization	628	603	550
Impairment losses	—	—	54
General, administrative and other	491	748	460
	5,138	5,228	5,052
Other expenses from managed and franchised properties	3,691	3,405	3,124
Total expenses	8,829	8,633	8,176
Operating income	1,673	1,102	1,100
Interest income	10	9	15
Interest expense	(618)	(620)	(569)
Equity in earnings (losses) from unconsolidated affiliates	19	16	(11)
Gain (loss) on foreign currency transactions	26	(45)	23
Gain on debt extinguishment	—	229	—
Other gain, net	37	7	15
Income before income taxes	1,147	698	573
Income tax expense	(465)	(238)	(214)
Net income	682	460	359
Net income attributable to noncontrolling interests	(9)	(45)	(7)
Net income attributable to Hilton stockholders	$ 673	$ 415	$ 352
Earnings per share:			
Basic and diluted	$ 0.68	$ 0.45	$ 0.38

Figure 16: Hilton Worldwide Holdings Inc. Consolidated Statement of Operations, Source: Hilton Annual Report 2014

can observe that the Debt over EBITDA was more than 5X[22] respect to the average of the competitors it may be considered a high: Marriot's registered a 2,5X while Hyatt 0,9X and Starwood 0,8X. It was, however, reduced by 9 times respect to the beginning of the operations from Blackstone.

[22] *Ratio breakdown: Debt is composed by long term debt (10803ml $) and non-recourse debt (752 ml $) and EBITDA is EBIT plus Amortization and Depreciation (2301 ml $)*

Third Section

In this third chapter we will discuss and evaluate the final outcome of the whole operation by analyzing also the sale of a portion of Hilton to the Chinese Group HNA. Moreover, we will examine the actual situation in the hotel sector, the financial statements of Hilton Worldwide in 2017 and the first two quarters of 2018. Finally, we will try to draw possible future scenarios.

The Spin-Off

In 2016, the Management of Hilton, led by Christopher J. Nassetta, decided that a part of the production should have been split from Hilton Worldwide by dividing the company in three entities, two of which completely new, but embedding the brand they were representing while composing the portfolio of brands under Hilton.

On June 2, 2006 the Form 10 Registration Statement was filed under the SEC (U.S. Security and Exchange Commission) giving birth to three publicly traded companies: Hilton (simplified), Park Hotels & Resorts and Hilton Grand Vacation (HGV). The aim of the operation was to create a capital light, fee-based business and generating a distinction between the owned properties and the properties that weren't fixed assets for the Hilton Worldwide Company but that injected cash flow through fees. Moreover, the spin-off was made in order to generate tax efficiency and to take advantage of the capital market that seemed florid during that period. Indeed the two new firm

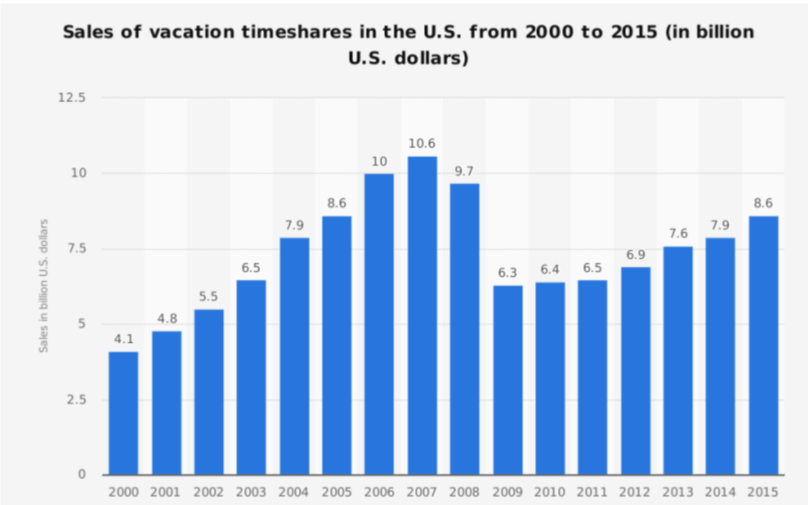


Figure 17:Sales of vacation timeshares in the US, Source: Statista/ ARDA, 2018

created from the spin-off made their debut on the NYSE under the ticker HGV for Hilton Grand Vacation and PK for Park Hotels & Resort Inc.

Behind the whole project there are the new tendencies driven by the customers: the timeshare sector was growing again after the collapse due to the crisis. That could have represented an opportunity for Hilton to gain competitive advantage respect to its competitors by making independent this unit. In 2016, HGV was to consider a rapidly growing timeshare company that markets and sells vacation ownership intervals ("VOIs"), manages resorts in top leisure and urban destinations, and operates a point-based vacation club. It had 46 resorts with 7,402 rooms located in the most visited places in the United States (e.g. Hawaiian Islands, New York City, Las Vegas…) featuring high quality services and spacious and luxury accommodations. The company counted 255,000 members that could choose the place where to spend their vacations having the possibility to exchange their VOI in order to visit any structure among the 4,600 properties available. Moreover, HGV offered the possibility to have experimental vacation offer such as cruises and guided tours. Since it was a leading innovator in the service it experimented a change from a highly capital intensive business to a capital efficient business by chasing the strategy of the fee-for-service and Just in Time inventory. This policy was pursued in order to reach a 50/50 sales mix of owned and fee-for-service inventory as to optimize growth and cash flows. The management of this new company was entrusted to Mark Wang that had led the operations of the timeshare segment for Hilton since 2008.

For what concerns Park Hotels and Resort, it was a leading lodging real estate company with a miscellaneous portfolio of historical and important hotels plus several resorts with significant underlying real estate value. In 2016, its high-quality portfolio consisted of 69 premium-branded hotels and resorts with nearly 36,000 rooms located in major U.S. and international markets. Over 85% of Park Hotels and Resorts' rooms serve the luxury and upper upscale customers and nearly 90% are located in the United States. Over 70% of its rooms are located in the central business districts of major cities and resort/conference destinations. The primary aim of the brand, in fact, was to mix the business travel with the luxury and beauty of the vacations. Park Hotels and Resorts was seeking attractive long-term total returns by enhancing the value of its exceptional properties and utilizing its scale to efficiently allocate capital while maintaining a strong and flexible balance sheet. The management of the firm was entrusted to Tom Baltimore as CEO and Sean Dell' Orto as CFO. Both of them possessing a long and good experience in the real estate sector.

Following the plan announced in February 2016 by Cristopher J. Nassetta, the spin-off was tax-free for the shareholders of its timeshare business, Hilton Grand Vacations, and the bulk of its real estate business, with the intention of electing real estate investment trust (REIT) status for Park concurrently with completion of the spin. Hilton's core Management & Franchise business will continue operating under the Hilton name. Hilton's shareholder were going to possess the three kind of stocks after the transaction, and some modifications to the distribution of the latter were made in order to respect the Internal Revenue Service. No approval for the operation was asked to shareholders and so the process was conducted by the management only. The election of Park Hotel and Resort as REIT costed approximately 200 million dollars to the Company in order to pay special dividends. Moreover, the whole spin-off operation costed Hilton 250 million dollars.

The exchange ratio for the existing shareholder was 1 share of PK for every 5 shares of HLT, and 1 share of HGV for every 10 shares of HLT. After the Spin-Off, HLT engaged to complete a 1 for 3 reverse stock split. The record date of the operation was on December 15th, 2016 while the distribution date was fixed on January the 3rd, 2017.

Figure 18:HGV first two years' stock price, Source: YahooFinance

Figure 19: PK first two years' stock prices, Source: YahooFinance

As we can see from the graphs above, the stocks of the two companies have been increasing their price consistently. The issuance created 206 million shares for PK and 96,9 for HGV and they opened at the first day at the price of 25,35 for HGV and 30,21 for PK. Today PK has an Enterprise Value of 9,46 billion dollars, with an EV/EBITDA of 12,88 and an operating Cash Flow of 527 million dollars. On the other hand, HGV has an enterprise value of 4,19 billion dollars, an EV/EBITDA of 10,36 and a lower operating cash of "only" 45 million.

The personal interpretation of the operation is to address at the will of the management to achieve a low grade investment grade credit profile and using these benefits in order to make the growth of the whole company consistent and always bigger. The Payout Ratio was maintained around 20%-25% in order to be appealing for investors, moreover, the leverage ratio had to be around 3.0X-3.5X.

By looking at the Investor Relations published prior to the spinoff, presented by the Hilton's CFO, Kevin Jacobs, the strategy of the company was clear:

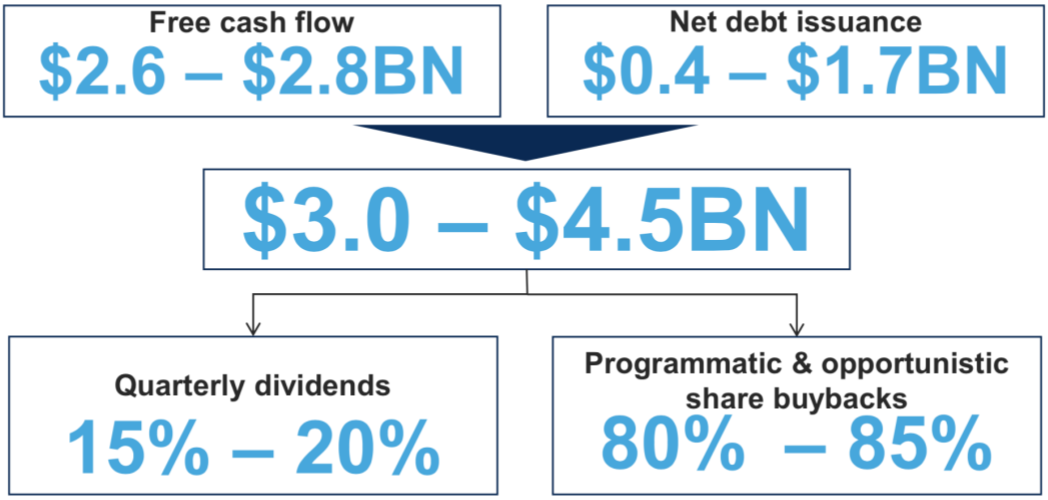


Figure 20: Hilton Projections on free cash flow and net debt issuance, Source: Hilton Investor Relation, 2016

In 3 years, the cash flow generation should have touched at least the 2,6 billion dollars while the issuance of net debt had to be 1,7 billion dollars maximum. The latter in order to pay quarterly dividends and, especially, to buyback shares in order to make the growth higher year over year. The Internationalization strategy was expensive for the firm, so the need for free cash flow generation was urgent. On the other hand, the results were extraordinary: from 2007 to 2016, Hilton appeared in 26 new countries, its pipeline growth was around 156% and the international service growth was 451%.[23] The strategy of the company was to sign the best deals while prioritizing efforts and especially optimizing the portfolio. In order to do so, they wanted to initiate the presence in a country and extending the latter by establishing facilities and platform. The last part of the strategy was to grow and optimize the platforms adding brands and creating a scalable profitable network for future growth. Since the IPO in 2013, Hilton reached huge performance by increasing its Adjusted EBITDA by 39% and so, reaching 2,969 million dollars. Furthermore it increased its Adj. EBITDA margin realizing the 41,2% of the latter and the HHonors members increased by 49% (58 million people). The net Debt reduction amounted to 2,6 billion dollars and the sell of the Waldorf Astoria to the Chinese and the closing of the operation with HNA[24] were changing the Hilton dimension.

[23] *Hilton Investor Relation, 2016*
[24] *Discussed on the next paragraph*

The sell to HNA

The will to internationalize the company lead Hilton to invest on emerging market significantly: that meant to expand their hotel network and business operations by hitting countries that were demanding for the western hotel chains in their country.

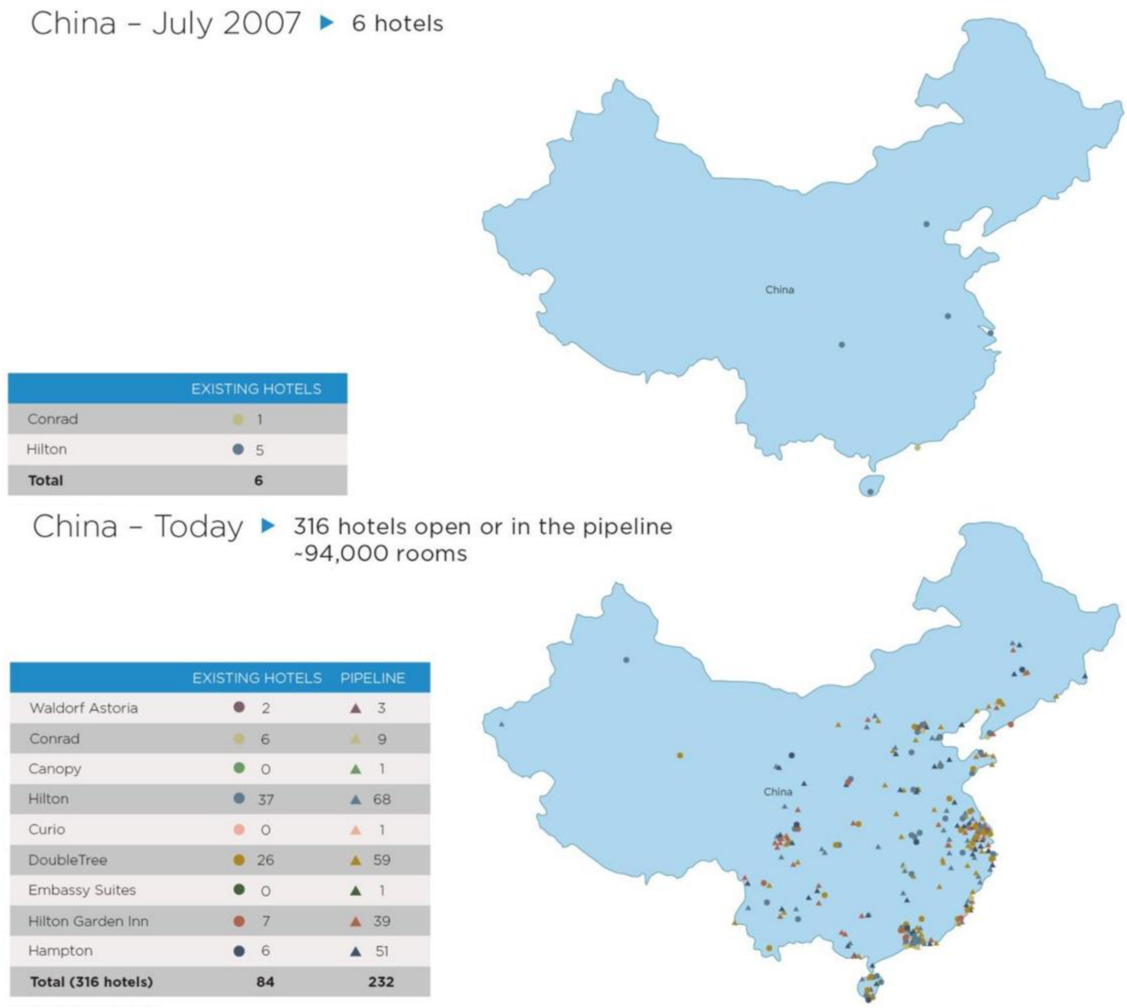


Figure 21: Hilton's hotel in China, difference between 2007 and 2016, Source: Greater China

As we can see from the illustrations above, the expansion was terrific: in 6 years the number of Hotels on the Asiatic country was increased by 78 hotels and the pipeline counted 232 properties while in 2007 it wasn't present on the soil. The huge operation conducted by Mr. Nassetta created interest among the Asian investors, huge curiosity started involving the management of HNA.

The Chinese group was founded in January 2000 following a transformation of Hainan Airlines, Chinese public company listed in 1999, and in July 2000 it was already creating a new branch by establishing the HNA Hotel Group. It was run by Chen Feng and Chen Guoping, backed by the Hainan provincial government, which is the largest shareholder. In 2003, Fortunes ranked the company as China's top listed, from that moment on it started investing everywhere in the world by diversifying: in 2010 it bought Allco Finance[25], in 2011 GEsea CO[26], in 2013 it takes 20 percent stake in HN Hotel[27] by starting investing in the hospitality sector, during the October of the same year it bought TIP Trailer Leasing[28], two years later, in 2015, it purchases Swissport[29] and started being a Uber strategic partner. During the last years it has acquired Categroup, an aviation catering group, for 1,5 billion dollars and purchased a 9,9% stake in Deutsche Bank for 800 million dollars, but we will focus on the acquisition of a 25% stake in Hilton hotels.

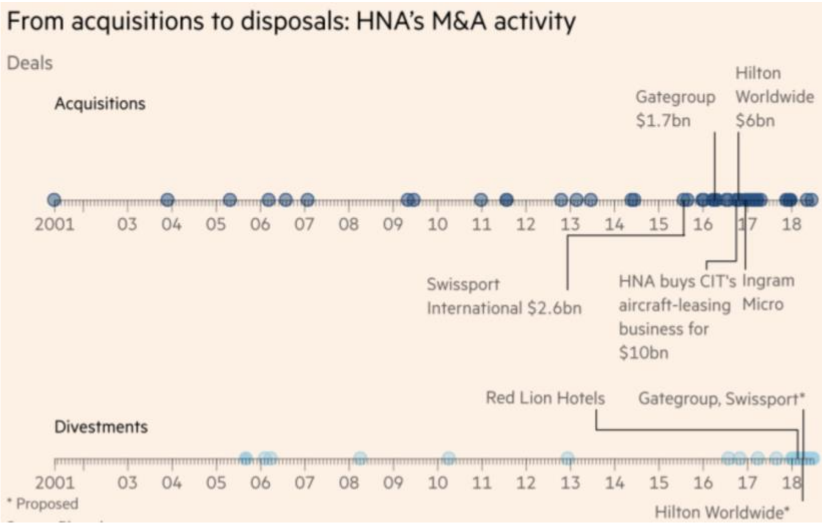


Figure 22: Timeline: HNA's Acquisition & Disposal, Source: FT.com, Bloomberg, 2018

In October 2006, rumors about the possibility for Blackstone to sell a significant stake of its Hilton shares started spreading around in Wall Street. At the end of the same month, Blackstone decided to sell the 25% of its property to HNA leaving the American private equity group, that was divesting over time, with only a 21% stake. The sell happened few days before the spin-off that split Hilton into three entities, this led people to think that the latter wasn't adding value to Hilton and raised a question among investors: Why did

[25] *Australian Aircraft leasing business*
[26] *Shipping container leasing company acquired for 1 billion dollars*
[27] *One of Europe top hotel chain*
[28] *Largest trailer leasing company in Europe*
[29] *Air Services Group bought for 2,8 billion dollars*

Blackstone sold such a significant stake before an operation that should add value to the company?

Actually, the private equity group sold the shares for $26,25 that is to be considered a huge result if we take in to consideration the IPO that took place in 2013 and that was priced $20 per share. On the other hand, some say that such an operation is not typical for a private equity firm that works on long term horizons, this appeared a short-sighted strategy made in order to lock in performance fees and appease Blackstone shareholders. Cristopher Nassetta, however, saw significant opportunity coming from the disposal, in fact, the deal, in its opinion, *"will open new opportunities for the brand and guests around the world, particularly in light of HNA's strong position in the fast-growing Chinese travel and tourism market, the largest outbound travel and tourism market in the world"* (Investopedia, October 24th, 2016). In fact, HNA in 2016, operated or had investments in 2,000 hotels with over 300,000 rooms and had 1,250 aircrafts carrying over 90 million people to 260 cities worldwide (Forbes, October 24th,2016). Furthermore, the operation brought huge returns for the private equity group, considering that in 2007 it paid $8,60 per share and that the investment was representing a 205% return for Blackstone (without counting the additional 35 cents dividend per share paid by HLT). (Bloomberg, November 3rd ,2016)

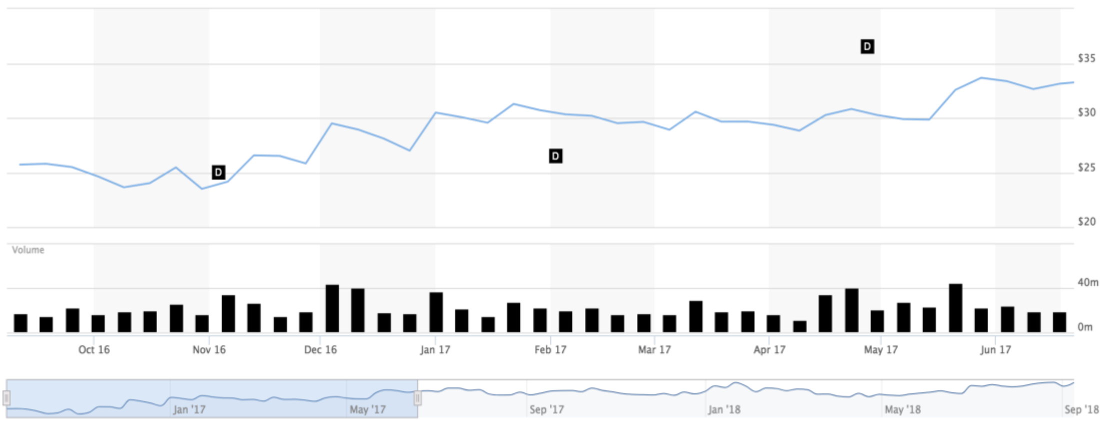


Figure 23. Blackstone share's prices after the sell to HNA, Source: Marketwatch, 2018

prospective were completely changed.

The whole operation costed HNA 6,5 billion dollars and the price paid by the Chinese group granted a 15% premium to the stock's closing price on the day of the acquisition. Let's not forget that the operation lead HNA to become the majority shareholder in

Hilton, but the operation granted HNA only 2 board seats and came with the obligation not to sell the shares for 2 years.

Meanwhile, Hilton's fiercest competitor, Marriot, completed the acquisition of Starwood hotel increasing its bargaining power in the hotel industry.

HNA's Crisis

In 2018, HNA announced that it was ready to put its Hilton's 82,5 million shares on the market. The company, owning the 25% of the American hotel company, sought to offload its balance sheet in order to recover partially for the significant amount of debts due in 2019 and 2020.

In the filings with the SEC[30] HNA said it didn't want to undisclosed information related to the timing and the execution of the operation, on the other hand the process would respect market conditions. The need for HNA to raise money was highlighted by the attempt to float its 65% stake of the swiss airline caterer group Gategroup but it had to withdraw the offer after negotiating with the management of the company. The only obstacle to the sale of the stake by HNA was the lock-up agreement signed when the acquisition of Blackstone's Hilton shares took place. Indeed, they were obliged not to sell the shares for 2 years unless the Hotel company's board approved the transaction. This was the reason why the Categroup SIPO

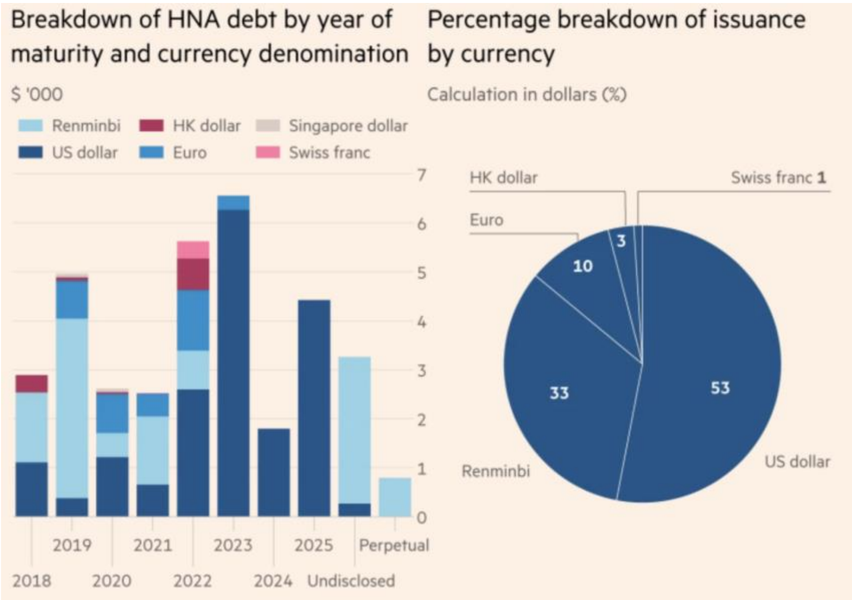


Figure 24: HNA's debts breakdowns, Source: FT.com, 2018

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[30] *Security Exchange and Commission*

didn’t happen. Hilton’s board, by the way, approved the transaction with the condition of a share buy-back. In fact, the hotel company let HNA sell 72,5 million shares out of the 82,5 million shares owned by the Chinese company buying back 10 million shares and granting that no shareholders had a bulky stake in Hilton. Moreover, the American hotel company could have increased the number of share in case the underwriters didn’t exercise their overallotment option. The news hit the market making Hilton share raise consistently after the rumors and especially the volume reached peaks that touched 52 millions of shares traded (see graph below).

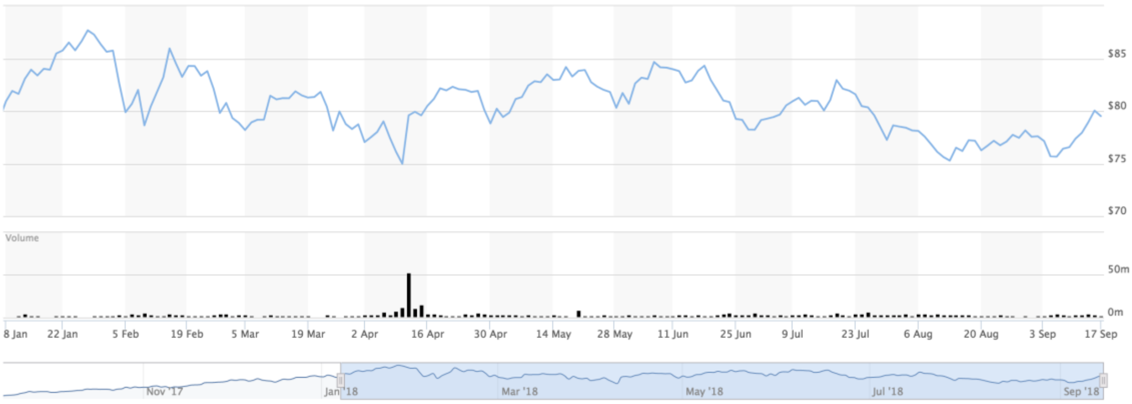


Figure 25: HLT stock prices Jan ’18 - Sep ’18, Source: MarketWatch, 2018

Figure 26: Wang Jian, co-founder of HNA, Source: Reuters

Unfortunately, on July, the co-founder of HNA, Wang Jian, died falling down from a wall near to a scenic church in France, Provence. This complicated enormously the plans of the corporation because of its role of major shareholder in the company with a 15% stake. The brand was risking because of its investments amounting to 40 billion that made the regional firm become an important actor in the hospitality and travel/leisure sector. While the co-founder, Chen Feng, assess that the problem of HNA is due to the poor liquidity, some investors are strictly convinced that the will to be present in several sector have made the company weak. Indeed, the debt of the firm is to be considered of around 30 billion dollars now (FT.com, July 4th, 2018).

Future Scenarios

In February 2018, Mr. John Gray was elected Chief Operating Officer of the Blackstone Group and Mr. Tony James was entrusted to the role vice-chairman in a full-time role. Both the managers have to report now to Mr. Schwarzmann that was pushed to leave its Chairman role because of its age and the increasing pressure he had to cope with. A change of this importance in a company like Blackstone is surely very significant for investors especially in the case when funds are expected to close in few months/years. Mr. Gray was certainly the best profile as a successor of Mr. Schwarzmann because of the trust he gained by achieving stellar performances when he was head of the Real Estate unity. But these kind of changes in the management don't come alone.

Indeed, during May 2018, Blackstone announced the exit from Hilton by selling its about 5,8% remained from all the little sales it did all over the 11 years spent owning the hotel company. It will make a sale of 15,8 million shares that at a price of more than 83,3$ per share would generate a return of nearly 1,32 billion Dollars. Hilton declared that none of that revenues would be injected in the company but they will benefit from the sale by repurchasing 1,3 million shares from Blackstone's selling shareholder. As we saw in the paragraph above, Blackstone has been gradually shredding its stake since 2014, a year after the IPO, cashing in almost 5 billion in only two tranches. Then the sell to HNA granted the American private equity group 6,5 billion dollars, so, considering this last sale the outcome of the investment is to be considered really good.

Another subject we have to observe is the growth related to the hospitality sector in order to understand the moves that Hilton could carry out from this moment on.

First of all we have to underline the performances of the hotel industry in terms of growth: as we saw in the first chapter, one of the most important metrics for the sector is the RevPAR. The latter has registered a consistent increase during the last 8 years, and, apart from two downturns timespans, it has been growing from1990 on.

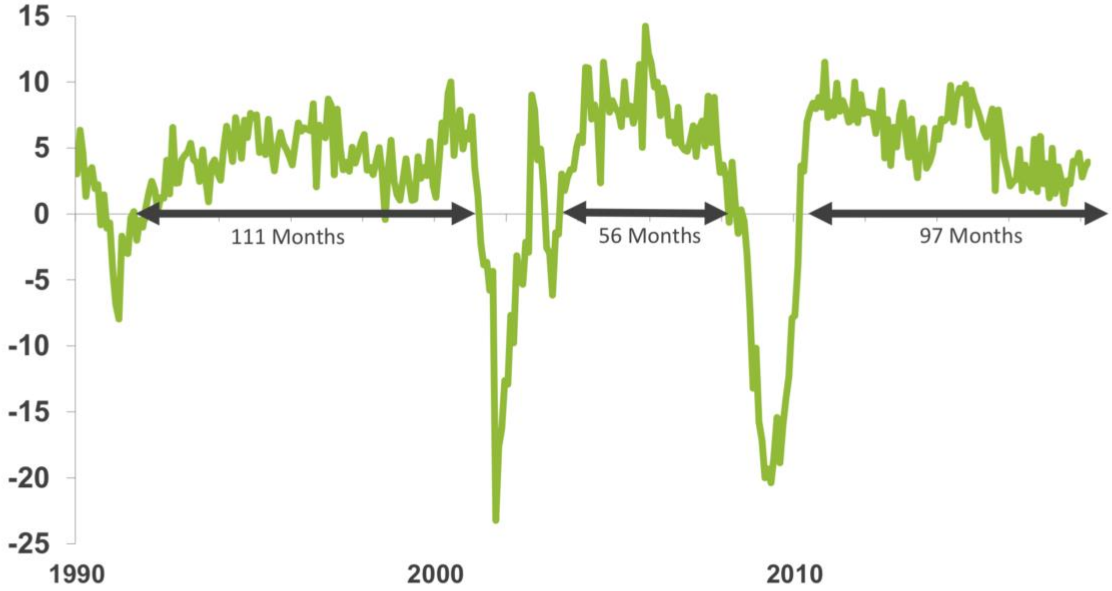


Figure 27: RevPAR percentage change 1990-2018, Source: STR

Moreover, the room supply has changed positively by 1,9% in the last year with a room demand increase of more than 2,8%. 2018 has been a great year for other metrics too such as occupancy: it has broken a record by reaching 66,1% and growing of the 0,8% over the year. ADR and RevPAR are record breaker too in 2018 by reaching respectively $127 and $84[31]. Room revenue increased by 4,9% too.

For what concerns the North American sector, the one where Hilton has the majority number of hotels worldwide, the RevPAR has increased 2,9% in the US: New York has

[31] *Growth over year respectively 2,1% and 2,9%. Source: 12MMA, March 12, 2018*

recorded an increase of 1,2% confirming its status of tourism's leader in the US while two of the most famous cities in the entire country, San Francisco and Washington D.C. have registered a decrease in the Revenue per available room respectively of 2,6% and 2%. By the way, the total growth of the RevPAR in the US is 3,3% in 2018.

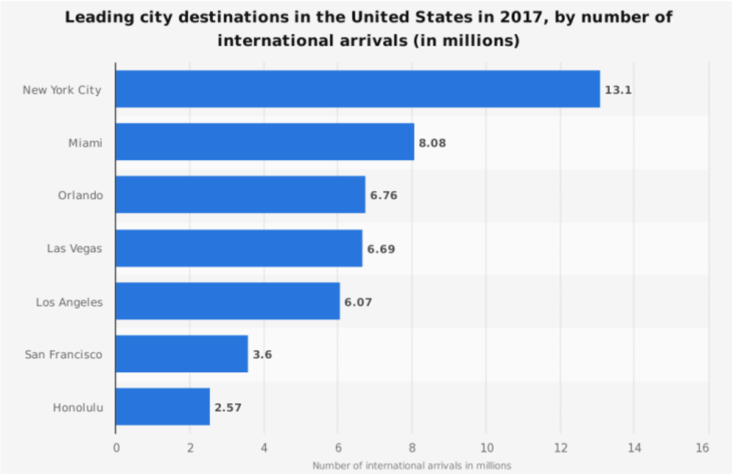


Figure 28: Number of visitors per city in the US, Source: Euromonitor

Another good metric used to understand the trend of the hospitality market is the ADR, as we can see from the graph below, it increased for every segment and it can be considered the real driver of the consistent RevPAR growth.

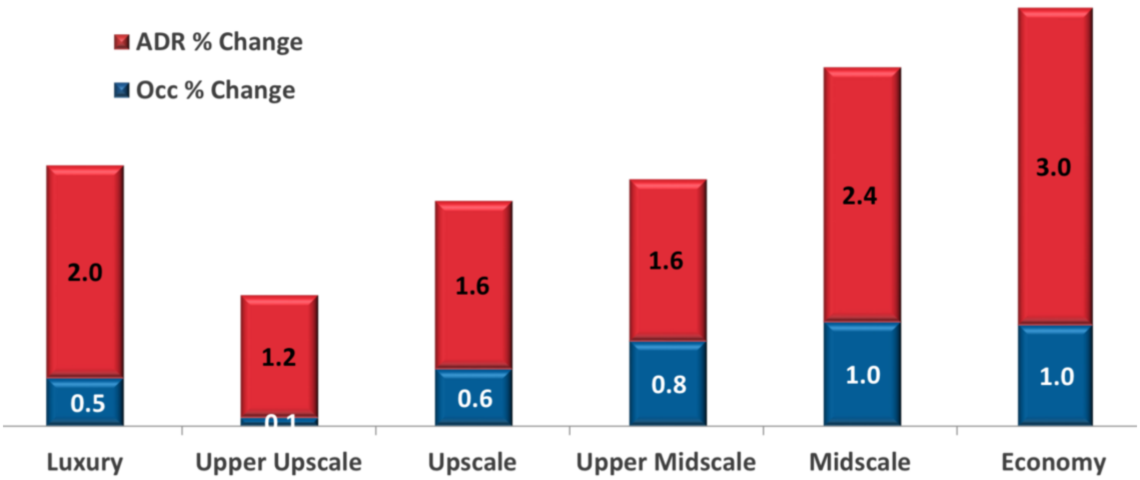


Figure 29: ADR and Occupancy % change over 2018 for each customer sector, Source: STR, 2018

Occupancy growth is still consistent but less significantly respect to the others metrics, anyway, it is increasing more slowly due to the fact that, especially for certain segments, the occupancy rate is so high that if it was growing more rapidly, the market would be saturated.

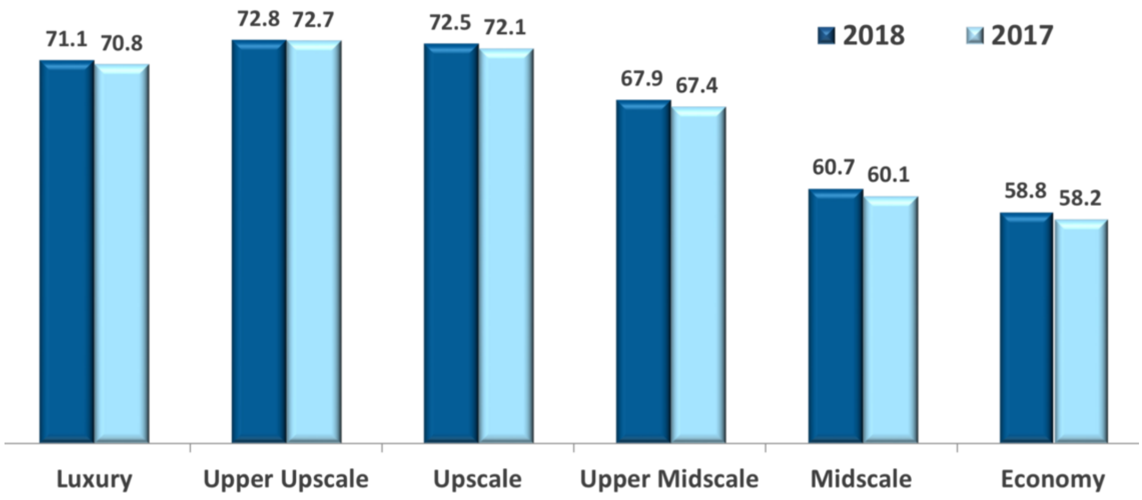


Figure 30: Occupancy rate in 2017 vs 2018 for segments, Source: 12MMA

As we can observe from *Figure 30,* the less saturated market is the economy one, this may be due to the fact that lower social classes struggle to find money to go on vacation since the economy is still recovering from the huge crisis of 2008.

Another subject that is important to highlight is that the demand is increasing more rapidly than the supply, this leads the hotel companies to invest in Real Estate, focusing on the location that are more requested from the customers. As we can see from the table below, the city where the number of rooms under construction is higher in the US is Nashville, TN. The statistics are a bit surprising because testify the fact that the attention of the public is moving to other destinations. Indeed, in the chart, we can see cities like Denver, Seattle and Dallas other than the always popular New York City.

Market	Rooms In Construction	% Of Existing
Nashville, TN	5,123	12%
New York, NY	11,965	10%
Denver, CO	4,610	10%
Seattle, WA	3,692	8%
Dallas, TX	6,647	8%

Figure 31: Rooms under construction in the US soil, Source: STR, 2018

For what concerns the stocks of Hilton's main competitors, we can observe that in the last year Marriott and Host have registered a good performance in terms of stock price together with Hilton that grew 19,97% over the year. On the other hand, companies such as Hyatt, Wyndham and Starwood didn't succeed in having a good market performance. For what concerns the C-Corp, where Hilton and Marriott are included, we can assert that in 2017 the two firms were trading at 15X and 16X NTM EBITDA respectively and comparing the performances with those recorded by huge brands such as Apple (trading at 12,5X NTM EBITDA) we can easily say that the hospitality sector is still really attractive and profitable. Since the growth in terms of RevPAR is consistent but still records a single digit increased over the last years, the brands operating in the hospitality sector should continue evolving by changing their business model and stop thinking as a simple hotel but more like an OTA (Online Travel Agency). These could grant the brands more visibility, more fees and good feedbacks from the user: indeed, Nassetta always believed that opening to the online world was one of the key move and strategy to implement in order to be competitive.

Figure 32: Hilton's competitors stock prices over the year, Source: Bloomberg

Conclusions

At the light of what we have been discussing all over the thesis, important messages have to be taken into consideration. First of all, we have to underline the fact that the transaction lead to a *win-win-win situation*. Indeed, Blackstone multiplied its investment by almost 3 times choosing the right timing for the exit and after leading Hilton out of the crisis through a good management. Moreover, the old Hilton’s management cashed in a 40% premium and saved the company. The bad administration of the Hotel firm was leading it to bankruptcy and the Beverly Hills headquarters were more concerned about the Hollywood life than on implementing the strategies that were necessary in order not to make a historical brand such Hilton collapse. The family’s scoops involving Conrad Hilton nephew, Paris, were changing the perception of the brand and laziness in the offices was influencing the company’s results. It is important, for that, underline the Blackstone’s vision about the subject. First of all, they understood that the room for improvements of the firm was huge, secondly, they made compromises in order to please the old management in terms of money. Indeed, even if the private equity market was booming during that years, the premium paid was up above the average. Another huge Blackstone’s merit was to assign the role of CEO to Christopher Nassetta: he was able to leverage the crucial flaws that were affecting the company. He introduced the *immersion* and *evaluation* programs in order to motivate workers and to make them conscient about what was going in the administrative offices and in the hotels. Moreover, he changed the company’s strategy by implementing a deep internationalization and digitalization of the firm. However, the operation had its up and downs, during the crisis, Blackstone lost nearly 70% of the investment made, making people concerned about the private equity group investment strategy. In any case, there’s something to underline in the way Blackstone cope with the crisis. The way they decided to negotiate the debt restructuring and the persistency in implementing the strategy during that harsh economic years resulted a value added for the firm. After the crisis, in fact, as we have seen in the last part of the work, Hilton recovered its position as a leader in the hospitality sector.

The subjects faced during this dissertation were many: we analyzed the LBO, the IPO, the internationalization strategy, the debt restructuring via the Spin-Off.

The last years for these two famous companies were troubled but also fruitful, working on this thesis helped me watching these kinds of operation from a different perspective. I tried to be as clear as possible in defining all the steps that lead to the actual situation and surely, most of my purposes have been achieved by finding a large number of authoritative sources. My personal interpretation for this dissertation is split in two main factions. On one side, the real estate market and so, the hospitality sector, is one of the most profitable in the whole economic system: when you buy a house, you know that in 20 years, that house, will still be there, at the same address. That was the reason that led to the crisis in 2008: buying houses was a safe investment, until the economy itself collapsed. This leads me to the other side of my thinking about the subject. It is a distinctive sign for the Private Equity firms, to divest from an initial investment in a time horizon in a range of 7 years to 12 years. Indeed, Blackstone sold the whole Hilton stake after 11 years with huge returns and having to cope with huge amounts of debt deriving from other operations they are still conducting. This happened while the price for Hilton's shares was skyrocketing: and in the last 4 years it almost doubled!

Why should a firm sell completely its stakes of a firm that is granting revenues?

Figure 33: Hilton shares' prices in the last 4 years, Source: Bloomberg, 2018

Moreover, the same tendency seems to affect the whole Real Estate market, if we look at the index containing the prices for the purchase of properties, it is increasing frighteningly, reminding the trend registered just before the crisis. The spin-off implemented by Hilton, that split the owned

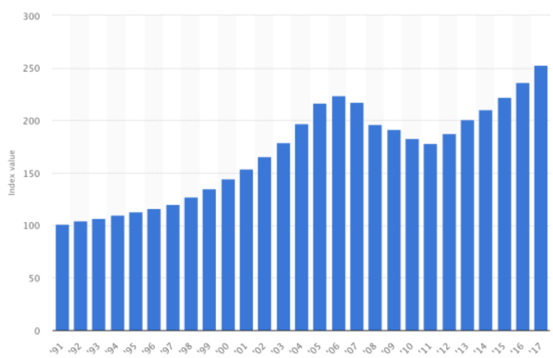


Figure 34: House purchase price in the US 1990-2018, Source: Federal Housing Finance Agency, 2018

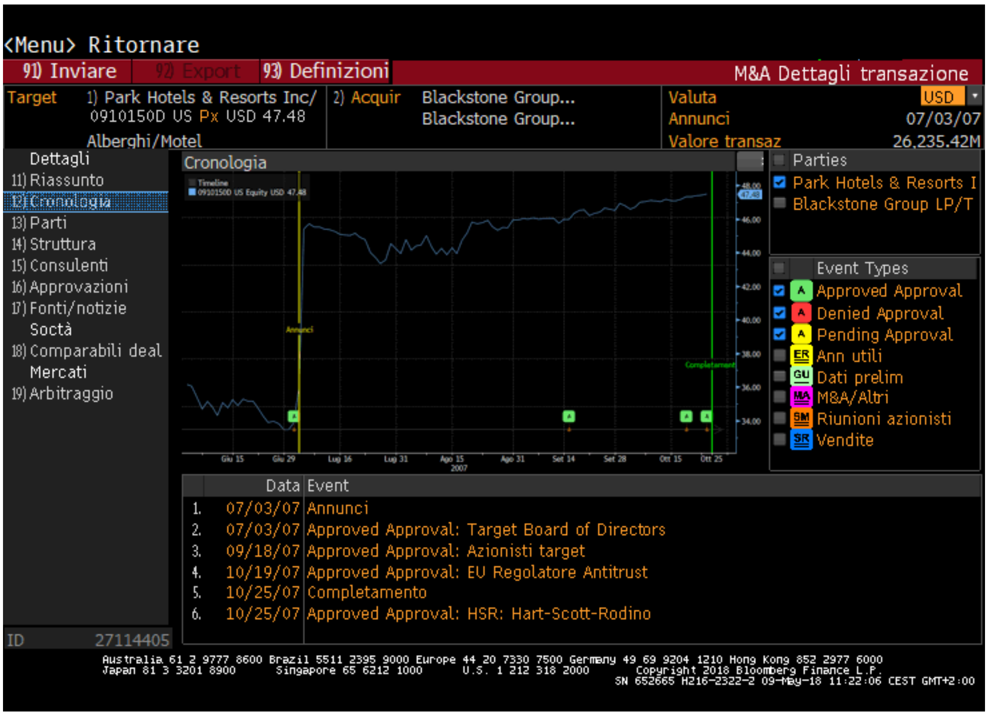
property from the timeshare and the franchised properties led me thinking that the future for the sector will reside in collecting fees more than owning hotels or resorts.

Is there the possibility that the real Estate market will collapse again?

Is Blackstone scared about a new economic downturn?

Appendix

Bloomberg's Screenshots - LBO

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91) Inviare
92) Export
93) Definizioni
M&A Dettagli transazione
Target 1) Park Hotels & Resorts Inc/ 0910150D US Px USD 47.48 Alberghi/Motel
2) Acquir Blackstone Group... Blackstone Group...
Valuta USD
Annunci 07/03/07
Valore transaz 26,235.42M
Dettagli
11) Riassunto
12) Cronologia
13) Parti
14) Struttura
15) Consulenti
16) Approvazioni
17) Fonti/notizie
Soctà
18) Comparabili deal
Mercati
19) Arbitraggio
Target
Nome* Park Hotels & Resorts Inc/Old
Ticker* 0910150D US
Settore Alberghi/Motel
Paese USA
Mkt Cap (M) 14,050.66
Azn circ (M) 389.75
Grandezza Consiglio --
Consiglio classif No
ESG Score pubb --
Score pubb gov --
Borsa prim* --
Auditor* ERNST & YOUNG LLP
Dipendenti* 7,140
Fine esercizio* 12/2013
Piano Poison Pill* --
Poison Pill approv* --
Acquir Blackstone Group LP/The
Nome* Blackstone Group LP/The
Ticker* BX US
Settore Titolo privato
Paese USA
Mkt Cap (M) --
Azn circ (M) 133.33
Grandezza Consiglio --
Consiglio classif No
ESG Score pubb --
Score pubb gov --
Borsa prim* New York
Auditor* DELOITTE & TOUCHE LLP
Dipendenti* 2,360
Fine esercizio* 12/2018
Piano Poison Pill* --
Poison Pill approv* --
ID 27114405
* Dati ad oggi. Altri dati come da data annuncio deal.
Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2018 Bloomberg Finance L.P.
SN 652665 H216-2322-2 09-May-18 11:22:26 CEST GMT+2:00


<Menu> Ritornare
91) Inviare
92) Export
93) Definizioni
M&A Dettagli transazione
Target 1) Park Hotels & Resorts Inc/ 0910150D US Px USD 47.48 Alberghi/Motel
2) Acquir Blackstone Group... Blackstone Group...
Valuta USD
Annunci 07/03/07
Valore transaz 26,235.42M
Dettagli
11) Riassunto
12) Cronologia
13) Parti
14) Struttura
15) Consulenti
16) Approvazioni
17) Fonti/notizie
Soctà
18) Comparabili deal
Mercati
19) Arbitraggio
Struttura
Legale
Imponibile --
Diritti dissenter Sì
Stato/sezione DE / 262
Azioni frazionate --
Lettera trasmissione Sì
Exchange Sì
Pagamenti non azionari No
Norma applicabile --
Expiration Time --
Scad fuso or --
Condizioni finanziamento No
Effetto materiale avverso No
Altre Info
Opzioni esercitabili (azioni) --
Proprietà target nva soc --
Proprietà acquir nuova soctà --
Scopo --
Date
Data accordo fusione 07/03/07
Scadenza dissenter 09/18/07
Data Drop Dead --
Data scadenza elezione --
Eventualità
Pag imprevisto titoli --
Pag cont imprevisto --
Go-Shop
Periodo Go-Shop --
Inizio Go-Shop --
Fine Go-Shop --
Termination Fees
Target ad acq USD 560.00 M
Acq a Target --
Sinergia
Ammontare costo sinergia --
Data costi sinergie --
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Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
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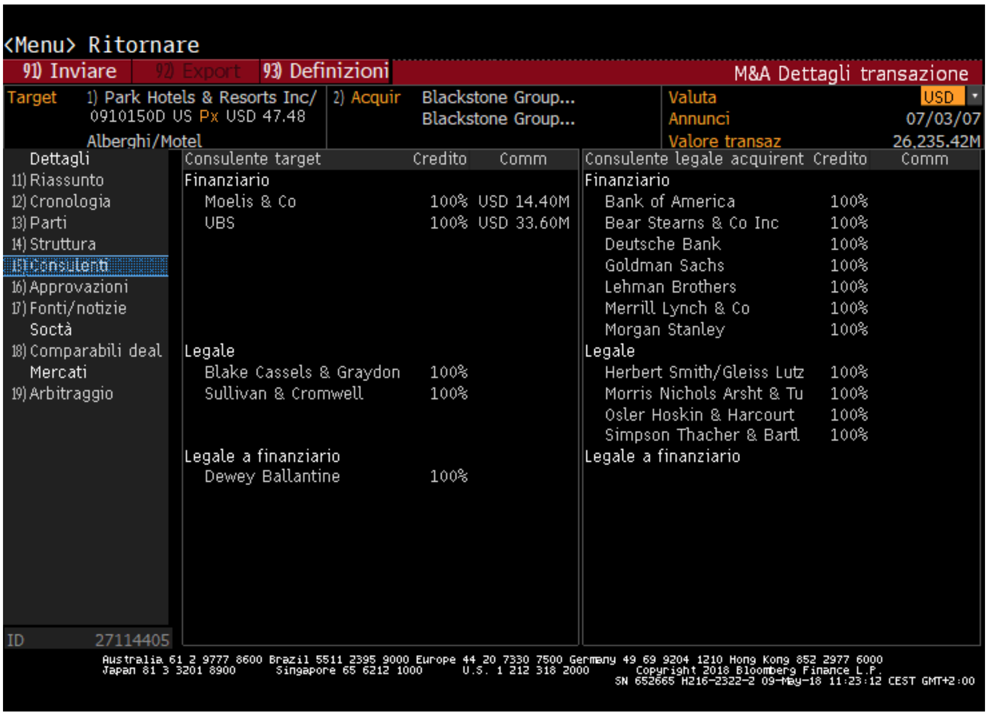
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15) Consulenti
16) Approvazioni
17) Fonti/notizie
Soctà
18) Comparabili deal
Mercati
19) Arbitraggio
ID 27114405
Consulente target Credito Comm
Finanziario
Moelis & Co 100% USD 14.40M
UBS 100% USD 33.60M
Legale
Blake Cassels & Graydon 100%
Sullivan & Cromwell 100%
Legale a finanziario
Dewey Ballantine 100%
Consulente legale acquirent Credito Comm
Finanziario
Bank of America 100%
Bear Stearns & Co Inc 100%
Deutsche Bank 100%
Goldman Sachs 100%
Lehman Brothers 100%
Merrill Lynch & Co 100%
Morgan Stanley 100%
Legale
Herbert Smith/Gleiss Lutz 100%
Morris Nichols Arsht & Tu 100%
Osler Hoskin & Harcourt 100%
Simpson Thacher & Bartl 100%
Legale a finanziario
Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
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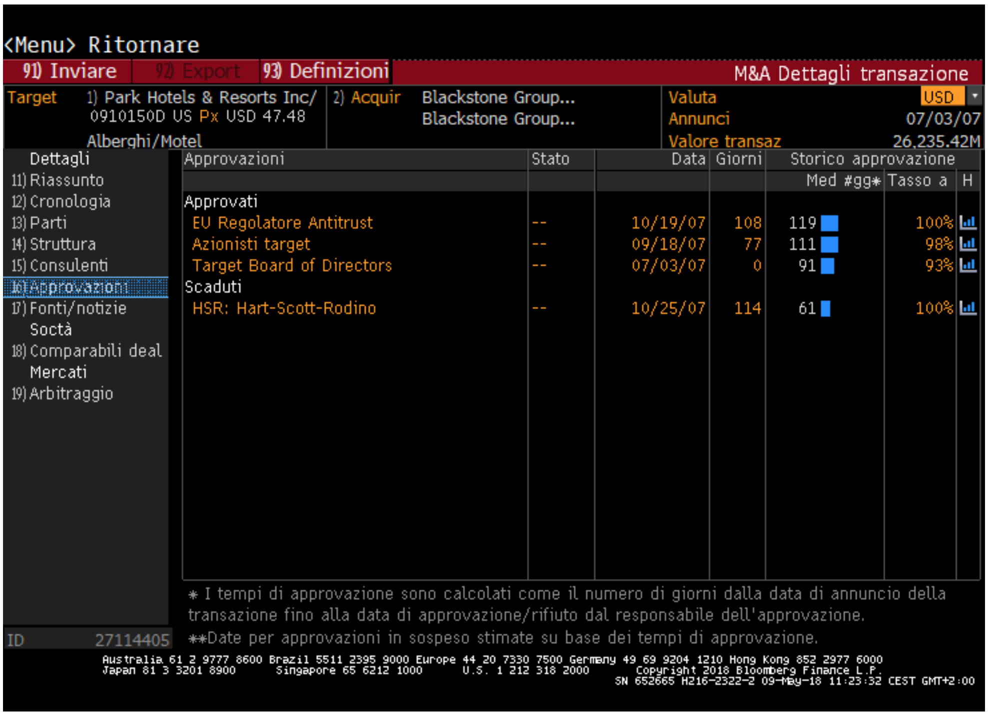
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13) Parti
14) Struttura
15) Consulenti
16) Approvazioni
17) Fonti/notizie
Soctà
18) Comparabili deal
Mercati
19) Arbitraggio
ID 27114405
Approvazioni Stato Data Giorni Storico approvazione
Med #gg* Tasso a H
Approvati
EU Regolatore Antitrust -- 10/19/07 108 119 100%
Azionisti target -- 09/18/07 77 111 98%
Target Board of Directors -- 07/03/07 0 91 93%
Scaduti
HSR: Hart-Scott-Rodino -- 10/25/07 114 61 100%
* I tempi di approvazione sono calcolati come il numero di giorni dalla data di annuncio della transazione fino alla data di approvazione/rifiuto dal responsabile dell'approvazione.
**Date per approvazioni in sospeso stimate su base dei tempi di approvazione.
Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2018 Bloomberg Finance L.P.
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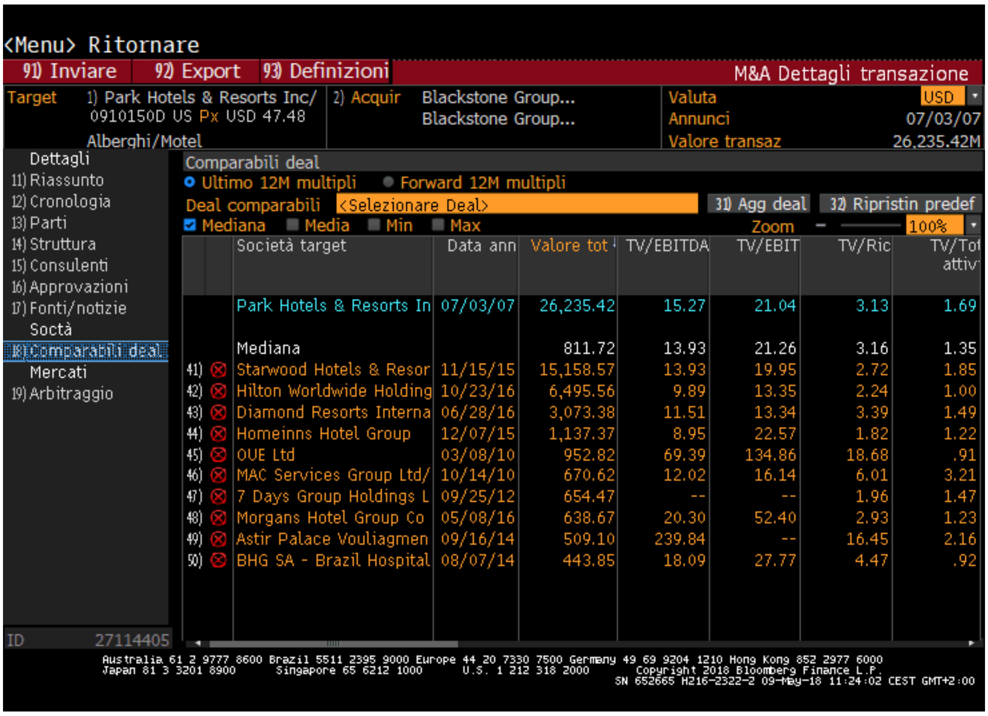

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M&A Dettagli transazione
Target 1) Park Hotels & Resorts Inc/ 0910150D US Px USD 47.48 Alberghi/Motel
2) Acquir Blackstone Group... Blackstone Group...
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13) Parti
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15) Consulenti
16) Approvazioni
17) Fonti/notizie
Soctà
18) Comparabili deal
Mercati
19) Arbitraggio
ID 27114405
Comparabili deal
Ultimo 12M multipli
Forward 12M multipli
Deal comparabili <Selezionare Deal>
31) Agg deal
32) Ripristin predef
Mediana Media Min Max
Zoom 100%
Società target | Data ann | Valore tot | TV/EBITDA | TV/EBIT | TV/Ric | TV/Tot attiv
Park Hotels & Resorts In | 07/03/07 | 26,235.42 | 15.27 | 21.04 | 3.13 | 1.69
Mediana | | 811.72 | 13.93 | 21.26 | 3.16 | 1.35
41) Starwood Hotels & Resor | 11/15/15 | 15,158.57 | 13.93 | 19.95 | 2.72 | 1.85
42) Hilton Worldwide Holding | 10/23/16 | 6,495.56 | 9.89 | 13.35 | 2.24 | 1.00
43) Diamond Resorts Interna | 06/28/16 | 3,073.38 | 11.51 | 13.34 | 3.39 | 1.49
44) Homeinns Hotel Group | 12/07/15 | 1,137.37 | 8.95 | 22.57 | 1.82 | 1.22
45) OUE Ltd | 03/08/10 | 952.82 | 69.39 | 134.86 | 18.68 | .91
46) MAC Services Group Ltd/ | 10/14/10 | 670.62 | 12.02 | 16.14 | 6.01 | 3.21
47) 7 Days Group Holdings L | 09/25/12 | 654.47 | -- | -- | 1.96 | 1.47
48) Morgans Hotel Group Co | 05/08/16 | 638.67 | 20.30 | 52.40 | 2.93 | 1.23
49) Astir Palace Vouliagmen | 09/16/14 | 509.10 | 239.84 | -- | 16.45 | 2.16
50) BHG SA - Brazil Hospital | 08/07/14 | 443.85 | 18.09 | 27.77 | 4.47 | .92
Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2018 Bloomberg Finance L.P.
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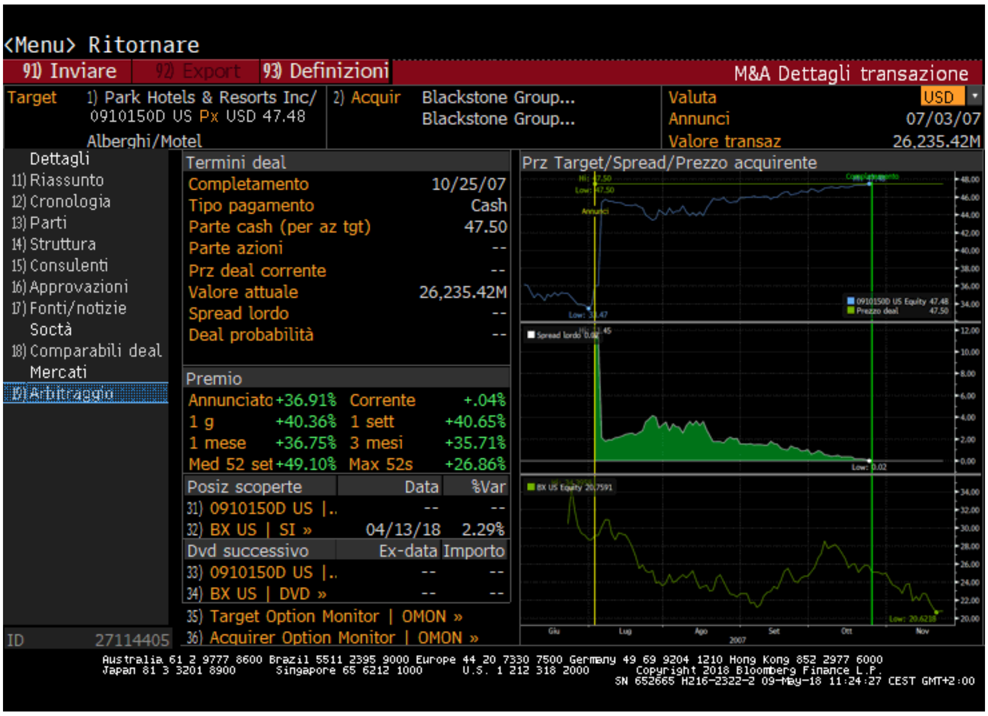

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M&A Dettagli transazione
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Valuta USD
Annunci 07/03/07
Valore transaz 26,235.42M
Dettagli
11) Riassunto
12) Cronologia
13) Parti
14) Struttura
15) Consulenti
16) Approvazioni
17) Fonti/notizie
Soctà
18) Comparabili deal
Mercati
19) Arbitraggio
ID 27114405
Termini deal
Completamento 10/25/07
Tipo pagamento Cash
Parte cash (per az tgt) 47.50
Parte azioni --
Prz deal corrente --
Valore attuale 26,235.42M
Spread lordo --
Deal probabilità --
Premio
Annunciato +36.91% Corrente +.04%
1 g +40.36% 1 sett +40.65%
1 mese +36.75% 3 mesi +35.71%
Med 52 set +49.10% Max 52s +26.86%
Posiz scoperte Data %Var
31) 0910150D US | .. -- --
32) BX US | SI » 04/13/18 2.29%
Dvd successivo Ex-data Importo
33) 0910150D US | .. -- --
34) BX US | DVD » -- --
35) Target Option Monitor | OMON »
36) Acquirer Option Monitor | OMON »
Prz Target/Spread/Prezzo acquirente
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SUMMARY

The financial markets are continuously changing, characterized by volatility, uncertainty and, due to the 2008 crisis, one of the less reliable sectors to operate in has become the *real estate market*. For that reason, the aim of this work is to analyze and to better understand how The Blackstone Group acquired Hilton Hotels in 2007. We will take a deeper look at the operation and its characteristics, at the operational improvements, at the financial statements, as well as the exit strategy. In order to do so, we have to comprehend the environment in which the operation has taken place, the core values and the history of the firms involved in the process and the main characteristics of the *Leveraged Buyout*. Another aspect we have to take into consideration is the Hotels' Industry and the Hilton's competitors.

So, this work is split into three main sections: the first one is about the description of the companies taking parts in the operation, the sector analysis, the competitors' identification and the use of the leveraged buyout in the North-American market.

The second section is about the operation, the analysis of the financial statements, the composition of the offer, the price paid for the acquisition, the evolution of the companies works and the sources of financing.

The last part of this work is focused on the exit strategies and the future scenarios. Furthermore, it will include a judgement on the operation, covering all its shades and its final outcome.

The whole work is developed accurately, after the collection of all the necessary information, in order to be able to discuss this subject: the goal is to make it *comprehensible, well-defined, logical* and *complete*.

The Actors

The *Hilton Worldwide* was founded in 1919 in the USA. The first hotel had been bought by Conrad Hilton and it was called "The Mobley". It was located in Cisco, Texas and the price paid for the entire building was of about 40.000$.

After that, the decade of the *forties* was noteworthy for the Hilton Worldwide Company. Other than listing in the New York Stock Exchange in 1946, in 1943 the HW turned into the first American Firm to operate in the hotel sector and it already had several hotels in New York, some of them very known such as the *Roosevelt* and the *Plaza.* At the end of that decade, Hilton was the first hotel corporation to have accommodations in *Porto Rico* and, moreover, in 1949 the firm acquired one of the most popular hotels in New York, the *Waldorf Astoria*.
In 1982 the *Conrad Hotels* was founded, a new company in the group created in order to offer a network of luxury hotels in the main destinations all around the world. The evolution of the company never stopped during these years: in 1987, the still functioning fidelity program *HHonors* was introduced, granting rewards to clients based on miles and bookings made with Hilton.
in the first years of the new millennium, Hilton expanded its business again by creating the *Hilton Worldwide Resort,* a branch offering luxury properties in exotic locations. It was in 2006 that *Hilton Hotels Corporations* bought back *Hilton International*: the firm was reunited again for the first time since 1967. The price paid for the operation from *Hilton Hotel International* to the English counterpart *Ladbrokes PLC* was 3,3 billion pounds.

<u>2007 is the crucial year during which the subject of this thesis takes place</u>. *Hilton Hotels Corporation* is acquired by the American Private Equity Group *Blackstone.* Cristopher Nassetta is nominated new CEO in the same year and he is the maker of the expansion process, in which Hilton is still involved. The company became private with the 2007 acquisition, but in 2013, six years later, it had its second IPO at the New York Stock Exchange (NYSE) with the name of Hilton *Worldwide Holdings Inc.*

On the other hand, The Blackstone Group was founded in 1985 by Stephen Allen Schwarzman and Peter George Peterson in New York starting with just 400.000$ in seed capital. The name of the firm comes from the names of the founders: *Schwarz* means *black* in German and *Peter* means *stone* in Greek.
The group formed the Real Estate Department in 1992 and, the following year, it is already the largest independent asset manager in the world. After several years of

operations and subsequently to the opening of other firm 's groups, such as the corporate debt one, the *Blackstone Group* completes the IPO worth 4,13 billions dollar, listing in the NYSE with the ticker BX in 2007. It's the same year during which *Peterson* leaves the firm and the LBO to acquire Hilton takes place. This operation is still considered one of the biggest ever made in the whole world with a price paid of 26,3 billion dollar.
The Group, moreover, owns interest in the hospitality sector by *Extended Stay America* and *La Quinta Hotels*. In 2013, 6 years after the acquisition of the Hilton Group, Blackstone has become the *principal global private equity real estate manager with 64 billion $ of assets under management.*

The LBO

2007 saw the third consecutive profitable year for overall lodging industry and hotels proved quite appealing targets for private equity investors (*Guinn, 2007*). Between 2000 and 2006, in fact, Hilton was offering high returns to investors, with an average of 20.3%. The American hotels chain registered remarkable performances in terms of operational performance and sales growth, but this notwithstanding, these extraordinary returns for investors and the international expansion lead Hilton to search for a partner in order to support their ambitions and activities. The debt levels, in fact, increased due to the expansion strategy and Hilton's cash flow was not sufficient for covering the expenditures of the internationalization.
As of 2007, therefore, Hilton was investing intensively outside the US in order not to make big piles of money generated from franchising: repatriation of gains was hostile due to tax implications. The investments abroad meant deployment of huge cash flow percentages and so, the search for a partner became a primary goal for the American company. The private equity market was booming and the necessity of a partnership with a firm characterized by strong expertise in the *real estate* sector was crucial.
Blackstone, on the other hand, came from several acquisition in the hospitality sector. In fact, between 2004, 2005 and 2006, the private equity group incorporated as many as 5 hotel companies: *La Quinta Corporation, Wyndham International, Boca Resorts, Extended Stay America* and *MeriStar REIT*. The acquisition of Hilton Worldwide would

have meant becoming the first private equity group in the world operating in the real estate sector. *Jonathan Gray*, responsible of the housing market for the Blackstone Group, had the feeling that there was a fast-growing interest among investors in the real estate sector. Moreover, he understood that the market was underestimating *Hilton*'s hotels by devaluing the market price of the properties.

The willingness to make the operation became concrete in 2006, when the negotiation between Gray and Matthew J. Hart[32] started. At the beginning the deal was questioned by the press and the CEOs themselves because of the discrepancies that were emerging regarding the price that should have been paid.

The conditions for the LBO were favorable anyway: The industry and the company were mature, granting an acquisition that could have increased its value, moreover there were feasible exit options, since making Hilton private again would have led to another IPO once the value had grown over time. Another important feature of the operation would have been the exploitation of the competitive advantage that Hilton had reached over the years. The synergies due to the expertise of the two firms and the possibility to invest granted by Blackstone would have made the difference once the deal would have been completed and there was room for expense reduction since 6316 million dollars of expenses reduced the 7438 million dollars of revenues (*Hilton Hotel Corporation Financial Report, 2006*). Furthermore, Blackstone could have sold the Hilton properties in case there was the necessity to cover the debt issued for the acquisition and the asset could have been used as collaterals to secure the debt too. Even though the Hilton's balance sheet was not clean with 6556 million dollars of debt, the LBO was under a traditional proposal.

Jonathan Gray and Matthew J. Hart together with Stephen Bollenbach[33] started negotiating again at the end of 2006 riding the wave to privatization that was hitting the whole continent. Notwithstanding the divergences that occurred during the first meetings, the CEOs decided to meet again because the conditions, adjusted to the constraints imposed by Hilton, could have brought benefits to Blackstone, anyway. The previous offer, made in August 2006, was of about 30$ for a spot price of the action that was around 20$. After September 2006 the price of the stocks skyrocketed from a maximum

[32] *President and COO of Hilton Hotels Corporation from May 2004 until October 2007.*
[33] Hilton CEO, 2007

of 28,53$ registered during the Q3 of 2006 to a maximum of 35,79$. The market in fact relied on the private equity operation and, moreover, Blackstone was used to invest in that kind of firms. The news about the possibility for the Private Equity group to buy the hotel chain made the public hopeful and ready to invest on the operation.

After the second meetings, Hilton decided to ask UBS an opinion about the deal and the Swiss firm advised the American company underlining the fact that the market was underestimating the value of the stocks. Hilton wasn't supposed to accept an offer below 42$.

Ultimately, The Blackstone Group and Hilton Hotel Corporation entered into an exclusive negotiation with requested due diligence for both counterparts. During May 2007 the offer was completed, and Blackstone engaged to guarantee a 40% premium over the closing day price of the stock.

The operation was closed on June 29th, Hilton stated that the closing would have brought large benefits to the shareholders and so, the price of the stock rose by 6.4% reaching 36,05$ per share. The final price paid by Blackstone was 47,5$ per share generating an effective premium of about 42%. The Private Equity Group became the largest hotel equity manager and added to its portfolio of 5 hospitality company, the most important one.

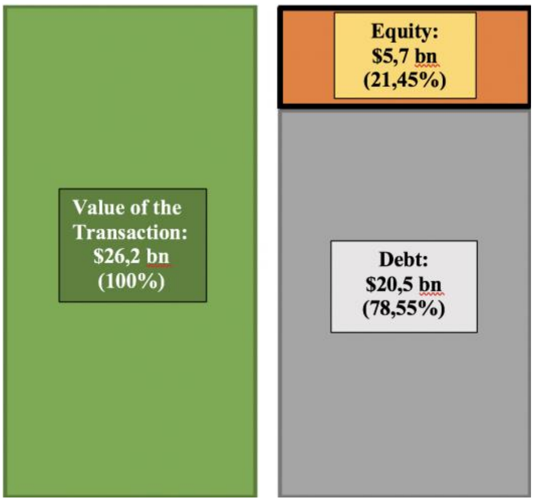
The Price paid for the entire acquisition by Blackstone amounted to 26 billion dollars and evaluating the firm 12.2x the EBITDA registered during the 12 months before the operation.

The 3rd of July the LBO was concluded between Gray and Bollenbach and Blackstone bought Hilton Hotels out. The firm paid the total amount using 20,6 billion dollars using financing sources and the remaining 5,4 billion dollars with equity coming from its funds BREP VI and BCP V. The Hilton debt was transferred to the American PE group and the proceeds of the operation were divided between AXA Financial[34], Barron Hilton[35], the *charitable trust* of the family[36] and the other shareholders.

In that years, the LBO was ranked 10th among the greatest acquisition of all time and the first for Blackstone. The premium paid for the purchase was one of the higher paid in the history and exceeded hugely the premiums paid previously by the Blackstone Group for

[34] Holding 7,9% of Hilton
[35] Conrad Hilton son, Holding 5,3% of Hilton
[36] Holding 5% of Hilton

Wyndham (19% premium) and Fairmont (28%). The premium was above the average of the north American LBO market and of the M&A too, respectively 25,62% and 30,55%. Blackstone borrowed a massive portion of debt corresponding to 20,6 billion dollars and injected 5,4 billion dollars of equity in order to complete the acquisition.



The debt quota was furnished by a syndication of banks composed by seven[37] high reputable financial institution that participate to the funding for the 80%: Bear Stearns (whose USD 4 billion securities were transferred after the acquisition of the latter by JPMorgan), Bank of America, Deutsche Bank, Goldman Sachs, Lehman Brothers, Merrill Lynch and Morgan Stanley. These institutes not only provide the loans to the private equity group but acted also as financial advisors. Hilton on the other hand, hired UBS and Moelis Advisors for helping them in making the operation work out.

Thus, this transaction is one of the 10 largest to that date, given the fact that the company had a net debt of more than USD 6.5 billion dollars and the advising companies valued the enterprise 26.3 billion dollars. For what concerns the financing of this operation, the BCP V and BREP VI funds only placed USD 5.7 billion in the form of equity and the rest of the enterprise value was financed from outside capital under the Leveraged Buy-Out process.

After the completion of the Leveraged Buy-Out the management of Hilton was almost completely replaced by Blackstone, introducing in the Hotel firm new people that, as we will see later, will result of key importance to the good outcome of the acquisition.
The new board, in 2007, was composed by the following people:

[37] *The total number of financial institutions participating in the syndication was 26.*

Name	Position
Cristopher J. Nassetta	President, CEO and Director
Johnathan D. Gray	Chairman of the Board of Directors
Michael Chae	Director
John G. Schreiber	Director
William J. Stein	Director
Simon Vincent	Executive Vice President and President Europe, Middle East and Africa

The team, chosen by Nassetta, was charged with implementing an internationalization strategy: the neo-CEO understood that there were many possibilities for the Hilton *resurrection* after the 2008 crisis, thanks to the fact that the company's core business was focused on providing the hotel services in the North American soil more than making it stronger abroad too. The manager, thanks to its ambitions, wanted to develop the business in the emerging market such as Asia and Middle east.

One of the first thing Nassetta wanted to change in Hilton culture was to avoid people that were heading to make changes with superficiality, namely, he introduced the "immersion": every corporate manager should have spent at least three days in the front lines, cooking, housekeeping, and working in the front desk. They needed contact with the customers in order to make profitable changes. Furthermore, a system for employees' performances evaluation was implemented, stimulating competition and efficiency between workers. These kinds of strategies lead to cutting high percentages of costs in the long term thanks to the being thorough in deciding what to change in the hotels and in the headquarters as well. Indeed, the most successful battles carried out by Nassetta were meant for changing the systemic inefficiency that pervaded the Californian HQs. So, the HQs were moved on Washington DC, there, other competitors such as Marriot, Host and Choice had located their offices and these moves attracted different types of investors. Another factor that was creating added value at that time was the emerging World Wide Web reality: Nassetta thought firmly that having a competitive advantage in providing services to the clients through the internet would have made Hilton great again. The first changes were made on the HHonors side: the digitalization of this service made it easier for customer to get the rewards and to be in contact with the Hilton company. In addition, the integration of the timeshare unit (considered an exclusive and independent department until the acquisition) into the company generated a 44% leap of revenues and most of the economic benefits that involved the Nassetta era were due to the employment of Jacobs as CFO.

The Crisis

In 2009 Hilton started meeting each bank and participating to the syndication. After several months of negotiation, the banks, that were losing around 5,1 billion dollars from the operation started two years before with the private equity group, decided to concede to the American firm several changes to the terms of the loans.

As a result, in 2010 the company completed the restructuring of the remunerated debt in order to bring financial costs to an operating result level of about half compared to the one obtained during the LBO in October 2007. It was therefore necessary to call on creditors to share the 5,1 billion dollars losses attributable to Blackstone, the recovering of the losses was carried out between 2008 and the end of 2012.

In terms of accounting, with the restructuring, Hilton's debt became more liquid and safer, but on the other hand the remaining debt increased because of the longer maturities: this offset the loss incurred in the restructuring for the financial institution. Following the restructuring in June 2010, Goldman Sachs and Bank of America sold respectively 600 and 1,700 million dollars of mezzanine debt from Hilton Worldwide distributing them to 150 institutional investors in 7 tranches; everyone subscribed to the offer. In addition, in November 2010, in a context where the delinquency rate associated with loans to the hotel sector was 15.94%, there were negotiations between these two entities to place 2.66 billion dollars of Commercial Mortgage Backed Securities, and the operation failed.

Post Buyout

After the crisis, Hilton had to face several problems related to the collapse of the entire economy. The real estate sector was hit badly by the events of 2008 and the prices of the properties was declining rapidly. Pessimism about the American hotel chain giant and it was reflected to the Blackstone Group too. The management of Hilton Worldwide, however, continued on believing that, the mix of hard work and capabilities could have led the company out of the troubled waters.
In 2011, the hotel industry's performances started rebounding sharply and Blackstone's Mr. Studzinski[38], that was engaged on renegotiate the debt with investors and banks, understood that it was time to stop buying debt back and start selling it to investors. In 2 years, investments in the real estate sector rose from 19 to 25 billion dollars. This meant that it was the right timing for starting to sell instead of continuing buying.

The IPO

"Hilton Worldwide Holdings Inc. ("Hilton Worldwide") announced today the pricing of its initial public offering of 117,640,624 shares of common stock at a price to the public of $20.00 per share. Hilton Worldwide is offering 64,102,564 of such shares and a selling stockholder is offering 53,538,060 of such shares. The selling stockholder has granted the underwriters an option to purchase up to an additional 17,646,093 shares at the initial public offering price less the underwriting discount. The shares are expected to begin trading on the New York Stock Exchange on December 12, 2013 under the ticker symbol "HLT." The offering is expected to close on December 17, 2013, subject to customary closing conditions." (Hilton Newsroom, December the 11th, 2013)

On December 2013 this announcement specified the number of shares, the total amount, the stock exchange and the date of the Secondary IPO made by Hilton through Blackstone. As we analyzed before in this case study, 2013 resulted one of the best years for the Real Estate sector since 2004 in terms of IPO. For that, Blackstone, after having done the same things few months before with *Extended Stay America*, understood that it

[38] *Head of Corporate Advisory and restructuring practices*

was the right time to offer Hilton Worldwide Holding's stocks to the public. The Private Equity Group directed the operation by offering 11,5% of Hilton's shares in the proposal. After the debt restructuring, Blackstone had invested a total of around 6,8 billion dollars on the hotel company: with the IPO, it wasn't selling any of its stocks, though. It maintained its 76% of the company. That meant that it was raising up to 2,37 billion dollars from the offer and that the initial investment was becoming successful. In fact, in 2007, Hilton was valued 26,7 billion dollars debt included: in 2013 the IPO was made for a total value of 32,5 billion dollars. This meant that the American private equity group was earning huge amounts of money from the operation that almost everybody was disapproving at the beginning. The use of proceeds of the offer is identified by the repayment of 1,25 billion dollars of debt. The occupancy rate was raising rapidly in that year and other hotel firms were attempting to make an IPO. Despite that it resulted as the second biggest IPO in 2013 overcoming the results of highly marketed offers such as *Twitter*.

The IPO was immediately considered a great success, not only for the amount *issued*: some sources claim the IPO was oversubscribed by a factor 9 *(Yu et al., 2013).* Moreover, on the first day, the price of the shares reached 21,5$ at closing. For what concerns Blackstone, it seemed that it was the first step to exit the 2007 LBO. On the other hand, Blackstone's CEO, Mr. Schwarzmann stated that he was intentioned to remain the owner of the firm for a long lapse of time. In fact, Blackstone, in the first days after the launch of the IPO, started realizing that, by maintaining the 76,4% of the company and calculating the Enterprise Value as 20$ per the number of shares issued, it owned 15 billion dollars by having invested roughly 6,5 billion dollars in 2007 registering an almost 3x for invested capital on enterprise value.

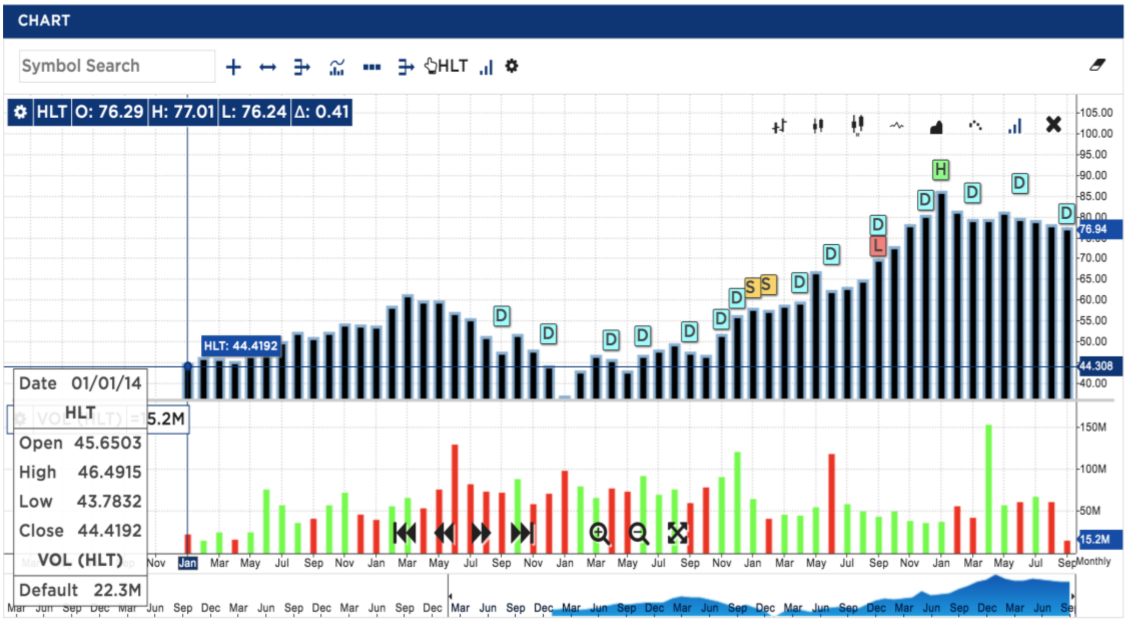


Figure 35:NYSE chart of the prices of the Hilton's stock publicly traded during the first two years, source: NYSE.com

As we can observe from the figure above, the listing on the NYSE registered a good result. The trend is ascending and, generally, the Hilton IPO is taken into consideration as an example useful to show how the real estate sector started growing again from 2013 on. The price on the NYSE, on the first day, was 45,65 USD per share: a huge profit for the underwriters that subscribed the whole amount of shares. One of the main features of this offer, as we said previously, was the commitment of Blackstone in remaining the owner of the company with a 76,4% stake.

The will to internationalize the company lead Hilton to invest on emerging market significantly: that meant to expand their hotel network and business operations by hitting countries that were demanding for the western hotel chains in their country.

The expansion was terrific: in 6 years the number of Hotels on the Asiatic country was increased by 78 hotels and the pipeline counted 232 properties while in 2007 it wasn't present on the soil. The huge operation conducted by Mr. Nassetta created interest among the Asian investors, huge curiosity started involving the management of HNA.

The Chinese group was founded in January 2000 following a transformation of Hainan Airlines, Chinese public company listed in 1999, and in July 2000 it was already creating a new branch by establishing the HNA Hotel Group. It was run by Chen Feng and Chen Guoping, backed by the Hainan provincial government, which is the largest shareholder. In 2003, Fortunes ranked the company as China's top listed, from that moment on it

started investing everywhere in the world by diversifying: in 2010 it bought Allco Finance[39], in 2011 GEsea CO[40], in 2013 it takes 20 percent stake in HN Hotel[41] by starting investing in the hospitality sector, during the October of the same year it bought TIP Trailer Leasing[42], two years later, in 2015, it purchases Swissport[43] and started being a Uber strategic partner. During the last years it has acquired Categroup, an aviation catering group, for 1,5 billion dollars and purchased a 9,9% stake in Deutsche Bank for 800 million dollars, but we will focus on the acquisition of a 25% stake in Hilton hotels.
In October 2006, rumors about the possibility for Blackstone to sell a significant stake of its Hilton shares started spreading around in Wall Street. At the end of the same month, Blackstone decided to sell the 25% of its property to HNA leaving the American private equity group, that was divesting over time, with only a 21% stake. The Blackstone group sold the shares for $26,25 that is to be considered a huge result if we take in to consideration the IPO that took place in 2013 and that was priced $20 per share. Moreover, Cristopher Nassetta, saw significant opportunity coming from the disposal, in fact, the deal, in its opinion, *"will open new opportunities for the brand and guests around the world, particularly in light of HNA's strong position in the fast-growing Chinese travel and tourism market, the largest outbound travel and tourism market in the world"* (Investopedia, October 24th, 2016). In fact, HNA in 2016, operated or had investments in 2,000 hotels with over 300,000 rooms and had 1,250 aircrafts carrying over 90 million people to 260 cities worldwide (Forbes, October 24th,2016). Furthermore, the operation brought huge returns for the private equity group, considering that in 2007 it paid $8,60 per share and that the investment was representing a 205% return for Blackstone (without counting the additional 35 cents dividend per share paid by HLT). (Bloomberg, November 3rd ,2016).
At the light of what we have been discussing all over the thesis, important messages have to be taken into consideration. First of all, we have to underline the fact that the transaction lead to a *win-win-win situation*. Indeed, Blackstone multiplied its investment by almost 3 times choosing the right timing for the exit and after leading Hilton out of the crisis through a good management. Moreover, the old Hilton's management cashed in a

[39] Australian Aircraft leasing business
[40] Shipping container leasing company acquired for 1 billion dollars
[41] One of Europe top hotel chain
[42] Largest trailer leasing company in Europe
[43] Air Services Group bought for 2,8 billion dollars

40% premium and saved the company. The bad administration of the Hotel firm was leading it to bankruptcy and the Beverly Hills headquarters were more concerned about the Hollywood life than on implementing the strategies that were necessary in order not to make a historical brand such Hilton collapse. The family's scoops involving Conrad Hilton nephew, Paris, were changing the perception of the brand and laziness in the offices was influencing the company's results. It is important, for that, underline the Blackstone's vision about the subject. First of all, they understood that the room for improvements of the firm was huge, secondly, they made compromises in order to please the old management in terms of money. Indeed, even if the private equity market was booming during that years, the premium paid was up above the average. Another huge Blackstone's merit was to assign the role of CEO to Christopher Nassetta: he was able to leverage the crucial flaws that were affecting the company. He introduced the *immersion* and *evaluation* programs in order to motivate workers and to make them conscient about what was going in the administrative offices and in the hotels. Moreover, he changed the company's strategy by implementing a deep internationalization and digitalization of the firm. However, the operation had its up and downs, during the crisis, Blackstone lost nearly 70% of the investment made, making people concerned about the private equity group investment strategy. In any case, there's something to underline in the way Blackstone cope with the crisis. The way they decided to negotiate the debt restructuring and the persistency in implementing the strategy during that harsh economic years resulted a value added for the firm. After the crisis, in fact, as we have seen in the last part of the work, Hilton recovered its position as a leader in the hospitality sector.

The subjects faced during this dissertation were many: we analyzed the LBO, the IPO, the internationalization strategy, the debt restructuring via the Spin-Off.

The last years for these two famous companies were troubled but also fruitful, working on this thesis helped me watching these kinds of operation from a different perspective. I tried to be as clear as possible in defining all the steps that lead to the actual situation and surely, most of my purposes have been achieved by finding a large number of authoritative sources. My personal interpretation for this dissertation is split in two main factions. On one side, the real estate market and so, the hospitality sector, is one of the most profitable in the whole economic system: when you buy a house, you know that in 20 years, that house, will still be there, at the same address. That was the reason that led to the crisis in 2008: buying houses was a safe investment, until the economy itself collapsed. This leads me to the other side of my thinking about the subject. It is a distinctive sign for the Private Equity firms, to divest from an initial investment in a time horizon in a range of 7 years to 12 years. Indeed, Blackstone sold the whole Hilton stake after 11 years with huge returns and having to cope with huge amounts of debt deriving from other operations they are still conducting. This happened while the price for Hilton's shares was skyrocketing: and in the last 4 years it almost doubled!

Why should a firm sell completely its stakes of a firm that is granting revenues?

Figure 36: Hilton shares' prices in the last 4 years, Source: Bloomberg, 2018

Moreover, the same tendency seems to affect the whole Real Estate market, if we look at the index containing the prices for the purchase of properties, it is increasing frighteningly, reminding the trend registered just before the crisis. The spin-off implemented by Hilton, that split the owned property from the timeshare and the franchised properties led me thinking that the future for the sector will reside in collecting fees more than owning hotels or resorts.

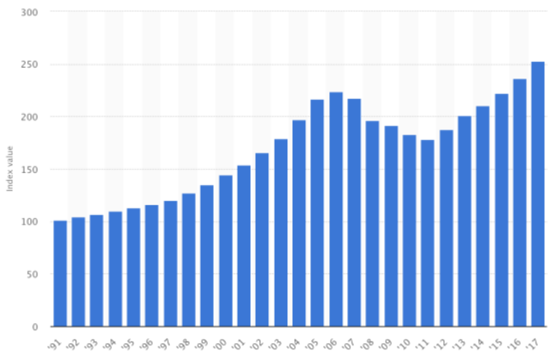


Figure 37: House purchase price in the US 1990-2018, Source: Federal Housing Finance Agency, 2018

Is there the possibility that the real Estate market will collapse again?

Is Blackstone scared about a new economic downturn?