AMERICAS MERGER REPORT

CHAIN BRIDGE RESEARCH

f/k/a IG RESEARCH

19 March 2021 – 10:30 EDT

Deal Terms

1 STAY = $19.50

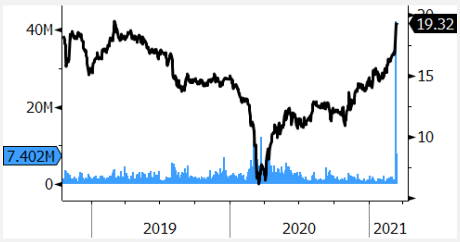
Target: Extended Stay

Country	United States
Bloomberg	STAY
Sector	Lodging
Share price ($)	19.34
Market cap ($m)	3,426.9
Free float (%)	89

Acquirer: Consortium of Starwood and Blackstone

Country	United States
Bloomberg	N.A.
Sector	PE
Share price ($)	N.A.
Market cap ($m)	N.A.
Free float (%)	N.A.

STAY Price Chart



Status

HSR filing deadline (T+10BD) March 29, 2021

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Extended Stay (STAY) / Consortium

AGREED MERGER

The deal spread of 0.9% appears to be somewhat tight but a cheap option on a price increase. Given that downside and deal risk is limited we would go long STAY on a potential price increase.

Extended Stay America and its paired-share REIT, ESH Hospitality, announced that it has signed a definitive agreement to be acquired by a 50/50 joint venture between funds managed by Blackstone and Starwood Capital for $19.50 per paired share.

Regulatory Risks and Timing

- HSR approval is required
- Blackstone Real Estate Partners ("Blackstone") and Starwood Capital Group will own a 50/50 joint venture
- We note that both Blackstone and Starwood own hotel assets.

Product market

- Starwood has several hotel assets in its portfolio. However, in the overall hotel market the combined market share is not significant.
- We note that Starwood owns InTown Suites that competes in the extended stay market.
- Although we note that STAY stated in its 10-K the following: All 646 system-wide hotels currently operate under the Extended Stay America brand, which serves the mid-price extended stay segment and accounts for approximately 43% of the segment by number of rooms in the United States.
- In June 2013, Starwood acquired InTown Suites, one of the largest owners of economy extended stay properties in the U.S. In 2013, the company owned and operated 138 properties (17,978 rooms), representing ~25% of the extended-stay sector. Today, it has almost 200 locations in 22 states and more than 25,000 guest rooms which equals to a ~5% market share.
- Based on our findings, InTown and STAY are direct competitors in the extended stay market. The extended stay market consists of 545,000 rooms. A potential combination of InTown and STAY would represent 87,700 room and a 16% market share.
- Further segmentation of the extended stay market based on pricing is a key to decide if the current acquisition could cause rigorous antitrust review. Based on STAY 10-K in the mid-price segment they own 43% of the market.
- As per our findings on biz-stay.com InTown Suites competes in the Economy Chains segment and STAY in the mid-range segment

Geographic market

- Based on previous precedents, the geographic market for hotels and motels is local
- Antitrust issue might arise in case of a wider product market definition (extended stay market irrespective of pricing) in some local markets.
- InTown Suites are concentrated in the South-Eastern region of US.
- Key overlapping MSAs are Houston, Dallas, Atlanta, Charlotte and Norfolk

Key mitigating factor

- We note that a key mitigating factor is that STAY will be owned by Starwood and Blackstone in a 50%-50% JV.
- Given the $300m regulatory related reverse break fee we believe that the consortium is willing to do its best to receive antitrust approval and close the deal.
- We also note that there are other competitors like AirBNB, Vrbo, Sonder etc. present which we did not include in our market share calculations.
- In case antitrust regulators see some degree of substitutability among upscale, mid-tier and economy price segments the competition appears to be so intense that a lengthy deal review appears to be a wild card scenario.

CBR summary

- Starwood's InTown and STAY are competitors in the wider extended stay market with a ~16% combined market share. However, in some of the above mentioned overlapping MSAs (most likely in Norfolk) asset divestiture might be required. Other MSAs seem to be competitive, not causing any antirust related issues. We note that all key competitors are present in the overlapping MSAs.
- In case of a narrow product market definition based on pricing of the rooms - which is a more likely scenario, the two companies are not direct competitors and HSR approval is likely to be granted in the initial phase.

Shareholder Vote

- Starwood's equity stake might ward off other bidders and shareholders have limited alternatives that would grant a bigger return compared to accepting the consortium's current offer.

Counterbid

- Based on our ROIC calculations there is limited room for bump. However, our LBO calculation justifies a higher, low-20s bid. Compared to precedents' valuation and given the company performed steadily during a travel freeze, we cannot rule out other suitors approaching the company.
- Starwood's equity stake in Extended Stay may ward off competing buyers

Valuation:

- STAY was trading below the wider peer group average. One may argue that its more stable cash flow and higher margins justify a higher takeout multiple.
- In a highly unlikely deal break we see downside around $17.00
- STAY's FY1 EV EBITDA multiple of 14.3x is close to precedents' average, similar to the premium of 15%.

Key terms of the merger

Transaction Details	
Announcement Date	March 15, 2021
Offer terms	1 STAY = $19.50
% owned by STAY stockholders	0%
Deal Size (Market Value)	$3,462m
Offer structure	All cash merger
Target's Board Recommendation	Yes
Voting Agreement	The transaction has been unanimously approved by ESA's Board of Directors and has also been approved by ESH's Board of Directors. Completion of the transaction, which is expected to occur in the second quarter of 2021, is contingent upon customary closing conditions, including approval of the Company's stockholders. In connection with the transaction, an affiliate of Starwood Capital, which owns approximately 9.4% of Company's outstanding paired shares, has entered into a support agreement whereby it has agreed to vote its shares in favor of the transaction.
Target Incorporation	Delaware (US)
Merger Agreement	Click here for the merger agreement
Synergies	■ N/A

Indicated Closing Date

- Completion of the transaction, which is expected to occur in the second quarter of 2021

Dividends

- The Company **does not expect to pay its regular quarterly distribution during the pendency of the transaction except for the previously declared $0.09 distribution on March 26, 2021 (xdate was March 11**. However, under the terms of the merger agreement, the acquiror may request that ESA pay a special distribution immediately prior to the closing of up to $1.75 per paired share, in which case the cash consideration paid in the merger will be reduced by the amount of the distribution.

Financing

- The transaction is not contingent on receipt of financing.

STAY capitalization

- **STAY Equity**
  - The authorized capital stock of the Company consists solely of 3,500,000,000 shares of Company Common Stock, 350,000,000 shares of Company Preferred Stock of which 25,000 shares are designated as Series A Preferred Stock, 3,500,000,000 shares of excess stock, par value $0.01 per share, of the Company ("Company Excess Common Stock"), into which the Company Common Stock is convertible under the Company Certificate of Incorporation, and 350,000,000 shares of excess stock, par value $0.01 per share, of the Company ("Company Excess Preferred Stock") into which the Company Preferred Stock is convertible under the Company Certificate of Incorporation of which 25,000 shares are designated as Excess Series A Preferred Stock. As of the close of business on March 12, 2021 (the "Capitalization Date"), (i) 177,560,635 shares of Company Common Stock were issued and outstanding, each of which is paired with one share of Hospitality Class B Common Stock, (ii)
  - Each Paired Common Share is comprised of one share of Company Common Stock and one share of Hospitality Class B Common Stock. There are no Unpaired Shares (as defined in the Organizational Documents).
  - (b) The authorized capital stock of Hospitality consists solely of 4,300,000,000 shares of Hospitality Class A Common Stock, 7,800,000,000 shares of Hospitality Class B Common Stock, 125 shares of Hospitality Preferred Stock, 350,000,000 shares of preferred stock, par value $0.01 per share, of Hospitality ("Hospitality Penny Preferred Stock"), 4,300,000,000 shares of excess class A stock, par value $0.01 per share, of Hospitality ("Hospitality Excess Class A Stock") into which the Hospitality Class A Common Stock is convertible under the Hospitality Certificate of Incorporation, 7,800,000,000 shares of excess class B stock, par value $0.01 per share, of Hospitality ("Hospitality Excess Class B Stock") into which the Hospitality Class B Common Stock is convertible under the Hospitality Certificate of Incorporation, and 350,000,000 shares of excess preferred stock, par value $0.01 per share, of Hospitality ("Hospitality Excess Preferred Stock") into which the Hospitality Penny Preferred Stock is convertible under the Hospitality Certificate of Incorporation. As of the Capitalization Date, (i) 250,493,583 shares of Hospitality Class A Common Stock were issued and outstanding, all of which were owned by the Company, (ii) 177,560,635 shares of Hospitality Class B Common Stock were issued and outstanding, each of which is paired with one share of Company Common Stock, (iii) 125 shares of Hospitality Preferred Stock were issued and outstanding, (
- **STAY Debt**

	Payments Due by Period						
	Total	2021	2022	2023	2024	2025	Thereafter
ESH REIT Term Facility [1]	$ 623,022	$ 6,309	$ 6,309	$ 6,309	$ 6,309	$ 6,309	$ 591,477
2025 Notes [2]	1,300,000	—	—	—	—	1,300,000	
2027 Notes [3]	750,000	—	—	—	—	—	750,000
Corporation Revolving Credit Facility	49,765	—	—	—	49,765	—	—
Operating lease obligations [4]	81,676	2,221	806	552	503	503	77,091
Finance lease obligations [5]	5,149	850	397	400	402	429	2,671
Interest payments on outstanding debt obligations [6][7][8]	630,237	118,156	117,499	117,362	116,920	81,755	78,545
Purchase obligations [9]	67,562	17,438	18,245	18,330	12,924	625	—
Total contractual obligations	$ 3,507,411	$ 144,974	$ 143,256	$ 142,953	$ 186,823	$ 1,389,621	$ 1,499,784

- **STAY Net Leverage** — FY1 Net Debt/EBITDA 6.3x

Valuation Multiples

1-day premium	The $19.50 per paired share consideration represents a premium of 23.3% over the 30-day volume-weighted average share price ending March 12, 2021 and a premium of 15.1% over the closing stock price on March 12, 2021.
LTM EV/Sales	6.0x
FY1 EV/Sales	5.5x
FY2 EV/Sales	5.2x
FY1 P/E	38.4x
FY2 P/E	24.5x
FY1 EV/EBITDA	14.3x
FY2 EV/EBITDA	12.4x

Timetable

Confidentiality Agreement	March 10, 2021
Date of the Merger Agreement (T)	March 14, 2021
Deal Announcement	March 15, 2021
HSR filing deadline (T+10BD)	March 29, 2021
Proxy filing	By mid-April 2021
Expiration of HSR waiting period (+30D)	April 28, 2021
Shareholder meeting	By end of May 2021
Special dvd declaration (X-10BD)	By end of May 2021
Settlement (CBR est.) (X)	By early June 2021
End date	September 14, 2021

Deal close definition

- The closing of the Mergers (the "Closing") shall take place remotely by electronic exchange of signatures at 9:00 a.m. (New York City time) on the third (3rd) Business Day following the satisfaction or, to the extent permitted by applicable Law, waiver by the applicable party of the last of the conditions set forth in Article VIII, or at such other place, time or date as Parent and the Paired Entities shall agree in writing

Solicitation Clause

- There is a non-solicitation clause with a fiduciary out prior to the shareholder vote
- There is a four business day matching period which may be reduced to two.
- "Superior Proposal" means a bona fide written Acquisition Proposal (provided that, for purposes of this definition, references in the definition of "Acquisition Proposal" to "15% or more" shall be deemed references to 50% or more) that the Company Board and the Hospitality Board determine in their good faith judgment, after receiving the advice of their financial advisor outside legal counsel, and after taking into account all the terms and conditions of the Acquisition Proposal, (A) would result, if consummated, in a transaction that is more favorable to the holders of Paired Common Shares (solely in their capacity as such) from a financial point of view than those contemplated by this Agreement (including any revisions to this Agreement that are proposed in writing by Parent in response thereto and any other information provided by Parent) and (B) is reasonably likely to be consummated, after taking into account (x) the financial, legal, regulatory and any other aspects of such proposal, (y) the likelihood and timing of consummation (as compared to the transactions contemplated by this Agreement) and (z) any revisions to this Agreement that are proposed in writing by Parent in response thereto and any other information provided by Parent.

Company Intervening Event

- "Intervening Event" means a material event, fact, development, change in circumstance or occurrence with respect to any of the Paired Entities and the Paired Entities Subsidiaries that (a) is neither known, nor reasonably foreseeable, by the Company Board or Hospitality Board, as applicable, as of or prior to the execution and delivery of this Agreement and (b) first occurs, arises or becomes known to the Company Board or Hospitality Board, as applicable, after the execution and delivery of this Agreement and on or prior to the date of the Requisite Vote; provided, however that none of the following will constitute, or be considered in determining whether there has been, an Intervening Event: (i) the receipt, existence of or terms of an Inquiry or Acquisition Proposal or any matter relating thereto or consequence thereof and (ii) changes in the market price or trading volume of the Paired Common Shares or the fact that the Paired Entities meet or exceed internal or published projections, budgets, forecasts or estimates of revenues, earnings or other financial results for any period (provided, however, that the underlying causes of such change or fact shall not be excluded by this clause (ii)).

Key conditions to the merger

- **Shareholder approvals** — Yes

	The affirmative vote of (i) the holders of a majority of all the issued and outstanding shares of Company Common Stock entitled to vote at the Company's Special Meeting (the "Requisite Company Vote") and (ii) the holders of a majority of all the issued and outstanding shares of Hospitality Class B Common Stock and Hospitality Class A Common Stock entitled to vote at Hospitality's Special Meeting, voting together as a single class, (the "Requisite Hospitality Vote" and, together with the Requisite Company Vote, the "Requisite Vote") are the only votes of the holders of any class or series of capital stock of the Paired Entities or Paired Entities Subsidiaries necessary to adopt or approve this Agreement, the Mergers and the other transactions contemplated by this Agreement.
No injunctions	Yes
No legal prohibition	Yes
Regulatory Approvals	Yes
Reps and warranties	Yes
Covenants fulfilled	Yes
Performance of Obligation of the Company	Yes
No Company or Parent MAC	Yes
REIT opinion	Yes
No Frustration of Closing Conditions	Yes

STAY MAC Definition

- "Parent Material Adverse Effect" means any effect, event, development or change that, individually or in the aggregate with all other effects, events, developments or changes, would reasonably be expected to be materially adverse to the ability of Parent, MergerCo 1 or MergerCo 2 to consummate the Mergers before the End Date.
- "Company Material Adverse Effect" means any effect, event, development or change that, individually or in the aggregate with all other effects, events, developments or changes, is, or would reasonably be expected to be, materially adverse to (i) the business, results of operations or financial condition, assets of the Company and its Subsidiaries, taken as a whole or (ii) the ability of the Company or Hospitality to consummate the Mergers before the End Date;

STAY MAC Carve-outs

Provided, however, that in the case of clause (i), no effect, event, development or change resulting from, arising out of, attributable to or relating to any of the following shall be deemed to be or constitute a "Company Material Adverse Effect," and no effect, event, development or change (by itself or when aggregated or taken together with any and all other such effects, events, developments or changes) to the extent resulting from, arising out of, attributable to, or related to any of the following shall be taken into account when determining whether a "Company Material Adverse Effect" has occurred or would reasonably be likely to occur:

- (a) general economic conditions (or changes in such conditions) in the United States or any region thereof or any other country or region in the world, or conditions in the global economy generally;
- (b) conditions (or changes in such conditions) in the securities markets, credit markets, currency markets or other financial markets in the United States or any region thereof or any other country or region in the world, including (i) changes in interest rates in the United States or any other country or region in the world and changes in exchange rates for the currencies of any countries and (ii) any suspension of trading in securities (whether equity, debt, derivative or hybrid securities) generally on any securities exchange or over-the-counter market operating in the United States or any region thereof or any other country or region in the world;
- (c) conditions (or changes in such conditions) in any of the industries in which the Company and or its Subsidiaries conduct business;
- (d) political conditions (or changes in such conditions) in the United States or any region thereof or any other country or region in the world or acts of war, sabotage or terrorism (including any escalation or general worsening of any such acts of war, sabotage or terrorism) in the United States or any region thereof or any other country or region in the world;
- (e) any Force Majeure event; (f) the announcement of this Agreement or the pendency or consummation of the transactions contemplated hereby, including (i) the identity of Parent and its affiliates and (ii) the impact thereof on relationships, contractual or otherwise, with customers, suppliers, licensors, distributors, partners or employees (provided that this clause
- (f) shall not apply to any representation or warranty in Section 5.5 and, solely to the extent related thereto, the condition set forth in Section 8.2(a));
- (g) the taking of any action expressly required by this Agreement or with the consent of Parent in writing ;
- (h) changes in law or other legal or regulatory conditions (or the interpretation thereof), or changes in GAAP or other accounting standards (or the interpretation thereof), in each case, after the date hereof;
- (i) changes in the stock price of the Paired Common Shares or the trading volume of the Paired Common Shares, or any failure by the Company or Hospitality to meet any public estimates or expectations of the revenue, earnings or other financial performance or results of operations of the Company or Hospitality for any period, or any failure by any Paired Entity or Paired Entities Subsidiary to meet any internal budgets, plans or forecasts of its revenues, earnings or other financial performance or results of operations (but not, in each case, the underlying cause of such changes or failures, unless such changes or failures would otherwise be excepted from this definition); or
- (j) any litigation by the stockholders of the Paired Entities related to this Agreement, the Mergers or other transactions contemplated hereby;
- except to the extent such effects, events, developments or changes to the extent resulting from, arising out of, attributable to or related to the matters described in the foregoing clauses **(a) through (e) and (h) disproportionately adversely affect** the Company and its Subsidiaries, taken as a whole, as compared to other companies that conduct business in the United States and in the industries in which the Company and its Subsidiaries conduct business

(in which case, such adverse effects (if any) shall be taken into account when determining whether a "Company Material Adverse Effect" has occurred or would reasonably be likely to occur solely to the extent they are disproportionate).

Break fees

- **Break fee**
  - Upon a termination of the Merger Agreement, under certain circumstances, the Paired Entities will be required to pay a termination fee to Parent of $105 million, except that the termination fee will be $61.25 million if (1) a third party submits a Qualified Proposal (as defined in the Merger Agreement) prior to April 14, 2021, (2) prior to April 28, 2021, the Paired Entities provide notice to Parent of their intention to terminate the Merger Agreement to enter into a definitive agreement providing for the implementation of such Qualified Proposal, and (3) the Company terminates the Merger Agreement in order to enter into a definitive agreement with such third party providing for the implementation of a Superior Proposal within a specified time.
- **Reverse break fee**
  - Upon termination of the Merger Agreement in certain other circumstances, Parent will be required to pay the Company a termination fee of $300 million. Blackstone Real Estate Partners IX L.P. and Starwood Distressed Opportunity Fund XII Global, L.P. have each guaranteed certain payment obligations of Parent under the Merger Agreement up to $150 million (plus certain other payment amounts).

Antitrust related clauses

- **Jurisdictions**
  - US
- **Divestiture obligation**
  - No
- **Litigation obligation**
  - No
- **Reverse break fee (regulatory)**
  - Yes – $300m

Specific Performance

Yes

Governing Law

State of Delaware

Key STAY shareholders

Shareholders	%
SAR PUBLIC HOLDINGS	9.4
Starwood Capital Group Management	9.4
Vanguard Group Inc/The	8.1
FMR LLC	6.2
BlackRock Inc	4.4
River Road Asset Management LLC	3.2
Dimensional Fund Advisors LP	3.2
Zimmer Partners LP	2.7
Hawk Ridge Capital Management LP	2.0
Long Pond Capital LP	2.0
Others	**49.5**

Source: Bloomberg

Company descriptions & rationale for the merger

EXTENDED STAY DESCRIPTION

- Extended Stay America-branded hotels are designed to provide an affordable and attractive alternative to traditional lodging or apartment accommodations and are targeted toward self-sufficient, value-conscious guests who need lodging for a week or longer. Guests include business travelers, leisure travelers, professionals on temporary work or training assignments, persons relocating, the temporarily displaced, those purchasing a home and anyone else in need of temporary housing.
- Under its structure, ownership of a Paired Share represents an ownership interest in hotel properties through ESH REIT and an ownership interest in franchising and hotel management business, including the operation of owned hotels, through the Corporation. This structure permits STAY to enjoy some, though not all, of the benefits of a REIT (i.e., while ESH REIT is taxed as a REIT for U.S. federal income tax purposes, all distributions paid by ESH REIT to the Corporation are subject to corporate level tax, effectively eliminating approximately 59% of the tax benefit of REIT status).

- STAY is the largest integrated owner/operator of company-branded hotels in North America. Business operates in the extended-stay segment of the lodging industry, and it has the following reportable operating segments:
    - Owned hotels—Earnings are derived from the operation of Company-owned hotel properties and include room and other hotel revenues, which accounted for 98.1% of total revenues for the year ended December 31, 2020.
    - Franchise and management—Earnings are derived from fees under various franchise and management agreements with third parties, which accounted for 1.9% of total revenues for the year ended December 31, 2020. These contracts provide STAY the ability to earn compensation for licensing the Extended Stay America brand name, providing access to shared system-wide platforms and/or management services.
- STAY is also the only major hotel company focused solely on the extended stay segment. It targets product and service offering to an underserved customer base within the lodging industry and the extended stay segment. In addition to owning and operating hotels, it has increased and seek to continue to increase our fee-based income stream, which is driven by franchising brand to third parties. Core operations include intense focus on the delivery of a consistent, quality guest experience; the efficiency of scalable marketing and distribution platforms; maximizing the value of our brand, in-part through rebranding our hotels to the Extended Stay America Suites brand or the Extended Stay America Premier Suites brand, each of which STAY expects will operate under the Extended Stay America umbrella brand; and maximizing the value of owned real estate through investment in hotels. It intends to continue to (i) maximize and grow core operations, (ii) create and curate value within our real estate portfolio, (iii) increase the number of franchised hotels under the Extended Stay America umbrella brand and (iv) optimize capital deployment on behalf of key stakeholders.
- As of December 31, 2020, STAY owned and operated 563 hotel properties in 40 U.S. states, consisting of approximately 62,700 rooms, and franchised 83 hotel properties for third parties, consisting of approximately 8,500 rooms. All 646 system-wide hotels currently operate under the Extended Stay America brand, which serves the mid-price extended stay segment and accounts for approximately 43% of the segment by number of rooms in the United States.

ESH REIT

- ESH REIT owns 563 hotel properties, five of which are subject to ground leases, that are leased to and operated by subsidiaries of the Corporation as described above. ESH REIT has elected and expects to continue to be taxed as a REIT

Industry

U.S. Lodging Industry

- The lodging industry is a significant part of the U.S. economy and **consists of over five million hotel rooms**, according to AHLA. Lodging industry performance is generally tied to both macro and micro-economic trends in the United States and, similar to other industries, experiences both positive and negative operating cycles. Following a growth cycle of more than ten years, the lodging industry entered into a recession in early 2020 resulting from the COVID-19 pandemic, particularly due to certain government-imposed regulations and changes in customer behavior. For the first time since 2010, RevPAR declined for the U.S. lodging industry. According to PwC, RevPAR for the overall U.S. lodging industry declined 47.3% in 2020, and is expected to grow 19.1% in 2021. According to PWC, room supply declined 8.6% in 2020 and is expected to grow 5.2% in 2021.

U.S. Extended Stay Segment

- **Extended stay hotels** represent a growing segment within the U.S. lodging industry, with approximately **545,000 rooms** for the year ended December 31, 2020, according to Highland. The extended stay segment tends to follow the cyclicality of the overall lodging industry. **Extended stay hotels are differentiated by price point into economy, mid-price and upscale segments.** STAY's business is focused on the mid-price extended stay segment, which accounted for approximately 31% of the supply of extended stay rooms in 2020, approximately 43% of which are branded Extended Stay America.

Seasonality

- The lodging industry is seasonal in nature. The Company's revenues are generally lower during the first and fourth quarters of each calendar year as is typical in the U.S. lodging industry. Because many of the Company's hotel operating and general and administrative expenses are fixed and do not fluctuate with changes in revenues, declines in revenues can cause disproportionate fluctuations or decreases in the Company's quarterly earnings and operating cash flows during these periods.

- ESH REIT's revenues and earnings are generally highest during the fourth quarter of each calendar year as rental revenues contingent upon lessee hotel revenues are not deemed as earned for accounting purposes until certain lessee hotel revenue thresholds are achieved, which typically occurs in the fourth quarter. ESH REIT's cash flows generally remain consistent each quarter.

Competition

- STAY operates in a highly competitive industry, with sources of competition including **other extended stay hotel brands, transient-oriented hotel brands that compete for both transient and extended stay guests and alternative lodging (including serviced apartments and private homes and rooms and apartments rented on the internet, also referred to as "peer-to-peer inventory sources").** In addition, STAY faces competition for both **quality acquisition opportunities and locations to build new hotels and for hotel owners and developers as potential franchisees**. It also faces competition from **third-party intermediaries** and, increasingly, from **new channels of distribution, such as large companies that offer online travel services as part of their business model** and **search engines**.
- Extended Stay, which operates 650 midpriced hotels, focuses on a corner of the lodging industry that provides longer-term stays, often catering to construction crews, emergency responders and cost-conscious corporate workers. The company's system-wide occupancy rate was 74% last year, according to a filing, according to 44% across the U.S. hotel industry.
- In addition to the hotel-operating company, an Extended Stay affiliate owns 564 hotel properties with 62,000 rooms, making it largest hotel real estate investment trust in North America, according to the company.

CONSORTIUM DESCRIPTION

- The Consortium is led by Starwood Capital Group and also includes Blackstone Group.
- Blackstone was part of a group that bought Extended Stay out of bankruptcy in 2010 and took it public three years later. The firm has been a prolific investor in hotel real estate and operating companies in the past, including Hilton Worldwide Holdings Inc., La Quinta and others.
- Extended Stay America, Inc. ("ESA") and its paired-share REIT, ESH Hospitality, Inc. ("ESH" and together with ESA, the "Company") (NASDAQ: STAY) announced that it has signed a definitive agreement to be acquired by a 50/50 joint venture between funds managed by Blackstone Real Estate Partners ("Blackstone") and Starwood Capital Group ("Starwood Capital") for $19.50 per paired share in an all-cash transaction valued at approximately $6 billion.

STRATEGIC RATIONALE FOR THE MERGER

- Doug Geoga, Chairman of the Boards of the Company said, "After a thorough review of the Company's business plan, the Boards concluded that the immediate cash premium offered by this transaction is compelling for stockholders. We are delighted with this outcome."
- Bruce Haase, CEO and President of the Company said, "We are pleased to announce this transaction with Blackstone and Starwood Capital, two of the most experienced investors in the hospitality space with impressive track records of building value in a wide variety of real estate assets, and we look forward to this partnership and continued growth." He added, "The Boards and senior management are especially grateful to the excellent team of leaders and associates who have made this company such a leader in the lodging industry and we are confident in the Company's continued success under private ownership."
- Tyler Henritze, head of US acquisitions for Blackstone Real Estate commented, "Travel and leisure is one of Blackstone's highest conviction investment themes, and we have confidence in the extended stay model. We helped create this company nearly twenty years ago, and believe our expertise puts us in a unique position to add long-term value."
- Barry Sternlicht, CEO of Starwood Capital, added, "Extended Stay has demonstrated resilience over the past year despite persistent challenges due to government lockdowns and travel restrictions. We are excited about the Company's growth opportunity as restrictions ease and we're confident that, in partnership with Blackstone and the Company, our team has the right experience to drive continued success."

Key risks

REGULATORY RISKS AND TIMING

- HSR approval is required
- Blackstone Real Estate Partners ("Blackstone") and Starwood Capital Group will own a 50/50 joint venture
- We note that both Blackstone and Starwood own hotel assets.

Product market

- Starwood has several hotel assets in its portfolio. However, in the overall hotel market the combined market share is not significant.
- We note that Starwood owns InTown Suites that competes in the extended stay market
- Although we note that STAY stated in its 10-K the following: All 646 system-wide hotels currently operate under the Extended Stay America brand, which **serves the mid-price extended stay segment and accounts for approximately 43% of the segment by number of rooms in the United States**.
- In June 2013, Starwood acquired InTown Suites, one of the largest owners of economy extended stay properties in the U.S. At original acquisition, the company owned and operated 138 properties (17,978 rooms), representing ~25% of the extended-stay sector. Today, it has almost 200 locations in 22 states and more than 25,000 guest rooms.
- Based on our findings, InTown and STAY are direct competitors in the extended stay market. The extended stay market consists of 545,000 rooms. A potential combination of InTown and STAY would represent 87,700 room and a 16% market share.
- Further segmentation of the extended stay market based on pricing is a key to decide if the current acquisition could cause rigorous antitrust review. Based on STAY 10-K in the mid-price segment they own 43% of the market.
- As per our findings on biz-stay.com InTown Suites competes in the Economy Chains segment and STAY in the mid-range segment

Upscale Chains	Number of Properties
AKA	9
Element	35+
Hyatt House	85+
Residence Inn	760+
Homewood Suites	340+
Staybridge Suites	250+
Sonesta ES Suites	40+
GrandStay Residential Suites	7
Larkspur Landing	11
Hawthorn Suites	100+

Mid-Range Chains	Number of Properties
TownePlace Suites	340+
Home2 Suites	110+
MainStay Suites	40+
Candlewood Suites	300+
Home-Towne Suites	11
Extended Stay America	655+
My Place	55

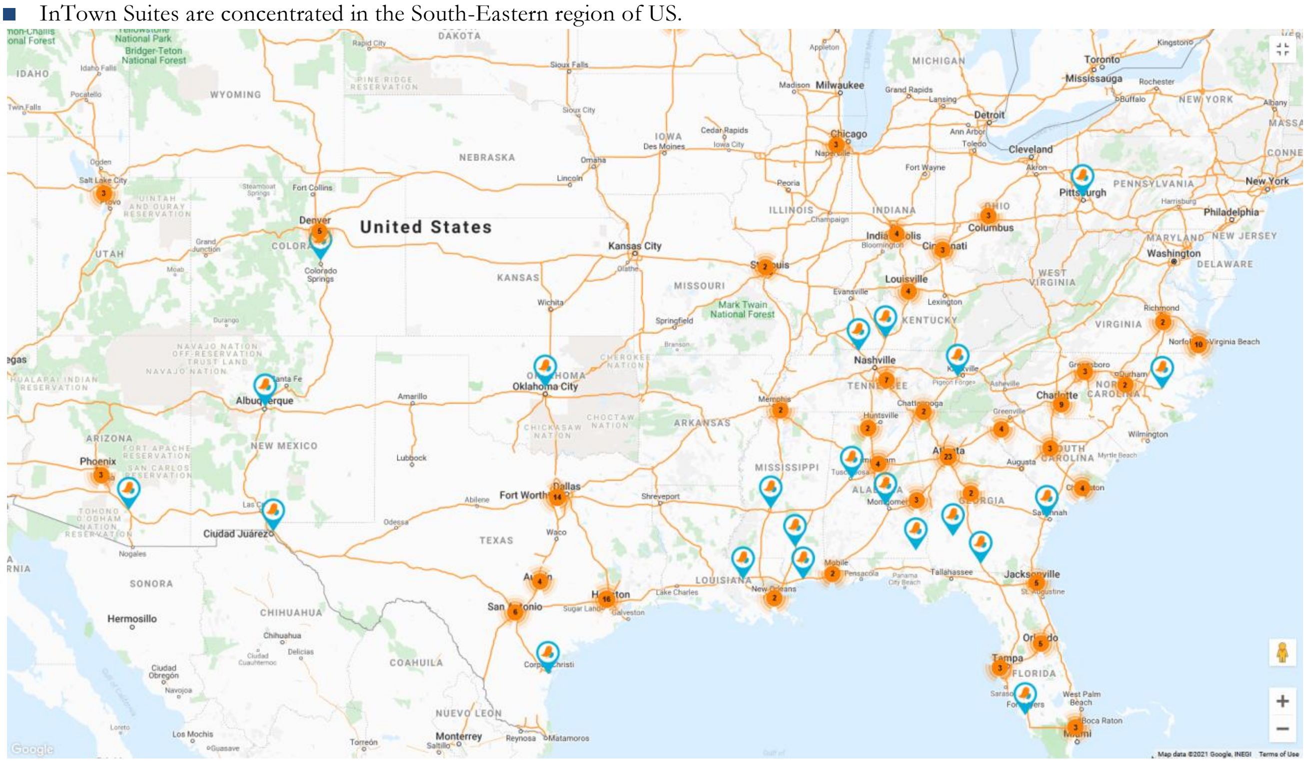
Economy Chains	Number of Properties
Suburban	50+
WoodSpring Suites	10+
Affordable Suites of America	18
Studio 6	50+
Crossland	46
Value Place	185+
InTown Suites	130+

Geographic market

- Based on previous precedents, the geographic market for hotels and motels is local

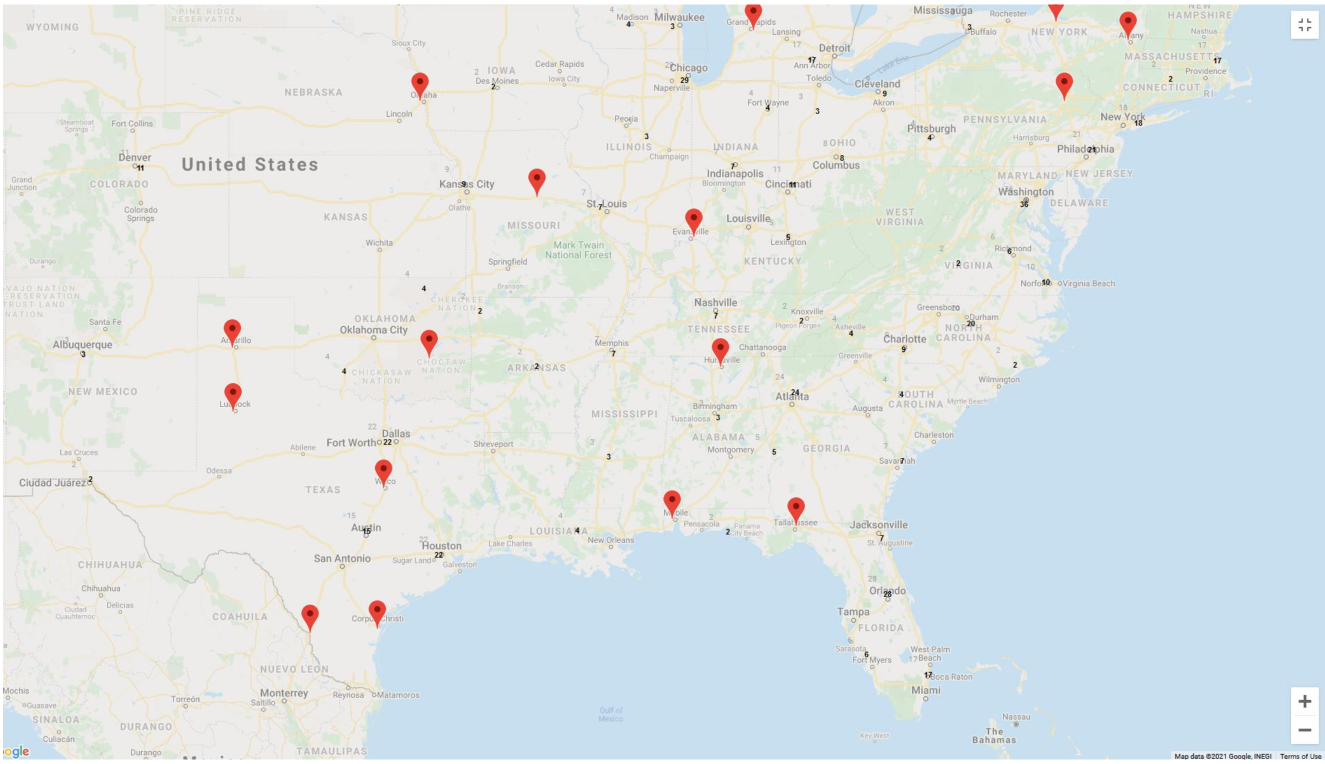
Antitrust issue

- Antitrust issue might arise in case of a wider product market definition (extended stay market irrespective of pricing) in some of the local markets.
- InTown Suites are concentrated in the South-Eastern region of US.



Source: intownsuites.com

- As of December 31, 2020, 15.8% of STAY rooms were in California, 10.4% of its rooms were in Florida, 7.5% of its rooms were in Texas and 5.5% of its rooms were in Illinois.



- Key overlapping MSAs are
  - Houston STAY 22 – InTown 16
  - Dallas STAY 22 – InTown 14
  - Atlanta STAY 24 – InTown 23
  - Charlotte STAY 9 – InTown 9
  - Norfolk STAY 10 – InTown 10

- **As per or finding all key players are present in the above mentioned MSAs**
  - In Houston there are 11 Candlewood and 13 Staybride location (both IHG), 13 TownePlace and 17 Residence Inn (both Marriott), 8 Value Place, 16 Home2, 13 Studio6
  - In Dallas there are 8 Candlewood and 6 Staybride location (both IHG), 16 TownePlace and 23 Residence Inn (both Marriott), 6 Value Place, 21 Home2, 17 Studio6
  - In Atlanta there are 2 Candlewood and 4 Staybride location (both IHG), 6 TownePlace and 12 Residence Inn (both Marriott), 1 Value Place, 15 Home2, 6 Studio6
  - In Charlotte there are 3 Candlewood and 3 Staybride location (both IHG), 6 TownePlace and 10 Residence Inn (both Marriott), 1 Value Place, 11 Home2, 3 Suburban, 17 Studio6
  - In Norfolk there are 4 Candlewood and 2 Staybride location (both IHG), 1 TownePlace and 5 Residence Inn (both Marriott), 1 Value Place, 1 Home2, 1 Studio 6

Key mitigating factor

- We note that a key mitigating factor is that STAY will be owned by Starwood and Blackstone in a 50%-50% JV.
- Given the $300m regulatory related reverse break fee we believe that the consortium is willing to do its best to receive antitrust approval and close the deal.
- We also note that there are other competitors like AirBNB, Vrbo, Sonder etc. present which we did not include in our market share calculations.
- In case antitrust regulators see some degree of substitutability among upscale, mid-tier and economy price segments the competition appears to be so intense that a lengthy deal review appears to be a wild card scenario.

CBR summary

- Starwood's InTown and STAY are competitors in the wider extended stay market with a ~16% combined market share. However, in some of the above mentioned overlapping MSAs (most likely in Norfolk) asset divestiture might be required. Other MSAs seem to be competitive, not causing any antirust related issues. We note that all key competitors are present in the overlapping MSAs.

- In case of a narrow product market definition based on pricing of the rooms - which is a more likely scenario, the two companies are not direct competitors and HSR approval is likely to be granted in the initial phase.

SHAREHOLDER VOTE

- Starwood's equity stake might ward off other bidders and shareholders have limited alternatives that would grant a bigger return compared to accepting the consortium's current offer.

COUNTERBID

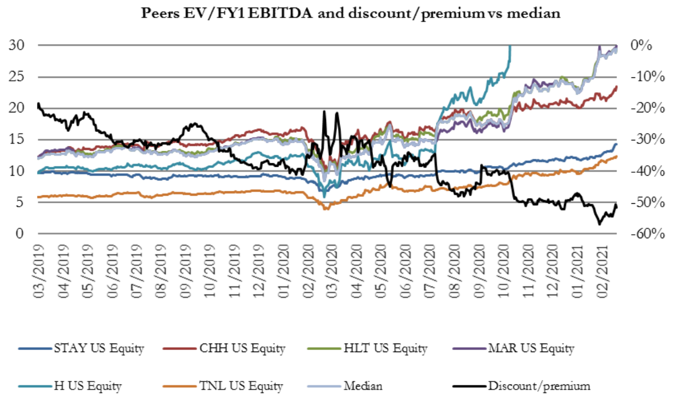
- Based on our ROIC calculations there is limited room for bump. However, our LBO calculation justifies a higher, low-20s bid. Compared to precedents' valuation and given the company performed steadily during a travel freeze, we cannot rule out other suitors approaching the company.
- Starwood's equity stake in Extended Stay may ward off competing buyers

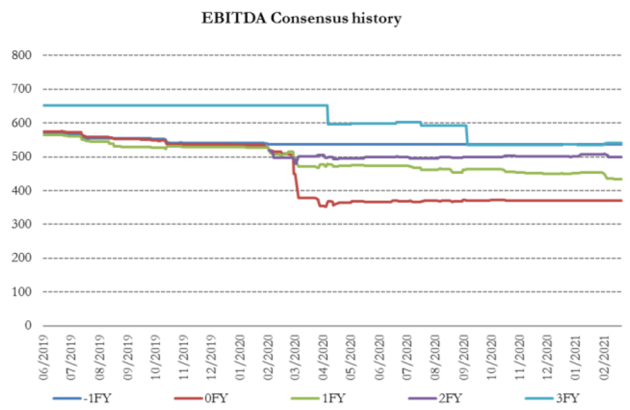
Valuation

PEERS AND STANDALONE

- STAY was trading below the wider peer group average. One may argue that its more stable cash flow and higher margins justify a higher takeout multiple.
- In a highly unlikely deal break we see downside around $17.00

Company	Price	Mkt Cap (mn)	FY1 EV/ EBITDA	FY2 EV/ EBITDA	EBITDA CAGR	FY1 EBITDA Margin	FY1 PE	FY2 PE	EPS CAGR
EXTENDED STAY AM	19.31	3,430	14.2x	12.4x	13.4%	38.6%	38.0x	24.3x	43.5%
CHOICE HOTELS	114.68	6,271	23.2x	19.2x	20.2%	31.1%	35.4x	27.3x	24.1%
HILTON WORLDWIDE	127.14	34,962	30.0x	19.7x	44.7%	23.4%	67.7x	33.0x	64.2%
MARRIOTT INTL-A	155.95	49,768	30.1x	19.3x	48.1%	15.1%	78.8x	34.1x	76.0%
HYATT HOTELS-A	89.55	8,910	70.8x	19.8x	-	4.9%	-	-	-
TRAVEL + LEISURE	65.11	5,457	12.5x	9.5x	56.8%	23.4%	21.2x	14.6x	34.6%
Average			**30.2x**	**16.6x**	**36.6%**	**22.8%**	**48.2x**	**26.7x**	**48.5%**





PRECEDENTS

- STAY's FY1 EV EBITDA multiple of 14.3x is close to precedent's average, similar to the premium of 15%.

Announce Date	Target Name	Acquirer Name	Total Value (mil.)	Payment Type	TV/FY1 EBITDA	Premium	Deal Status
05/11/2020	Target Hospitality Corp	TDR Capital LLP	472.03	Cash	6.7x	36%	Proposed
20/08/2019	Hilton Grand Vacations Inc	Apollo Global Management Inc	4337.48	Cash	8.9x	39%	Proposed
06/05/2019	Chesapeake Lodging Trust	Park Hotels & Resorts Inc	2,540	Cash and Stock	14.1x	9%	Completed
14/12/2018	Belmond Ltd	LVMH Moet Hennessy Louis Vuitton SE	3626.83	Cash	21.8x	42%	Completed
05/10/2018	NH Hotel Group SA	Minor International PCL	1,402.21	Cash	4.9x	0%	Completed
06/09/2018	LaSalle Hotel Properties	Pebblebrook Hotel Trust	5,294	Cash or Stock	16.5x	9%	Completed
30/04/2018	ILG LLC	Marriott Vacations Worldwide Corp	5008.73	Cash and Stock	14.0x	15%	Completed
10/08/2017	Starwood Waypoint Homes	Invitation Homes Inc	8,201	Stock	25.0x	5%	Completed
29/06/2016	Diamond Resorts International Inc	Apollo Global Management Inc	3073.38	Cash	6.8x	24%	Completed
Average					**13.2x**	**20%**	

LBO

- We see some room for a PE company to offer additional premium to the current share price up to the low $20s/STAY share.
- Our assumptions include
    - Offer at $19.50/ODP share
    - 3% LT growth rate
    - Adj Net debt as of 4Q20
    - LT EBITDA margin 45%
    - Equity participation 50%
    - Leverage 1.9x in FY 21
    - Interest coverage 7.2x in FY21, 6.2x in FY22

- Credit spread 5.5%
- 20% tax rate
- IRR target 13.5%
- No synergies

Sensitivity tables

		Bid Price				
		$19.50	$21.00	$22.00	$23.00	$24.00
EBITDA Marg	35.0%	10.5%	10.3%	10.2%	10.1%	10.0%
	40.0%	12.0%	11.9%	11.8%	11.7%	11.6%
	45.0%	**13.5%**	13.4%	13.2%	13.1%	13.1%
	47.0%	14.1%	13.9%	13.8%	13.7%	13.6%
	50.0%	14.9%	14.7%	14.6%	14.5%	14.4%

		Bid Price				
		$19.50	$21.00	$22.00	$23.00	$24.00
LT Growth	0.0%	12.9%	12.8%	12.7%	12.6%	12.5%
	2.0%	13.3%	13.2%	13.1%	13.0%	12.9%
	3.0%	**13.5%**	13.4%	13.2%	13.1%	13.1%
	5.0%	13.9%	13.7%	13.6%	13.5%	13.4%
	7.0%	14.3%	14.1%	14.0%	13.9%	13.8%

		Bid Price				
		$19.50	$21.00	$22.00	$23.00	$24.00
EV/EBITDA	9.0x	3.0%	1.8%	0.9%	0.1%	-0.7%
	10.0x	5.4%	4.2%	3.4%	2.6%	1.9%
	14.3x	**13.5%**	12.4%	11.6%	10.9%	10.2%
	12.0x	9.5%	8.4%	7.6%	6.9%	6.2%
	13.0x	11.3%	10.2%	9.5%	8.7%	8.0%

		Bid Price				
		$19.50	$21.00	$22.00	$23.00	$24.00
Equity Part.	40.0%	14.8%	14.6%	14.5%	14.4%	14.3%
	45.0%	14.1%	13.9%	13.8%	13.7%	13.6%
	50.0%	**13.5%**	13.3%	13.2%	13.1%	13.0%
	55.0%	13.0%	12.8%	12.7%	12.7%	12.6%
	60.0%	12.6%	12.4%	12.3%	12.3%	12.2%

		Bid Price				
		$19.50	$21.00	$22.00	$23.00	$24.00
Interest Margin	5.0%	13.7%	13.6%	13.5%	13.4%	13.3%
	5.2%	13.6%	13.5%	13.4%	13.3%	13.2%
	5.5%	**13.5%**	13.4%	13.2%	13.1%	13.1%
	5.7%	13.4%	13.3%	13.2%	13.1%	13.0%
	6.0%	13.3%	13.1%	13.0%	12.9%	12.8%

Source: CBR and Bloomberg

ROIC

By our ROIC calculation we don't see room to improve the current offer.

- We assumed:
  - 20% effective tax rate
  - no synergies – we note that with a combination of Starwood's extended stay asset potential synergies would not be more than $30m-$50m p.a. used in our sensitivity table. That would not change the conclusion of our ROIC calculation.

ROIC calculations

Deal value ($m)	2021	2022	2023
Bid price (/ sh.)	*19.50*	*19.50*	*19.50*
O/S (m)	*178*	*178*	*178*
Market value (m)	**3462**	**3462**	**3462**
Net Debt (m)	2756	2756	2756
Deal value (m)	**6218**	**6218**	**6218**
ROIC calculation			
BEST Operating Profit (m)	**214**	**279**	**322**
Synergies	*0*	*0*	*0*
Adj. Operating Profit (m)	**214**	**279**	**322**
Tax (20%)	*43*	*56*	*64*
NOPAT (m)	**171**	**223**	**258**
ROIC	**2.8%**	**3.6%**	**4.1%**

Sensitivity tables

Price vs Operating profit

		Bid price ($/share)				
		19.5	21.0	23.0	25.0	27.0
2020 Op. Profit ($m)	214	2.8%	2.6%	2.5%	2.4%	2.3%
	280	3.6%	3.5%	3.3%	3.1%	3.0%
	322	4.1%	4.0%	3.8%	3.6%	3.4%
	350	4.5%	4.3%	4.1%	3.9%	3.7%
	370	4.8%	4.6%	4.3%	4.1%	3.9%

Price vs Synergies

		Bid price ($/share)				
		19.5	21.0	23.0	25.0	27.0
Ann. Cost Syn. ($m)	0	4.1%	4.0%	3.8%	3.6%	3.4%
	10	4.3%	4.1%	3.9%	3.7%	3.5%
	20	4.4%	4.2%	4.0%	3.8%	3.6%
	30	4.5%	4.3%	4.1%	3.9%	3.7%
	50	4.8%	4.6%	4.4%	4.1%	3.9%

Price vs Tax rate

		Bid price ($/share)				
		19.5	21.0	23.0	25.0	27.0
Tax rate	10%	4.7%	4.5%	4.2%	4.0%	3.8%
	15%	4.4%	4.2%	4.0%	3.8%	3.6%
	20%	4.1%	4.0%	3.8%	3.6%	3.4%
	25%	3.9%	3.7%	3.5%	3.4%	3.2%
	30%	3.6%	3.5%	3.3%	3.1%	3.0%

Synergies vs Tax rate

		Annual cost savings ($m)				
		0	10	20	30	50
Tax rate	10%	4.7%	4.8%	5.0%	5.1%	5.4%
	15%	4.4%	4.5%	4.7%	4.8%	5.1%
	20%	4.1%	4.3%	4.4%	4.5%	4.8%
	25%	3.9%	4.0%	4.1%	4.2%	4.5%
	30%	3.6%	3.7%	3.9%	4.0%	4.2%

Source: CBR and Bloomberg

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