FINAL TRANSCRIPT

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the China Lodging Group Q4 2010 Earnings Conference Call hosted by Ida Yu. My name is Christina, and I'm your event manager. During the presentation, your lines will remain on listen-only. (Operator Instructions). Please note that today's conference call is being recorded.

I'd now like to hand the conference over to your host, Ida. Please proceed.

Ida Yu - *China Lodging Group Ltd - IR Manager*

Hello, everyone. Thank you, Christina and welcome to our fourth quarter and full year 2010 earnings conference call. Joining us today is Matthew Zhang, our Chief Executive Officer; and Jenny Zhang, our Chief Financial Officer. Following their prepared remarks, the CEO and the CFO will be available to answer your questions.

Before we continue, please note that the discussion today will include forward-looking statements made under the Safe Harbor provisions of the United States Private Securities Litigation Reform Act of 1995.

Forward-looking statements involve inherent risks and uncertainties. As such, our results may be materially different from the views expressed today. A number of potential risks and uncertainties are outlined in our public filings with the SEC. China Lodging Group does not undertake any obligation to update any forward-looking statements except as required under applicable law.

On the call today, we will also mention adjusted financial measures during the discussion of our performance. The calculations of those measures to comparable GAAP information can be found in the earnings release that was distributed earlier today.

As a reminder, this conference call is being recorded. The webcast of this conference call will be available on the investors' section of China Lodging Group's website at ir.htinns.com.

I would now turn the call over to our CEO. Matthew, please.

Matthew Zhang - *China Lodging Group Ltd - CEO*

Thank you, Ida; and good morning, everyone. Thank you for joining this conference call today. I'm very pleased to announce that China Lodging Group achieved another quarter of solid performance, and closed 2010 with significant results in network expansion and profitability.

First, our network continues to expand rapidly, with 70 new hotels added in the fourth quarter. We accomplished 202 new hotels opening in year 2010, and 86% growth from 236 hotels at the end of last year.

As of December 31, 2010, HanTing had a network of 438 hotels in operation, consisting of 243 leased-and-operated hotels, and 195 franchised-and-managed hotels, covering 65 cities in China, compared with 236 hotels covering 39 cities at the end of last year.

In addition, at the end of 2010, we had 162 hotels of pipeline, including 69 leased-and-operated hotels and 93 franchised-and-managed hotels. Those 600 hotels in operation and in pipeline in total cover more than 90 cities.

Our fast and solid nationwide expansion has further enhanced our brand recognition and our attractiveness to our customers. We are confident to leverage our excellent execution capability and brand value to achieve higher profitability in the coming years.

Secondly, on the operational side, we further improved our IT system to increase customer satisfaction and operation efficiency. Launched two years ago, our online booking reached 20% in the fourth quarter 2010. At the end of 2010, HanTing Club was awarded the best loyalty program by Qunar.com, a leading travel search engine company in China.

Thirdly, we have further strengthened our loyalty program. At the end of 2010, we had more than 2.6 million individual members, a 75% increase from a year ago.

In 2010, 61% of room nights sold were contributed by individual members, and 12% were contributed by corporate members, improved from 59% and 9% a year ago respectively. Our fast-growing loyalty program and our loyal customer base fuels our continuous expansion.

Now let's look at the key operational metrics. In fourth quarter 2010, ADR were improved to RMB194, a 10% increase from RMB177 in the same quarter last year, due to our strengthening brand, successful yield management, and price increase during China Shanghai Expo in October 2010.

Occupancy rate was 87% compared with 95% in same quarter last year and 95% in the previous quarter. The year-over-year decrease was mainly attributable to the increased percentage of new hotels still in the ramp-up stage and increased occupancy in Shanghai after Expo.

With the higher ADR offset lower occupancy, RevPAR reached RMB168, the same as the fourth quarter last year.

Our mature hotels demonstrated continuous solid performance improvement. The RevPAR for hotels at least 18 months in operation was RMB181 for the quarter; increased 6% in the same quarter last year. The improvement was mainly driven by higher ADR as a result of strengthening brand, successful yield management, and the Expo-driven price increase in Shanghai.

For the full year of year 2010, ADR was RMB197 representing 13% year-over-year growth from RMB174 in 2009. Occupancy rate for all hotels in operation was 93% compared with 94% in 2009. RevPAR was RMB183, a 12% increase from RMB163 a year ago.

For the full year 2010, we reached 38% year-over-year increase in net revenues. Net income attributable to the Company was RMB216 million, 5 times of the net income in 2009.

EBITDA was RMB445 million (Company corrected after the conference call), increased 107% from previous year. This was a combined result of favorable macroeconomic environment improvement, our excellent execution, successful yield management, and extra benefit from Shanghai Expo.

From the management estimates, Shanghai Expo contributed approximately 7.7% to our blended RevPAR, and 6.4% to our net revenues in full year 2010.

The macro economy in China continues to grow strongly, leading to increasing travel demand. With a strong footprint in developed cities, we gradually penetrate into second and third tier cities owing to our disciplined investment approach, and returns achieved in the second and third tier city hotels remain very attractive. We are confident that our expansion will continue to derive fast revenue growth and steady improvement in margin in the coming years.

In 2010, we plan to add approximately 200 hotels. We will evenly split it between leased-and-operated and franchised-and-managed hotels. We expect our net revenue to grow 34% to 38% in 2011.

Now I will turn the call to Jenny Zhang, our CFO, to walk us through the financials in more details. Jenny?

Jenny Zhang - *China Lodging Group Ltd - CFO*

Thank you, Matthew. Hello, everyone. I'm glad to report to you the financial results of the fourth quarter and the full year of 2010.

Total revenues for the quarter came out in line with our guidance, increasing 29.2% year over year to RMB479 million, primarily as a result of our enlarged hotel network.

Revenues from leased-and-operated hotels and the franchised-and-managed hotels grew 23.3% and 164.9% respectively. Total revenues for the year increased 37.8% to RMB1,838 million, with revenues from leased-and-operated hotels and the franchised-and-managed hotels growing by 32.5% and 190.4% respectively.

Total revenues from franchised-and-managed for the year accounted for 7% of total revenues, improved from 3% in 2009. Net revenues for the quarter were RMB453 million, representing an increase of 29.2% year over year. Net revenues for the year were RMB1,738 million, representing 38% increase from 2009.

Hotel operating costs for the quarter were RMB323 million, or 71.4% of net revenues. Total hotel operating costs, excluding share-based compensation expenses, represented 71.3% of net revenues compared with 76.3% for the same quarter in 2009, and 61.4% in the previous quarter.

The decrease in hotel operating costs as a percentage of net revenues year over year was primarily due to increased RevPAR and the growth of franchised revenue. For the full year of 2010, our hotel operating costs were RMB1,180 million, or 67.9% of net revenues, compared with 79.7% in 2009.

Selling and marketing expenses for the quarter were RMB19.2 million. Selling and marketing expenses, excluding share-based compensation expenses, was RMB19.1 million, or 4.2% of net revenues, compared with 4.0% for the same quarter in 2009, and 4.1% in the previous quarter.

For the full year of 2010, excluding share-based compensation expenses, our selling and marketing expenses accounted for 4.1% of net revenues, compared with 4.6% in 2009.

G&A expenses for the quarter were RMB33 million. General expenses, excluding share-based compensation expenses, were RMB31 million, or 6.8% of net revenues, compared with 7.2% of net revenues in the same period of 2009, and 6.4% in the previous quarter.

For the full year of 2010, excluding share-based compensation expenses, our G&A expenses accounted for 6.3% of net revenues compared with 6% in 2009.

Pre-opening expenses for the quarter were RMB46 million, an increase of 502% year over year, and 29% sequentially. The increase in pre-opening expenses were a result of our acceleration of leased-and-operated hotel openings from 28 in 2009 to 70 in 2010, and leased-and-operated hotel pipeline expansion from 21 at the end of 2009 to 69 at the end of 2010.

Income from operations for the quarter was RMB31 million. Excluding share-based compensation expenses, adjusted income from operations was RMB34 million, representing a 5.8% year-over-year increase.

Income from operations for the quarter was impacted by the significant pre-opening expenses driven by the number of new leased-and-operated hotel openings. As noted by Matthew earlier, those addition of leased-and-operated hotels, we believe, will contribute to our profit base in future years.

For the full year of 2010, income from operations was RMB256 million. Excluding share-based compensation expenses, adjusted income from operations was RMB269 million, representing a 219% increase from the year of 2009.

Net income attributable to the Company for the quarter was RMB35 million, or 7.7% of net revenues, up 76% from RMB20 million in 2009. Excluding share-based compensation expenses, adjusted net income attributable to the Company for the quarter increased 65.9% year over year to RMB38 million.

For the full year of 2010, net income attributable to the Company was RMB216 million, up 407% from RMB43 million in 2009.

EBITDA for the fourth quarter of 2010 was RMB90 million, compared with RMB69 million in the same quarter of 2009, and RMB155 million in the previous quarter.

EBITDA from operating hotels was RMB136 million, an increase of 77.1% from the same quarter of 2009, and a decrease of 28.5% sequentially. EBITDA from operating hotels was 30.1% of net revenues, improved from 22% for the same quarter of 2009.

The year-over-year increase was a result of enhanced profitability of mature hotels and the expansion of our network, while the sequential decrease was mainly due to the low season and the Expo closing in October.

For the full year of 2010, EBITDA was RMB445 million, up 107% from 2009. EBITDA from operating hotels was RMB556 million, up 120% from 2009.

Net operating cash flow for the quarter was RMB75 million for the quarter and RMB469 million for the year.

Cash spend on the purchase of property and equipment was RMB156 million for the quarter and RMB397 million for the year.

As of December 31, 2010, we had cash and cash equivalents of RMB1.1 billion. We expect to achieve net revenues in the range of RMB410 million to RMB430 million in the first quarter of 2011. For the full year of 2011, we expect our net revenues to grow between 34% to 38% year over year.

The above forecast reflects the Company's current and preliminary view, which is subject to change.

With that, we will now open the call to any questions that you may have. Operator?

QUESTIONS AND ANSWERS

Operator

Sorry for any interruption, ladies and gentlemen. Your question and answer session will now begin. (Operator Instructions).

Operator

(Operator Instructions). [Ella Gee, Oppenheimer & Co.].

Ella Gee - *Oppenheimer & Co. - Analyst*

First of all, I noticed that your occupancy rate for mature hotels declined; that you were 91% in this quarter versus 97% one year ago. Could you explain that?

Matthew Zhang - *China Lodging Group Ltd - CEO*

Yes. I think that there's several impacts for this. If you talk about mature hotels that -- as you know, that after Expo, Shanghai has a dip of the traveling population, so our occupancy in Shanghai dropped to some certain extent. And as you also know that our Company -- our hotels in Shanghai has a big proportion of our total network, so that gives a major impact on the occupancy drop.

The second reason is that, as we mentioned even in the last year, we start to do the yield management by increase our -- to balance the ADR and occupancy to reach the similar level, or even higher RevPAR. That is a result you can see from that our RevPAR is still in the increase trend, even for the mature hotels.

Ella Gee - *Oppenheimer & Co. - Analyst*

So regarding the second point, so you're saying that you are trying to raise ADR a little bit. While you may sacrifice occupancy a little bit, but net-net, the RevPAR is still expected to be up?

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Matthew Zhang - *China Lodging Group Ltd - CEO*

Yes, that's a practice we already started from the beginning of last year to reach the optimized combination between the ADR and occupancy to reach the same level, even higher level of RevPAR, yes.

Ella Gee - *Oppenheimer & Co. - Analyst*

Got it. And so far, how much sequential -- sequentially speaking, how much raise in ADR have you been practicing, and what's the feedback from the market?

Jenny Zhang - *China Lodging Group Ltd - CFO*

For the full year, our ADR has increased substantially. Part of that was due to the Expo, but even beyond the Shanghai area, we had overall ADR increase on like-for-like basis around 6% to 7%. So it has been thoroughly implemented throughout the country.

Ella Gee - *Oppenheimer & Co. - Analyst*

Got it. And also, I want to ask regarding your 200 new hotels for 2011; will they be opened at mostly at new cities, or existing cities?

Matthew Zhang - *China Lodging Group Ltd - CEO*

The current pipeline we have we will add about 30/35 new cities on top of our current city coverage. So by the end of the year, we will -- more than 90, closer to 100 cities for the total network.

Jenny Zhang - *China Lodging Group Ltd - CFO*

However, if you count the number of hotels added for the new cites we get into, you will most likely to be one to two hotels within one year. So the significant majority of the hotels added will still be the cities we already cover today.

Ella Gee - *Oppenheimer & Co. - Analyst*

Got it. So given the strong industry competition, do you think the new hotels you open at the existing cities, do you think they will dilute the mature hotels at those cities occupancy rate? Also do you think it will maybe take longer for new hotels to ramp up to a matured level?

Matthew Zhang - *China Lodging Group Ltd - CEO*

At this stage, we do not see such a trend. I think that for the matured hotel, we still continue to expect 4% -- 2% to 4% increase in RevPAR, even though there's new hotels opened nearby. But on the other hand, that the new hotels we open, we still keep a very disciplined return approach to the site selection, which will reach the very favorable and reasonable return criteria.

Ella Gee - *Oppenheimer & Co. - Analyst*

Okay, thank you. And just a quick follow-up on my first question. I actually noticed that you provided a very detailed impact from the Shanghai Expo in the end of your press release. When I calculate your RevPAR for your mature hotels, and if I excluded Shanghai Expo impact, and I see that quarter over quarter, RevPAR for mature hotels is down around 11% from 3Q. It seems a little bit higher than your historical seasonality, so I'm wondering if it's also because of the lower traffic in Shanghai post-Expo, or is there any other reasons?

Matthew Zhang - *China Lodging Group Ltd - CEO*

Yes. I think if you look at the fourth quarter last year that the major reason for that is the dip after Expo in Shanghai. And we have a significant number of hotels in Shanghai as a percentage of the total network. That's impact a lot.

Jenny Zhang - *China Lodging Group Ltd - CFO*

Ella, but if you look forward, I believe Shanghai still as the commercial center of China, it still will be very dynamic city with a lot of traveling traffic. I think the reduced amount of traveling in Shanghai is actually a short-term situation. We actually have things on the operation perspective, we know that demand is gradually bouncing back.

Ella Gee - *Oppenheimer & Co. - Analyst*

So regarding that, in the first quarter, how do you see the occupancy rates trend year over year?

Matthew Zhang - *China Lodging Group Ltd - CEO*

The first quarter is still low season. I think that the first quarter of this year will be not as strong as last year. But after the China Lunar Year, we see a very strong bounce-back from the demand to our occupancy rate, and the traffic bounce back significantly.

So we are optimistic about the future demand in Shanghai and also in China, given the macro economic condition and our strengthening brand.

Ella Gee - *Oppenheimer & Co. - Analyst*

Got it. Thank you very for taking my questions.

Matthew Zhang - *China Lodging Group Ltd - CEO*

Thank you, Ella.

Operator

Adam Krejcik, Roth Capital Partners.

Adam Krejcik - *Roth Capital Partners - Analyst*

Just a follow-up on the last part there about Q1 guidance. It seems to me maybe -- I'm just trying to see how conservative that number is, or if I'm missing something in terms of modeling, because in order to get to your guidance range, it seems like RevPAR would have to be down quite a bit year-on-year. Is that correct in terms of the trend you're seeing in Q1? And was that mainly slowdown in travel in terms of January and February?

Jenny Zhang - *China Lodging Group Ltd - CFO*

Our experience in the first two months is somehow interesting. Maybe it's because of the timing of this Chinese New Year. This typical seasonal low season seems longer than the earlier years we have experienced, so the January and the first half of February seems to be relatively low compared to the earlier years. However, as Matthew mentioned earlier, starting from mid-February, we see a very strong performance all across the country. So that has, I think, had an impact on our guidance for the first quarter.

Adam Krejcik - *Roth Capital Partners - Analyst*

And what's the rough allocation in terms of how many leased-and-operated hotels you'll be opening I guess in the first half of the year versus the second half? Is it fairly equally weighted, or is it more back end weighted again this year? And then the same for managed hotels.

Matthew Zhang - *China Lodging Group Ltd - CEO*

I think that for the leased-and-operated hotels for the first half of the year, one-third of the planned hotels will open in the first half of the year, and two-thirds will open in the second half. For the franchised-and-managed hotels, they will be more evenly split across quarters.

Adam Krejcik - *Roth Capital Partners - Analyst*

Got it. And then, Jenny, in terms of EBITDA margin trends for 2011, given your more recent operated expenses and, obviously, there's no Shanghai Expo this year, just trying to get a sense in terms of what kind of pressure we might see on the EBITDA margin in 2011 versus 2010. Any kind of directional guidance there or commentary would be very helpful.

Jenny Zhang - *China Lodging Group Ltd - CFO*

We clearly see 2011 as a year of investment for us. First of all, we have increased the number of leased-and-operated openings planned for this year; 100 versus 70 last year. And then secondly, because last year's opening was heavily skewed towards the end of year, so more than half of the new hotels opened last year actually will need to go through their ramp-up in 2011.

So we have run our statistics; basically, in 2010 the hotels in the ramp-up stage, the [contributed] room nights only account for 7% of the total room nights available, while that number will increase to 18% in 2011. So a significant portion of our hotels are going to be in the ramp-up stage.

So those two factors are going to have an impact on our margin in this period. However, we believe those investments are going to pay back in future years. As we move into 2011 and 2013, the margin will have a strong bounce-back because of expanded mature hotel base.

Adam Krejcik - *Roth Capital Partners - Analyst*

Got it. And then I guess just finally, there's been some discussions about changing the tax policy, favorable tax policy, for lower middle-income citizens, as well as more affordable lower income housing. I was wondering what your general thoughts are about these macro issues, and if there's any way to quantify or the potential impact that it can have on the travel industry, and I guess especially economy hotel operators like yourself.

Jenny Zhang - *China Lodging Group Ltd - CFO*

We believe this is a very positive signal that the Government is taking meaningful measures to boost domestic demand; and why -- when consumers have more disposal income, I think traveling is going to be a major trend, and the major area they are going to put those incremental money available. So overall, we think is a strong signal that we will have continued strong growth in the demand side. It's very good news.

Adam Krejcik - *Roth Capital Partners - Analyst*

Great. Thank you very much.

Operator

Billy Ng, BofA Merrill Lynch.

Billy Ng - *BofA Merrill Lynch - Analyst*

Basically, just three questions. The first one is on the growth guidance; understanding that January/February was a bit soft. So the first Q guidance was a bit low, but we see that the growth will increase in terms of percentage for the whole year guidance. The whole year guidance is still a very good guidance, but relatively speaking, the first quarter guidance is a bit soft.

So my question is, when you get into [play] down the year when you have the Shanghai Expo getting into the picture, the comp's supposed to be a bit tougher, but it seems like the growth will accelerate from Q2 to Q4. So is that mostly because of the new hotel contribution, or do you see the room rate or RevPAR will be able to pick up from this point? And if that's the case, what's your guidance in terms of the RevPAR for the year, what do you see for the trend?

That's my first question.

And second question is just, basically, can you tell us a bit on, or comment on the Motel 168 acquisition? We heard some of your competitors are looking at that, so I just wonder whether the development of that incident will impact your growth strategy this year or next year; or if your competitors get it or not, whether you will adjust your growth target or not.

And then my final question is just, can you just tell me maybe --? This is similar to the first question. You mentioned there's a pretty strong pick-up of the room rate or RevPAR after the Chinese New Years. Can you tell us a bit about more on do you see more momentum, or any room for you to raise room rate in the next three to six months?

Thanks.

Matthew Zhang - *China Lodging Group Ltd - CEO*

First of all the RevPAR for the whole year of year 2011 for the mature hotel, we still very strongly believe they will increase; they will increase about from 2% to 4% for the mature hotel. Given that we'll have a significant number of new hotels opening to the line that will have -- they will going through a ramp-up stage, and picking up their performance. So the blended I would say I will see slightly decrease from the year-over-year of last year.

On the second question for the Motel 168, that -- first of all, I think that we are organically very strong planned for growth. The growth from the revenue and the unit addition, will more than 30% to 40% in the next years. So organically, I think that we do not need a major acquisition to be part of that, because we have already planned organic growth which is very fast already.

But on the other hand, we are looking into all the opportunities of potential M&A targets, but as you know that we are very disciplined in terms of evaluation and decision-making by the criteria of a better shareholder value creation.

So that's for the Motel 168. Although we cannot discuss any more details, but I'm very sure, very certain, that we're very disciplined in judgment of this target.

Jenny Zhang - *China Lodging Group Ltd - CFO*

Just to build on what Matthew has addressed, to further answer the question of revenue growth, we need to be aware that the main driver of our revenue growth is the opening and ramp-up of the lease-and-operated hotels. As you can see, excluding the Expo impact in 2010, the growth was -- revenue growth was 29%, and that was relating to our opening in 2009 of lease-and-operated hotels which was only 30; and the last year, we opened 70. So as our -- those new hotels go through their ramp-up stage, we will significantly boost our revenue line in 2011. So, yes, we do expect revenue growth from the second to fourth quarter to be significantly stronger than the first quarter.

And also to further emphasize, the organic growth is the core path of our expansion. No matter what happens with M&A opportunity, our plan for this organic growth will not be impacted.

Billy Ng - *BofA Merrill Lynch - Analyst*

Thanks so much.

Matthew Zhang - *China Lodging Group Ltd - CEO*

For the price increase, Billy, we already -- we are the first one to start the price increase, even start from the beginning of the last year, because at beginning of the previous year that our occupancy was so high.

We see the potential inflation, labor increase, that I think is the better balance between the price and the occupancy is one method to offset some of the impact of the inflation. So we already started that, and we will continue to do that throughout this year.

Billy Ng - *BofA Merrill Lynch - Analyst*

Thanks.

Operator

Justin Kwok, Goldman Sachs.

Justin Kwok - *Goldman Sachs & Co. - Analyst*

I would like to get more color on your product [implementation] side, and with the new openings targeted, or the opening targets you have laid out to the investors. And how should we look at the -- in terms of segment, how much of them will be on the midstream Express side, on the high-end, on the low-end side? How do you see the room rate trend in terms of the RevPAR growth for this year in terms of these different segments?

Thanks.

Matthew Zhang - *China Lodging Group Ltd - CEO*

You mean from the Tiers or different brands?

Justin Kwok - *Goldman Sachs & Co. - Analyst*

From the three different products that you have.

Matthew Zhang - *China Lodging Group Ltd - CEO*

Three different products. Okay. We will open -- about from 15% to 20% of our new openings will be these new two products other than HanTing Express. And these two products will focus mainly on the first Tier and the second Tier cities. We do not plan to go to a third Tier city yet.

And the price for the Seasons Hotel, performance is very strong; was a very good return; an even better return sometimes than the Express Hotels. We started the Hi Inn just a couple of years ago, which we're still fine-tuning this product by adding new sites to understand better from the customers' feedback, but from a performance perspective is in a reasonable acceptable level at this point.

Justin Kwok - *Goldman Sachs & Co. - Analyst*

I see, thanks. Just, as you said, a 2% to 4% RevPAR growth for the mature hotels for 2011. How shall we look at this number for Seasons and for Hi Inn? Are you looking at the same range? Or do you think that, as you said, Seasons are performing well, so do you see even faster growth for Seasons in terms of pricing and price hike, etc?

Thanks.

Matthew Zhang - *China Lodging Group Ltd - CEO*

I think it will be in a ball-park number the same level of growth for those two products than HanTing Express.

Justin Kwok - *Goldman Sachs & Co. - Analyst*

Okay, thank you.

Operator

Fawne Jiang, Brean Murray Carret

Fawne Jiang - *Brean Murray Carret - Analyst*

Two questions here. Number one is regarding your store-opening schedule, and I think that your competitors have been pretty aggressive in opening franchised hotels. And given your pretty strong pipeline at the end of 2010, I just wonder whether Matthew is being conservative of planning opening 100 leased-and-operated hotels -- of franchised hotels, sorry; or is there any consideration you want more disciplined growth for that segment?

Matthew Zhang - *China Lodging Group Ltd - CEO*

I think that the growth speed and the quality are always a balanced approach. We are -- I said we are consistently from the past instance of our execution, of our discipline, that we are more quality sensitive. So we, according to our past knowledge that the 200 number is balanced and comfortable for our growth in terms of quality and in terms of [fit].

Fawne Jiang - *Brean Murray Carret - Analyst*

Got it. Second question is actually regarding your expenses. Jenny, I just wonder, do you see any operating leverage on your SG&A for the coming year?

Jenny Zhang - *China Lodging Group Ltd - CFO*

As we step into a fast growth [space] for at least an (inaudible), we do need to invest a little bit more on our development and construction team. So we expect SG&A to develop stable in 2011 compared to the normalized, excluding Expo 2010 levels.

In terms of other operating expenses, we expect the structure overall to be relatively stable, but with the fixed cost portion to have a decreased trend, but other items like labor and consumables and utilities maybe have some increase due to the inflation. But overall, the margin on normalized business compared with 2010 will be more or less stable.

Fawne Jiang - *Brean Murray Carret - Analyst*

Got you. Just one quick follow-up on the labor costs. What's the estimated labor cost, potential increase for labor costs?

Jenny Zhang - *China Lodging Group Ltd - CFO*

We are estimating 6% to 10% right now. We do need to see how the Government play out the minimum salary increase.

Fawne Jiang - *Brean Murray Carret - Analyst*

Thanks, that's all my questions.

Jenny Zhang - *China Lodging Group Ltd - CFO*

You're welcome. Thank you.

Operator

Lin He, Morgan Stanley.

Lin He - *Morgan Stanley - Analyst*

My first question is actually a follow-up on your franchise business strategy. Matthew just mentioned that you want to keep a balance between speed, extension speed and the quality. Can you elaborate a little bit more? What kind of risk have you seen from being super-aggressive in the franchise business?

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Matthew Zhang - *China Lodging Group Ltd - CEO*

I think that different people have a different view, but from my perspective, I think that some of the locations the -- our very quick number of room increase in a certain market will hit the performance of the hotels dramatically. So, given that, if we will put more emphasis on leased-and-operated hotels, then we normally do not allow the franchise [hotel] to enter the same market, or the same area.

So that if we are put leased-and-operated hotels and franchised-and-managed hotels in a nearby situation, they are very close to each other, then maybe the demand cannot grow as quick as the supply grows. So that's our major consideration. That will hit our performance for leased-and-operated hotels, but, at the same time, that will hit the franchised hotel as well because their performance will under expectation. We took a rather longer term consideration for that.

Lin He - *Morgan Stanley - Analyst*

Okay, I've got it. Thanks. And the second question is regarding the geographic mix of new openings this year. Do you think that this year, the proportion of Tier 3 cities or Tier 2 cities is going to go up?

Matthew Zhang - *China Lodging Group Ltd - CEO*

There will be in year 2010 that we have about Tier 1, Tier 2, Tier 3, about a 50/25/25 mix; something like that. It will go in more towards 40/30/30 mixture; and that will consist about a couple of years. And, later on, it will be more heavy towards Tier 2 and Tier 3 cities.

Lin He - *Morgan Stanley - Analyst*

Okay, I've got you. So you think this would also have an impact on the [blended] RevPAR?

Matthew Zhang - *China Lodging Group Ltd - CEO*

I think that the major driver for the blended RevPAR is the ramp-up, because that given the -- our definition of the Tier city is based on the RevPAR. It's not based on the administrative definition. So we see the moving up for the Tier 3 cities to upgrade to Tier 2 cities after a couple of years' operation in that city. It's a dynamic process.

But the major impact of the RevPAR is the ramp-up of new cities, and other new hotels, and the percentage of new hotels within the total pipeline.

Jenny Zhang - *China Lodging Group Ltd - CFO*

On a weighted-average basis, Lin, because we are spreading towards more to second than a third Tier cities, it will have some impact on the blended RevPAR. But, at the same time, the rental will also move down, because we apply similar IRR standards to each investment decision. So you're going to see the rental decrease will, more or less offset that impact on the RevPAR side.

Lin He - *Morgan Stanley - Analyst*

Okay, thanks. That's very helpful. That's all my questions.

Jenny Zhang - *China Lodging Group Ltd - CFO*

Thank you, Lin.

Operator

Kenneth Fong, JPMorgan.

Kenneth Fong - *JPMorgan - Analyst*

My first question is on the expansion plan to Tier 2 and Tier 3 cities. How should we think about the investment return as far as EBITDA margin going forward, like the next one to two years? So, in short, how should we think of the EBITDA margins for individual hotels for Tier 2 cities, Tier 3 cities, as compared with Tier 1 cities?

That's my first question.

Jenny Zhang - *China Lodging Group Ltd - CFO*

In terms of a per-hotel basis, if we look at the ramp-up, the mature hotels in Tier 3, Tier 2, cities actually have, on average, a similar, or even slightly higher EBITDA margin compared with their Tier 1 cities, because we apply the IR approach in the investment decision with the lower revenue line as the denominator. It may drive it slightly higher, EBTIDA percentage, for the lower Tier city.

On a blended basis this year, as we mentioned earlier, is a year of investment, so we expect EBITDA margin will be lower than 2010. But, nevertheless, we believe it will still be higher than that of 2009. It will overall be an upward trend.

Kenneth Fong - *JPMorgan - Analyst*

Thanks. My second question is on the opening of new hotel rental expenses. With all your competitors speeding up their new hotel openings, do you see that the rents for new locations actually coming up dramatically for a similar location for now as compared with one year ago? What kind of percentage have you seen rentals increase?

Matthew Zhang - *China Lodging Group Ltd - CEO*

I think that today from HanTing's perspective, we have different site-selection criteria than the other two. So, given our mixed-blended situation, I do not see a rental increase, because we are moving towards more portion of our new-opening towards the Tier 2 and Tier 3 cities.

Kenneth Fong - *JPMorgan - Analyst*

Which means that within Tier 2 and Tier 3 cities, there's still plenty of room to grow, and you haven't run into a situation that you and the other two competitors compete for the same location?

Matthew Zhang - *China Lodging Group Ltd - CEO*

The competition exists for a long time. That doesn't change a lot during these recent years and the coming years. But, on the other hand, our -- just like I said, we prefer some of -- as you can see that our rental percentage as a percentage of revenue is higher than our competitors, because we are always take the best location of the Tier 2 or Tier 3 cities. And then they may not want these locations because they have different business models or financial models. So that does not impact us a lot.

Kenneth Fong - *JPMorgan - Analyst*

So for a similar location in Tier 2, Tier 3 city, compared to a year ago, what is the percentage of rent have you seen increasing?

Matthew Zhang - *China Lodging Group Ltd - CEO*

That varies dramatically from no increase to 20% maybe. That differs city by city, and location by location as well. But also, as you can see that for the high increase of rental are majorly the areas in the Tier 2 and Tier 3 cities, with the new commercial center area; which is not in the old, or previous old center of the city.

So these new cities, new [CBDs], has very high growth in terms of the rental. But on the other hand, if you go to the previous center of the city, that increase is still reasonable.

Jenny Zhang - *China Lodging Group Ltd - CFO*

From the financial perspective, because China is going through such a quick urbanization process, so the attractiveness of one location could be very different to the way you looked at it three years ago, versus how you look at it today. So from the financial perspective the rental and the RevPAR expectation actually move more or less, in parallel; because we are not really competing with people [who set up] the hotel industry for those properties. Our main competitors are actually hoteliers.

So given that, the affordability of the rental is in a similar ball-park. And with our brand strength, we definitely have the edge. And we also, because we are a very reputable hotel Group in the market, so we are also attractive to most of the landlords as we are considered credible and reliable.

Matthew Zhang - *China Lodging Group Ltd - CEO*

Adding on that, net-net, our site-selection criteria has not been changed. That will purely base on the IRR which could have generated from a potential site. So that's our criteria. That always been there, no matter what the rental may be, and no matter what the RevPAR will be, and no matter what the location will be. So the financial model we have built up is very solid, and has been executed for several years already.

Kenneth Fong - *JPMorgan - Analyst*

Thank you. That's very helpful.

Operator

Praveen Choudhary, Morgan Stanley.

Praveen Choudhary - *Morgan Stanley - Analyst*

A couple of questions from me. The first one is simple. The margin that you mentioned for 2011, EBITDA margin versus 2009, it will be higher. I think that's very well understood. I was thinking in terms of, if I remove the Expo factor in 2010 from both revenue, as well as from EBITDA, then your margin will be 21% versus a reported 25%. Would it be fair to say that in 2011 your margin will be between 21% and 25%, higher than what it would have been without Expo factor?

Jenny Zhang - *China Lodging Group Ltd - CFO*

We cannot be very specific in the margin guidance, Praveen, but you have to factor in, as I mentioned earlier, the new 2011 we are going to have an increase in the pre-opening expenses because of more leased-and-operated hotels opening. And also, we will have a significant higher proportion of hotel rooms will be in the ramp-up stage. So those have the potential to adjust the margin to actually be lower than 2010, even on a normalized basis.

On the other hand, we will work hard to improve the per-hotel revenue for the mature hotels. So the outcome will be how significant those different forces play out eventually.

Praveen Choudhary - *Morgan Stanley - Analyst*

Very helpful. The second question is about when you go to new cities, do you go with first hotel to be leased-and-operated, or the first hotel to be franchised-and-managed? Or do you think like that?

Matthew Zhang - *China Lodging Group Ltd - CEO*

Well, that's case-by-case approaches. But we normally will go to a new hotel if we have less understanding, or there will be less referred Express hotels from other peer groups, then we are not certain the outcome of the new hotel, we probably prefer the franchised-and-managed hotels.

For a new city, if we are certain with the reference of other players we can more confident of the hotel operation results which is also that is favorable to meet our return criteria, then we'll go for the leased model. That varies case by case.

Praveen Choudhary - *Morgan Stanley - Analyst*

And my last question is we are seeing that Home Inns' growth rate has slowed down from a year-over-year perspective. Obviously, 7 Days and HanTing quotas are still very high year-over-year basis. Has it anything to do with the size, and should we expect in two years' time when you become as big as Home Inn you will have difficulty to grow at this rate? And I'm talking about revenue here, and when it normalizes.

Or you think it's very specific to specific company, without naming any name?

And the related question is something that has previously been asked. What are the reasons some of the other competitors are adding a lot more franchise models? Because they think that finding a hotel which is already there but running at a 50% utilization, and putting their own name, is easier than finding a land or a building which you can renovate from inside, at a cheaper rate of, let's say, $1 million? At some point in time this has to run out. I don't understand how many China buildings are available out there which can easily be converted into hotels.

Those two questions from me.

Jenny Zhang - *China Lodging Group Ltd - CFO*

If you look at the overall market, I think the branded hotel chains account for a very small portion of the overall hotel supply in China. So the growth space, I think, is still huge there. The question is more first do the current hotel groups have developed attractive products to tap into the different segments of the market; and secondly, the execution of different stage. Does everyone capture growth opportunity at the right timing?

And given the hotel investment takes a relatively long lead time from identifying a project to a hotel, open and ramp-up, it's typically more than one year.

So I believe that some of our competitors when they experience financial crisis, naturally people react by slowing down investment. And that will impact the growth rate one or two years later. However, that may not be a long-term issue given the growth potential is still there.

To be more specific about HanTing I think, first of all, we have been taking a relatively disciplined approach in making our investment decision. So we have always been looking at how to generate more shareholders' return. So our choice has been more to grow the revenue and the profit on a more steady and highest bid, instead of purely just growing the number of hotels or rooms.

So our expectation for ourselves for the next few years is we will continue to have high growth rate, as you can see. And we don't expect that to slow down very significantly even after two or three years. And one particular stress we have there is we have early on developed a [macro] brand strategy. That will enable us to tap into a wider range of customers. So we are very positive about our own growth prospect.

Praveen Choudhary - *Morgan Stanley - Analyst*

Right, one of the small clarifications that I had here, and maybe I don't understand here, when you mentioned that branded-budget hotel is a small portion of the overall lodging space in China, which I totally agree with you, the other kind of lodging space can be converted as franchised-and-managed, not necessarily leased-and-operated, because they're already a lodging space, isn't it?

Jenny Zhang - *China Lodging Group Ltd - CFO*

Not necessarily. Actually, out of the leased-and-operated hotels we have signed, we have seen a significant more portion of them actually used to be lodging facilities. Our most recent capture of [the market] that is 40% to 50% of the new hotels we signed up as leased-and-operated hotels actually used to be lodging facilities.

Praveen Choudhary - *Morgan Stanley - Analyst*

Okay, that's very helpful and that explains a lot of things. Thank you very much, Jenny. Thanks, Matthew.

Operator

We currently have no more questions in our queue at this time.

Jenny Zhang - *China Lodging Group Ltd - CFO*

Okay. Thank you, everyone. Thank you for spending time with our conference call. We enjoyed taking your questions, and we look forward to talking to you in the next quarter earning's call. For more information, please visit our IR website and you may register and get email alert.

Thanks. Goodbye.

Operator

Ladies and gentlemen, that concludes your conference call. You may now disconnect your lines. We thank you for joining and hope that you have a very good day. [y1]445, please correct it as consistent with CFO discussion part.