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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to the China Lodging Group Q1 2012 earnings conference call. (Operator Instructions). There will be a presentation followed by a question and answer session. (Operator Instructions). I must advise you that this conference is being recorded today, Thursday 10 May 2012.

I'd now like to hand the conference over to your first speaker today, Miss Ida Yu. Thank you. Please go ahead.

Ida Yu - *China Lodging Group Limited - IR*

Thank you, Laura. Hello, everyone. Welcome to our first quarter 2012 earnings conference call. Beforehand can you please note that the discussions today will include forward looking statements made under the safe harbor provision 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 findings with the FEC. China Lodgings 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. Reconciliation 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, as well as the mandatory presentation slides, are available on the investor section of China Lodging Group's website at ir.htinns.com.

Joining us today is Mr Qi Ji, our founder, executive chairman, and chief executive officer, and Jenny Zhang, our chief financial officer, who will discuss our Company's performance for the first quarter 2012. Following their prepared remarks, CEO and CFO will be available to answer your questions. Now, I would like to turn the call over to Jenny. Jenny, please.

Jenny Zhang - *China Lodging Group Limited - CFO*

Good morning, everyone. Thank you for joining our earnings call today. Today, I am pleased to announce the results for the first quarter of 2012. As shown on our presentation, page 3, net revenues for the quarter RMB649 million, an increase of 53% year-over-year exceeding the high-end of our previously guided range of RMB605 million to RMB620 million, thanks to our GAAP expansion and RevPAR improvement.

As shown on page 4, in the first quarter of 2012, we opened 36 net new hotels, with nine net new leased hotels and 27 net new managed hotels. It brought the total hotel count to 675. As of 31 March 2012, we successfully expanded our footprint into 111 cities across China. In addition, at the end of the first quarter 2012, we had 336 hotels in the pipeline - more than doubled from a year ago. The pipeline contains 107 leased hotels and 229 managed hotels, both growing from last quarter.

In response to the strong demand from franchisees and based on our managed hotel pipeline, we increased our new opening target for managed hotels to 140-150, with our leased hotels opening target of 120 unchanged. Our total new opening target is increased to 260-270. As shown on page 5, with the acceleration of managed business, our (inaudible) will shift towards a close to even split between leased and managed hotels.

In the long run, we see ourselves in the business as hotel operators, hotel managers and the brand owners, with management business constituting an increasing portion of our revenue. Han Ting Express, with its wide market recognition and established network will be the main brand we franchise and manage in the near term. Seasons Hotel and Hi Inn in a much earlier stage of their life cycle will have a limited number of managed hotels this year. We intend to accelerate their expansion with more managed hotels as each of them reaches a more mature stage.

With that, I would also like to go through the selection of the data that are most meaningful when reviewing our business results. First of all, let's turn to page 7 and take a look at our RevPAR. In the first quarter of 2012, our RevPAR is came in at RMB156 representing a 9% increase from the same quarter 2011. The year-over-year RevPAR improvement was achieved in parallel to the vast hotel count growth of 43% and the city coverage expansion from 71 to 111.

The year-over-year RevPAR improvement was mainly driven by strong performance in occupancy, as shown on page 8. In the first quarter, occupancy reached 91%, up from 82% the same period last year, attributable to robust travel demand, our successful seasonal promotions, a more mature hotel mix and the rebound of the Shanghai market from post-Expo weakness experienced in the first quarter of 2011.

The ADR for all hotels was RMB172 in the first quarter of 2012, compared with RMB175 in the first quarter of 2011. The year-over-year decrease was mainly attributable to the city mix shift towards lower tier cities and our seasonal promotions, partially offset by the same-hotel ADR appreciation.

Page 9 provides a more detailed view of our same-hotel RevPAR change. In the first quarter of 2012, our same-hotel RevPAR appreciated by 10% across China and 8% for the hotels outside of Shanghai. The appreciation outside of Shanghai was attributable to a 3% growth in ADR and a 5% growth in occupancy. The appreciation of same-hotel RevPAR indicated a robust market demand and was also attributable to our successful branding efforts. In Shanghai, the same-hotel RevPAR appreciation was also attributable to a lower comparison base as a result of post-Expo market weakness in the first quarter of 2011.

On page 10, our EBIT margin improved by 3.4% points year-over-year in the first quarter. The adjusted hotel operating costs improved a half point, mainly a result of higher RevPAR in the first quarter of 2012, compared with that for 2011. The pre-opening expenses as a percentage of net revenue decreased by 1.7 points and adjusted SG&A expenses by 1.2 points, mainly due to expansion of our revenue base.

On page 11, our net cash balance closed RMB630 million at the end of the first quarter. Additionally, this March, we entered into a credit facility with the Industrial and Commercial Bank of China, under which we can draw down up to RMB500 million by 21 May 2015. For the first quarter, the operating cash flow were RMB101 million, which is 159% higher than the same period last year. We continued to deploy our cash into our network expansion, with the total cash flow of RMB255 million this quarter. We believe that our cash balance, our operating cash flow and our available credit facility will be sufficient to fund our expansion plans in the near future.

With that, we will now open the call to questions. Operator.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Your first question comes from the line of Chenyi Lu from Cowen and Company. Please ask your question.

Chenyi Lu - *Cowen and Company - Analyst*

Morning. Thank you. This quarter the RevPAR actually increased year-over-year and then during the - in your press release, basically, you said that it was because of higher promotion that leads to higher occupancy rates. Based on that, can you give us a view as to what the RevPAR, including the occupancy rate, and also ADR going forward in 2012? Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

We continue to see robust demand from the market as we move into the second quarter. So, we continue to expect a positive occupancy performance in the coming quarter. We also observe a healthy same-hotel ADR appreciation.

Chenyi Lu - *Cowen and Company - Analyst*

So, basically are you continually going to do the promotion in the second and third quarter?

Jenny Zhang - *China Lodging Group Limited - CFO*

Our promotion, in the first quarter, is targeted towards the low season. So, as we move into March, most of the promotion already comes to a [peak].

Chenyi Lu - *Cowen and Company - Analyst*

Great. Thank you. That's all my questions.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you.

Operator

Your next question comes from the line of Ella Ji from Oppenheimer. Please ask your question.

Ella Ji - *Oppenheimer - Analyst*

Thank you. Good morning Jenny and (inaudible). So, first of all, I'm wondering if you can give us a little bit more color in terms of the market that you are seeing in the second quarter. In additional to the normal seasonal recovery are you seeing a more - a better recovery or is it just a very normal recovery on the market?

Jenny Zhang - *China Lodging Group Limited - CFO*

(Inaudible) the market demand seems to be robust. We see strong demand continue into April and May so far.

Ella Ji - *Oppenheimer - Analyst*

All right. You didn't really - you outperformed in first quarter but you maintained your full year guidance. Was this just because of conservatism or is there any other reason?

Jenny Zhang - *China Lodging Group Limited - CFO*

The first quarter revenue does come higher than our previous guidance. Since we - there's just two months apart from our last announce of guidelines. I think the uncertainty we are seeing in the second half will remain something you should wait and see.

Ella Ji - *Oppenheimer - Analyst*

Got it. Then, I have a question for Ji. (Spoken in foreign language).

Jenny Zhang - *China Lodging Group Limited - CFO*

Ella. Qi Ji is on the other line. I think the operator will need to take a minute to connect him.

Ella Ji - *Oppenheimer - Analyst*

So maybe, we can wait for - he can answer my question when he's returned to this line.

Jenny Zhang - *China Lodging Group Limited - CFO*

Sure. I'll keep a record of that. Let's just move to the next question for the moment and we'll come back to Ella's question once Qi Ji comes back on the line. Okay great.

Qi Ji - *China Lodging Group Limted - CEO*

(Spoken in foreign language).

Jenny Zhang - *China Lodging Group Limited - CFO*

(interpreted) Let me translate for Mr Ji. There is three main things that he did after he reviewed the role of CEO. First of all, he decided on accelerating the franchise business. As you can see from our quarter date, we have decided to increase the new opening target of our franchise hotels from the 140 to 150 this year. There will continue to accelerate our expansion through the franchise and managed model in the future.

Secondly, we have consolidated our new brands in the development projects and plans. We have set up a separate business unit to run the two smaller brands and I have more specific strategies and positioning to our two smaller brands. We have seen very positive performance in the past few months after those adjustments.

Thirdly, to prepare the organization for our future expansion, we also reviewed our headquarters and their regional structure to review our human resource pipeline to get the whole organization ready for the future vast expansion. Those are the main things he did.

Operator

Your next question comes from the line of Grace Lam from Citi Group. Please ask your question.

Grace Lam - *CitiGroup - Analyst*

Hi. Good morning. Thank you for taking my question. Actually, I have a question for Ji. (Spoken in other language).

Jenny Zhang - *China Lodging Group Limited - CFO*

(interpreted) Let me translate the question and the answer. The question was there is news saying that we are going to accelerate the franchise business and are we going to decrease our franchise fee? Mr Ji's answer is, first, the price decrease is not in any major magnitude. That's not our approach of competition in the franchise logic. The discount is mainly offered to the serial franchisees. When they join us with multiple hotels, we will offer them some discount. We also offer some franchisees in the remote cities some discounts to support them and also support ourselves to expand our network.

So the financial impact of that is very limited. The reality is that the demand from the franchisees is very strong in recent years. In the past, Han Ting has not done much marketing to the franchisees. We basically waited for the franchisees to come to us and picked and chose those that have a good fit to become our franchisees

Starting from this year, we have decided to be more proactive in marketing ourselves. Han Ting, as a franchiser and hotel manager, has a lot of unique advantages. We had the highest RevPAR and we also generated the highest (inaudible) in the hotel market. We should have made our name better known among the potential franchisees. So that's the main output that we are going to make to accelerate our franchise expansion in the future.

Operator

Your next question comes from the line of Adam Krejcik from ROTH Capital Partners. Please ask your question.

Adam Krejcik - *ROTH Capital Partners - Analyst*

Hi, everyone. I had a couple of questions. First, going back to the pricing, so the ADR this quarter - just curious, can you break down how much of the pricing has been expanding into lower tier cities and how much is versus the pricing promotions this quarter? Is there going to be any change to that going forward in Q2 and for the rest of the year?

Jenny Zhang - *China Lodging Group Limited - CFO*

When you look at our ADR, there are a few different factors playing there. First of all, at the same-hotel level, we are seeing an ADR appreciation. The overall same-hotel RevPAR appreciated 1% -- it's basically 3% out of Shanghai and a decrease of 2% in Shanghai and they're blended into approximately 1% across the Board. The promotion activity decreased the ADR by approximately close to 1%. We also have a few points of impact coming from the city mix shift because we opened an increased amount of new hotels in our - in the third tier cities.

So, if you blended the three practices together that came to our ADR decrease of 2% this quarter. Going forward, I believe the same-hotel ADR appreciation will continue and the city mix shift will also remain there. But the promotional factor, I don't expect that to repeat into the second quarter.

Adam Krejcik - *ROTH Capital Partners - Analyst*

Okay. Can you remind us what the approximate split of hotels in tier one cities versus tier two and tier three is right now?

Jenny Zhang - *China Lodging Group Limited - CFO*

Currently, tier one cities account for 46% of our hotels and operations and tier two accounts for 34% and tier three accounts for 20%.

Adam Krejcik - *ROTH Capital Partners - Analyst*

Got it. Okay. My next question is on CapEx. This quarter seemed a bit high considering, I think, the number of leasing operated hotels you opened. So was there any - are they items in the capital expenditure line or can you elaborate on why that was a bit higher than usual?

Jenny Zhang - *China Lodging Group Limited - CFO*

The capital expenditure comes not only from the hotels opened in that quarter but also from all the hotels that are under construction during that period. We also booked major maintaining activities. When we capitalize those, we also put them under the CapEx in the investment cash flow. So they all contribute to our investment cash outflow.

Adam Krejcik - *ROTH Capital Partners - Analyst*

Was it a larger amount of maintenance CapEx than usual relative to new openings and planned openings?

Jenny Zhang - *China Lodging Group Limited - CFO*

No. The maintenance CapEx this year, I think, is in line with the prior year. The main cash expense in this quarter are for those hotels under conversion. As you can see, we have a big pipeline. So it goes into the CIT.

Adam Krejcik - *ROTH Capital Partners - Analyst*

Okay. Got it. My final question is on the loan or the credit facility you got. So, is that primarily for new expansion or is it specific to potentially looking at M&A deals or some smaller change? Can you just elaborate on what you might use that credit facility for.

Jenny Zhang - *China Lodging Group Limited - CFO*

While we forecast our cash flow with our current leased hotel expansion plans, our cash balance is going to decrease to RMB200 million to RMB300 million at the end of this year. So at some point we are going to need loan facility to continue to support our leased hotel expansion. We have been very well prepared for that, so we started to work with the banks early on and we successfully secured a three to five year loan to support the next years. So that's the intention of this loan facility. Currently we don't have any significant big acquisitions going on at the moment.

Adam Krejcik - *ROTH Capital Partners - Analyst*

All right. Got it. Thanks and congratulations on a nice quarter.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you, Adam.

Operator

Your next question comes from the line of Fawne Jiang from Brean Murray. Please ask your question.

Fawne Jiang - *Brean Murray - Analyst*

Good morning. Thank you for taking my question. First one's actually regarding your pipeline. You seem to have built a very nice pipeline in the last quarter. Just wondering, what's the percentage under your pipeline of hotels that are currently in conversion? Also, just wondering whether that ratio has changed in the past few quarters?

Jenny Zhang - *China Lodging Group Limited - CFO*

The ratio has been fairly stable. Currently, 74% of the leased hotels in the pipeline are under conversion and 65% of the franchised in the pipeline are under conversion, which is pretty much the same as a quarter ago.

Fawne Jiang - *Brean Murray - Analyst*

Got it. Thanks Jenny. Next question is actually regarding - just wondering whether you could give us updates regarding the conversion periods -- is there any change from the past quarter? Also, what could be - given the current period, what's the implied pre-opening cost for 2012?

Jenny Zhang - *China Lodging Group Limited - CFO*

Currently, we remain at approximately seven months conversion period. We start - we are expecting our pre-opening expenses per hotel to be roughly in line with what we experienced last year.

Fawne Jiang - *Brean Murray - Analyst*

Got it. Last question is actually regarding your margin. Last year, from the second quarter, you actually had a very nice pick up from the first quarter sequential in terms of margin trend. Just wonder, given what you're saying right now for 2012, are we expecting a single level of margin improvement for the second quarter?

Also, it seems like for your hotel operating expenses, labor costs and the consumables are the ones we see slightly increased as a percentage of revenue versus the other lines, where we see a pretty nice declining trend. Just wondered whether you could comment on that and how we should look at the margin for the second quarter?

Jenny Zhang - *China Lodging Group Limited - CFO*

Sure, our business is a highly seasonal business, especially with our meaningful exposure in the northern part of China. When we go through the winter we experience a significant decrease in revenue and a higher utility cost. So that tweaks are Q1 P&L with a lower revenue level but a higher utility cost. So the second quarter, as a high season, also with a lower utility cost, typically will have a significantly higher margin compared with the first quarter. We expect that pattern to repeat this year.

Also, in terms of the personnel costs and the consumables, those two lines basically represent the most inflation sensitive cost items in our cost structure. We are seeing approximately a 10% same-hotel salary increase. On top of that, because of the high revenue achievement, we also pay out more bonuses to our staff. So that's the main driver of the personnel cost increase exceeding our revenue increase.

On the consumables and food and beverage items, it's widely known that food items largely cost - have been also fairly inflation sensitive. So we did experience price increases in those areas. But when you blended all of our custom together, we are also going to see we are enjoying the benefits of economies of scale. So, we are seeing significantly decreased C&A ratio and also a decrease in the pre-opening ratio. That has contributed to a meaningful improvement in our operating margins. We also expect this trend to continue through this year.

Fawne Jiang - *Brean Murray - Analyst*

Thank you. That's very helpful. Thanks Jenny.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you. Fawne.

Operator

Your next question comes from the line of Billy Ng from Bank of America. Please ask your question.

Billy Ng - *Bank of America - Analyst*

Hi. Good morning and thanks for taking my question. Basically, just want to ask Jenny when you say you see Q2 that the demand is pretty robust, can you elaborate a bit on whether you see your pricing power is getting stronger or you can raise room rate or you see occupancy rates continue to improve. And also in terms of the overall industry, the (inaudible) dynamic, what are you seeing right now and compared to last year, if we recall correctly, last year we see Q2, basically I think the major change, raising room rate more meaningfully last year in Q2. So are we seeing something happening in this Q2 as well?

Jenny Zhang - *China Lodging Group Limited - CFO*

Sure. While we manage our old pricing we basically try to balance the ADR in the occupancy to maximize our RevPAR. As you can see, our presentation, page nine, our non Shanghai same hotel ADR appreciated 3% in the third quarter, which is in line with the two earlier quarter's trend.

So I would say we are continuing the ADR appreciation pattern and at the same time we are seeing an increase in the occupancy fairly (inaudible). I think that indicates the market demand is robust and our brand is very well received by the consumers.

Going forward, we expect a similar trend. In Shanghai in Q1 our same hotel RevPAR appreciation was as high as 18%. A big part of that is due to a lower comparison base, but we also need to record it to our management team who has achieved above 100% occupancy in our (inaudible) Shanghai hotels.

We have taken a more conservative pricing tactic in Shanghai but a (inaudible) treatment I think is still quite strong.

So that's our current practice and we continue to see our branding to be successful in driving up ADR as well as the occupancy.

Billy Ng - *Bank of America - Analyst*

Thanks. Can I have a follow up question? Basically, do you see a difference in terms of demand in tier one or tier two and tier three cities? Are you seeing stronger demand or stronger pricing power or room to raise room rate in tier one cities or in other tier cities?

Jenny Zhang - *China Lodging Group Limited - CFO*

It's a little bit difficulty to generalize by tier. It's more a city by city denomination.

Billy Ng - *Bank of America - Analyst*

Okay, one last question. Basically, when we see, so pretty much how about in terms of the business travel versus leisure, we know the overall macro data1Q China has a relatively soft GDP growth and that kind of pre-date data will improve in the second half so since it's not had too much impact on your own performance. So if we see the GDP improve and pick up, do you think the leisure business or the business travel business is going to pick up more? What's your feel on that right now?

Jenny Zhang - *China Lodging Group Limited - CFO*

Currently, our customer base is very balanced between business travel and the leisure travel. So (inaudible) less sensitive to the small change or fluctuation of the GDP ratio. If the GDP grows, does increase, I think of course that would be a positive sign for all statures including us. But even if the GDP has some minor decrease, I think our performance is still quite resilient.

Billy Ng - *Bank of America - Analyst*

Thanks.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you, Billy.

Operator

Your next question comes from the line of Justin Kwok from Goldman Sachs. Please ask your question.

Justin Kwok - *Goldman Sachs - Analyst*

Good morning. Thanks for taking my question. I put your more focus on the different brands that you're operating (inaudible) or number for the overall portfolio. Do you mind walking us through a little bit on what are you seeing in terms of the performance of the three different brands? Are you seeing divergence in these or, say, the higher end brand moving faster or the other way round, or how are you assessing the growth of different market segments for this year or next year with the current operations that you're seeing? Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

Sure. Our three products are at different stage of their lifecycle. Han Ting Express is a relatively mature product and also is to accelerate its expansion. So that should be the main brand that we will introduce to our franchisees and we expect more franchise hotels coming from this brand.

The Seasons, we have validated the business model and we are in the initial stage of building up an established network. So we are going to see the hotel count double for Seasons this year and we will further accelerate it in the next few years. And we believe the demand in the midscale limited service segment is going to grow very fast.

The Hi Inn Hotel is in an earlier stage. We are still fine tuning this business model and the brand positioning, so currently it's a new hotel added to Hi Inn relative to Seasons is smaller.

However, we see both lead brands actually have very big potential market not only come from the consumers demand which has been growing, and also we are seeing a huge consolidation [opportunities] for each of the segments. So we are very confident that we are going to enjoy significant growth of all of them.

On top of that, after our organizational adjustment to set up separate use for the two smaller brands, we are seeing significant performance improvement on the same hotel basis for both Seasons Hotel and Hi Inn, which is very encouraging.

Justin Kwok - *Goldman Sachs - Analyst*

Thank you. I have another question which is on the margins which you have discussed. In the first quarter, we've seen improvement in terms of the (inaudible) expansion of (inaudible) and net revenue, but on the other hand we're also seeing a half a percentage point increase for direct operating costs versus the revenue side, even though the salary and also the food and beverage costs have been increasing.

I just want to get a sense that, are you expecting this operating cost improvement trend to continue for the full year or is it only seasonal for the first quarter? Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

For the full year, overall speaking, we think there is a possibility our hotel operating cost as a percentage of net revenue we will have some decrease which is already shown in the first quarter.

For the next few quarters, for each quarter you will be subject to how much RevPAR appreciation that we can achieve in that specific quarter. But I am relatively positive for the full year.

Justin Kwok - *Goldman Sachs - Analyst*

Thank you. That's my question.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you, Justin.

Operator

Your next question comes from the line of Lin He from Morgan Stanley. Please ask your question.

Lin He - *Morgan Stanley - Analyst*

Hi, good morning Jenny and Ida. First of all, congratulations on the good quarter. A couple of questions. First of all, the RevPAR role. You achieved a pretty strong same store RevPAR growth for hotels outside Shanghai. Can you remind us, is there also a similar low base (inaudible) playing there or, in other words, do you think that 8% same store growth outside Shanghai is sustainable?

Jenny Zhang - *China Lodging Group Limited - CFO*

That's a very good question, Lin. Thank you for asking that. Internally, we would look at a same hotel RevPAR trend with a longer time horizon. So if you go to our presentation, page nine, you look at the line you will see that Q1 2011 was a dip. We reported a -2% on the same hotel RevPAR decease and -1% for hotels outside of Shanghai.

I think you know of course the Q1 2012 performance is in practice and also very encouraging, but if you put it into a longer time horizon, add the two Q1 together and average it, it's still in line with our long term expectation of approximately 4% kind of long term RevPAR appreciation.

Lin He - *Morgan Stanley - Analyst*

Okay, got you. Now I have two questions for Qi Ji. Is he still on the line?

Unidentified Male

Yes.

Lin He - *Morgan Stanley - Analyst*

Qi Ji, (spoken in foreign language).

Jenny Zhang - *China Lodging Group Limited - CFO*

(interpreted) Let me translate. The question is regarding some negative publicity recently relating to the hygiene standard of the economy hotel chains, and there we were also asked why Han Ting has decided to accelerate the franchise hotel business, on three concerns about the quality control.

So Mr Ji answers that first of all Han Ting has been a latecomer to the franchise business and it has always been the more conservative one since developing this model. We took time to watch how the development, how the market developed, how the franchisee behaved and already our own human resources and the control capability have been established.

Now we feel more comfortable that we see opportunity in the demands, we see franchisees become more mature than a few years ago and our standards have not changed because of the decision to accelerate a franchise hotel. If there are any hotels that cannot meet our quality standards, we will have no hesitation to decline the request to become a franchisee.

Even with our decision to accelerate the franchise in the management business, we do not aim to become the fastest rollout of the franchise program. The current change is more a fine tuning to our tough attitude which now seems to be over conservative.

In terms of the hygiene issue, the negative publicity has been somewhat exaggerated, the situation which exists. What the journalists have reported in (inaudible) in the seven days, we don't believe that's a common situation across the whole chain. But of course, this is a good lesson for everyone in this business that we need to put in more effort to educate our cleaning ladies.

We haven't seen this has had any major impact on the industry as a whole.

Operator

Your next question comes from the line of Jamie Zhou from Macquarie. Please ask your question.

Jamie Zhou - *Macquarie - Analyst*

Hi, guys. Congratulations on a strong quarter. My questions actually are answered by a prior analyst, so congratulations.

Jenny Zhang - *China Lodging Group Limited - CFO*

Jamie, I cannot hear you. Can you repeat the question?

Jamie Zhou - *Macquarie - Analyst*

Hi, can you hear me?

Jenny Zhang - *China Lodging Group Limited - CFO*

Yes, it's better now.

Jamie Zhou - *Macquarie - Analyst*

Okay, I just want to say congratulations on a strong quarter. My questions were all answered earlier. Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you.

Operator

Your next question comes from the line of Tian Hou from T H Capital. Please ask your question.

Tian Hou - *T H Captial - Analyst*

Hi, Jenny. The question is related to your Q1 marketing. So I look at the number, the marketing expense as a percentage of revenue is quite low, so Jenny would you please give us some kind of color on that? Also, what's the trend going forward?

Jenny Zhang - *China Lodging Group Limited - CFO*

Our spending in the marketing expenses have a certain element associated with the revenue which could be very stable, but there is also a big portion relating to advertising and marketing programs which could be quite arbitrary when it happens. In the first quarter this year, we didn't spend much on advertising and certain marketing programs, so that has made our first quarter certainly in the marketing expenses relatively low.

We expect in the next few quarters that spending will be higher, so the award - the SNM as a percentage of revenue this year we do expect that to be lower than last year as a result of revenue base and economy of scale.

Tian Hou - *T H Captial - Analyst*

That's helpful. And the second question's related to tax rate. So if I look at the effective tax rate it's like 10%, in that range. So what's going to be going forward?

Jenny Zhang - *China Lodging Group Limited - CFO*

Currently we're expecting the full year effective tax rate to be in the range of high teens.

Tian Hou - *T H Captial - Analyst*

Okay, that's all my questions. Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you, Tian.

Operator

Your next question comes from the line of Vivian Hao from Deutsche Bank. Please ask your question.

Vivian Hao - *Deutshe Bank - Anaylst*

Hi, Jenny. Actually my question has already been covered. Thank you.

Operator

Your next question comes from the line of (inaudible) from [UOB] Asset Management. Please ask your question.

Unidentified Participant

Hi, good morning management. I have a couple of questions. The first one is, can you talk about the challenges the industry is facing right now, even in the medium term?

And my second question is, can you talk about where you plan to expand your number of stores going forward, number of hotels? Is it more in the first tier cities or can you elaborate on that?

The third question is how do you plan to increase your RevPAR by 4% in the long term?

And the last question is, when do you expect the free cash flow to deposit? Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

I didn't hear your first question very clearly, Jihuang. Do you mind repeating that?

Unidentified Participant

Yes, sure. Can the management share some views on the challenges the industry is facing right now and even in the medium term? Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

I see. Currently we see very strong demand from the consumer side and we also continue to see the opportunity of consolidation. So I think growth and expansion will remain as the same for the industry in the near future.

In terms of the challenges, I think to cope with such robust expansion, each organization is facing challenges in the human resource and organization capability side. So that's where our executive teams spend most of our time.

In terms of your question on how we are going to do to achieve the appreciation of our RevPAR, we see in the long run the main opportunity will come from the ADR appreciation. Our branding as a premium or high quality hotel product has a made us have a strong pricing power in the market. So we have been acting as the pricing leader in the past few years and we continue to discuss.

With that said, our appreciation from time to time, if you look at it in the near term from quarter to quarter, could be driven by a combination of changing ADR and changing occupancy and our management may also consider the market situation and our own comparative positioning (inaudible) the two metrics to maximize the RevPAR in the long run.

In terms of your question on the free cash flow, that will be subject to how much new leased and operated hotels we open and whether we conduct any acquisitions in our expansion. So I don't have a firm answer on that, but clearly our operating cash flow has been growing meaningfully year over year. For (inaudible) in the first quarter this year, our operating cash flow has grown by 159% and we remain confident the cash flow will grow strongly in the coming quarters and the years.

So where we may cross the line with the new cash flow is more dependent on the expansion speed. It may take another three or four years to get to the free cash flow level.

Unidentified Participant

Regarding my second question just now, can you talk about where will be the focus for our expansion going forward and how the RevPAR in those areas compare with what we are operating in right now? Thank you.

Jenny Zhang - *China Lodging Group Limited - CFO*

Sure. If you look at our pipeline, we are seeing fairly balanced distribution between the tier one, two and three cities. Going forward, we are going to have our franchise hotels to have a heavier focus on the tier three cities to leverage our franchisees' local knowledge and network. Our leased and operated hotels, we'll have more focus on the markets that we are more familiar with.

Operator

There are no further questions at this time. I'd now like to hand the conference back to today's presenters. Please continue.

Jenny Zhang - *China Lodging Group Limited - CFO*

Thank you everyone (inaudible_ today. We may, China Lodging Group will attend a few investor conferences including the (inaudible) Hong Kong Summit, Credit Suisse China Investment Conference in Hangzhou and the CLSA Corporate Access in Shanghai and the JP Morgan China Conference in Beijing. To get timely news and updates from us, please register at our investor relationships website, ir.htinns.com.

We look forward to talking to you in the next quarter earnings call. Good bye everyone.

Editor

Statement in English on this transcript were spoken by an interpreter present on the live call. The interpreter was provided by the Company sponsoring this Event.