



GRAND RESIDENCES

BY ROYAL RESORTS®

ADVISORY COUNCIL MEETING
OCTOBER 18, 2018





General Introduction

GRAND RESIDENCES ADVISORY COUNCIL MEETING, OCTOBER 18, 2018

Advisory Council Members: Douglas Bayerlein, Hugo Carlos Berlanga, Evelyn Hogue Dowell, Robert Boyd Stevens, Joseph Whitlock

The annual Grand Residences Advisory Council meeting was held at the resort on October 18, 2018. All Advisory Council members were present.

Prior to the meeting, Council toured the resort with Resort Manager Daniela Trava, visiting a villa to learn more about the work to keep them in optimum condition. The full overhaul of villas in the preventive maintenance program will be completed in 2018. Suppliers also check appliances such as the refrigerator, stove, dishwasher, washer and drier on a monthly basis. The air-conditioning system, Jacuzzis, pergolas and plunge pools are cleaned. Furniture is sanded, painted and varnished and mattresses are deep cleaned twice a year. She also explained that the sofas will be reupholstered in a new fabric of a similar shade, starting in Phase I.

During the tour, Daniela Trava briefed Council members about the new anti-slip product for the pool decks. It was applied to tiles three times this year to create a base coating and will be reapplied on a monthly basis. Results have been good and it will also be used on the terrace tiles in penthouse units

Council members visited the basement offices and storage areas used by different departments such as Food and Beverages, Activities, the 24-hour resort laundry and IT. Daniela Trava showed representatives the new tiles in the walkways, a replacement for the epoxy paint floor. Tiling is a less expensive alternative, is easier to maintain and much brighter. She also explained that the bakery has been enlarged with a new proving room and oven so that all bread can now be baked on the premises.

In the security office, Council saw the security camera monitors for public areas and elevators. An additional 10 cameras were installed in 2018. They also toured the machine house to see the generators, boilers and the reverse osmosis water purification system.

After the tour, Council members met with CEO Dr. Kemil Rizk, Chief Financial Officer Fernando López, Vice President of Resort Operations Armando Millet and members of their staff in the Bicaci Room, the new multipurpose room used for meetings and events.

Daniela Trava gave a general presentation on the resort, starting with guest satisfaction ratings. She mentioned that Grand Residences is in the prestigious 'Trip Advisor Travelers' Choice 2018 top 25 luxury hotels in the world and TripAdvisor Travelers' Choice 2018 for Mexico in four categories: Top 25 Hotels in Mexico,

Top 25 Luxury Hotels in Mexico, Top 25 Hotels in Mexico for Best Service and Top 25 Hotels in Mexico for Families. It is currently ranked No. 2 on Trip Advisor in the Puerto Morelos area, No. 18 in the Riviera Maya out of 420 hotels, and No. 30 out of 999 hotels in the Yucatán Peninsula.

Grand Residences also won the Loved by Guests 2018 Gold award given by Hotels.com to resorts that receive outstanding ratings and the Expedia+VIP Access Best of 2017 award as one of the world's top 500 hotels. Additionally, in the Medallia exit survey conducted by Leading Hotels of the World®, Grand Residences is rated No. 2 in Mexico and No. 66 in the world among the more than 400 luxury hotels and resorts in the collection. In the most recent report of social media scores achieved by Leading Hotels of the World properties, Grand Residences is number 22 in the world.

Resort occupancy from January to September 2018 was 58.70 percent on average, based on 144 rooms, down from 65.18 in 2017. This reflects a trend seen throughout the Mexican Caribbean this year and it is forecast to continue in 2019. There are a number of contributing factors: increased competition from new luxury hotels in the area and more hotel rooms; security concerns, particularly in the US market; and the seaweed landings on area beaches this summer.

Daniela Trava listed Grand Residences' participation in community initiatives such as weekly beach and street cleaning in Puerto Morelos and the 2018 turtle season statistics: 38 nests and 2,411 baby turtles released to date, with seven nests still to hatch.

She also went over projects carried out in 2018. This includes the preventive villa maintenance program, which entails two days of maintenance and two days of housekeeping projects, over and above the attention each unit regularly receives.

Other 2018 projects include painting building façades and roof waterproofing, maintenance to the main Jacuzzi pool and fountains and installation of handrails in private pools. The tiling on the dome above the motor lobby was replaced and the main entrance arch and signage were repaired. The tennis court lighting was changed for a more energy efficient system and the gym carpet was replaced. Machine house repairs were carried out on the reverse osmosis tanks and the wastewater treatment plant.

CEO Rizk gave a presentation on fractional industry trends and private residence clubs

before briefing Council on the two new products unveiled in June 2018: a Grand Residences Points membership, which is packaged with the Royal Resorts Signature Club Elite membership. He explained that the new membership is proving popular and enables the company to tap into a larger pool of prospects interested in the vacation flexibility that points offer. It gives members the option to buy more points on future stays and upgrade to the next level of membership; there are three levels.

Grand Residences Points members make reservations at the resort based on a separate points inventory; stays are subject to availability and reservation windows and policies. Points memberships are for 40 years and do not have residual rights. Points members pay an annual Club Service Fee which is similar to that paid by fractional members. Finally, as Signature Club Elite members, they have lifestyle, travel and destination benefits that are different to those available to President's Circle members. The President's Circle, which is exclusively for Fractional members, still offers the highest level of Signature Club benefits.

Dr. Rizk said that the Royal Resorts sales centers are selling Grand Residences Fractional and Points memberships. In the first four months of the Points program, points sales outpaced those of fractions by four to one and the signs for 2019 are encouraging.

He also commented that rental guests help keep resort services such as restaurants operating. Rental rates are kept high to ensure the right level of clientele.

He ended by saying that Management is committed to maintaining the exclusivity of the resort and Leading Hotels of the World standards.

CFO López began his financial presentation by briefing Council on the 2017 year-end numbers, which were better than anticipated. Resort revenue increased by 1.4 percent as did Dues income by 1.1 percent. Total Operating Expenses were 3.7 percent less, the result of savings in certain line items such as Housekeeping Services, Housekeeping Maintenance, Amenities and Sports Services, among others. General and Administrative expenses were also less, but the Credit Card Commission for Club Service Fees was 23 percent higher than forecast and the Taxes line item also showed a 7.5 percent increase.

He then explained the 2018 financial statement in detail. The Income Statement Comparison accompanying this summary

shows budgeted and actual (forecast) income and expenses as of September 30, 2018 with estimates to the end of the year. The 2018 budget was prepared using an exchange rate of 18.5407 pesos per dollar but the average exchange rate for the year is estimated at 19.1055, a variation of 3.05 percent.

He commented that Total Revenue for 2018 is expected to be 0.9 percent more than forecast and there is a difference of 0.5 percent in Resort Operating Expenses. The Electricity line item was 37.8 percent higher than forecast due to the rise in commercial electricity rates across the Yucatán Peninsula. However, savings in other line item categories such as Housekeeping services (-10.2 percent), Maintenance and Machine House (-7.3 percent), Water & Sewage (-14 percent), Landscaping (-14.6 percent), Sports Services (-15.1 percent) and Telephone (-19.4 percent), among others, mitigated the impact on Resort Operating Expenses.

General and Administrative expenses were 3.7 percent less than forecast and Net Income was 6.1 percent less than budgeted.

When asked about the electricity rate increase, Management commented that the Federal Electricity Commission has not explained clearly why the commercial rate increased so dramatically in the region during 2018. Further increases cannot be ruled out in the future.

The alternative energy industry is expanding in Mexico and prices are falling, making it a much more viable option. Therefore, as a long-term solution, Management is studying the possibility of working with companies supplying clean energy from solar and wind farms and gas sources at a lower rate.

CFO López then presented the proposed Resort Operating budget for 2019 mentioning that the policy is to budget conservatively and control expenditure. However, despite this, Resort Operating Expenses are 8.6 percent

higher due to increases in several line items and taking into account the cost of living increase and a less favorable exchange rate. Given the unprecedented electricity price hike in 2018, a higher rate was used in next year's budget, a 29.1 percent variation. The Internal Laundry shows a 9.8 percent increase due to the purchase of a new mangle. The increase in Fixed Assets and Major Repairs expenses is due to the installation of additional anti-slip flooring in the pool areas. Property tax is also expected to be higher in 2019.

After the budget review, CFO López explained that the decision had been made to increase the Club Service Fee for 2019 by 3 percent to offset the increase in Resort Operating Expenses. He stressed that the primary concern of Management is to keep Club Service Fees as low as possible.

Council voted to approve the Club Service Fee increase.

The annual Club Service Fee for 2019 and the breakdown is as follows:

Villa	CSF 2019						
	Normal 2 Bedroom	Normal 3 Bedroom	W/Roof Garden 2 Bedroom	W/Roof Garden 3 Bedroom	W/Roof Garden 4 Bedroom	W/Pool 2 Bedroom	W/Pool 3 Bedroom
CSF	1,823.53	2,127.73	1,945.38	2,249.58	2,552.10	1,884.87	2,189.08
VAT	291.76	340.44	311.26	359.93	408.34	301.58	350.25
3% Occupancy Tax	54.71	63.83	58.36	67.49	76.56	56.55	65.67
Total	2,170.00	2,532.00	2,315.00	2,677.00	3,037.00	2,243.00	2,605.00
% Increase	3%	3%	3%	3%	3%	3%	3%

In closing, the Advisory Council recommended that Management look for more ways to promote the restaurants to increase member use and support for resort businesses.

ECONOMIC AND FINANCIAL PREMISES FOR BUDGET PREPARATION

The Grand Residences operations budget is calculated in pesos and then converted into USD using the estimated exchange rate.

Exchange rate

For the calculation of the 2018 Forecast, after nine months of the year, the average exchange rate for 2018 is expected to be 19.1055 Pesos per Dollar. The average exchange rate estimate used in the 2018 budget was 18.5407. This represents a variation of 3.05 percent.

The Banco de Mexico (Mexico Central Bank) survey and the consensus of major financial institutions forecast an average exchange rate of \$18.7783 Pesos per \$1USD for 2019. This premise was used to calculate the 2019 budget and would represent a 1.71 percent appreciation of the Peso against the Dollar when compared to the exchange rate forecast for 2018.

Cost of living

Another relevant premise taken into account in the preparation of the resort operations budget is the increase in the cost of living. For budgeting purposes we are considering that the increase in the cost of living in Mexico for our employees will be 4 percent.

Inflation

The majority of our operational expenses will be affected by an inflation rate of 3.64 percent. This estimate is in line with the consensus of the major financial institutions in Mexico and the Mexican Government.

Utilities

After a double-digit percentage rise in electricity rates in 2017, the trend was not expected to continue in 2018 and an annual increase of approximately six percent was forecast. However, Comisión Federal de Electricidad or CFE, the government-owned company with a monopoly on electricity production in Mexico, adjusted the commercial rate charged to companies throughout the Yucatán peninsula by 100 percent, thus seriously affecting the resort's financial results. While we are not expecting another rise of this magnitude in 2019, we have factored in higher rates in the 2019 budget.

Income Statement Comparison Forecast 2018 vs Budget 2019 (US Dlls)

2018			DESCRIPTION	2019 BUDGET	FORECAST VS BUDGET		ACTUAL/ INTERVALS
BUDGET	FORECAST	%			2018 VS 2019		
					VARIANCE	%	
			GENERAL REVENUE				
5,434,179	5,470,978	0.7%	Dues Income	5,709,903	238,926	4.4%	1,805.79
5,434,179	5,470,978	0.7%	Total Dues Income	5,709,903	238,926	4.4%	1,805.79
			OTHER INCOME				
3,000	2,351	0.0%	Guest Laundry	2,237	(114)	-4.9%	0.71
24,000	36,440	51.8%	Other Income	31,953	(4,488)	-12.3%	10.11
27,000	38,791	43.7%	Total Other Income	34,189	(4,602)	-11.9%	10.81
5,461,179	5,509,769	0.9%	Total Revenue	5,744,093	234,324	4.3%	1,816.60
			RESORT OPERATING EXPENSES				
764,406	686,603	-10.2%	Housekeeping Services	727,427	40,824	5.9%	230.05
329,771	344,073	4.3%	Housekeeping Maintenance	333,720	(10,353)	-3.0%	105.54
114,811	113,341	-1.3%	Amenities	109,278	(4,063)	-3.6%	34.56
656,897	904,936	37.8%	Electricity	1,168,371	263,435	29.1%	369.50
976,260	905,112	-7.3%	Maintenance & Machine House	958,680	53,568	5.9%	303.19
101,532	87,297	-14.0%	Water & Sewage	91,059	3,762	4.3%	28.80
351,029	334,121	-4.8%	Security	353,584	19,463	5.8%	111.82
293,757	270,855	-7.8%	Front Desk/Concierges	266,710	(4,144)	-1.5%	84.35
236,437	233,086	-1.4%	Internal Laundry	255,846	22,760	9.8%	80.91
-	-	0.0%	Fixed Assets and Major Repairs	24,037	24,037	100.0%	7.60
160,909	137,487	-14.6%	Landscaping	146,449	8,962	6.5%	46.32
142,080	120,647	-15.1%	Sport Services	108,734	(11,914)	-9.9%	34.39
69,577	56,053	-19.4%	Telephone (Net Result)	55,598	(455)	-0.8%	17.58
158,220	171,486	8.4%	Social Activities	169,085	(2,401)	-1.4%	53.47
16,292	16,341	0.3%	Operational Services	19,213	2,872	17.6%	6.08
291,656	304,338	4.3%	Resort Insurance	300,850	(3,488)	-1.1%	95.15
25,368	24,424	-3.7%	Gym	31,367	6,943	28.4%	9.92
30,476	33,209	9.0%	Members Transportation	34,509	1,300	3.9%	10.91
64,596	64,596	0.0%	High Speed Internet Connection	64,596	-	0.0%	20.43
4,784,073	4,808,004	0.5%	Total Resort Operating Expenses	5,219,112	411,108	8.6%	1,650.57
			GENERAL & ADMIN EXPENSES				
503,403	505,373	0.4%	Management Fee	512,714	7,342	1.5%	162.15
312,512	303,546	-2.9%	Corporate Services	330,108	26,562	8.8%	104.40
105,011	96,454	-8.1%	Accounting/Warehouse/IT/Purchasing	113,993	17,539	18.2%	36.05
53,537	48,222	-9.9%	Administration/General Management	49,987	1,765	3.7%	15.81
121,223	109,494	-9.7%	Human Resources	132,814	23,320	21.3%	42.00
9,950	4,730	0.0%	Other Expenses	4,970	240	5.1%	1.57
14,414	10,156	-29.5%	Auditing	12,612	2,456	24.2%	3.99
32,400	32,208	-0.6%	Membership Services	32,124	(84)	-0.3%	10.16
1,152,450	1,110,183	-3.7%	Total General & Admin Expenses	1,189,322	79,139	7.1%	376.13
(475,344)	(408,418)	-14.1%	Total Operating Income	(664,342)	(255,924)	62.7%	(210.10)
			FINANCIAL EXPENSES/INCOME				
18,836	19,864	5.5%	Credit Card Commission CSF	20,659	795	4.0%	6.53
18,836	19,864	5.5%	Total Financial Expenses/Income	20,659	795	4.0%	6.53
			TAXES				
336,969	328,317	-2.6%	V.A. Tax	388,060	59,743	18.2%	122.73
63,182	61,559	-2.6%	Occupancy Tax	72,761	11,202	18.2%	23.01
-	-	0.0%	Income Taxes	-	-	0.0%	-
79,063	95,566	20.9%	Property Tax & Other Exp.	98,521	2,955	3.1%	31.16
479,214	485,442	1.3%	Total Taxes	559,341	73,899	15.2%	176.89
(973,394)	(913,724)	-6.1%	Net Income	(1,244,342)	(330,618)	36.2%	(393.53)