CORPORATE PARTICIPANTS

Alan R. Pickerill  Expedia, Inc. - Executive VP & CFO
Mark D. Okerstrom  Expedia, Inc. - CEO, President & Director

CONFERENCE CALL PARTICIPANTS

Mark Alan May  Citigroup Inc, Research Division - Director and Senior Analyst

PRESENTATION

Mark Alan May  Citigroup Inc, Research Division - Director and Senior Analyst
And it's my pleasure to welcome the team from Expedia. Mark Okerstrom is the company's new President and CEO. Congratulations.

Mark D. Okerstrom  Expedia, Inc. - CEO, President & Director
Thank you.

Mark Alan May  Citigroup Inc, Research Division - Director and Senior Analyst
And Alan Pickerill, the company's new CFO. So congratulations, guys.

Alan R. Pickerill  Expedia, Inc. - Executive VP & CFO
Thanks. Glad to be here.

Mark Alan May  Citigroup Inc, Research Division - Director and Senior Analyst
And good timing.

Mark D. Okerstrom  Expedia, Inc. - CEO, President & Director
Yes, perfect timing.

Mark Alan May  Citigroup Inc, Research Division - Director and Senior Analyst
Yes. We had quite a bit of interest to meet with Mark and Alan today, and so I want to make sure to -- we have plenty of time at the end for questions for everyone -- at the end. So please be prepared. And you're welcome to ask those. We only have 15, 20 minutes.

QUESTIONS AND ANSWERS

Mark Alan May  Citigroup Inc, Research Division - Director and Senior Analyst
But maybe just talk a little bit about -- it should be -- imagine, a pretty smooth transition. But in terms of any other things that are top of mind for you guys in terms of the biggest risk that you feel like -- that you need to manage during this period.
Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. Well, I think you said it. It should be a seamless transition this week. I mean, employees are back to work. I think by Friday last week, everyone’s back to work. I’ve got about 7,000 e-mails from employees in my inbox saying how excited they are. I mean, everyone misses Dara, obviously. He’s was a fixture of that place. But over the course of the last -- particularly the last 6 years -- I mean, we’ve been working together for 11 years. The last 6 years, his desk is here, and mine’s here, and like we literally are -- always bouncing ideas off of each other. Now I had a certain focus on finance, corporate strategy, mergers and acquisitions work, plus our internal operations. And he was focused more on the brands and product. So the focus for me is going to shift, but the strategy was a joint strategy, and it does continue. And I think going forward, I think we’ll end up doing what we might have done anyways. My ambition is just do it faster and better with probably more of an operational focus because that’s what I enjoy in addition to doing the deals.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Yes. I don’t know if there are any -- I can open it up with questions maybe around the transition. And there are -- if there are any questions out here at the front. Yes?

Unidentified Analyst

I have one just on the Trivago stuff. I'm sure you guys have had a bunch of questions about it. Any changes you can call out in terms of your efficiency on that channel or your share of traffic that’s coming from that channel? A lot of investors seem to think that Priceline has adjusted. Their ROI threshold is up. I don’t know if you guys have a perspective on that piece either.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. So I think it's important we talk about what's happening at Trivago is -- I think it's less actually a specific advertiser phenomenon. I think more potentially, it's just a byproduct of the changes that they've made to the marketplace. I almost hate to make this analogy. But for those who've been following the industry for a while, it feels a little bit like the TripAdvisor transition in 2013 when they went from pop-up windows to metasearch in that anytime you make a big change to a marketplace, it takes advertisers a while to actually recalibrate all of their models. And to the extent that you are passing different types of leads, in this case because of the landing page score that Trivago rolled out, the traffic may have just a differential value. It takes advertisers a while to recalibrate their model. And if you remember what we did in 2013 with TripAdvisor is we ultimately pulled way back. Because we don’t want to risk overspending. We're going to pull back and recalibrate our models. And then over time, things reached a more normalized state. So I think there’s a little bit of that going on here at Trivago. I don't think I would take the last 1.5 months to 2 months and say this is the new normal. I think there’s a period of volatility that they're experiencing after the normalization of the landing page scores so that everyone’s got the landing page. And I suspect that what we've seen over the last 1.5 months, 2 months is not the future steady state. It will be something different.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

I't like the timing of the market’s reaction for this, though, the travel marketing market is -- was a little different, though, than TripAdvisor. It seemed like that the pullback in the market reaction was a little quicker at that point. Was there something that’s -- is it because there weren't as many alternatives at the time and now there kind of are? Or what’s sort of different here, where initially it felt like marketers didn't pull back? They actually upped their spend.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

For Trivago?
Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Yes. Marketers actually upped their spend to maintain certain levels of traffic, and it took a while for them to readjust. Why the...

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Well -- so from an advertiser's perspective, what was happening was that Trivago was classifying characteristics of landing pages that would produce a good landing page score. And with a good landing page score comes regular CPCs. With a bad landing page score comes -- essentially, you got to pay more to get your spot. And so what -- from an advertiser's perspective, what you do is you say, "Hey, well, the old landing page I could use, produced a certain amount of yield on traffic because if they didn't like that hotel, I can show them another hotel or maybe I could sell advertising on it. This new landing page that they want is going to be something less than that because they wanted to go back to Trivago. So what advertisers do is they start testing. Okay, am I better off just to keep the landing page I want and pay the premium? Or am I better off just to comply and take the CPCs and get my landing page score to tenants. So everyone is testing. And while they're testing, a few things happened. One is there is extra monetization that's happening in the marketplace, and Trivago spoke a lot about that, that there was some overmonetizing during this period because that testing is happening. And two is you create a lot of noise and ripple in your historic data because the CPCs that you were paying were not necessarily a byproduct of the intrinsic value of the traffic you were getting. It was modeled by this landing page score. And then in June, essentially when everyone complied, the big advertising marketplace hit a landing page score of 10. Now all of that dynamic settles out. And so there's not all of this test anymore. People started to now figure, what is the intrinsic value of the traffic that I'm buying, and that requires a fair bit of data to collect over time. And what we did, remember back in TripAdvisors when we were doing that, we actually started to pull back. Now when you're in a marketplace that's competitive as ours, ultimately, if there is profitable traffic to be had for us, we're going to go after it and get it. So it's not a unilateral situation where one player can say, "I'm going to take more profit." And another player could step in and say, "Well, I see surplus there." I mean, that dynamic generally happens over the long term.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Right. Any other questions on Trivago? I'm just going to ask you a little bit about the -- thinking a lot of questions around the EBITDA growth in the first half of the year and then the guide. I think in the first half, you've got easy expense comps, and they start to normalize in the back half of the year. So I mean, that's the -- that is the biggest factor for us in terms of the shape of the year that's different than what we usually see, which is generally more of a back-end loaded year.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Well, one of the more significant factors driving that is largely just the expense comp. So in the beginning of 2016, we were essentially carrying essentially double cost as we were integrating the Orbitz acquisition. In the back half of the year, we were able to essentially shed that. So the first part of this year, you've got easy expense comps, and they start to normalize in the back half of the year. So I mean, that's the -- that is the biggest factor for us in terms of the shape of the year that's different than what we usually see, which is generally more of a back-end loaded year.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Got it. And people do seem to be expecting a mild acceleration in bookings in the second half of the year despite maybe what is a -- give us your view of the travel market backdrop. Maybe it's mixed depending on what the commentary is. Do you think that, that sort of expectation is reasonable based on what you're seeing in the market and also based on your own, I guess, comps -- the company's stock comps?
Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Well -- so I won’t comment on what we’re seeing right now. I would say that the comp for Q3 is a wee bit easier than the comp in Q2. It’s 100 basis points easier for the hotel business. But there’s so many puts and takes going on right now. That’s sort of a tailwind for us. The other tailwind is that the HomeAway business is very seasonal and very Q3 loaded. So that’s going to be a tailwind for us. The headwinds is that we still have essentially a quite clean comp, some of the pullback that we did in some of our regional brands. So that can continue to be a drag. And then really through Q3 last year, in September, we started to actually ramp up our spend again after we had some of the integration issues. So there’s a lot of puts and takes that are happening in Q3. And then Q4, we started to get into sort of cleaner comps, cleaner water. And we won’t have as much of, call it, easy comp tailwind that we’ve got -- we had in Q2 and that we got in Q3.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

And you mentioned the regional brand headwind. Can you kind of frame that, maybe explain to folks that maybe aren’t aware of what that means and frame kind of the magnitude of the headwind that, that represents?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Let me take that? Or you want to take that?

Alan R. Pickerill - Expedia, Inc. - Executive VP & CFO

No, I can cover that. Yes. I mean, I think the -- there’s a couple ways to kind of cut it. If you think about when we bought Orbitz worldwide, the day it closed in September of 2015, we owned 100% of that business. There’s components in that business that we shed over the period of, say, 6 to 9 months after acquiring it. It included clients on the Orbitz Partner Network, Orbitz for Business. It included shutting down Hotel Club, some of the e-booker sites. And so when you’ve heard us talking about that headwind, that’s really what’s happening there. A lot of that business was not particularly profitable. And so at the bottom line, it really didn’t hurt us. But the thing we talked about last quarter in terms of just the room night growth is that we do now have these regional brands. Think of them as consumer brands, Orbitz.com, CheapTickets, Wotif, that group of brands, those businesses are -- we said they represent kind of high single-digit -- mid- to high single-digit percentage of the room night mix thing in the quarter. And you can think of them as kind of growing flat to slightly up. The challenge for those businesses is a couple things: One is they’re mostly focused on given markets. So Travelocity and Orbitz are focused on North America, and so they are, a, subject to what are the relative growth rates in North America. And then also, we are asking those brands to be -- have more of an eye towards profitability than the global growth brands. So they’re not going to be market makers and page search and metasearch. I mean, they’re going to try to get the traffic they can get, but that’s going to also have an impact on their growth rates.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

But at the same time, we’re really driving the profit growth for those businesses.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

How would you characterize just the broader backdrop for the travel market as a whole?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

I’d say, generally speaking, no major change. And I say generally speaking because, certainly, isolated pockets, obviously, southern part of the U.S. right now with all the storms, those are impacting overall travel patterns, at least. Attacks like we saw in Barcelona impact overall travel patterns.
From our perspective, because it's such a global, diversified business, generally, things like that don't have a meaningful impact on our overall result.

Mark Alan May  - Citigroup Inc, Research Division - Director and Senior Analyst
Not the fact that they seem to be sort of clustered right around the same time?

Mark D. Okerstrom  - Expedia, Inc. - CEO, President & Director
Well, yes. I think we -- again, I won't comment on what we're seeing right now. Generally, even when that has happened, people have just shifted where they want to travel, and we haven't seen an overall reduction in travel activity. Generally, it's been more of where pieces -- where people go. We have said, though, that, listen, if there's a lot of terrorist activity, that could have a chilling effect. But it's not something that we're necessarily seeing right now.

Mark Alan May  - Citigroup Inc, Research Division - Director and Senior Analyst
Okay. Any -- maybe I'll pause there and see if there are any questions.

Unidentified Analyst
Yes. A quick question on (inaudible). You've obviously ramped a lot of remodeling and advertising for that particular property more recently quite dramatically year-over-year. What type of sort of GMV growth do you think you're accelerating to? I mean, a week ago, I think Airbnb reported they had 45 million guests over the summer. And up until recently, they only had 100 million in total cumulatively over their entire lifetime. So they're seeing, obviously, some very attractive guests, room night, GMV growth, whatever it is. So what do you think you're accelerating ways growth to? And then within a reasonable sort of 1-, 2-, 3-year time frame, how much can you reduce the leakage at HomeAway in terms of people that are booking outside and obviously, not the paying service fee?

Mark Alan May  - Citigroup Inc, Research Division - Director and Senior Analyst
Yes. Mark, if it's possible, when you're talking about kind of the booking scale of HomeAway, if you could talk about kind of combined online, off-line, the broader opportunity in online.

Mark D. Okerstrom  - Expedia, Inc. - CEO, President & Director
Well, let me frame that up first, which is when we acquired HomeAway, estimates were about $14 billion to $16 billion of gross bookings were being facilitated by the platform. Now HomeAway, at the time, did not have visibility into every single one of those bookings. It was a calculation that was done based upon referral activity and a bunch of assumptions. We looked at that at due diligence. We thought, actually, it looks right. Broadly speaking, we got comfortable with it. I think that even though we haven't redone that calculation, I would expect the whole thing is growing because traffic has been growing and conversion has been improving. But I don't know what the total off-line piece is now. Trailing 12 months online, about $7.5 billion in bookings, which is probably nicely double what it was than when we first bought them. In terms of what to expect in terms of growth rates, I mean, the last couple of quarters, we've been in that 40%, mid-40s range. And there's a few different dynamics at play here. I think one is that HomeAway has always had a pretty decent portion of their traffic come from search engine optimization. And that, just long term, is something that Google is doing their best to get rid of and to monetize. So they've got a bit of a headwind on traffic. The tailwind for them is that they are now monetizing by transaction, so we are starting to essentially be able to light up the performance marketing channels there. We're not fully ramped up, but we are in the process and we're, call it, third to fourth inning. And I suspect by the end of the year, we'll be up to full strength there. So that's kind of the tailwind to traffic. And then underneath that, conversion is improving really nicely, and it's really coming
from 2 places: First is actually just improving the overall traveler experience. If you've been on the HomeAway sites, you'll notice the significant
difference over the course of the last 12 months. It's just getting much more usable from a user interface perspective, looking a lot more like modern
design, like we would expect to see. But importantly, conversion has also helped us with the second thing, which is controlling leakage, which is
what you mentioned. And if you think about, well, how big could leakage be, well, there's $15 billion of bookings we thought on the platform 2
years ago, and now trailing 12 months, we've got $7.5 billion. Well, you know there's at least $7.5 billion of leakage, and it's probably more. So what
are we doing to actually stop the leakage? A whole bunch of things. I'd say it's a combination of carrots and sticks. On the carrot side, we've been
incenting travelers to actually ensure that we book on platform by providing Book with Confidence guarantees, and insurance programs that help
protect them from people taking their security deposit without justification or any sort of fraud. We protect them from that. And then on the
supplier side, the homeowner side, putting in place liability insurance and damage protection for on-platform bookings. And we're also starting
to implement more kind of carrot-type things. So we've -- we are launching a revenue management tool that essentially will help property owners
-- the professional managers or individual owners, help better manage their properties; revenue by looking at their peer set; and potentially, other
factors in the local area around accommodation prices. We have recently also introduced a closed-loop communications platform. It's early stages
right now. It's actually just on the interface that's on the HomeAway platform. It will go to SMS, text message, and it will go to voice as well in the
next, call it, 4 to 6 months, I would say, and that will also help avoid this leakage problem. And the last thing is we do have now pretty much
complete control of our sort order. And so you can start to introduce incentives and disincentives for people taking bookings off platform, which
we can generally judge by virtue of conversion rates for certain properties versus comps. So it's going to be a long process, but the progress is
great so far and the opportunity is huge.

Unidentified Analyst
And with this low single-digit leakage, do you think you can get there in 2 years, 3 years?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director
I'd hope so. I would hope so, but it's hard to say.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst
So maybe along the same lines. But given that -- I think by the end of the year, you're expecting the majority of properties to be online bookable,
right?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director
Yes.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst
So given that, it would seem like you'd start to really push on performance channels a lot more than what you are today and that you'd expect over
the 4 -- 12 months to close that gap between that $7.5 billion to $15 billion. Is that right way to think about this?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director
Yes. I mean, I think you're thinking about the right -- definitely, the right levers. I think online bookability is a piece of it. We're trying to shift more
of it to the instantly bookable as well, which is a good, strong conversion driver. I think about 1/4 of the properties now would be instantly bookable
or so.
Alan R. Pickerill - Expedia, Inc. - Executive VP & CFO

Yes. We -- there's 1.5 million online bookable listings. And think of it as being about 1/3 that's instantly bookable.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. 1/3 are instantly bookable, so we'll migrate that on -- that number higher. And so those are big, big catalysts. But for performance marketing to work, it's not just that. We've had to implement a complete new performance marketing technology stack that are tagging all of the pages, building on the data warehouses, building out the bidding algorithms, et cetera. We had a great guy on that. He used to run online marketing for Hotels.com. And I think by the end of the year, they'll be up to full steam at it.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

And I think getting back to an earlier question, do you have a sense of what the underlying organic growth is on kind of global online/offline bookings for...

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

For alternative accommodations?

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Or -- and even HomeAway, specifically, either/or.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. Well, I mean, I think the HomeAway number is -- there's a few ways you look at it. But when you look at sales in the online numbers, bookings is growing to a mid-40% range or has been. What's happening with the overall platform-facilitated bookings, they're not growing that fast in terms of penetrating into the opportunity. But it's hard to say exactly

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Would you look at traffic growth as kind of an indicator of that or...

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

You could. But of course, with SEO headwinds and performance marketing tailwinds, it's hard for us to get a completely good read from our numbers. I mean, I think if you looked at our growth and Airbnb's growth, I think you're going to get in the number that's like mid-double digits probably, and that's not how fast the market is growing. I don't think. So it's hard for me to estimate what the overall things -- what the overall market is growing into. But the real growth vector is the online movement. And I don't see -- really, from the perspective of HomeAway, I don't see any cap on their growth rate aside from just execution essentially across their plan.
Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

And just given where your -- the inflection point you’re about to hit in terms of online and instant bookable becoming much larger -- a vast majority of the experience, how do you think about the trade-off and how big the market opportunity is here still? How do you think about the trade-off between growth versus profitability? And if there’s any reason why you wouldn’t focus even more so on pushing the lever on growth and performance and other channels maybe even at the detriment of pushing out the magic $350 million target that’s out there.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. Well, I think we’ve always tried to strike a balance. I think that’s what you’ll see us do as well. But I think above all, I mean, we’re focused on financial returns periods. So we wouldn’t do something artificial or something bad for the business to hit the $350 million. And similarly, we wouldn’t pass on a great investment opportunity and miss the $350 million. We’re -- right now, the $350 million is $350 million, and we see that as an attainable target. And we’re in the middle of 2018 planning. I think if something came up, we would do it. But there’s nothing right now that I’m sitting on that says, “Gee, what are we going to tell these guys?” That’s not the spot we’re in.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Right, okay. And when you think about longer term in your model for HomeAway, how should we be -- how do you guys think about the long-term margin profitability profile of that business maybe relative to the core OTA business?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Do you want to take that one?

Alan R. Pickerill - Expedia, Inc. - Executive VP & CFO

Yes. I mean, we don’t know with tremendous precision. But I think we’re pretty comfortable that it could look like similar margins to a hotel-only OTA.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

When I covered HomeAway since -- prior the IPO process and before it was acquired, its legacy as a rollout made it challenging to be as efficient as possible not just from a cost perspective, but in terms of rolling out new product features and just having consistency across the globe. I haven’t had a chance to really talk to you or hear how you’ve -- what kind of progress that you guys have made in terms of really creating a more homogeneous platform globally.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. Well, there’s broadly 3 pieces to the way that we think about that: First of all is platform consolidation, tech platform. We are -- the vast majority of the business now is on a common platform. There’s a few little pieces left, Australia, for example, that we’re in the process of getting onto the global platform. The second piece is brands. There is a lot of brands out there. So far, we’re fine keeping them the way they are, but it does complicate life to some extent. And so the team is actively thinking about what is -- in what countries do we have a lead brand, do we get rid of some of these brands, do we keep them all. I think it’s an active dialogue. And the third piece of it all is organization. When you do all these acquisitions, particularly in Europe, you end up with these small country teams, if you will. And the HomeAway team is looking hard at organization with the goal of ultimately getting to a much more centralized global-type organization or the type that you’d see at a place like Hotels.com, for example.
Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Okay. I was going to move on from HomeAway, but maybe if there are any questions or...

Unidentified Analyst

I think your recent survey estimated that the weighted average traveler fees is running something like 8% to 10% now, and I was curious if you could comment on -- if that's directionally correct. And then I was also curious if there's an opportunity -- or if you already are dynamically moving the traveler fee around based on peak season or occupancy. Will you repeat the first part of the question?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. So the first part of the question was around what's the average -- what's sort of the range of the traveler fee in terms of percentage of bookings. So I won't comment on the number. I'll just say that it's really -- to answer your second question is we're always testing it. We are optimizing fee across a whole bunch of dynamics. We're testing elasticity around it. It has been generally trending up in terms of yield, and I think you're directionally in the ballpark.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

What kind of -- was there any other question? What kind of opportunity is there from a partner network standpoint when it comes to vacation rentals? Is that something that we should be thinking about or...

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Any your fee in terms of us redistributing the inventory to third parties?

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Yes, yes.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Untapped. It could be large. I think particularly on the stuff that's instantly bookable, the stuff that looks like hotel. I think that's something that could be distributed quite easily. So it's something we're thinking about and something we're thinking about once we get the integration into our core lodging stack, which we're doing right now live on 11 Brand Expedia points of sale, about 60,000 properties. I think the next question -- logical question is, do we start distributing that to our Expedia affiliate network?

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Got it. Maybe a question on sales and marketing efficiency. I think it's running 55%, 60% gross profits today. Kind of how do you see that trending, short, medium, long term? And kind of what are the key levers behind that?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. Well, I think the aspiration is that in the short and medium term, that ratio might go up. And in the long term, it'll come down. And what's happening and what's driving it to go up is, ultimately, just mix. We're growing significantly faster in the non-U.S. markets than we are in the U.S.,
and those markets are generally less efficient. Now each of those markets is generally year-after-year getting more efficient, but they're all dragging essentially the overall number up. So I think if you got to a spot where you are at maturity in these markets, and we’re nowhere near that now, you could start to see some sales and marketing leverage. But so far, I mean, the delevers that we see is all – it’s like healthy mix-driven, so we’re going to continue to push it.

**Mark Alan May** - Citigroup Inc, Research Division - Director and Senior Analyst

So just to clarify, it’s fair to say that it’s really mix-driven. And on a region-by-region, country-by-country basis, you're saying what’s – you characterize it as stable to declining (inaudible).

**Mark D. Okerstrom** - Expedia, Inc. - CEO, President & Director

Yes. I’d say it’s generally stable. I think the other – if you look at a constant channel efficiency, I think those have been generally constant as well. But within a country, once you have full penetration of the hotel inventory, essentially, then you’re at a spot where you actually start to get better marketing efficiency over time. Because as you’re adding properties, you’re adding demand from variable channels, which, again, is generally less efficient when you're dragged.

**Mark Alan May** - Citigroup Inc, Research Division - Director and Senior Analyst

I assume one of the key factors, and that is just kind of repeat, loyal customer base.

**Mark D. Okerstrom** - Expedia, Inc. - CEO, President & Director

Yes.

**Mark Alan May** - Citigroup Inc, Research Division - Director and Senior Analyst

What’s the general sense of what portion of your business comes from kind of repeat, loyal, lower-cost customer?

**Mark D. Okerstrom** - Expedia, Inc. - CEO, President & Director

Yes. Well, we've said that about 2/3 of our bookings comes from branded channels, so to speak.

**Mark Alan May** - Citigroup Inc, Research Division - Director and Senior Analyst

Branded channels, including low-cost branded?

**Alan R. Pickerill** - Expedia, Inc. - Executive VP & CFO

You've got e-mail, direct type in, loyalty programs.

**Mark D. Okerstrom** - Expedia, Inc. - CEO, President & Director

Someone types in Expedia into Google, that’s (inaudible).
Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Sure. Maybe I’ll just pause there and see if there are any questions. No? Just while we're on the regional mix and how that's impacting expense ratios, about 45% of your business is coming outside the U.S. Maybe talk a little bit about some of the regions or countries that are really working well for you, where you guys are kind of pushing maybe a little bit more aggressively than others.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes. Well, I'd say just generally, to cap it off, the opportunity for us is huge. I mean, 2/3 of the travel market is not in the U.S., and we're skewed wildly the other way. The -- our traditional non-U.S. markets that have always been very strong have been Canada, Australia, even the English-speaking markets, the U.K., for example. We're doing now very well in Southeast Asia. We're doing very well in places like Japan. Korea has been great for us, Taiwan. Brazil has turned into a brighter spot after some overall macro troubles there. So lots of opportunity. We're getting more serious about India. Again, India has been a tough market for us given the regulatory landscape, given the competitive intensity that we saw in that market. We're in a position now where we're able to step a little bit harder into that market going forward.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Okay. The company both bought and sold assets over the years. When we think about Expedia from a portfolio perspective over the next 1, 2 years -- 1, 2, 3 years, do you see Expedia being more of a buyer of assets or a seller, do you think?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Definitely more a buyer.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Yes?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

And so do you see that being in terms of product, geo? Kind of how would you think about where that -- where your focus is right now?

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Well, I mean, first of all, I'd say there's nothing that we need. We have everything that we need. And we will -- probably if you compare the last 5 years to next 5 years, focus more internally on operations and actually, realizing the full potential of the assets we have. But we'll continue to be opportunistic. We -- I would expect that acquisitions are being more non-U.S. than U.S. The corporate travel space is interesting to us. We have made a number of investments and small acquisition in the hotel technology space like ALICE, for example, or GoConcierge. So there might be little things like that. But again, there's no -- there's nothing big that we need. It's more going to be opportunistic.
Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Maybe I can just pause, see if there are any questions from the audience. One initiative inside the company in terms of investments is around cloud. Maybe if you can talk to -- focus a little bit about what you're doing there, where you are in that transitional period. And as we look out over the next year or so, how we should think about costs related to that, any sort efficiencies that you might be able to...

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Sure. So overall, what we're doing with cloud is we're taking a bunch of stuff that we used to have in our own physical data centers, which was super asset-heavy, and we're renting it from Amazon, essentially. And the way to think about that mathematically is if you look at over the course of the last 3 to 4 years on data center and infrastructure, let's just say we spent, call it, $600 million. I don't know if that's the exact number. It's going to be around in that ballpark. So we got $600 million of assets sitting in the data center, all of which has to be replaced every 3 to 5 years. And then if you think if we're going to double this business in the next 5 years -- don't put that in your models, I'm just using it to make it simple. Now suddenly, on that $1.2 billion that I got to replace every 3 to 5 years. And it creates the most exponential curve of CapEx that we wanted to get away from. It's fine to have your own data centers if you're not growing. We're growing too fast. To do it in Amazon provides a very credible alternative to it. What it will do to us, it will essentially reduce our CapEx and it will increase our free cash flow. But it will put pressure on our EBITDA because cloud gets expensed. And this year, for example, we said we'd spend about $110 million in cloud expense. A lion's share of that's with AWS. About 50% of it sits in cost of sale. About 50% sits in R&D. And that's just EBITDA that is gone. But cash flow, which is -- we said it's going to be cash flow accretive. And a couple of years from when we started it, we still absolutely believe that. We're not done yet at the end of this year. By the end of this year, we're going to be in a situation where we've got -- we think most of our lodging stack in the cloud. We still got air to go. There's a whole bunch of stuff that still got to go out there, so I would think about the $110 million as kind of the endpoint on a triangle. It's got to annualize, and then we're going to grow from there. And that's not going to be $600 million, I don't think. And the great thing about it is that, ultimately, it comes with real performance benefits as well. One of the reasons the $600 million is the $600 million is because I got basically have 2 of everything. Because if one data center goes down, I got to have a backup. We got to run things in active, active. And not only that. I got to build this stuff to the entire peak. So actually just using AWS and actually being able to expand elastic when I need it gives me a benefit. And then for disaster recovery, I just fail over a different machine and we don't even really notice it. The other great benefit is in places like Asia, where there -- many times, low bandwidth connectivity, we've got latency that's exacerbated by the fact that I got a whole database that calls back to Arizona and then send them to Singapore. When I'm out in the cloud, we can actually operate like right close to the edge, and that could produce some real speed advantages. And the last thing is the way users deploy code. I mean, the -- our engineers would have to order 100 boxes with this build. Sure, if that's going to be 6 weeks. Now it's -- they spin off in instance, and they're out live, like, 10 minutes.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

And given that you still have to transition air and maybe other regions and brands and whatnot, in terms of the crossover point where, I'm sure you've got some duplicative costs and some ramp-up costs and things like that, it's unlikely to be next year. It sounds like it's maybe 2019 or something beyond that.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Well, in terms of being accretive from a free cash flow perspective?

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Yes. Breakeven.
Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

It could be I think 2019. Yes, it’s possible that it could be earlier. You’ll never see it because we’re -- I’m comparing this versus the money I would have had to spend. But you’re already this year, CapEx on infrastructure is actually down year-over-year. We’re actually able to sweat our assets longer because we know we’re moving out. So from a cash flow perspective, it’s probably going to be a readily apparent good decision, definitely by 2019, hopefully a little earlier.

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

Okay. Just maybe pause. We have time maybe for one question.

Unidentified Analyst

Curious if you think if there’s a margin opportunity maybe if you look at it on, say, EBITDA less CapEx to normalize for the cloud expenses. But I think that ratio is much lower than Priceline. And I know part of it is mixed with your air revenue. But curious if you think there’s an opportunity to close the gap there or if it’s structurally due to mix.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Well, I think closing the gap is ambitious. I think that there’s an opportunity for EBITDA less CapEx to improve as a percentage of revenue from where it’s been because we’re not going to have all of this infrastructure cost. But I think if you compare us to Priceline, we’re just structurally different businesses. If I just looked at the like-for-like businesses, Hotels.com, match it to Booking.com, Priceline to Hotwire, rentalcars to CarRentals.com, I can match up the businesses and get pretty close, where I can actually look at the cost structure -- fixed cost structure of our businesses and compare it to the Priceline fixed cost structure. And those fixed cost structures actually look pretty darn close. So the difference is really 3 things: They don’t have a Brand Expedia; they don’t have an Egencia, which is a corporate travel business; and their hotel business is twice as big. So we will not apologize for Egencia, nor for Brand Expedia. We will apologize for our hotel business not being twice as big as it is, but that’s my mission for the next 5 years, so...

Mark Alan May - Citigroup Inc, Research Division - Director and Senior Analyst

It’s probably a good place to stop. Thanks, Mark. Thanks, Alan.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Sorry. Yes, thank you.

Alan R. Pickerill - Expedia, Inc. - Executive VP & CFO

Thank you.

Mark D. Okerstrom - Expedia, Inc. - CEO, President & Director

Yes, thank you.