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# EDITED TRANSCRIPT

EXPE - Q2 2016 Expedia Inc Earnings Call

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**OVERVIEW:**

EXPE reported 2Q16 adjusted EBITDA of $331m.





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## PRESENTATION

**Operator**

Good day and welcome to Expedia's Q2 2016 earnings call. Today's conference is being recorded. At this time I would like to turn the conference over to Mr. Alan Pickerill, Vice President - Investor Relations at Expedia. Please go ahead, sir.

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**Alan Pickerill** - *Expedia, Inc. - VP-IR*

Thank you and good afternoon. Welcome to Expedia, Inc.'s financial results conference call for the second quarter, ended June 30, 2016. I am pleased to be joined on the call today by Dara Khosrowshahi, Expedia's CEO and President; and Mark Okerstrom, our CFO and EVP of Operations.

The following discussion, including responses to your questions, reflects management's views as of today, July 28, 2016 only. We do not undertake any obligation to update or revise this information.

As always, some of the statements made on today's call are forward-looking, typically preceded by words such as we expect, we believe, we anticipate or a similar statement. Please refer to today's press release and the Company's filings with the SEC for information about factors which could cause our actual results to differ materially from these forward-looking statements. You will find reconciliations of the non-GAAP measures to the most comparable GAAP measures discussed today in our earnings release, which is posted on the Company's IR website at IR.ExpediaInc.com. I would encourage you to periodically visit our Investor Relations site for important content, including today's earnings release.

As a reminder, we sold our 62.4% ownership stake in eLong on May 22, 2015, which was previously a consolidated entity of Expedia, Inc. For GAAP accounting purposes the results of eLong our included in our results through the date of the sale. In order to allow investors to compare our current results on a like-for like basis with our historical results, our commentary earnings release and on this call is principally focused on our results excluding eLong, which should be considered in addition to the GAAP results on a fully consolidated basis.

Finally, unless otherwise stated all references to cost of revenue, selling and marketing expense, general and administrative expense and technology and content expense also exclude stock-based compensation and depreciation expense, and all comparisons on this call will be against our results for the comparable period of 2015.

With that, let me turn the call over to Dara.

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Thanks, Alan. The second quarter was one in which the strength and breadth of the Expedia, Inc. range of businesses really shone through. Trivago continued to grow scale and gain share in the global travel advertising market. The HomeAway transition and the Orbitz migration each continued to progress well and deliver ahead of plan. Egencia continue to execute on its near-term objectives while remaining on track to deliver on sizable long-term potential.

And although we delivered nicely against our profit objectives with adjusted EBITDA of 18% to $331 million, we did see room night growth decelerate more than we're satisfied with. I'll touch on each of these factors in a bit more detail.

Trivago topped $200 million in standalone revenue this quarter, for growth of 41% or 38% currency neutral. On a trailing 12-month basis, Trivago generated over $660 million of revenue and has become a leading scale player in the travel advertising space while building profitability.

A little bit of perspective here. We have grown Trivago revenue nearly sixfold since 2012, when we partnered up with the founding team. And today Trivago's TTM revenue is greater and growing faster than TripAdvisor's when we spun off that company.

I'm sure investors are wondering about the put/call arrangement that we have in place with the Trivago founders, so let me update you now. Neither Expedia nor the Trivago founders exercised their option under the open put/call window this year, and we have instead agreed to explore the feasibility of an IPO of Trivago shares with the preliminary and ambitious goal of completing the IPO before year end.

An IPO would allow investors to value Trivago as a separate standalone company. Note that this is an IPO and not a spinoff. Expedia does not plan to sell any of our shares in an IPO, and there are no guarantees that an IPO will ultimately be pursued or be successful. The put/call window could reopen in March 2017 if an IPO is not completed by then. And due to legal limitations, our ability to comment further on an IPO or on future performance is extremely limited.

Therefore, we will not be updating or otherwise commenting on our outlook for Trivago for this quarter or beyond, or answering related questions on the call.

The HomeAway transition continues to go very well. We have now implemented the traveler service fee in all major markets, allowing us to increase investments in technology and product as well as marketing in order to build our brand globally. HomeAway Q2 revenue grew 36% year on year on a pro forma basis, driven by strength in both subscription and transactional revenue. And based on current trends, we expect revenue growth to accelerate in the second half of the year.

Although this transition is not easy, we believe the pivot from pure classified advertising to a travel e-commerce business is a winning plan that will allow us to create better products for consumers and drive more bookings through our homeowner and property manager partners. In addition, as we move more of HomeAway's business to online bookable, we will be more aggressive in offering HomeAway inventory on our OTA brands, which will drive even more booking volume and will give our huge global customer base more places to stay.

The Orbitz migration is running nicely ahead of planned timelines with Orbitz and CheapTickets apps as well as the e-bookers site and app now on the Expedia platform. And the migration of the Orbitz for Business clients on to the Egencia platform is complete. Although we still have some migration work to do with a number of Orbitz Partner Network customers, something that will continue into 2017, we are pleased that the heavy lifting of the Orbitz Worldwide integration is largely behind us. Orbitz generated a healthy $54 million in adjusted EBITDA, representing a margin of approximately 28%.

Given the speed with which we have executed the integration, we are incrementally optimistic about the delivery of Orbitz-related synergies in the back half of the year.

Now, the good work on the Orbitz front did, however, come at an operational cost with our room night growth decelerating more than we planned. The weight of the Orbitz book of business combined with other recent acquisitions and organic growth in our core business strained our infrastructure and affected network quality and uptime. We have addressed the vast majority of these issues and believe that they are now largely behind us.

In addition, given the shift of the team's focus towards integration, our test and learn velocity was not where we wanted it to be, and our conversion rate increases slowed on a year-on-year basis versus prior quarters. The result of this included a slowdown in the metasearch channel not only due to continued weakness at TripAdvisor, partially due to Instant Book, but also Trivago, where we saw our click share decrease.

With the largest part of the Orbitz integration now complete, the teams are back to core execution mode with focus on regaining momentum on the conversion and marketing fronts. We're operating in a very dynamic and competitive market and are no strangers to speed bumps along the way. And we continue to expect to deliver a strong year for the Company.

Now I will turn it over to Mark on the financials.

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**Mark Okerstrom** - *Expedia, Inc. - CFO and EVP-Ops*

Thanks, Dara. The adjusted EBITDA of $331 million that we delivered in Q2 was a solid result. From a brand perspective we saw good results relative to our expectations on Hotels.com, Egencia, Expedia Affiliate Network and Travelocity. And as Dara mentioned, the profits delivered by the Orbitz brand so far in 2016 have been better than we had expected. The HomeAway and Trivago teams are also executing very well and delivering great results.

Hotel revenue grew 14% in Q2 on room night growth of 20%. Orbitz contributed approximately 8 percentage points of room night growth for the quarter. In addition to the factors Dara described earlier, lower organic room night growth in Q2 compared to Q1 was also driven by the shift of Easter into the first quarter this year and a small impact from Leap Day in Q1, which, if normalized, which have reduced room night growth in Q1 by about 3 percentage points and increased Q2 by about 1 percentage point.

There have been a number of terrorist attacks in recent geographies over the past months. When isolated events occur, we historically have seen an immediate reduction in bookings and an increase in cancellations for the impacted destination. Typically, most of that demand gets diverted to other destinations. And over time, normal travel patterns seem to return.

Though we are hopeful to see the same patterns repeat themselves, the frequency of recent events is giving us reason to be incrementally cautious. This is something that we will continue to monitor as the year progresses.

Average daily rates declined less than 1% in Q2 and revenue per room night decreased by about 5 percentage points. The gap between the two narrowed again this quarter, down to 440 basis points compared to about 540 basis points in Q1. We saw continued broad strength in our other product lines with air tickets up 45% and rental car days up 36%. Note that Orbitz added 30 percentage points to ticket growth and 24 percentage points to rental car days in Q2. Our ad and media revenue grew 42% on solid performance for both Trivago and our Media Solutions group.

From an expense perspective, setting aside the inorganic components from HomeAway and Orbitz, we saw leverage in cost of revenue again this quarter as the teams continue to drive efficiencies. You will see that the year-over-year organic growth in direct and selling and marketing expenses was lower in Q2 than in Q1, partially in conjunction with the lower topline trends with variable performance-based marketing making up a large portion of this expense category.

We did, however, see an elevated pace of growth in technology and content expenses, as we had expected, driven by an increase in costs to support Orbitz integration efforts and growth in the core business, accelerated hiring as we brought Orbitz team members onto our Brand Expedia team early this year and expenses associated with the migration of certain functionality to the cloud. We expect the growth in tech and content expense to remain elevated but to begin to moderate in the back half of year. G&A expense grew a bit faster than revenue this quarter on some discrete legal and professional fees. Note that we are expecting to see leverage in G&A expense in the back half of the year.

Turning to our financial expectations for 2016, on a consolidated basis excluding eLong, we continue to expect full year adjusted EBITDA to grow 35% to 45% year-over-year. We do think that the contribution to full-year adjusted EBITDA for Orbitz and HomeAway combined will be higher than our previous expectations with a relatively lower contribution from the rest of the business.

Please note, however, that we are forecasting modestly improved organic room night growths in the back half of the year, and if that does not occur we would likely see full year adjusted EBITDA growth closer to the lower end of the stated range.

In terms of the shape of the back half of the year I would just remind you of some discrete items that will favorably impact Q4 results. Orbitz synergies will be close to full run rate and we will get a full quarter benefit from HomeAway in the fourth quarter. We will also be comping the Paris attack, significant deal-related costs and the purchase accounting impacts of deferred revenue for both Orbitz and HomeAway.

Before closing, I did want to give a bit more color regarding the buildout of our new corporate headquarters slated to take place over the next few years. In March this year we had indicated that capital outlay for the full buildout could run in a range of $1 billion to $1.2 billion. Since then we have looked more closely at the design with a focus on budget and phasing, and we now believe we can have the property ready for use in 2019 for something closer to half of the previous estimate. We expect to share more details as those plans are finalized.

With that let's open it up for some questions. Operator?

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Naved Khan, Cantor Fitzgerald.

**Naved Khan** - *Cantor Fitzgerald - Analyst*

I've got a couple of questions. So, Dara, you touched on the slowdown in the room night growth and how resources being devoted towards Orbitz could have contributed to that. Can you share some more details on what exactly was affected so that we can get some degree of comfort that this is more of an internal operational issue versus some competitive dynamic?

**Mark Okerstrom** - *Expedia, Inc. - CFO and EVP-Ops*

I'll take this one. Let me just bridge you from the [Q1] organic room night growth of 24% down to 12% and give you a sense of it.

First of all, at the time of our Q1 call we were expecting a deceleration of somewhere between 500 and 700 basis points. The majority of that was coming from Easter, as I mentioned in my prepared remarks. And we were also lapping over some significant ramp up in both the Wotif and Travelocity businesses, Travelocity because we had taken over control of sales and marketing after the acquisition and Wotif because we had them on the platform. And then the law of large numbers, et cetera. So that was what we had expected.

We did -- I mentioned in a few investor conferences in May -- that we had seen some slowdown and signaled that we were seeing a little bit more. And really, the majority of that incremental slowdown, we believe, is self-inflicted.

There were a couple of big drivers there. One is we did have some network and infrastructure stability issues really focused in the first half of the quarter. A lot of this was driven by just organic growth in the business but also as we moved the Orbitz book of business on to our network infrastructure, it wobbled a little bit and it took us a while to get it stabilized. The good news is that it is now stabilized and the teams have done a great job getting that back on track.

The second self-inflicted wound, if you will, was a decision we had made really to divert the vast majority of the Brand Expedia team, tech and product resources, towards the integration effort -- and to good result. We've actually got the Orbitz brands onto the Expedia platform faster than we had expected and we are seeing the financial benefit of that. The cost, however, was that our test and learn velocity, in terms of the rate at which we were testing and releasing new features, was slower on a year-on-year basis than it would have been the same time last year. And that has an impact on conversion.

And when you impact your conversion, it impacts not only the transactions that are coming to you directly but also in variable channels. And Dara mentioned the slowdown that we were seeing in the metasearch channel.

So that was really the majority of that call it 500 to 700 basis points of incremental slowdown beyond that which we had expected. The rest of it -- it's very difficult to pinpoint. Certainly, we do remain in an intensely competitive marketplace. And any time we stop the innovation pace, we have competitors that are very quick to respond and take share. And we certainly did see that in the metasearch channels.

Also, it's really hard to read the news and see what's happening in the overall geopolitical environment, particularly with the terrorist attacks and the frequency of the recent terrorist attacks in Europe. And even though we can't pinpoint an overall impact exactly on that, it wouldn't surprise us if that is having some impact as well.

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**Naved Khan** - *Cantor Fitzgerald - Analyst*

Okay, that's very helpful. And then just to follow up on your answer, if I look at the room night growth by geography, it seems like the slowdown in international room nights was more pronounced. Is there anything to call out there?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Yes. I think, in general, international points of sale have a higher concentration in the metasearch channels than the domestic points of sale, where we have bigger brand traffic. And, of course, the macro environment could be affecting international more. The last is actually a comp issue, which is we had brought in or consolidated Brand Expedia, the joint venture with AirAsia last year at the same time, so you are just seeing a comp effect there.

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**Naved Khan** - *Cantor Fitzgerald - Analyst*

Got it. The second question I had was really around the HomeAway integration. I think, Dara, you talked about how you can start to offer up some of the HomeAway inventory into the core Expedia. Can you talk about the timing of that and when we can start to see that?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

We don't have specific timing at this point on it. The real focus for HomeAway right now is to build up the online bookable muscles. And we are really, really pleased with the progress there, over 1 million online bookable listings, overall listings growing at 20% plus, actually accelerating versus how fast listings were growing there.

That's the focus right now of the HomeAway team, and then taking some of that revenue and reinvesting in marketing to make sure that our homeowners and property managers get plenty of traffic.

We will have more to say about distribution on Expedia and Hotels.com and all of our other brands. So, stay tuned there.

And I think, in general, the theme that you should look for is a much deeper integration of the HomeAway inventory onto the Expedia platforms, in general. Prior, when we worked with HomeAway as partners before, the integration was more of a link-off experience. It was a little bit of a shock for users.

And this HomeAway inventory is going to be fundamental to our product on a long-term basis. So we are making the kinds of investments that we have to, to make sure that the integration is perfect and our clients who are online bookable and especially instant bookable get plenty more traffic the way they want that traffic.

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**Naved Khan** - *Cantor Fitzgerald - Analyst*

Thank you.

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**Operator**

Brian Fitzgerald, Jefferies.

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**Brian Fitzgerald** - *Jefferies LLC - Analyst*

I want to know if you could give us any initial feedback on the Facebook Dynamic Ads that I think Trivago is running for travel. Are they running across Facebook and Instagram? And then maybe any initial comments on your traction with the Messenger bot?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

As far as Facebook, the Dynamic Ads go, we are experimenting and really starting to scale up with Facebook across our brands on a global basis. The spend there is now getting to real significance. And our engineering teams have been working with the Facebook engineering teams in a very productive way. And basically all of the brands are experimenting with Facebook and finding veins, both traffic and conversion veins, that are awfully interesting.

So our spend is up significantly. It looks like it's working and we think that the momentum there will continue. You certainly see it in the Facebook results.

As far as the Facebook Messenger bot, I think it's too early to tell. It's a promising technology. I think messaging technology in general, whether on Facebook or other platforms, is something that we are quite interested in, both in terms of messaging itself and the platform and in terms of AI and machine learning that we can build in behind it to radically improve customer experience.

So at this point, so far so good. But it's not something that we've scaled yet.

**Brian Fitzgerald** - *Jefferies LLC - Analyst*

Got it. Thanks, guys.

**Operator**

Mike Olsen, Piper Jaffray.

**Mike Olsen** - *Piper Jaffray & Co. - Analyst*

In the HomeAway business, how would you describe any impact that you are seeing on booking rates as a result of the booking fee? Based on the results and the qualitative guidance you gave for HomeAway, it seems that the answer is probably minimal. And then do you believe that you are seeing any impact on either HomeAway or your core OTA business from alternative accommodation sites at this point?

**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

I'll answer the second one first, which is that the HomeAway results have been pretty great. So we expected to be bringing in a really strong company, and we wrote a big check to bring in HomeAway. And I'd say so far the results have been better than expected. So I think that this alternative lodging space is -- it's just a big space.

And HomeAway is benefiting from that, and obviously Airbnb, which is the other big player in the category, is clearly benefiting from it as well.

The reaction -- when we did bring in the booking fees, etc., we did see a conversion decrease initially. But the great news is that the team, the HomeAway technology team -- now they have got traffic and they are able to optimize the site in a way that they were not able to. So conversion is actually up on a year on year basis, because of the optimization work, because of the feature work that the teams are embarking on. And I think that that momentum is going to continue for some period of time.

When we look at HomeAway conversion versus, let's say, Hotels.com or Expedia conversion in like destinations, HomeAway conversion is far lower. So, we think we've got plenty of work to do there. And we think that we have got plenty of upside there.

The other factor that we want to look at is subscription renewals and subscription renewal rates. And again, things look good there. So I think, anytime you change your model you introduce some uncertainty into the marketplace, we've had to overcommunicate to our homeowners and our partners, but I think now we are settling down and we can both build a great business together.

**Mike Olsen** - *Piper Jaffray & Co. - Analyst*

Thank you.

**Operator**

Lloyd Walmsley with Deutsche Bank.

**Lloyd Walmsley** - *Deutsche Bank - Analyst*

I'm wondering if you can just attribute any of that organic slowdown in room night growth to the hotel effort at loyalty pricing discounts and the ad campaigns supporting those. Are there markets where there may not be enough independent supply to backfill and replace what the chains are doing?

And as a follow-up to that, when you take a step back and look at the magnitude of some of the discounting they are doing and you listen to Marriott on their earnings call this morning talking about seeing net pressure on ADRs from what they are doing, how do you guys think this plays out? Do they keep doing this at a net loss to themselves? Or do you think, ultimately, they pull back on this? Would love your perspective on that. Thanks.

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Listen, it's very difficult for us to speculate as to what the Marriotts and the Hiltons of the world are going to do. These are really smart, big companies and they are making their own decision. I think the question that you asked about is it affecting us is clearly a question that we asked ourselves because we saw the slowdown in room nights. And we have 18,000 statisticians looking every which way at every angle to see whether it has affected us.

The short answer is that we haven't seen any real correlation in our performance in chain-heavy markets versus chain-light markets. You would think that in a market that has lots of chains, you would see some conversion degradation or performance degradation to the extent that inventory quality is lessening. But we haven't seen any of that whatsoever. It may happen, it may not happen. But to date we have not seen any correlation at all.

What we have seen is we have seen a shift of our bookings from some of the chains that are discounting to independents and/or chains that are not discounting. So there has been, certainly, share shift and maybe that was affecting Marriott ADRs. And the share shift actually, in an interesting way, is giving us some margin upside. So from that standpoint, that has not been bad, although we are not necessarily managing for margin.

I think the other perspective as to whether they are going to continue or not is, we attract brand-agnostic travelers as far as what hotel they are staying at or what chain they are staying at. And actually like if you look at Hotels.com on a global basis, the biggest chains in the world, the largest hotel chains, get less than 0.5% of searches on the Hotels.com site.

Just to make sure you understand that, someone who comes on Hotels.com, less than 0.5% of them are searching for a specific large brand out there. So these are folks who want a great hotel in Paris, and it's a terrific opportunity for great hotels in Paris to stand up and to market themselves to someone who hasn't yet become loyal to a chain.

And we have partners who are, at this point, standing up. The economy is a little bit weaker than it has been before. So we are seeing some promotional activity and discount activity. And so far we are satisfied with the quality of inventory.

Now, we will watch this. The big chains are marketing aggressively. So as far as competitive brand marketing activity, probably not good for us. But we haven't seen any direct effect as a result of their actions. And we will work with them because we definitely want to grow with the chains. We think that's a positive way to grow going forward, and we continue to have promising dialogue with them.

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**Lloyd Walmsley** - *Deutsche Bank - Analyst*

Thanks a lot.

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**Operator**

Tom White, Macquarie.

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**Tom White** - *Macquarie Research - Analyst*

Just on your comments about the trajectory for room night growth for the balance of the year, I heard some things about you are guiding to improvements but also heard some comments around terrorism fears and the macro, so trying to reconcile those two things. And then just on Brexit and terrorism, could you just give a bit more color on what you are seeing in terms of changes in traveler behavior? Are you seeing increases in cancellation rates? Are you seeing people book travel in other areas? Any kind of color you can give there would be great.

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Sure. Happy to, Tom. So with respect to the trajectory for room night growth, if you look at what I said around the self-inflicted piece of what we saw in the second quarter, half of the call it 500 -- around half the 500 to 700 basis points of decel that we had not anticipated is self-inflicted. And the chunk of that is related to the network instability and infrastructure that we have now solved.

So we are expecting to, through the back part of this year, work our way and claw back that piece of the business that was self-inflicted, both as network infrastructure issue, also as we ramp up test and learn velocity and get year-on-year conversion improvements back.

Against that, I guess, plan, if you will, that we are executing against, things that are in our control is this backdrop of just the increasing frequency of terrorism. And to put some numbers on it, historically we have seen these destinations that experience these types of terrible things drop, and then they pop back in a matter of weeks if not months. But if you take France as a destination, for example, which has had just a terrible go of it, room night growth pre the most recent Paris attacks was in and around the mid-20s. After the Paris attacks it settled out into low single digits. As soon as Brussels happened, it hit negative single digits. And since Nice it has been down double digits, like mid-20s.

So, we have not seen the recovery in France. And so, though we are hopeful that we will see a recovery, just the pace of this has got us into uncharted territory.

Now, the upside of this is that we are seeing places, particularly places in Spain, Ireland, etc. -- we are seeing increasing volume there. Clearly, people are shifting the places that they are traveling to. But we are cautious that this could just put a negative tone just on -- overall, at least European travel trends.

Just to touch on Brexit quickly, which was one of the other things you mentioned, the Brexit response was similar to what we see anytime we see currency moves. And it was really currency related. As soon as the pound devalued versus the US dollar, we saw bookings, particularly into London out of the US, increase pretty significantly. But beyond that, we haven't seen a significant impact. And I think for now we are not expecting to see one.

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**Tom White** - *Macquarie Research - Analyst*

Thanks.

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**Operator**

Jed Kelly, Oppenheimer.

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**Jed Kelly** - *Oppenheimer & Co. - Analyst*

Can you discuss the mix of listings that are incurring the HomeAway traveler fee between professionally managed properties and single-owner units? And is one group outpacing the other in terms of overall bookings growth?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

I'd say that in general the professional managers group is probably engaged a little more quickly. They've got a bunch of volume and they are leaning forward into the traffic growth that HomeAway is delivering now.

But we continue to work with our individual owners. They are an incredibly important component of our marketplace, and we see excellent progress in bringing them online and making them online bookable.

So it's a process. It's a communication and education process. And I'd say so far, so good.

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**Jed Kelly** - *Oppenheimer & Co. - Analyst*

Thank you.

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**Operator**

Heath Terry, Goldman Sachs.

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**Heath Terry** - *Goldman Sachs - Analyst*

A couple of questions -- I realize that revenue and bookings are not directly tied together. But curious if you could give us a sense of what drove revenue performance above booking growth -- organic booking growth. Obviously there's a lot of noise about cutting commissions and other things going in the space. So, curious if -- what it was that drove that outperformance.

And then on the HomeAway piece, do you have any sense of what kind of an impact, if at all, the booking fee has had on gross bookings on the site? I understand you don't report a gross bookings number for HomeAway, but if you could just quantify for us your best feeling for where that is.

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**Mark Okerstrom** - *Expedia, Inc. - CFO and EVP-Ops*

Sure, Heath. So simple answer on the first question is that both HomeAway and Trivago report into revenue and not into bookings. So you've got inorganic at HomeAway dropping directly into that and then Trivago organic revenue growth, obviously very strong and faster than the overall business with no bookings offset. So that's the big driver.

In terms of gross bookings on the site of the impact of the booking fee, we generally are seeing very strong results there. As a reminder, we now have 1 million online bookable properties, so more transactions are coming online.

Last quarter we actually reported a booked transactional revenue number, just to give you a sense of it. And what that represented is essentially the revenue that HomeAway derives from bookings that happen online, on a booked basis. Recognition happens on stay.

That number this quarter was well north of 200% year over year. So we are seeing really strong results there and we are able to actually put that increased volume and increase revenue that HomeAway has back into the business. And one of the most significant investments that HomeAway has been making is not only in product and technology to make the experience better for both owners and managers as well as consumers, but they have put a significant amount of money back into sales and marketing.

In fact, the first half of this year, direct sales and marketing spend up over 80% year over year. So we are really creating this flywheel, and it just seems the more volume we create, the more attractive online bookability becomes for owners and managers. And we are starting to get real traction there that we are very pleased to see.

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**Heath Terry** - *Goldman Sachs - Analyst*

Great, thank you.

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**Operator**

Michael Millman, Millman Research Associates.

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**Michael Millman** - *Millman Research Associates - Analyst*

Following up on an earlier question, the travel industry has typically argued that people will travel, particularly for leisure, always, regardless. So the question is, is it the -- is this true? Are you seeing this? And if so, where are the people going? Or, to put it another way, who in the industry are winners currently -- which is a difficult way to think of it, but nonetheless --

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Great question, Mike. What I'd tell you is that this is an unusual time where uncertainty and the kind of terrorist activity that we are seeing seems to be happening at an unprecedented rate.

Historically, whenever we've seen something happen locally, there has been a reaction. There have been significant cancellations and then you have a couple of weeks of call it business being -- running below normal.

And usually you see the patterns of travel work around the uncertainty or the interruption. So as an example, presently, we see Spain as a destination being incredibly strong. Why is that? It's obviously because France as a destination is weak. Turkey is weak. A bunch of other summer sun destinations that Europeans used to travel to are down. So, Spain is really strong.

Now, with all the activity here, is that having an overall effect on the travel market? I can only say maybe. We don't see it in general. Historically we've seen travel grow at GDP plus 3% to 4% and we've seen online travel grow faster than that.

We've got exposure to Asia in some markets, which make our growth rate even significantly higher than the overall travel growth rate. And I expect more of the same.

There may be a general slowdown. I wouldn't predict it because we haven't seen it before. But even if there is, we think companies like ours, companies that are strong on technology and customer and brand side, can grow through any kind of these interruptions.

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**Michael Millman** - *Millman Research Associates - Analyst*

So bottom line is you are saying locations may change and the strong will get stronger?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Destination is destination. Mix absolutely changes. But usually the person who wants to go on a summer vacation goes on a summer vacation.

If there's a general trend that I'd say is that usually when you see periods of uncertainty you see people staying closer to home. So, as opposed to going on that long trip or going -- Americans going to Europe, they will take their summer vacation in the States, if there's any pattern to that. But we are relevant for that and I think a lot of other companies are relevant for that kind of service as well.

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**Michael Millman** - *Millman Research Associates - Analyst*

So the biggest potential losers may well be the airlines, because --

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

It's tough to tell. I think right now the airline issue is more about capacity than demand, but I guess the two are certainly related.

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**Michael Millman** - *Millman Research Associates - Analyst*

Okay, thank you.

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**Operator**

Chris Merwin, Barclays.

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**Chris Merwin** - *Barclays Capital - Analyst*

I just had a couple. Dara, you talked about scaling up your ad dollars on Facebook. Can you talk a bit about how the ROIs on Facebook compared to what you are currently getting on Google, maybe just on a relative basis, and how we should think about the shift in marketing spend should impact you guys from a margin perspective in the near- or long-term?

And then secondly, as it relates to the traveler fee rollout on HomeAway, I imagine that's still going in line with your expectations now that the pricing change has been fully rolled out. But at some point, does it make sense to also include online payments as part of the lower-cost price option on HomeAway to maybe further accelerate the pace of that traveler fee rollout?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Sure. As far as the scaling up of ad dollars on Facebook on ROI, that's competitive information that we won't get into. But we are working with Facebook on a variable basis. We've got a bunch of data scientists looking at the return, and we would not be scaling up our spend on Facebook unless it was getting us more than satisfactory results.

We will look to maximize spend on an affordable basis in any variable channel, which includes Google, includes meta-search and now, more and more, it's including Facebook as well.

As far as the travel fee rollout in online payments, can you explain a little bit more what you are asking about?

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**Chris Merwin** - *Barclays Capital - Analyst*

Sure. Just to fully implement the traveler fee, I imagine a listing has to be not only online bookable but online payable. And I believe, and correct me if I'm wrong, that people can pay the lower cost option at HomeAway to have their listing online bookable, but it doesn't also mandate that it's online payable, which I imagine is a prerequisite for having a traveler fee.

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Yes. I think on the -- certainly, the two go together. And we are working to introduce more payment methods, online payment methods, especially on the international front -- PayPal, all kinds of credit cards, etc. And we are also looking to build out products like the traveler guarantee for HomeAway that incents travelers to book essentially on system because there are some bookings, obviously, that go off system, which is two people talking to each other and writing a check and hoping that the check lands someplace.

So we think that we can create a safe and cheap environment for consumers to come together with homeowners within the HomeAway platform, and we will be looking to optimize that a go-forward basis.

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**Chris Merwin** - *Barclays Capital - Analyst*

All right, thank you.

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**Operator**

Ron Josey, JMP Securities.

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**Ron Josey** - *JMP Securities - Analyst*

I know we have talked about this a little bit. But maybe on the Orbitz integration I'm wondering, Dara, what was different with integration of Orbitz versus that of Travelocity and others you've done, in which you saw the disruption in the core business and took your eye off the test and learn thesis or really process that you've been doing for some time? Just because I was somewhat surprised to see that this quarter.

And then, bigger picture, talking about HomeAway, can you talk a little bit more about where you are with adding urban inventory to the mix and when that might come into play? Thank you.

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

As far as Orbitz goes, the Orbitz integration was fundamentally different from Travelocity because, if you remember, Travelocity initially was a technology integration as it related to that asset, which was owned by Sabre. So Sabre really had to work with a bunch of the -- had to deal with the headcount issues, the employee issues. And we just had to deal with the technology integration. Orbitz coming in was not only an integrating technology but also took the efforts of lots and lots of people across the company because we were essentially bringing the company in. So that's one.

The second is that Orbitz is a number of brands. It's not just Orbitz, it's the ebookers brand, and we closed down HotelClub in Asia. We are integrating the Orbitz Partner Network and Orbitz for Business. So it is a substantially larger and more complex integration than the Travelocity integration.

And I do think that another factor is that, listen, we brought in Travelocity. We brought in Wotif and we brought in Orbitz. I don't know what the total time between those three integrations were, but it's three integrations one after the other. And I think that probably each integration maybe not just backed by 5% or 10%. And the 5% or 10% started adding up with the last integration, the Orbitz integration, being the biggest one and the most challenging one.

Super, super proud of the Company for getting it done. We knew that it was a challenge through the second quarter. And we said, you know what, let's put our heads down to get it done so we can get back to core execution. And we are there. And expectations for us internally are high. We think that we're going to execute. We have before and I think we will again.

As far as HomeAway inventory adding urban inventory to the mix, we are looking at adding inventory all over. I do think that our strengths tend to be in the resort area as far as sun destinations, mountain destinations, etc. But we are adding urban listings as well. And I think that as we integrate more fundamentally with Hotels.com, Expedia, Travelocity, Orbitz, the pace of urban listing acquisition is going to increase.

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**Ron Josey** - *JMP Securities - Analyst*

Great, thank you.

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**Operator**

Perry Gold, MoffettNathanson.

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**Perry Gold** - *MoffettNathanson - Analyst*

Are you guys seeing any early upside from your Accelerator program at this point? Is that where the improving trajectory in ADR and revenue per room night growth is coming from? Thank you.

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**Mark Okerstrom** - *Expedia, Inc. - CFO and EVP-Ops*

We are seeing upside. Again, I think it's early. There's still a lot of training to do and a lot of behavior for hoteliers to learn. But we are seeing great uptake. We have got thousands of hotels that are actively using the tool and we expect that it's going to go up significantly from there. The hotels that use it are finding exactly what they might expect, which is they are getting incremental volume when they need it at an overall yield which is attractive to them. So we are very pleased with it and I think there's more to come.

Not a big factor in the revenue per room night and ADR story at this point. The narrowing of the gap there is really largely due to the reasons that we predicted, is that we are getting to the end of our margin reduction strategy here and we are starting to see just better trends there. And that's something that we do expect to continue here over the next little while.

And the last thing that has helped that is something that Dara mentioned, which is, we are seeing a mix of our business towards independent hotels that are taking advantage of our marketplace and taking advantage of really the less attractive pricing that in many cases some of the big chain partners are providing to our consumers.

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**Perry Gold** - *MoffettNathanson - Analyst*

Thank you.

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**Operator**

Justin Patterson, Raymond James.

**Justin Patterson** - *Raymond James & Associates, Inc. - Analyst*

In terms of just sales and marketing, that came in quite a bit better than I think we were all expecting this quarter. And you also mentioned there was some room night growth deceleration around integration efforts. But have you been able to parse out just whether or not backing off the accelerator on marketing expense slowed room night growth? And is there a trade-off between spending for growth here that we should be thinking about?

And then, secondarily, on Europe you mentioned the metasearch factors being a part behind the deceleration there as well as the macro part. Is there any changes on the meta side you are perhaps contemplating, given those results?

**Mark Okerstrom** - *Expedia, Inc. - CFO and EVP-Ops*

Sure. So the vast majority of our direct sales and marketing is variable or performance in nature. And in a sense it's autoadjusting, which is when we have lower year-on-year conversion gains, as Dara mentioned, we had seen particularly at Brand Expedia, we automatically essentially adjust and pull back a little bit because we are very focused on making sure that we maintain the appropriate profitability.

And, that said, those channels themselves are the least profitable channels that we have. And so when we do have a slowdown in conversion, it does translate into room night growth. And the first channels to go are the ones that are most expensive. So there's a natural offset or a natural hedge that we see in our P&L.

With respect to macro and the challenge we saw in metasearch in Europe and changes, listen, I think the biggest change is that we are very focused on getting our year-on-year test and learn velocity right back up where it should be. We are hopeful that that will improve conversion rates and then we will hopefully see the exact reverse of what we saw in the second quarter, which is room night growth accelerating back up and sales and marketing going back up with it, hopefully a little bit less than room nights.

**Justin Patterson** - *Raymond James & Associates, Inc. - Analyst*

Got it. Thank you, Mark.

**Operator**

Dan Wasiolek, Morningstar.

**Dan Wasiolek** - *Morningstar - Analyst*

Just on the HomeAway brand I was wondering if you had any thoughts on the potential impact from some cities coming out and announcing maybe stricter enforcement of home share laws and how that might impact the HomeAway brand. Thanks.

**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

From a HomeAway standpoint, we tend to have a more significant portion of our business today in destinations that are not urban destinations and destinations that are mountain/beach destinations. And these are destinations that have had this business around for a long time. These are -- the majority, the vast majority of HomeAway's business are whole homes. All of HomeAway's business is whole homes. They are usually second homes and they are usually in destinations where the home rental, the seasonal home rental business has been around for a long time and is a very significant contributor to local economies, etc.

So we are watching with interest what's going on. Every single municipality is looking at this issue in a different way. We are working closely with those municipalities. And we think, in the end, this is a product that consumers want. It attracts travelers to destinations. Travelers bring jobs, they bring money. And we think that in working with these local municipalities ultimately we will come up with the appropriate laws to protect consumers and homeowners, and the residents of those municipalities as well.

This is a process that's going to take a long time. But we are in it for the long haul. And at this point, the activity that we see is affecting us less than, let's say, some of the other players out there.

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**Dan Wasiolek** - *Morningstar - Analyst*

Thank you.

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**Operator**

Peter Stabler, Wells Fargo Securities.

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**Unidentified Company Representative**

This is actually Rob on the call for Peter. One question -- last quarter, you noted some softness I think in the corporate travel environment, in terms of travelers trading down a bit. It seems like your Egencia business actually had a pretty nice quarter and held up quite nicely in terms of bookings and revenue growth.

So, just wondering if you could give us an update on trends in corporate and also what helped drive the rebound intake rates there.

Then a quick follow-up on HomeAway, wondering if you might be able to give us an update on when we might begin to see some HomeAway inventory on other Expedia brand sites. Thank you.

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**Mark Okerstrom** - *Expedia, Inc. - CFO and EVP-Ops*

Sure. So in corporate travel, absolutely Egencia had a great quarter, so hats off to the Egencia teams for good execution there. They did get a little bit of help from the Orbitz for Business integration and they actually completed the migration of those clients now, all of them, onto the Egencia platform. So that was some of what you saw in their numbers. But they did have a great organic quarter.

They did, however, continue to see evidence of that trade-down activity, particularly in Europe. Volume held up nicely, but in general transaction values were down year on year. And so there's no significant change on that front.

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

And I think, just to add on Egencia, the Egencia team now -- they have completed largely their VIA acquisition in the Nordics and now Orbitz for Business as well. So they are a little mini case of what we described on the Expedia front. I think that team finally can look forward to really steering their attentions on innovating and building that company. And we are very excited about their position now competitively.

We have invested in their platform, in technology. And if anything, we anticipate acceleration in growth for the Egencia brand in the back half of the year and especially going to next year. So we are pretty excited about that team, where they've got into, and even more excited about where they are going.

As far as HomeAway and when we might see the inventory on the core Expedia brand, no update as of now but news upcoming.

**David Hardy** - *Wells Fargo Securities - Analyst*

Thank you.

**Operator**

Justin Post, Bank of America Merrill Lynch.

**Jason Mitchell** - *BofA Merrill Lynch - Analyst*

This is Jason Mitchell here for Justin. I was just wondering if you have any kind of updates on how you are thinking about the TripAdvisor Instant Book platform. And given all the turmoil in the travel market, have you seen any impact on your bookings through Trip? And then just a follow-up on HomeAway -- with the new pricing plan for subscriptions, do you expect it to change your mix at all of properties between subscription and pay per booking?

**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Sure. As far as TripAdvisor goes, no change as far as our view there. Obviously, we are not in Instant Book at this point. We think the product has improved as far as the brand representation of players who are working with Instant Book. And so we will be in dialogue with TripAdvisor when we can, although I wouldn't expect anything to happen soon.

As far as the HomeAway new subscriptions and the change between PPB and subscription, I think it remains to be seen. I do think that one way or the other, more and more players are going to come online and make their listings online bookable. Whether they want to go through subscription or pay per booking is -- we are fairly neutral to it. And really we just want to make it easier for our users to become online bookable. And then, ones who have become online bookable are obviously over the long term, going to see the majority of demand in that marketplace because it's clearly what our consumers want. And ultimately we think it's going to be a win-win in this marketplace when consumer expectations are met with homeowners and property managers.

That's really what this model change is all about.

**Jason Mitchell** - *BofA Merrill Lynch - Analyst*

Great, thank you.

**Operator**

Kevin Kopelman, Cowen & Company.

**Kevin Kopelman** - *Cowen & Company - Analyst*

I wanted to ask a little bit about hotel supply growth. I think you added 25,000 hotels in the quarter. It was a very big number. Can you talk about key drivers there? Is there any seasonality? Just how we should be thinking about that, thanks.

**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Yes, I'd say on that one it's business as usual as far as adding the 25,000 hotels. It's growth of about 20% on a year-on-year basis and I think that team is just getting into a rhythm. As you know, we invested in our partner service team probably around two years ago. We really started investing in the sales team. And we continue to invest in that sales team, and they continue to deliver.

If there's any seasonality, I would say that we try to bring on a bunch of hotels prior to the big summer season when travelers are traveling. So usually at the beginning of the year, Q1 and Q2, the team really tries to sign up as many hoteliers and partners as we can. And probably during the summer we are a little more focused on managing rates and managing inventory and managing promotions so that we can deliver as much volume to our partners as we can.

But I think you should take the 25,000 as nothing unusual. It's going to be business as usual. And I think every quarter we are going to add some amount close to that number. Whether it's a little bit lower or a little bit higher really doesn't matter. I think from a long-term perspective you should look at supply addition as being a growth factor for this business. And then when we add HomeAway inventory, that will be a little bit of a boost.

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**Kevin Kopelman** - *Cowen & Company - Analyst*

Great. Thanks, Dara.

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**Operator**

Brad Erickson, Pacific Crest Securities.

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**Brad Erickson** - *Pacific Crest Securities - Analyst*

Just a follow-up from the previous question on some of the mix shifts you talked about to the independents from larger chains. Given the way you pursue those channels as targeted ROIs, to what degree might you pursue the independent segment more aggressively to capture outsized growth at the expense of some profitability in the future? Or is it more of a case of growth expectations kind of status quo but with an improved margin profile going forward? How should we think about that?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

If our business, if the fundamentals of our business had changed as a result of what's going on with the chains, we might react. We just haven't seen any fundamental change. So chain-heavy markets, chain-light markets are really acting the same as they always have. So for us it's about rolling forward with the formula that we have in place, which is adding to supply, driving conversion improvements on a site, using those conversion improvements to fund additional marketing and then keeping those new users in the marketplace through leading loyalty programs both at Hotels.com and Expedia.

So we will watch it. The margin improvements are probably going to be a financial positive. But there's not really an agenda on the margin side. We are really trying to offer the best hotel at the best rate to our consumers, and that's what we are solving for. Everything else flows from there.

I would say that in every market we are making sure that we have a wide selection of hotels that are providing us the best inventory at the best price. So we do look at market by market basis. Sometimes we will even look at neighborhood by neighborhood to make sure that where there are neighborhoods that are especially popular, we have a wide selection of hotels. We work with those hotels on inventory and pricing and promotion and sort, etc. And so far, the results have been good. And it's something that we will watch quite closely.

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**Brad Erickson** - *Pacific Crest Securities - Analyst*

That's helpful, thanks.

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**Operator**

And that does conclude the question-and-answer session. I'll now turn the conference back over to you for any additional or closing remarks.

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**Alan Pickerill** - *Expedia, Inc. - VP-IR*

Okay, great. Thanks, everybody, for joining. We will look forward to talking to you again next quarter. Dara, any closing remarks?

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**Dara Khosrowshahi** - *Expedia, Inc. - CEO and President*

Yes, just that we are very, very pleased with the activity that we see across the portfolio of brands that we have. The new additions have clearly been terrific, the HomeAways, Trivagos of the world. There's a lot of really good work going across the Company. We see the competitive environment as tougher than it ever has been. The integration work that we are doing clearly has had some execution challenges and the macro environment, it's a tough one.

But this Company has gained share year in, year out, regardless of the environment. And I think with the strategic scope that we have now, with a scope in metasearch, alternative lodging and scale that we have with the many brands that we have within our OTA business, we are better positioned than we ever have been.

So we expect excellent execution on a go-forward basis and nothing less. And I wanted to thank our employees for the great work this year and the great work coming up. Thank you.

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**Operator**

Thank you. That does conclude today's conference. We do thank you for your participation today.

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