

**2017 Technology, Internet, Media and Telecommunications Conference - Trivago**

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07:30 PM MST**

Mark Mahaney: The director of internet research here at RBC. Jim Shaughnessy and I run the internet research practice here. For our next speaker we're thrilled to have Axel Hefer. Did I pronounce that right? Hefer?

Axel Hefer: That's correct, yeah.

Mark Mahaney: Yeah. From Dusseldorf. I don't know if you're originally from Dusseldorf or not, but you're based there. He's the CFO of Trivago. So we're going to ask him a series of questions. There's a breakout right after this and we'll leave some time at the end of this for Q and A. Axel, thank you very much, danke shoen, for coming to this -- coming to our conference. This is our -- I think is our seventh, or it's our eighth. It's our eighth annual tech conference. Each session I'm going to add up that number to it.

So start off, just give us the mission, the long-term vision of Trivago. We've got a huge space called the online travel. We've had numerous players in the space -- Priceline and Kayak and TripAdvisor and Expedia and there's Trivago. And we all know the TV ads, but what's the long-term vision of the company?

Axel Hefer: So that's a big question. Let me try to be brief there. I mean, when you think about the overall travel space, where do we really sit. We sit on the search layer, so we are competing predominantly with -- from our perspective, with a general listers company called Google.

Mark Mahaney: I've heard of them.

Axel Hefer: And then some more specialized companies there. And I think the -- from a user perspective, the challenge that you're having and that will increasingly be solved over the next couple of years is that the accommodation search is very complex. So just to look for hotels is already very complex compared to flights, et cetera, so us coming from Dusseldorf to New York, we know what the direct connections are. We know what the best other connections are to New York. You don't even need a search for that. Hotels, absolutely impossible.

If you then add quality to it, not just a place, but the right place for the right trip, it is getting very complicated. A hotel that you liked on a business trip might not be the right one for a trip where you have some free time and want to, I don't know, go to the gym or whatever or a trip where you go with your wife. So, if you add that dimension to the search, it's getting very, very complex.

In addition, you have a change in user behavior where there are more and more users that actually are very heterogenous in their searches. So, for one trip they consider a five-star hotel. For one, they consider a private accommodation. For one, they go for a vacation rental space. So that makes it even more complicated. And our mission is to be the first starting point for users to solve that problem and to search for the perfect place, the ideal accommodation for their specific trip and then provide transparency in where ideally to book that place. And, you know, we think that there is a lot of value that is already created and will continue to be created going forward by solving that problem.

Mark Mahaney: Online travel has got to be one of the most fragmented industries like in terms of the supply base. I don't know how many hotels there are worldwide. The number's always thrown around about a million. That may be right and whoever actually proves it gets a prize. But it's somewhere. It's a big number like that. And then you throw in alternative accommodations and vacation rentals. And I think you just had some news that maybe you could go through I think with HomeAway. And so I would assume that all that leads to greater complexity. Does that create more of an opportunity for you or more of a challenge for you?

Axel Hefer: We think it's a great opportunity for us because the more complex the search becomes, the greater the value is actually that you can create by providing a tool to navigate through all the different options. And the greater the benefit is being specialized on this specific kind of searches versus being a more general search provider. In terms of alternative accommodation of vacation rentals and just non-hotel accommodation, we've been experimenting with a limited amount of properties for quite some time. And based on those tests, we decided to scale those tests further up and have integrated HomeAway as one of the largest providers of vacation rental properties and we're now gradually out there adventuring into the overall searches to go basically to the next level of complexity in our overall search algorithms.

Mark Mahaney: And just one more question on that and then, Jim, jump in on HomeAway. So, how long does this take? How much of the inventory? Like you just talked about the cadence. Will it be -- is it a year and then you'll have all of their inventory or how much of their inventory do you want to have?

Axel Hefer: We only want to have instant bookable inventory. That is key. Otherwise, the search product doesn't work.

Mark Mahaney: Yeah.

Axel Hefer: And so that limits the overall number as a starting point, but obviously, you know, everyone is working on that dimension, being it HomeAway, Airbnb, et cetera. So I think that that will be solved over time. The second thing that we consider is obviously

the description and the quality of the description. So, and the quality of the parameters that are attributed to the property. So can you actually find it and if it just says apartment 1 and the street, then it's not relevant and we will never be able to assess whether this specific property is relevant for your specific search. And so those are the two dimensions, but I mean, right now we are live with the six-digit number already, so and we'll gradually increase that at the pace that we consider being the right one.

Jim Shaughnessy: And then just to continue on this point, is building out alternative accommodations more broadly on Trivago a priority for the company? So do you see yourself adding inventory from some HomeAway competitors as well?

Axel Hefer: So, I think from a user perspective, you know, we need to provide to the user what the user wants. The user increasingly is considering these kind of options as alternatives to hotels. I mean, that's one dimension which is obviously important. The other one, more from a business perspective, is obviously the competition and the long tail of the marketplace is very important, but is also the most difficult to get. And that is a part where alternative accommodation is strategically quite interesting because it is ultra long tail, yeah. And so certain strength of certain advertisers and certain parts of the inventory can be mitigated by having a broad offering of alternative accommodation.

Jim Shaughnessy: Okay. And then from a unit economic standpoint from the extent that you're willing to go into this, I mean, is there any structurally fundamental differences between adding alternative accommodations and offering that to your consumers versus hotels?

Axel Hefer: I think time will tell. To a certain extent, you need to be fair. You need to compare it with a long tail of the hotels. You know, so because in a hotel like this it obviously has a lot of rooms is booked all the time, converting very well. So you need to go for the smaller and more nichey hotels. Conceptually, the commission is obviously very important that the advertiser is getting. You know, so if the commission for a private accommodation is much lower than for a long-stay hotel, then the ability to pay obviously and to pass part of that one as marketing budget to us is obviously low as well, but then you need to factor in also the conversion to look at the overall economics. Yeah. I think that's too early to say. But from a user perspective, it is for sure accretive.

Jim Shaughnessy: You have two very large customers, partners, you know, maybe competitors in some ways, Priceline and Expedia. And listening to the Priceline earnings call last night, you know, there was this comment about how some channels have become more competitive than channelesque and therefore they're going to switch dollars over to brand advertising campaigns. They didn't mention anybody. They were asked a couple of times about it on the earnings call. Just talk about the state of your relations now with Priceline and Expedia.

Axel Hefer: Yeah. I mean, we don't really comment on individual advertisers, but I mean in general it's a bit difficult to comment on that. We are in active dialogue with all our key advertisers on a daily basis. We've got key account managers assigned to all the important advertisers. For these two groups, there are obviously multiple people involved with the different brands. And I guess the relationships are normal, you know. So there is constant dialogue, you know, where you discuss business opportunities.

Sometimes you'll like something. Sometimes they like something, don't like something. So, but I would say that's business as normal, as usual.

Jim Shaughnessy: Okay. I think earlier this year or in the middle of the year there was a relevance assessment added to your network. So could you just explain what drove that and what the reaction and whether that's worked well or not?

Axel Hefer: So what's -- that's one of the biggest changes actually that have happened in the recent past on our marketplace. So we had -- go back a year. We had very clear rules what we would expect from an advertiser in terms of landing page experience for the users that we would pass on to them. And when you think about it, you know, the search is happening on us and so as a user you decide I want to stay in the Westin in New York. So what you expect after choosing that hotel, you expect a page where you can select options and book. You know, so you expect the book now button in a way. And that in a way has always been the clear intention of us and the clear rule.

The shortcoming of that system was that the only stick, in a way, that we had was not to allow somebody on the platform. You know, so if somebody would just give us different landing pages and with a different user experience, we could only say, "Okay. Fine. We don't accept you anymore. You have to stay off the platform." And so end of last year some of our larger advertisers realized that that is not a particularly credible threat for a sizable advertiser and started to test around with different designs which I can fully understand from their perspective, but from our perspective, that is a not as good user experience. And once you allow larger advertisers to deviate from your rules, in a way, you give them an additional advantage in the marketplace.

Jim Shaughnessy: Yeah.

Axel Hefer: And do the opposite what your strategic direction is, to make it more competitive, and in a way increase the competitiveness of the smaller advertisers, actually going the other direction. As a consequence, we had to act and we introduced the relevance assessment. And so the relevance assessment that we introduced end of last year was basically a set of criteria, what we think is a good experience and is a bad experience, and based on these criteria you would basically get a score. That then works very similar to quality scoring other searches, which is basically a modifier of the bids.

As a consequence, those advertisers that deviated significantly from what we think is ideal had to pay in a way a penalty or had to pay more to get the same. And they've done that for two quarters and that, in a way, complied with or (inaudible) complied with our guidelines end of Q2.

Jim Shaughnessy: Okay. And then there was -- as I've gone through this sort of transition, how has this change in philosophy affected the auction dynamic advertised on the site?

Axel Hefer: So, I mean, change -- it's not really a change in philosophy. I mean, our philosophy is unchanged.

Jim Shaughnessy: Right.

Axel Hefer: It's more that we just realized that there are shortcomings and saying, okay. In or out? We need to add more flexibility. Okay. You can come in, but then, you know, there was a price for it if you do these certain things. So I think the question is more how is the overall competitiveness in the marketplace changed? And there we've made some comments on our earnings call. I think what is fair to say that when we look at the current situation compared to last year that the commercialization is weaker. And where you can philosophical debates, whether it is now lower than it should be or whether it has been higher last year than it should be. But, I guess, you know, one thing that need to consider there and when you listen to these comments that we are making is that we had a significant change in the structure of the marketplace from 15 to 16 where one advertiser group has significantly increased air share air. And, you know, then that obviously helps us. So if somebody is bidding up, they need to pay for the next -- for every percentage point that you paid beyond your, in a way, natural market share, that is obviously increasingly expensive. And that's obviously -- it helps in the commercialization.

So, which in a way, long story short, we have a weaker commercialization now than we had a year ago and that is of the challenge in terms of year comps.

Jim Shaughnessy: Okay.

Axel Hefer: That's for sure.

Jim Shaughnessy: You are -- one thing that's unique about Trivago is the business model is the very strong dependency on or use of television advertising. I remember at the time of the spin there was the one question on this. Do they really have a secret sauce? How are they able to do TV advertising better than others? What's the answer? What's the core competency in TV advertising that Trivago has??

Axel Hefer: I think it's discipline to a certain extent, if I were to have to pick one word and focus. So why does it work for us? It works for us because we have been focusing it for a very long time and we've been very disciplined in testing something, analyzing the test, and then refining what we do and then doing that again and again and again. So that discipline and having complete framework how you test and how you then digest the feedback that you are getting from the test, that is very important. What we don't believe in is, you know, going to a creative agency and saying, okay, I want to spend \$50 million. Why don't you do a nice campaign and just broadcast it for three months? That's not the way we would do it or we are doing it. I mean, for us it is much more granular. Okay. This audience has worked with this spot very well. We pretested that spot, so there's a good chance that it actually will work again. We tested in one country. It works. We tested in another country. It works with that audience. And then we gradually improve it further and see that we basically buy more of what has worked well and buy less what hasn't worked well.

So I don't think it's really a secret sauce. It's really focus and discipline and then, to a certain extent, experience as well. If you've been doing it for a long time consistently, then obviously that helps a lot.

Jim Shaughnessy: Okay. And then let me ask, bringing it now to the just current fundamental trends. How do you get revenue growth to reaccelerate at the company?

- Axel Hefer: So the -- and you're talking about the year on year growth. I mean, as I said before, I mean, that we will have in a way not like for like comparisons until the third quarter 2018 and at least the first half of 2018 or '17 benefitted tremendously from the behavior or the reaction to the relevance assessment in terms of commercialization. And so that will put some blur in a way on the visibility from the outside. If you look at the underlying trend and look at, for example, two-year growth rates that we do when we are not doing our plan for next year, you see that there is fundamental growth in the business. It's just not visible because there is this additional noise in the marketplace. And so that's why are comfortable that the underlying business is growing already right now and so we'll continue to grow. Having said that, that doesn't mean that there are not initiatives that we are working on that have a positive impact on growth. And the core is obviously the product, yeah. So the more you improve the value proposition towards the user, the more likely you have users to use your product and the easier it is to communicate it. But there's nothing specific that we would like to comment on there, but they are product and marketing there are various innovations that are obviously in the pipeline.
- Jim Shaughnessy: Going back to revenue concentration for a minute, Priceline Expedia obviously a big portion of that. Do you have plans to engage the hotels more directly to make them a bigger part of the mix? Could that be one of your initiatives going forward?
- Axel Hefer: Yeah. I mean, it has been an initiative for quite some time. It's not that easy.
- Jim Shaughnessy: Yes.
- Axel Hefer: But obviously for us and also for the user, stronger activity by the, in particular, the hotel chains, would obviously be great. And so you can see that users have a higher likelihood of clicking on offers directly by the hotel than going through an OTA, so its users value a direct relationship with the hotel. So there is definitely demand. There are various reasons that hold that potential back in a way. Some are more structural. Where do the marketing budgets actually sit? You know, so in the overall hotel ecosystem. Others are on the conversion and booking technology on the websites, how optimized are the websites, et cetera. Others are on the bidding technologies that are used. So there are various challenges and we are addressing them with products that we are providing to our advertisers like an express booking, like an automated bidding. And I am very confident that over time that channel will grow, but it's nothing that happens overnight.
- Mark Mahaney: Okay. Okay. Let me ask one broad industry question and then maybe we'll ask one or two more questions and we'll open it up. We have a relatively large sized room here. We do have a breakout, but want to give everybody a chance to ask a question. Do you think there is something that's structurally changed in online travel? I don't want to put you on the spot, but I will. You know, Expedia, Priceline, you, and TripAdvisor, all four had -- the stocks have reacted negatively, but they've reacted to fundamentals, current or outlooks, that were less than investors thought would be the case. So is there something that -- is there maturity that's kicking in? Is Google in there disrupting everybody? Like what's -- do you think that there's something that's happening across the industry that investors need to know about?

Axel Hefer: It's a fair question and for us very difficult to answer, and particularly on the third quarter, because there are so many things that influence our numbers in the third quarter that we wouldn't see the underlying trend. So I'm sure that Expedia and Priceline would have a much better answer to that. I don't see from a macroeconomic perspective why there should be a big change, but, yeah, I mean we -- in the third quarter we wouldn't have seen it. I think that's for sure.

Mark Mahaney: Okay. Jim, anything else?

Jim Shaughnessy: Just going back quickly to the marketing channels, TV obviously a big portion of the mix. Maybe other marketing channels that you're focusing on or leading into and where do you see TV as a percent of the mix maybe in a few years relative to that?

Axel Hefer: Yeah. I mean, so TV is very important and in terms of delivering complex messages, it is still by far the biggest channel.

Jim Shaughnessy: Right.

Axel Hefer: Clearly. You've got other channels that you can use to supplement TV like out of home like radio, but TV has by far the biggest reach. Having said that you can see -- and it's different in different geographies that in the younger age group obviously TV usage is dropping very quickly. So online video is very important going forward, but as of today it's still a smaller channel. And our approach to the other brand advertising channels is, in a way, identical to TV. I mean, so we are running tests. I mean, those of you who are based in London probably have seen our out of home tests and in the summer did a very big test and in the UK. We analyzed the results and then we modify tests, do another test, and then gradually basically increase the spend and the frequency. And that's our approach to all the other branded advertising channels as well.

Jim Shaughnessy: All right.

Axel Hefer: All right. And will it become -- I mean, the summary, to answer your question, is really the mix will become broader and more heterogenous and brand advertisement in the years to come. I think that's clear.

Jim Shaughnessy: Any questions from the audience? Osham (phonetic).

Male 2: A couple of question. One, can you talk about how Priceline has faltered bookings (inaudible) strategies? Specifically, are they fitting (inaudible) with Expedia, for example. The ones that are non-Expedia, maybe they're bidding more there than they are elsewhere, but they're still bidding. They're still existing. So how specifically, other than the landing pages, how are they (inaudible) their strategy? Second question, vacation rentals. (inaudible) this morning. Can you talk about how you see that market kind of evolving for you guys over time?

Axel Hefer: Yeah. So I will not comment on specific advertisers, but in general, I would say that the general comment is that in the Q3 on our numbers that we've seen overall a lower level of commercialization without a significant change in the composition of our revenues, which basically means that compared to a year ago the profitability targets in a way are

different unless other things have changed in addition of our large advertisers. So it's not that there are significant improvements in their relative bidding strategies and all of the sudden, you know, the mix is changing that much. I think it's much simpler than that.

On the alternative accommodation, we've had quite some inventory already for testing purposes and now the big thing is now that we integrate a large dedicated player. That's what we announced today. Which gives us basically the next level of testing. So it's a different volume that we can test with and overall I think it will be very important from a user value proposition and from breadth of the overall long-tail offering. I don't think that it will have a very, very large share of the revenues in the near future because it is long-tail. So most of the users still go for hotels, but it is obviously growing very quickly.

Male 2: Last question. Are you seeing that (inaudible) for your advertisers only on your properties or are you seeing it on other (inaudible) track and also on Google (inaudible)? Like are you seeing it, are they doing it just -- you're saying they're doing it across the board. (inaudible) across the board, then you bring down the channel. You're effectively driving the price. You're the market major if you use the prices on the board, you know, (inaudible).

Axel Hefer: I'm not sure how we should see that. I mean, if everybody is reducing their bids 10 percent on TripAdvisor then it would look exactly the same from the outside, so I don't know. And I'm not sure how we could see that. I mean, if everybody does the same at the same time or predominantly everybody, then you can't see that. What you would be able to see is if one advertiser group is significantly reducing the overall exposure to a certain channel because they would drop in the rankings everywhere. And so I think the significant increase that we had from one advertiser group in 2016 and then the beginning of 2017. And then the normalization in terms of share, I'm not sure that we've seen exactly the same development in the other channels. But I would need to check. I'm not 100 percent sure.

Jim Shaughnessy: Okay. We've run out of time. We do have a breakout in the Gramercy room immediately after this. I want to thank Axel Hefer from Trivago. Thank you very much.

Axel Hefer: Thank you.