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TRVG.OQ - Trivago NV at Morgan Stanley European Technology, Media & Telecom Conference

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CORPORATE PARTICIPANTS

Axel Hefer *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

CONFERENCE CALL PARTICIPANTS

Sean Diffley

PRESENTATION

Sean Diffley

All right. Thanks, everyone, for joining us. My name is Sean Diffley. I'm the Internet, Media and Telecom Sector Specialist at Morgan Stanley, U.S. Very happy to have Axel here, CFO of trivago, Barcelona.

QUESTIONS AND ANSWERS

Sean Diffley

So Axel, as we're kind of coming up on the end of 2018 and heading into 2019, maybe review with us some of your kind of key learnings from '18 and some of your key strategic and financial priorities going into 2019.

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Sure. So obviously, it has been quite a ride in the last 12 months. I guess going through the year Q1, our key focus had been to stabilize overall the business with all the volatility that we have seen in the third and the fourth quarter last year. Actually, I guess, we were successful in doing. But what we realized, obviously, that it came at quite a high price. So we incurred a quite significant loss in the first quarter. And going to the second quarter with some further adjustments from our advertising happening, we felt that we needed to act and adapt to the current market dynamics. And I guess, current market dynamics, what are we talking about, I mean, there seems to be a tendency by the large players in the industry to emphasize more on profitability and a bit less so on market share gains and volume growth, which obviously, as a performance marketing channel, that we are de facto from their perspective is not a positive market environment. So we felt that we needed to recalibrate our overall activity on our marketing side to match the current market dynamic on our customers side, which we started to implement in the second quarter, end of the second quarter. And I guess, now with the third quarter being out, you can see the first effects of that. So some revenue decline, obviously, as a result of very significant adjustment and optimization on the marketing side, which we feel pretty good about, and we think that's the right direction and that we on the right track there. And, I guess, we will continue to use that level that we are -- or spend at the level that we currently are. And in the year-over-year comparison, obviously, that will have an impact for the next 3 quarters to come. In terms of then looking at next year, I guess, we are expecting growth in the second half of 2019 once we've lapped this recalibration effect and to overall improve absolute profit. At what level exactly, I guess, we will decide a bit more quarter-by-quarter. But we feel that it's a good discipline to improve the absolute profit. And while doing that, obviously, trade-off margin development versus revenue development.

Sean Diffley

All right. I guess following on from that, you clearly are emphasizing profitability over growth to a certain extent. How do you think about balancing those 2 things as CFO of the company? Where do you find the right balance there?

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Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. I think that right now we have a good base with approximately 10% adjusted EBITDA margin in the third quarter. And obviously, there are some volatility quarter-to-quarter. They are not all equal. But adjusting for that, I think we've got a good starting point. And as I said, I mean, from there, I think it is important to show absolute profit growth. And I guess we just need to appreciate that we are not growing 70% anymore, where I guess it's less important what kind of profit development you are showing, but we are a lot more in the normal profile where it becomes more important. But we don't have any firm view on how exactly that absolute profit growth should be composed or should be composed of. So to what extent which should come from revenue growth versus margin expansion or even revenue growth and margin contraction, I think is something that we decide quarter-by-quarter.

Sean Diffley

Okay. And you guys have talked about kind of the 50-50 split between branded and nonbranded traffic. How should we be thinking about kind of the changes in spend by channel? And what's going to be the rationale for maintaining that 50-50 split?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So, I mean, we always thought that approximately 50-50 is a good balance of investing into growth and growing our base. And I think that view is not unchanged or has not changed, sorry. So on the exact percentages, obviously, there is different elasticity by marketing channel, by market and by optimizing and by increasing the overall profitability targets for the different marketing channels. There is, obviously, some movement on a channel-by-channel, market-by-market basis, but I don't expect those changes to have a significant impact on this 50-50 mix. But to be honest, I mean, we will see over the next couple of quarters what the result of the optimization will be and what the (inaudible) are. But, I don't think we'll have kind of a big difference.

Sean Diffley

Okay. One of your large advertisers has talked about spending more opportunistically on performance marketing channels. Are you seeing any changes in the auction dynamics as a result of that?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Auction dynamics for us in the third quarter versus second quarter are pretty much the same. So so far there's no big change.

Sean Diffley

And then you recently talked about some meaningful product changes in 2019. I think you're going to do a redesigned app as one example. Maybe you can talk about some of the specific changes and what the priorities are as you roll these this out.

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So I will not talk about specific changes, but more about the philosophy. And so the app is just -- was one example that we showed during the earnings call to show the general idea. So the general philosophy is that we want to, obviously, give you, as a user, a tool that helps you to find or to book actually the hotel that you need at the best rate as fast as possible. But at the same time, we obviously, want to maximize your interaction with us. And as so overall, increase the efficiency of the overall product, but then capture more of that journey. Which means that we want to have you decide basically what you ultimately want to book on us, yes? And so what that means is that any kind of information that you need for your decision that is either not intuitively at the right place on our site and you click out because you can't find it or that is not even available on our site we would like to provide to you as a user, and what that will lead to, when you look at our financial metrics, it will reduce the number of click outs,



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as a consequence have a negative impact on our qualified referrals. But overall, improve the user value proposition and the seamless flow and the positive impact on the booking value and have, as a consequence, a positive impact on the revenue per qualified referral.

Sean Diffley

Actually it's the next question, on revenue per qualified referral. Maybe you could kind of breakdown each piece of that? How we should think about booking conversion, the device mix and geographic mix kind of going forward?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So on the -- let's start with the geographic mix. And rest of the world clearly has the highest growth potential. So that will have a negative mix impact on the RPQR. If you look at Americas, the higher potential is in Latin America, which again has a lower GDP per capita, lower RPQR. So also a negative mix impact. Developed Europe, I would say there is no clear mix effect in there. So overall, in terms of country mix, there will be a negative impact as in the past. In terms of device split, yes, there I'm not sure, I mean, how -- I guess -- sorry let me start again. So assuming that a user uses us as a user of us, so in a way what happens if he starts to use more devices, so somebody moves from just using his desktop to desktop plasma by phone, mathematically what happens because we will -- we don't attribute it or we can't -- [can't match] across devices, is that we will count that user twice. But obviously, he will still only book one hotel. So we double the QRs, we half the RPQR. So that is conceptually true, and that is conceptually what you have seen or what we have seen in the past and what we will continue to see. Whether a higher share of mobile traffic is necessarily bad, there I'm not so convinced. I mean, it's only bad if somebody uses you on mobile and then does the booking ultimately somewhere else. As long as the user is loyal to you and uses you with different devices, then it doesn't really matter. And there it is more a matter of the cross device matching so that you can actually match the different usage points to one full click chain that make you think that mobile is a significant disadvantage in terms of traffic quality. We would say that pretty much in most of the user journeys have a mobile element, and mobile is very important, no matter whether that specific mobile piece is showing the conversion or the desktop piece afterwards. On the -- sorry, you got 3 dimensions?

Sean Diffley

Yes, I think, just conversions. Yes, you hit on geographic.

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. On conversion, if you look at the QR versus RPQR, as I said before, the product changes are a headwind for the QR development and a tailwind for the RPQR development, same as marketing attribution where we become more and more targeted. So target, higher converging traffic, which obviously, has the same impact. And therefore, and I guess the general trends is that the QRs will continue to be under pressure and RPQR should benefit from it. On commercialization, which is then the last element of the RPQR, I guess you're, I mean, we don't plan for any improvement or any further deterioration. But that, obviously, is something that is volatile if you run an auction on a daily basis, and that can move in both directions.

Sean Diffley

Okay. Maybe you can talk about the alternative accommodation opportunity for trivago. I think you guys recently incorporated HomeAway into the platform. How that's going and how you think of that as an opportunity and are there any offsetting impacts on kind of the core businesses?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes, I mean, the alternative accommodation opportunity, I think, is a great opportunity for the whole industry, to be honest. And we are particular excited about it. And the reason why we are very excited about it is because what we see is that there is an increasing part of our user base that is

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considering various different accommodation options. And alternative accommodation is like the ultra-long tail. Yes, so you think about long-tail hotels, so alternative accommodation is then even more long tail, and as a consequence, has higher share of unique inventory, and as a consequence, has a greater value and benefit to the user to use a tool that can compare across multiple platforms. And that's not only from a pricing perspective, but also from just a visibility perspective. So conceptually for us as a search tool, that is something positive. The more users are using diverse accommodation types, the greater the value that you, as a search, can provide becomes. And that's why we are tragically very excited about it. How is our initiative going? We thought it really to focus on it last November when we announced the HomeAway integration. And since then, have integrated a bit more than 1 million accommodations. And as we said from the beginning, to us, the objective is not to show as much availability as possible immediately, but it is more to step-by-step increase the availability -- the divisibility on the platform, and at the same time, building more sophisticated algorithms that can show apartments, in particular, apartments, in a meaningful way. So yes, there is no benefit for a user if we just plug the search results with thousands of apartments. You need to increase divisibility dynamically and assess, okay, is it really relevant for that specific search for that specific trip? Or isn't it in one kind of accommodation or what kind of apartment is actually relevant. And there we are on good track and very happy with the initiative.

Sean Diffley

Is there any difference in demographics of people that are looking as a younger cohorts that's kind of looking for these types of accommodations?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

I guess, they're -- I wouldn't -- I mean, there are obviously certain cohorts that are not really keen on it. But the main user groups right now, I'd say, are intend to be either younger or families. And as a family, if you have a large family, it is increasingly difficult to find something in hotels. And so, in particular, vacation rentals become more and more relevant, plus obviously the benefit of having a kitchen, et cetera, when you have young children. So I would say those are probably the biggest use and the biggest crossover users, but it's becoming more relevant for everybody.

Sean Diffley

Okay. And maybe you can discuss the opportunity to increase your presence in hotel direct, and what tools are currently in place? Are there additional steps you can take to increase spend by hotels in that category?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So I guess we have worked with the large hotel chains for many, many years, helping them with their online marketing activities. We have activities that target individual hotels, smaller chains. So I guess we are working across various channels. We've got a property management system that smaller hotels can use to get direct access to our platform. We've got Hotel Manager tools that help the hotels to manage their content better online. So there are a lot of things we are doing. Having said that, given that there are many, many individual decision-makers and the technological complexity of that integration and also the activity, it is nothing that is really moving very fast. And it's nothing is happening really from one day to the other. So that is more a long-term project where, of course, we are very keen on helping the hotels to diversify their online marketing activities. And use us more efficiently as a direct channel.

Sean Diffley

Okay. Do you have any questions in the audience? All right. I'll keep it going. So maybe turning to margins. You'd previous talked about kind of a 25% long-term EBITDA margin. How should we be thinking about that? Is that kind of still in place? And kind of the drivers that get you there, kind of thinking about revenue and OpEx contribution margin. How should we be thinking about that?

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Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So when we came up with the long-term profitability guidance, at the time of the IPO, I guess, we were trying to get some supporting facts, because, I guess, if you're at breakeven, you can't say 20%, 25%, 30%, I mean it's a bit arbitrary. And so I guess what we looked at is okay, what is the profitability with our current overhead structure in our most profitable markets? And I guess, there we could see 25%. And the other thing that you looked at is okay what is our contribution margin, what's our variable profit in our regions, and again, there, in Developed Europe, we saw 25%, around 25%. And then, obviously, we looked at our fixed cost structure, and said, okay, with more growth and some optimization, et cetera, where could we ultimately get to. And that's how we came up with the 25% -- 25% plus. And looking at it today, and looking also at the our current performance, I think in Developed Europe, you can see that we are actually pretty close to what we said at the IPO. And I think there is more room to further optimize. So I guess on the contribution margins/return advertisement spend are probably a bit more positive on what we could ultimately achieve, whereas when you look at the overhead structure, there we are significantly away from what we originally guided to. So, I guess, there, we will probably end up a couple of percentage points higher. Putting both together, I think, 25%-plus is still realistic, and that's what we are aiming for in the long term.

Sean Diffley

You have a good look at kind of what's going on around the world. Maybe you can talk about kind of your state of the global economy right now. Any kind of, maybe pontificate a little bit, trends or places that people are traveling? And geopolitics always kind of gets thrown out as a question around does that impact people's travel habits? And with Brexit in the U.K., how are you guys kind of looking at trade in your platform?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So, okay, let me start with a part of your question that's a bit closer to the business. So, I mean, for us, you can obviously see things in the travel trends. If there is a terrorist attack somewhere, then obviously, that changes the travel patterns. Having said that, that for that specific country, only changes temporarily obviously. In terms of destination, that can have a more long-term impact. But we look at our business by origin of travel. So it doesn't really matter that much. And so if there is more uncertainty, and I don't know, in Turkey, then people travel more to Greece or vice versa. Obviously, what does have an impact from a macroeconomic perspective is consumer confidence and overall travel activity. If people travel less, then obviously, they don't need as many accommodations, and that has an impact on our volume. What the outlook of the global economy is, I'm not sure that I spend enough time on looking at that. But, yes, I guess, I mean, you are probably more of the expert than me, but there are obviously signs of whatever -- a more conservative outlook than in the last couple of years. But when exactly you will see some softening of the economy, I think is very difficult to predict. And I guess coming back to us as a company, we've got plenty of things that we need to focus on. And so we don't really focus on the global economy that much. And we have got a very high contribution margin. So I guess we are pretty flexible and react to any kind of macroeconomic change. And that will just be a distraction to think about too much about the timing of that, et cetera. So we focus more on what we can control. And there we've got plenty of work ahead of us.

Sean Diffley

Okay, maybe you could talk about your M&A strategy and what is it that you look for? I think personalization is definitely been a key area of focus. But what are kind of your criteria when you're assessing M&A?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. So M&A is, I guess, M&A has obviously plus and minuses. Clearly what's the plus, okay, if you buy something in particular in terms of technology, that you would want to develop anyway that accelerates your organic development, your organic trajectory. So that's obviously, very positive. And that is really one of the key focus areas where we are looking at our technological road map like personalization, for example, and where we are then scanning the market and seeing, okay, are there companies that would help us to accelerate what we want to build anyway. And on the negative side, as always, the distraction. So the bigger the acquisition is, obviously, the more work it is to integrate. The acquisition, the more distraction it is to the core business, the greater the expense in addition to the purchase price, obviously, it becomes. And for us, specifically, that

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is, I guess, a bit more severe challenge than for other companies. And the reason why I'm saying that is that we are very centralistic in the way we run the business. So we've got all management functions basically in Düsseldorf, and we've got developing centers in 3 other locations, but they are all close by. So in (inaudible), Amsterdam and in (inaudible). But all the decision-making, all the management of the company is really in one building. And we very much believe in having everybody close together, being able to exchange ideas very quickly and then decentralize decision-making but in a centralized place. And to deviate from that management philosophy and setup by integrating acquisitions that are somewhere else, that is not an insignificant challenge. And so, I guess, for a meaningful acquisition for us, the bar would just be higher in terms of integration efforts than for companies that have, I don't know, offices in whatever 50 countries around the planet, anyway, where it is relatively speaking, easy to integrate no matter where the target is sitting. So I guess, long story short, I mean, we are looking at opportunities, but we are probably a bit more selective than other companies for the reasons I just mentioned.

Sean Diffley

Okay. And then maybe you can talk about data management, user behavior, what opportunities do you see there to improve the quality of search results?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Yes. I mean, there's definitely a lot of opportunity to improve the quality of the search results. And there, one of the big levers is clearly personalization. I mean, the search results tend to be -- most of the algorithms still optimize very much for the average. And in particular, for searches that have a very heterogeneous demand, there is definitely room to optimize further. The other thing that is an opportunity is really to use less binary dimensions in the search results. And so as an example, if you are very keen on having a swimming pool, so then you can obviously select a filter on us and on all the other sites and then you will only see hotels with a pool. But then, perhaps, it's more important, it is for you better if that hotel has a pool that is open 24/7 rather than one that is open only over lunchtime, where you can't use it anyway. That's completely ignored. That's some information that is obviously relevant for the ranking within the filtered results. But that is currently not used and it's not very trivial to use that information, because you need to have it in a structured way. But that's just one example of how you can improve the overall quality as well, analyzing pictures, using that information also and the ranking of the search results. So there's quite a bit that can be done, but personalization, I guess, is the most tangible one to move first into segmentation and then ultimately into personalization of the search results for different distinct segments.

Sean Diffley

All right. And then my last question for you is just when you think about 2019, what do you see as your greatest opportunity and what's your greatest risk?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

I mean, the greatest risk is as we have, I guess, have experienced the last 2 years is some synchronized movement of our advertisers. Greatest opportunity, I guess, that is the same thing. So that obviously can be a headwind and a tailwind. If we ignore what other parties can do and what we can do ourselves, I still believe, I mean, the greatest opportunity at any point in time is always your product, yes? So if you improve your product, then that is the best thing that you can do. Obviously, you can improve the efficiency of your marketing, but the reason for any company to exist is the product and the value proposition towards the user. And there, I see big opportunity, as I said before, in terms of complementing our existing value proposition that is obviously very focused on availability and price transparency by different alternative accommodation types and getting there a more complete offering. But also in the user flow, making that more seamless, even making the handover easier from us to advertisers, so there is plenty of opportunity in the product, and that, I guess, would always be the biggest opportunity.



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Sean Diffley

And I guess -- no, that's helpful. And your marketing and brand, obviously, have been one of your greatest assets. How have you kind of evolved that evolution and the messaging and the trivago guy? I can remember. Like how have you kind of learned over the course of being a public company how that's kind of developed and anything that's changed there?

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

I think that has not so much -- I mean that has nothing to do with our listing. And so, I guess, we really rolled out the mister trivago concept globally in '15, '16. And it has been and still is one of the most successful concepts that is out there. Concept that we had before was less successful, trivago knows. It looks beautiful and very nice spots, but they just didn't work well. And I guess, where we currently are is we are running a lot more concepts in parallel. So we moved away from just having one concept globally to derisk the overall creative process as well. Because if you have only one concept, then that is eventually wearing out, obviously, you don't have anything to replace it. So there, we are much more diverse in our current creatives. But that's predominately for testing purposes. And we are, I guess, we are getting faster at integrating the insights that we are gathering in individual test markets. And then adapt the spots on the go. So I think we are in a much better position right now versus 12 months ago and comfortable that we will continue to have well performing spots there given the testing and also the number of test markets and the number of creative concepts that we are testing currently.

Sean Diffley

Okay. Axel, thank you very much. Appreciate it.

Axel Hefer - *trivago N.V. - CFO, MD of Finance, Legal & International and Member of Management Board*

Thank you.

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