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PARTICIPANTS

Corporate Participants

Mark D. Okerstrom – Chief Financial Officer & Executive Vice President, Expedia, Inc.

Other Participants

Scott W. Devitt – Analyst, Morgan Stanley & Co. LLC

MANAGEMENT DISCUSSION SECTION

Scott W. Devitt, Analyst, Morgan Stanley & Co. LLC

We're going to kick it off. I'm Scott Devitt, Morgan Stanley's consumer Internet analyst. Very happy to have Mark Okerstrom, CFO of Expedia, with us today, made the flight down from Seattle, and we appreciate you being here.

Mark D. Okerstrom, Chief Financial Officer & Executive Vice President

Great to be here.

QUESTION AND ANSWER SECTION

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Thanks. We know Expedia is one of the largest global online travel agencies and the biggest in the U.S. You've had a lot of successes in 2013. The stock's done very well. As you look into 2014, how do you think the business is positioned and what are the top priorities for 2014?

<A – Mark Okerstrom – Expedia, Inc.>: Sure. Great question. Well, we feel good about how we're positioned in 2014. A lot of the big investments that we've made are now behind us. We're in a position where across our core global leisure brands, Brand Expedia, Hotels.com, EAN, our private label business, they're really in growth-and-scale mode. So the focus for those businesses are really about expanding geographically, expanding the hotel count, pushing more aggressively in mobile and really just operating the platforms that we've built.

We're then very focused on a couple of the key future growth drivers for a business: eLong in China, which I think is incredible opportunity for us and we're going to continue to invest aggressively towards the long-term Chinese opportunity; Egencia, our corporate travel business which is the fifth largest corporate travel agency in the world, really doing to corporate travel what Expedia did to leisure travel and they're just few years behind, focused on finishing up the VIA Travel acquisition integration, a deal that we did to create a number one position for ourselves in Nordics; and then also Trivago, which is the leading hotel-only meta search provider who's been incredibly strong in Europe, bringing Trivago even more aggressively into the U.S., Canada, Australia, as well as Latin America and Asia Pacific throughout this year. So, we feel good about our position, and it's really for us about the next chapter of growth.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: In 2013, earlier on, there were some performance issues with Hotwire. How is the business positioned now? Is it at a size relative to the bigger business where it's just less relevant and kind of what's been put in place relative to some of the stuff that Priceline has done that I think created some headwinds early in 2013?

<A – Mark Okerstrom – Expedia, Inc.>: Sure. Well, as you mentioned, the biggest challenges for us in 2013 with respect to Hotwire, due a larger part due to Priceline's introduction of Express Deals, were just changes in the competitive landscape. There were some headwinds that started with Hurricane Sandy with respect to car supply and the consolidation in the U.S. car industry, there was also a challenge. But really it was a shift in the competitive landscape.

Since that happened, we've got new management in place at Hotwire. And the team is very much focused on monetizing some of the key assets that really are Hotwire. They got a great brand name and really loyal customer following, particularly in the U.S. They're in the hotel business, which is where really all of the profits in this industry sit. They've got pricing power because they've got the opaque model. And they've got a consumer that really likes to book last minutes.

So you put all those things together, and it's a great asset for us. It is a meaningful part of our business. They found their footing. We expect them to be relatively stable in 2014 and really be focused on how beyond 2014 they reenergize that business for growth.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: It's interesting, the Internet companies broadly, over the past half decade, have transitioned more aggressively into traditional TV advertising.

<A – Mark Okerstrom – Expedia, Inc.>: Yeah.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: The travel industry was one of the first ones and it was more integrated component of the ad campaigns for a longer period of time.

Booking.com recently announced it's going to spend $220 million to $240 million on TV advertising. As this industry's evolved – TripAdvisor initiated an initiative offline or in traditional TV. As it's evolved and more money is being spent, is that suggesting the returns are good, or is it suggesting that everybody needs to be there and that the returns are less good as more dollars are being put into that channel?

<A – Mark Okerstrom – Expedia, Inc.>: Well, it's hard to draw conclusions around the overall efficiency of that channel from recent activity. I would say that television advertising has always been a key part of our business and was a key part of Brand Expedia right from the start, Hotels.com. Really, all of our major leisure brands have been pretty active in television advertising. And over the years, we've found it a great way to just create brand loyalty to create diversified marketing channels, so you're not overly reliant from the likes of Google or other online marketing channels. And that's always been a key part of what we've been doing. Of course, adding Trivago into the mix, into our family of business that was really built on television advertising just puts more of a focus on that across our group.

With respect to what other players are doing, listen, I would just say that, for us, again, television advertising's been a key part of our mix. When you see TripAdvisor, when you see Booking.com going into television advertising, it suggests to us that they're trying to do what we've been trying to do, which is diversify their mix, be less exposed to the likes of Google, develop more of a direct relationship with the customer. It makes sense. And as they come into the market, even though that it does create more competitive intensity in the U.S. market, we also do see some of the other players, more traditional OTAs, pulling back a little bit and making room for them.

So, we think it will be noisy in television advertising in the U.S. in 2014, but I wouldn't have it signal to people there's a massive shift in the industry.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. A couple questions around sales and marketing efficiency and customer acquisition cost, something that was hotly debated in 2013 certainly.

<A – Mark Okerstrom – Expedia, Inc.>: Yeah.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: You've got emerging players, one of which you own with Trivago, you've got Kayak, you've got TripAdvisor, now you've got Google giving initiatives that are getting deeper into the funnel. And so, how should investors think about sales and marketing efficiency over the next two, three, five years? Is it going to be something that for the OTAs that is continuously rising, or do you get to a point in time where you get over a hump? Competitive climate seems to be shrinking a little bit, you benefit from the relationship with Travelocity, and there's other things going on. How though do we think about that over the longer term?

<A – Mark Okerstrom – Expedia, Inc.>: Well, I would say from an overall P&L perspective for us, we are not particularly focused on getting leverage from direct sales and marketing. We look at this industry -- it's so huge, over $1 trillion. We're 3% to 4% of this industry. We have a huge amount of opportunity for geographic expansion ahead of us. Every market that we go into we're generally able to build that flywheel of acquiring new customers through channels like TripAdvisor, like Trivago, like Google, and converting them into loyal customers and creating better marketing efficiencies over time.

And as long as we see those fundamentals, we're going to continue to invest aggressively in doing that and then we're going to find leverage on other parts of our P&L cost of sale, G&A, growing technology and content in line with or slower than revenue. So that's the overall umbrella, I would say, our strategy.

With respect to the efficiencies of particular channels, though, I would just say the big global OTAs, and I'll speak for Expedia, often, we're more isolated from efficiency degradation than some of the smaller players, and that's because we are constantly testing and learning and refining and improving our platforms, improving our supply position, improving our online marketing.

And that results in conversion enhancements that essentially enable us to keep marketing efficiencies relatively stable and yet drive more volume. If you're a smaller player who can't compete in that game, you can't increase conversion. Often, you do find your efficiencies degrading.

So we've been happy with the efficiencies that we've seen across the online marketing channels for a number of years since we've really re-platformed. We're happy with what we see in meta search. And for us, it's business as usual.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: I mentioned TripAdvisor. They have – used to be part of your family. And in the past year-and-a-half to two years, they've been making inroads in terms of, I don't know, maybe being an OTA or some version of an OTA over time with TripConnect and with assisted direct book if that's what we're going to call it now. And so how do you think about that? You spend a lot of money with them. How do you think about that company over time in terms of a friend versus foe, something you have to spend dollars on that's ultimately getting deeper into the funnel?

<A – Mark Okerstrom – Expedia, Inc.>: Well, I would say TripAdvisor is a great friend of ours. Obviously, there's a historic relationship, but they're really a great marketing channel for us and we very much respect that business, that management team. We respect the channels. It's a great channel for us. And I think when Steve Kaufer looks at his P&L and his cost structure and he looks at our P&L, our cost structure, he'll say, I'm very happy to be in the advertising business, thank you very much, and I'll leave the transactions to you. And it certainly, I expect, is their attention.

That said, they are moving deeper down the funnel. And just to offer you one rational for why they might be doing them, what you find in an industry like ours where you have a couple of global players who are constantly improving conversion, really focused on making their consumer experiences better and better is you can find differential between the competitors who are bidding in your auction. And if I were running a media business, I would want to make sure that to ensure that I had healthy auctions, I equalize the playing field a little bit. And so I would go deeper down the funnel. And I think that's where TripAdvisor is going.

We're comfortable with TripAdvisor going down the funnel, as long as when a customer comes to Brand Expedia or a Hotels.com or Hotwire from TripAdvisor, they know they're coming and making a booking on one of our brands. We have the opportunity to market to them. And really, TripAdvisor remains the great customer acquisition channel that it is. And we get great new customers from them. And to the extent those lines start to blur, then we'll have discussions with them. But I think we're going to continue to have a long and fruitful relationship with TripAdvisor and very much a friend for us.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Would you have an interest in being a provider of the direct booking product?

<A – Mark Okerstrom – Expedia, Inc.>: Well, I think we're always interested in making consumer experiences better. Again, I think it really comes down to what is the direct implementation, what does that look like and how far do we get, how close do we get to that line where a customer gets confused about whether they're booking on TripAdvisor or whether they're booking on Brand

Expedia or Hotels.com. And the closer you get to that line, the more disinterested we become. Provided the line is very clear, then we're very interested in it.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. Okay. Switching gears a little bit. ETP and/or the agency model, I guess, is another way to think of it and your efforts in Europe. How do you think you're doing there? What's the progress? And how do you think about that business now that you've have it several quarters to actually have it underway?

<A – Mark Okerstrom – Expedia, Inc.>: Well, we're very happy with Expedia Traveler Preference. Again, this was a product that we launched to enable us to offer the consumers the choice to whether pay us in advance, called the merchant model historically, or pay the hotel at the time of booking. Something that we didn't have the ability to do at scale. We had agency inventory in secondary and tertiary markets but not in the major markets. And that was something that was a little bit of a headwind for us, particularly in places like Europe where the agency model had become very popular with consumers, very popular with suppliers.

So we developed a product. Again, it gives consumers the choice, hotels that sign up for the program really put that choice in the hands of consumers. At our last call, we had 45,000 hotels signed up. And really, the hotels that had signed up have seen about a 1,000-basis-point increase in their growth rate sequentially before and after signing up in the program. So they're very happy.

And for us, we've essentially opened up the aperture of the consumer that would be willing to do business with us. A lot of consumers, surprisingly to many of you, will only book merchant. Right now in Argentina, travelers wanting to go into Miami, for example, they'll only book merchant. They're worried about the currency risk. Us having, that's a big advantage. A lot of our competitors don't have that.

Similarly on the agency side, a lot of consumers will just book agency, and we have them both. And it opens up the aperture for us. Uptick, we say globally has been very positive, and it does give us a particular advantage in Europe where that model is more popular with consumers.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. Any views on longer-term mix in terms of the merchant versus agent and the effects it has on the working capital dynamics?

<A – Mark Okerstrom – Expedia, Inc.>: Well, to answer the last part first, we did see some working capital impact in terms of less free cash flow growth from growth in our merchant business this year versus last year. And I would expect that to continue throughout this year and for some time. It's manageable. It's something we've been planning for for a long time. We've got a healthy balance sheet, so we're not particularly concerned about it.

With respect to mix, what we've seen is that for hotels that are participating in the program, for stand-alone hotel, the mix is about 50% agency, 50% merchant in terms of room nights. When you add in, for those hotels, our package business, the Hotwire opaque business, prepaid bookings that are – all of those are essentially merchant bookings, you get to 75% merchant.

So we think the merchant business is going to continue to be a big part of our business going forward, but we're absolutely thrilled to have the agency product. On our last call, we mentioned that if you exclude eLong, which is predominantly an agency player, even backing that out, we're now up to 15% of our room nights being done in the agency model, and that's growing up 100% year-on-year. So we do expect that shift to continue.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. And I want to leave enough time for questions. I had a couple more and then we'll kick it over questions. When you do, raise your hand, just wait for a microphone to show up.

And you recently guided to 13% to 16% EBITDA growth in 2014. You gave a little bit of color around the Travelocity partnership. I was wondering if you can just kind of reiterate what you've said publicly and then also to the extent that you haven't shared the contribution of that deal in terms of the EBITDA growth rate, if you can talk about that a little bit.

<A – Mark Okerstrom – Expedia, Inc.>: Sure. So we've said a bunch of stuff about Travelocity except for how much of our 2014 EBITDA comes from Travelocity, which is what everyone wants to know. So let me just – let me recap some of the highlights.

One is that we are essentially live with Travelocity now and the Expedia platform in the U.S. across all products. Canada is about to come. We expect that on a full-year run rate basis when fully optimized, the Travelocity deal to contribute about $40 million to $65 million of adjusted EBITDA. Again, that's fully rolled out, fully optimized. That's not the 2014 number.

We have said that, really, the ultimate performance of that business will be dictated by a number of things. One was the timing of the rollout and again we're largely rolled out except in Canada. Two is the conversion of the websites. The Brand Expedia website, and1 that platform converts incredibly well for Brand Expedia customers. And it's still too early to tell whether those loyal customers that loves the gnome are going to love it as much as they like the old Travelocity website. So that's a bit of an unknown. And then thirdly, as we just don't know how much Travelocity is going to spend on sales and marketing and how long it's going to take them to really get their sales and marketing models working.

And so there's still a lot unknown. We do think it's going to be accretive to adjusted EBITDA margins. We're pleased with the progress so far, and we hope there will be more Travelocity-type deals in our future.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. And Trivago, that's way the gentleman pronounces it on the commercial.

<A – Mark Okerstrom – Expedia, Inc.>: Trivago.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Trivago. Do you think it's moving fast enough as it relates to mobile? You've had Kayak in their evolution as a business before they were acquired by Priceline go to what I would call meta book or assisted book, whatever you want to call it. And now you have TripAdvisor doing what it's doing. How does Trivago think about mobile and going deeper like some of the other companies are doing?

<A – Mark Okerstrom – Expedia, Inc.>: Well, they are thinking a lot about it. They, in Q4, hit a mark of about 30% of their leads being sent via mobile devices. So it is a big part of their business. I would say there's a lot of work they can still do to optimize the mobile experience, but that team is one that's very, very focused on their core hotel search technology. They're very focused on geographic expansion. It's a business that prior to our acquisition had doubled revenue every year for five years. Last year, they grew revenue in excess of 85% year-on-year.

So, do we think they should be doing more in mobile? Yes. Do they think that they should be doing more in mobile? Yes. But they've made some tradeoffs, and so far we've been happy with the tradeoffs that we've made and I think there's lots of upside left for them.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay, good. Thanks. We've got about 10 minutes left. We'll pause to see if there's questions. Just raise your hand. And if not, I can...

<A – Mark Okerstrom – Expedia, Inc.>: You've done such a great job just covering all the questions.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: I don't know what else. We can talk a bit about the 12th Man if you want to.

<A – Mark Okerstrom – Expedia, Inc.>: Yeah, we can talk about that.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: We can talk about the Seattle economy.

<A – Mark Okerstrom – Expedia, Inc.>: We talk about this nightclub environment we've got here.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Yeah. I don't – yeah...

<A – Mark Okerstrom – Expedia, Inc.>: Except for the spa-like easy listening music that we're greeted with, yeah.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Anyone? Okay. More broadly, as it relates to mobile beyond Trivago, how do you feel like Expedia's assets are positioned? As different companies are going at a different pace in terms of M&A and organic transitions into mobile, where do you think that you are?

<A – Mark Okerstrom – Expedia, Inc.>: We feel good about our position in mobile. If you look across our leisure brands, everyone is in pretty darn good shape. Brand Expedia has just got amazing mobile apps, and they're going to launch something later this year on iPad that is even more amazing. Hotels.com has got great apps.

We bought a company called Mobiata that had built an app called FlightBoard and one called FlightTrack and FlightTrack Pro that were built by these six guys in Ann Arbor, Michigan, and had blown away every other online travel company to become – they had three of the top five paid apps in the App Store. So we bought them in 2010, and they've been working on developing the Brand Expedia apps. So we feel pretty good about the position. We, at the time of our last call, were up to 90 million downloads across all of our brands.

So we feel good about the position. We feel good about mobile overall. If you look at the dynamics that we see in mobile, we are seeing a lot more same-day, next-day booking activity, particularly on smartphone. We do think a decent chuck of that is incremental. It's a different booking window from what we've seen in the past.

We do think that we have an opportunity, particularly with Brand Expedia, to take advantage of the one-stop-shop nature and the limited real estate on mobile. Brand Expedia offers air and hotel and soon to offer car and destination services packages. Uniquely positioned, it's really the only remaining global multi-product OTA. We think that lends itself well in mobile. We think Hotels.com, with its broad inventory, has an advantage in mobile.

And generally, I'd say that any time there's been a technological shift in our industry, the benefits of that shift is accrued to the OTAs, to the ones that have invested heavily in technology. And that's certainly been the case with us, and so we feel good about mobile overall.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: So I'm going to – I'll ask you the question you've been asked 5,000 times.

<A – Mark Okerstrom – Expedia, Inc.>: Is it about Liberty?

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Oh, no. No. Maybe I'll ask that one [indiscernible] (21:32)

<A – Mark Okerstrom – Expedia, Inc.>: Sorry. I just gave you the next question.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Priceline has a 40% adjusted EBITDA margin. You have a 20% adjusted EBITDA margin. I think the last time that I brought this up, you said, well, if our business was as big as their business in Europe, then we'd have a 40% EBITDA margin. Is there anything else in terms of, as you look at the longer-term margin profile of the business, not necessarily in terms of closing that gap but in terms of expanding the margin profile of Expedia?

<A – Mark Okerstrom – Expedia, Inc.>: Well, I think the fundamental difference between our businesses is just the scope of the assets. And again, if you look at the – and this is probably the discussion we had before. But if you look at the Priceline business which is Booking.com, Priceline, Agoda, rentalcars.com and Kayak from an infrastructure standpoint, that's essentially Hotels.com, Venere.com, Hotwire, CarRentals.com, which we own, and Trivago.

That's probably the cost base you're looking at, and yet they're running a global hotel business the size of our entire business on top of that cost base. So does it have great EBITDA margins? Absolutely. Do we look at that business and say, boy, is there a lot of upside potential there? Absolutely. But on the other side, you've got Brand Expedia, the only remaining full-service OTA now in 31 countries with multi-product offerings. You've got Egencia, the fifth largest corporate travel business in the world. You've got eLong, the second largest OTA in China. So you've got these other amazing assets that are essentially relative to Booking.com. And that group, they're all subscale and yet they're all gaining share in their relative markets.

So we do think over a long term there is an opportunity. We're very focused on driving bottom line, adjusted EBITDA, EPS and free cash flow growth over time, less focused on margin expansion. Do we think there's a long-term margin expansion story here? Yes. Is this something that we're going to guarantee you're going to see 2014 or 2015? No.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. We track hotel listings that are added to the system, particularly in Europe, and your business continues to grow. Priceline has more hotels, at least by our tracking. They continue to add at a faster pace. So what do you think is – what's the reason that that is happening? Are there things that you can do in your business, whether it's ETP or otherwise, to start to close the gap of available inventory, particularly in Europe?

<A – Mark Okerstrom – Expedia, Inc.>: Well, I would say a lot of what we've done from an infrastructure standpoint is largely complete. ETP was a big piece of that puzzle and making sure that we had an agency hotel platform at scale. So we've got that rolled out now.

You've also got to have the ability, of course, to – when you get a hotel signed up, to have them displayed on your website with great photos and descriptions in local language and [ph] 35 (24:40) different languages around the world, and you've got to have the ability to market them globally in all online channels. And those components are components we've built over the course of the last three or four years.

2013 was a year where we had a lot of our field sales force, our market managers, focused on converting existing hotels to ETP hotels. And in 2014, we are going to have the ability to free up more resources and really focus on, in fact, adding new hotel properties.

And from that point forward, it becomes about really optimizing that manufacturing process of adding hotels, getting them live on the site with great content and getting them marketed. That's something that Booking.com has done a fantastic job over the course of the last 8 to 10 years. They've got a great formula. We built the formula, and now it's about optimizing that.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. You did a deal with HomeAway, I believe, to access inventory and repopulate through your platform. How's that progressing? How do you think about that category in terms of using their inventory and potentially populating it throughout your service as a growth area for the business? That was something that was talked about quite extensively, a focus, right, as I recall.

<A – Mark Okerstrom – Expedia, Inc.>: Right. Yeah. Well, we think it's interesting. And we know a fair bit about the vacation rental industry just by virtue of our experience with TripAdvisor and we built that business in TripAdvisor and did a number of acquisitions to add to that platform. Historically, that industry has lent itself more to a listing space model as opposed to an online real-time booking capability model. And really, to do business on OTA, you've got to have that real-time rate stability, real-time bookability. HomeAway has been investing in actually building that capability.

And so this partnership is a way for us to both experiment with that and test and learn our way into whether or not there's a real opportunity here. We like working with HomeAway. They're a great partner. We hope it turns into something big right now. It's in like a lot of things we do, really in test-and-learn mode, and we're going to see the results.

And I would say that I think if you look very long term in this industry, the vacation rental piece of it could be a meaningful piece of our industry. But again there's a lot of online booking infrastructure that's got to be built, and we're very happy that HomeAway is our partner in building that out.

<Q – Scott Devitt – Morgan Stanley & Co. LLC>: Okay. Last question. Do you think Robinson Canó has enough to plug the hole that you have during the summer season? No, the last question is Liberty. What are they going to do? Your business, TripAdvisor, whatever you want to talk about, I mean, in 23 seconds.

<A – Mark Okerstrom – Expedia, Inc.>: I can't believe I raised that. Foolish. Alan Pickerill, our IR expert, is shaking his head at me. I have no idea what they're going to do. I have no idea. We're thrilled to have Liberty as a shareholder. John Malone's just a brilliant capital allocator, and I think that I, Dara, I think we've learned a lot just from being around him, and we would be thrilled to have them continue as a partner from now into eternity. And as always, we're open to creative things. So that's the case now. It's been the case for the last time immemorial. And in terms of what will happen, we just don't know.

Scott W. Devitt, Analyst, Morgan Stanley & Co. LLC

Mark, thanks a lot for coming. We appreciate it. Thank you.

Mark D. Okerstrom, Chief Financial Officer & Executive Vice President

Thank you. Yeah. Appreciate it.