REFINITIV STREETEVENTS

EDITED TRANSCRIPT

TRVG.OQ - Q1 2023 Trivago NV Earnings Call

EVENT DATE/TIME: MAY 03, 2023 / 12:15PM GMT

CORPORATE PARTICIPANTS

Axel Hefer *trivago N.V. - MD of Legal, Marketplace, People & Culture and Technology, CEO and Management Board Member*

Matthias Tillmann *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

CONFERENCE CALL PARTICIPANTS

Dae K. Lee *JPMorgan Chase & Co, Research Division - Analyst*

James Lee *Mizuho Securities USA LLC, Research Division - MD of Americas Research & Senior Internet Sector Analyst*

Kevin Campbell Kopelman *TD Cowen, Research Division - MD & Senior Research Analyst*

Lloyd Wharton Walmsley *UBS Investment Bank, Research Division - Analyst*

Ronald Victor Josey *Citigroup Inc., Research Division - MD*

Stanislav Nikolaev Velikov *Wells Fargo Securities, LLC, Research Division - Associate Equity Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen. Thank you for standing by, and welcome to the trivago Q1 Earnings Call 2023. (Operator Instructions) I must advise you the call is being recorded today, Wednesday, the 3rd of May 2023. We are pleased to be joined on the call today by Axel Hefer, trivago's CEO and Managing Director; and Matthias Tillmann, trivago's CFO and Managing Director.

The following discussion, including responses to your questions, reflects management's views as of today, Wednesday, May 3, 2023 only. trivago does 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 similar statements.

Please refer to the Q1 2023 operating and financial review and the company's other filings with the SEC for information about factors which could cause trivago's actual results to differ materially from these forward-looking statements. You will find reconciliations of non-GAAP measures to the most comparable GAAP measures discussed today in trivago's operating and financial review, which is posted on the company's IR website at ir.trivago.com.

You are encouraged to periodically visit trivago's Investor Relations site for important content. Finally, unless otherwise stated, all comparisons on this call will be against results for the comparable period of 2022.

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

Axel Hefer - *trivago N.V. - MD of Legal, Marketplace, People & Culture and Technology, CEO and Management Board Member*

Thank you, everyone, for joining us for our Q1 2023 earnings call today. Demand in the first quarter has been robust and we have seen the start of a strong recovery in travel in Asia, driven by the reopening of Japan and China. In our Western markets, the economic outlook has remained uncertain. And we've seen our users mitigating the negative effect of inflation, shifting to shorter trips and cheaper destinations when comparing prices on trivago.

In an environment where price comparison is on top of everybody's mind every day, we have ramped up our brand marketing activities and are preparing to continue to invest into our brand and the communication of our value proposition in the summer.

In the first quarter, we've seen solid growth of our branded traffic and expect our brand marketing activities to continue to fuel a positive development of our direct traffic. Our product development continues to be focused on our core value proposition, comparing prices for accommodation.

We've made good progress on improving our coverage of directly bookable rates and have surpassed the 50% coverage threshold in our test markets. Another focus area has been the improvement of our price comparison display across accommodations and travel dates. We are excited about the improved value proposition to our users that these improvements will yield later in the year and expect to improve our competitive positioning.

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Okay. Thank you, Axel, and good morning, everyone. Let me briefly walk you through our financial performance in the first quarter before we open it up for questions. As Axel mentioned, we had a strong start to the year with year-on-year referral revenue growth in January, exceeding 30% as a result of continued robust travel demand trends and elevated average booking values. The strong growth was largely driven by the recovery from COVID-related travel restrictions in January 2022 in our segment Developed Europe and Rest of World.

As a result of the cadence of the recovery in the first quarter of 2022, our year-on-year growth rates decelerated in February and March. In addition, we did not see the same uptick in monetization as last year, leading to a decrease in monetization year-on-year, in particular in our segment Americas. Our referral revenue growth in the first quarter was 11%. Other revenue declined to EUR 1.7 million as we started to phase out certain B2B products like display ads in the second half of last year.

Our net income was EUR 9.9 million compared to a net loss of EUR 10.7 million last year, which was largely driven by the nonrecurrence of the incremental expense of EUR 21.1 million in Q1 2022 in relation to the proceedings brought by the ACCC against us. As planned, we have ramped up our brand marketing investments earlier this year, which led to a decline in return on advertising spend, in particular, in Developed Europe and Rest of World.

The increase in marketing expenses was partly offset by higher referral revenue. And as a result, our adjusted EBITDA decreased only slightly from EUR 21.1 million in the first quarter of 2022 to EUR 18.6 million in the first quarter of 2023, in line with our expectations.

In summary, despite higher brand marketing investments and lower monetization levels compared to last year, we continue to achieve a strong adjusted EBITDA margin of 16.8%, while growing our referral revenue. As mentioned in our shareholder letter, we have decided to stop providing qualified referrals and revenue per qualified referrals going forward.

As we continue to run product tests that aim to increase the value of our referrals, there is significant volatility in click out behavior, which makes it difficult to compare these metrics to prior periods. We believe that it is not helpful to look at these metrics to understand or model our underlying business dynamics. However, we will continue to comment on the key drivers of our referral revenue development.

So let me give you some color on the dynamics in the first quarter for the different regions. Starting with our segment Americas. Our referral revenue declined by 7% year-on-year. The decline was largely driven by a loss in performance marketing volumes as we did not observe the same uptick in monetization in our own auction as last year, and we continue to focus on profitability.

In Developed Europe, the recovery in travel demand from Omicron-related travel restrictions, elevated ADRs and successful brand marketing campaigns contributed to the referral revenue growth of 19% year-on-year in that segment. We observed the deceleration in referral revenue growth rates throughout the quarter, reflecting the strong improvement in referral revenue from January to March last year.

The recovery was strongest in our segment Rest of World. Referral revenue growth was 51% as we saw recovery in many Asian markets, most notably in Japan. We saw a strong increase in average booking values in that segment, driven by elevated ADRs and an increase in booking conversion, while our monetization was roughly stable compared to the same period last year.

Now moving on to advertising expenses. In anticipation of a strong travel recovery in Europe and Rest of World, we ramped up our brand marketing investments early in the year. We are very happy with the results as we saw a nice acceleration in the brand traffic growth rate compared to the fourth quarter in 2022.

As expected, our return on advertising spend decreased as a result of higher brand investments in both segments. However, absolute contribution still increased compared to the same period last year due to the increase in referral revenue.

In Americas, our overall marketing expenses and contribution decreased slightly as the decrease in monetization year-on-year was stronger compared to the other 2 segments. The decline in advertising spend was largely driven by an algorithmic reduction in performance marketing expenses as we continue to focus on profitability. Overall, our marketing expenses were 59.5% of revenue, up from 55.4% in the previous quarter and 52.7% in the same period last year.

I will now discuss our operational expenses, excluding advertising expenses and the penalty imposed by the Australian Federal Court in Q1 2022 relative to last year. In the first quarter, our operational expenses decreased slightly compared to the same period in 2022.

Compensation expenses, including share-based compensation, decreased mainly as a result of headcount reductions compared to Q1 2022. Further, we recorded lower commission fees for acquiring traffic as our white label product is fading out. This was partly offset by an increase in TV production costs, IT-related costs, mainly due to the setup fee for the onboarding of independent hotels and higher expected credit losses on trade receivables.

We further improved our cash position and remained well capitalized with approximately EUR 297 million in cash, cash equivalents, restricted cash and short-term investments.

Finally, let me give you some color on early trends in the second quarter. Our referral revenue declined by a low single-digit percentage rate in April as our monetization was very strong in the comparable period last year. However, in the last week of April, we have seen our referral revenue growing again year-on-year. The main trends remain stable. We continue to see elevated average booking values in all regions, driven by higher ADRs and slightly offset by shorter length of stay.

Demand continues to be robust, while auction dynamics are stable. We remain optimistic about our ability to ramp up our brand marketing investments in the upcoming months in order to further grow our brand baseline traffic across all 3 segments.

With that, we expect a decrease in return on advertising spend and contribution in the second and third quarter year-on-year as we continue to invest into future branded traffic growth. We further expect that the increase in marketing expenses in the second quarter relative to the first quarter will be compensated by a seasonal increase in revenues. And consequently, we expect that our adjusted EBITDA in the second quarter of 2023 will be similar to that in the first quarter.

For the full year 2023, we continue to expect that despite a ramp-up in marketing investments and a normalization in auction dynamics, our adjusted EBITDA will exceed that of 2019 as a result of our cost discipline and more efficient marketing investments compared to prepandemic years.

In summary, we are committed to delivering higher adjusted EBITDA margins compared to prepandemic and believe that we are well positioned to increase our brand investments, thereby growing our direct traffic.

With that, let's open the line for questions. Operator, we are ready...

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question today goes to Lloyd Walmsley of UBS.

Lloyd Wharton Walmsley - *UBS Investment Bank, Research Division - Analyst*

Two questions, if I can. First, the shareholder letter talked about kind of referral revenue growth in the quarter being in line with expectations. So just curious if the shift in marketing from customers was something you had seen earlier in the year and kind of expected and I guess more broadly, like how much communication and visibility do you get from customers?

And then the second one, just staying on this topic of the focus of increased profitability from OTAs. Are you seeing this across your clients? Or is it really driven by 1 client? And -- do you have any sense of whether this is kind of how broad this is versus just shifting priorities among your clients' marketing? Anything you could share there would be helpful.

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Thank you, Lloyd. Yes, let me start with your first question, and then I'll pass it on to Axel for your second question. I mean, obviously, the monetization, that is something we can control at least. So we do make assumptions and we do look at the cadence we saw in prior years. And based on that, we model different scenarios. But ultimately, that's something we have to take as it comes, and then adjust our marketing expenses.

The comment in the shareholder letter was basically relative to when we last spoke in February. And by then, we hinted at auction dynamics already. So it's something that we that we saw and we expected monetization to be a bit softer. But then again, the exact level, that's nothing we know. But roughly, I would say it was in line. And then monetization, obviously, is only 1 piece.

The other is demand and average booking values, conversion rates. So this all goes into referral revenue. And there, as I said, trends were stable throughout the quarter, and that is roughly what we expected. And hence, overall, referral revenue were in line with our expectations.

Axel Hefer - *trivago N.V. - MD of Legal, Marketplace, People & Culture and Technology, CEO and Management Board Member*

Yes. On your second question, the focus on profitability versus growth or the balance between the 2. I mean if we go back 1 year, I mean, the vast majority of travel companies was focused on volume, on capturing the recovery, the returning traveler, and winning over the returning traveler as a customer.

This year, the sentiment is obviously a bit different. I mean, there is a lot more geopolitical instability, there is more economic instability, uncertainty. And in times of uncertainty, I mean, some advertisers choose obviously, to focus more on profit. But it's really a case-by-case decision. I mean every partner is taking a different decision on the trade-off. And our expectation is with the general environment stabilizing and uncertainty fading that the balance will shift further to growth again.

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

And then, Lloyd, just to add to that, I think that's what Axel said is right, And then 1 other point, I think I mentioned it vaguely in my remarks, but historically, it has not been uncommon for us to see an increase in monetization going into the peak season.

Last year, the seasonal effect was just more pronounced going into April. And in a way, we see a normalization now. So we did not see an increase in monetization to the same extent this year, and that is contributing to the year-over-year decrease. So I guess, in addition to what Axel said, there's also a comp effect here.

Lloyd Wharton Walmsley - *UBS Investment Bank, Research Division - Analyst*

Okay. Okay. So a little bit of optimism, things will start to move back to growth. That's helpful.

Operator

The next question goes to Doug Anmuth of JPMorgan.

Dae K. Lee - *JPMorgan Chase & Co, Research Division - Analyst*

This is Dae on for Doug. So first one, I was wondering if you had any more color you could provide on how 3Q is shaping up so far? And in terms of seasonality for the rest of the year for revenue. How do you expect that to play out?

And then secondly, I mean, it sounds like ROAS in 2022 was higher than what it could have been if you were to go back with the ROAS that you have now. So how should we think about where ROAS should shake out relative to 2022 levels? Would you expect ROAS this year to be closer to 2021? Or should it be closer to 2019? Any more color on that, if you could provide us would be helpful.

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Yes, sure. So yes, let me give you a bit more color on referral revenue. I mean, we don't guide revenue specifically. I think we provided more guidance around EBITDA for the second quarter, also for the full year. And the simple reason for that is that it's more controllable from our perspective, and there's still some volatility, not only in the absolute levels, but in particular, in the year-over-year comparisons.

But some more color, starting on a global level, I mean what I said is that our referral revenue grew more than 30% in January, and growth rates decelerated in February and March. So we ended the quarter at 11% or in the quarter, we grew 11%. In April, as I said, referral revenue was slightly negative. The deceleration in referral revenue growth rate was largely driven by the strong uptick in monetization during that period last year.

As we are lapping this effect, comps are getting easier again and referral revenue was already up, as I mentioned, year-on-year in the last week of April.

Now when we look at the different regions, the cadence was very similar, just at different levels. To give you an idea, referral revenue in Europe was roughly flat in April year-on-year. In Americas, referral revenue declined in April by a high-teens percentage. And in Rest of World, it was still up over 30%.

And again, in all regions, we saw an improvement in the last week of April. So that overall referral revenue grew again. I hope this gives you a bit of color how the cadence and shape was and how to think about referral revenue maybe for the rest of this quarter.

Now on ROAS, we expect the quarterly distribution of our ad spend to be similar to last year, just with a slightly higher share of spend in Q1 at the expense of Q3 and Q4. As we said, overall, we plan to increase our ad spend. We see, in particular, an opportunity to ramp up brand investment relative to last year, as we plan to add some markets there where we have not been active last year in Rest of World and given the strong performance last summer, and you have seen that in Q1 already.

So yes, ROAS, I mean, when we talk about margin and relative to 2019 and last year, we said, we expect that will be down a little bit, and that is reflected by lower ROAS. If you look at the range 2019 to 2022, then I think we're still planning to be closer to 2022 than to 2019. But again, with the ramp-up in brand investment, we expect ROAS to be down in the coming 2 quarters relative to last year.

Operator

The next question goes to Brian Fitzgerald of Wells Fargo. Brian.

Stanislav Nikolaev Velikov - *Wells Fargo Securities, LLC, Research Division - Associate Equity Analyst*

This is Stan Velikov for Brian. Actually, I have 2 questions related to the softness in auction bidding that you saw in Q1. First, why do you think it was more pronounced in the Americas? And second, what are you seeing in auction dynamics this quarter across the various regions?

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Yes. Thank you. I can start with the second part of your question. I mean -- and that makes it a bit more complicated. So there are 2 things, how to look at it. One is sequentially and 1 is year-over-year. And I think -- the 1 comment I made is that sequentially, auction dynamics are relatively stable. So historically, we have seen a slight increase in monetization going into the summer months.

Last year, there was just more pronounced. And this year, we see a normalization of that, which means monetization is slightly ticking up and roughly -- but roughly stable, what we have seen so far from January to April.

In the year-over-year, that led to a bigger decline in March and April. And now we're seeing it starting to get a bit better as comps are getting easier. And then Axel, do you want to take the first part of the question?

Axel Hefer - *trivago N.V. - MD of Legal, Marketplace, People & Culture and Technology, CEO and Management Board Member*

Yes, sure. I mean, so it's actually -- it's a good question, but it's difficult to answer because you obviously see overall regions that are then -- that have a mix effect of the different countries within the region and then mix effect of the different advertisers within those countries.

So it's more an advertiser-by-advertiser decision rather than a country-by-country decision. And depending on the market share mix and the country mix, you have then a different outcome. And in Americas, the outcome was greater than in other regions.

Operator

The next question goes to James Lee of Mizuho.

James Lee - *Mizuho Securities USA LLC, Research Division - MD of Americas Research & Senior Internet Sector Analyst*

Great. Two here. First, on ADR trends. And I think you guys mentioned the shareholder letter is elevated across all regions. I was wondering if you can maybe break it down by region a little bit? And what is your outlook for the rest of the year?

And also number two, can you give us a sense of what the demand is for summer travel for Europe that looked like based on the search results? And any changes in terms of booking windows, any change in length of stay? Any incremental color would be helpful.

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Yes, sure. Thanks, James. Let me start with the booking value. So in the first quarter, year-on-year, the average booking value for us increased around 10% globally.

ADRs, as you probably know, were up slightly more than that with the highest increase in Rest of World. And we had an offsetting effect from slightly shorter length of stay. That was very similar in all regions and globally, it was around, let's call it, 5%.

In April, we observed a deceleration in the average booking growth rate to a low single digit as we start lapping the increase from last year. If you look at the different regions in Americas and Europe, average booking values were slightly higher compared to April last year. And then in Rest of World, we still see higher increase in the mid-teens. And there was no notable change in length of stay in April compared to the first quarter.

Now to your first question on demand. On a super high level, we saw a nice recovery in Europe and Rest of World, as you can see in the numbers in the first quarter. In Rest of World, demand continued to increase in April as in particular, in Asian markets, we continue to observe a recovery post-COVID. In Europe, I believe the market demand was similar in April compared to last year.

In terms of booking windows, there is no big change. So I think we see that normalized compared to prepandemic. So booking windows from what we see are pretty normal again with an average booking window for us being between 30 and 60 days, slightly different by region, but not vastly different.

Yes. And I think that is true for all regions. So there's nothing really to call out. I mean the booking window 30 to 60 days, that tells you that in Europe, we just started to see summer demand. So it's a bit early to talk about trends. In general, what we have seen is that so-called Tier 2 destinations are increasing in demand.

We have seen that the share of international travelers going up in certain European countries, also in the U.S. there the increase was even stronger than in most European markets, which might also be driven by the strong U.S. dollar relative to the Euro and other currencies. But largely, looking at these trends like urban travel, city trips, domestic international, I think by now, we are largely recovered, and it's not that we see very different mixes to what we saw pre-pandemic.

Operator

The next question goes to Ron Josey of Citi.

Ronald Victor Josey - *Citigroup Inc., Research Division - MD*

Axel, Matthias, I want to ask about just progress on 2023 growth initiatives like direct hotel bookings that we talked about, I think, last quarter, and then just a little more clarification on Asia specifically. I think we said strong recovery in Japan and the reopening of China. Just talk to us about the trends there, when do you think or how do you think that progresses going forward any other dynamics around Asia Pac that we should know about?

Axel Hefer - *trivago N.V. - MD of Legal, Marketplace, People & Culture and Technology, CEO and Management Board Member*

Sure. So on our growth initiatives, I mean, they are obviously marketing and product initiatives. On marketing, as Matthias said, I mean, we started to invest into brand marketing, and we expect to continue to do so.

On the product side, we're making good progress on the increase in coverage and are testing in parallel or running in parallel, some tests to prepare for the point in time later in the year when our coverage is sufficient to really launch features that then differentiate the product further. So we are happy with the progress, but from a user perspective, you will start to see some changes later in the year. So it will still take some time.

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Yes. And just to quickly add to that. I mean, as we said before, we don't think that this will have a significant or notable financial impact 1 way or the other for 2023. So we do incur some costs in onboarding independent hotels, but that's all included in the numbers and outlook I shared. But on the revenue margin side, there's nothing you should be aware of at this point.

And then on your second question, I mean, obviously, it's hard to predict how this will continue. But I think last year already with the start of Golden Week in Japan, we saw a nice recovery in that country. And obviously, given the size of the country, it has a bigger share and bigger weight for our segment, Rest of World.

But equally, we have seen a very nice recovery in smaller countries like Singapore, Hong Kong, Malaysia. So I think it's starting now in across the region, really. And we have started already to ramp up investments compared to last year, and so far, I have seen a nice response.

So I think the trend continues to be there, and it is a growth opportunity for us. We haven't been active for over 2 years during the pandemic in some of these markets. And it's just very nice to see that with the absence of in particular brand marketing during that period, that once you start come back, that there is a positive response. And yes, I expect that we will continue to see that region recovering. And if we do that, we will continue to invest into that. And we think it's an opportunity for us to grow the Rest of World segment for us relative to the other 2 segments.

Operator

(Operator Instructions) And our next question goes to Kevin Kopelman of TD Cowen.

Kevin Campbell Kopelman - *TD Cowen, Research Division - MD & Senior Research Analyst*

Great. Can you give us more color on the consumer reaction you're seeing so far from the investment in brand advertising and maybe how that's compared to brand campaigns you've launched in the past?

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Yes, sure. Thanks, Kevin. I mean we talked about the change in messaging before. And what did we change? I mean the core message is a price comparison, obviously, but we said in the current environment, with high inflation, everybody is focusing on saving money and it's on everybody's mind, top of mind, so to speak.

And that's why we tried to sharpen that message a little bit more even. And it's not only the brand message, but it's also the combination with product features. We launched price alert. We focus on that in our e-mail marketing, et cetera. So it's really holistic approach. And I think that's showing effects.

Where can we see that, so a, in the brand traffic we see on our platform, there it's visible. It's also visible in the direct response we see from our -- in particular, TV campaigns. And there when we compare our current campaign, and I mean, obviously, as we are in May, we start to ramp up. So the exciting time is only starting now.

But if I compare that to last year and the year before, we do see that the response is greater than what we have seen before. And that makes us confident that we should scale up and ramp up our investment, and that is what we are planning. And that is why the guidance on ROAS, ad spend, and EBITDA is what it is because we think it's an opportunity for us.

Kevin Campbell Kopelman - *TD Cowen, Research Division - MD & Senior Research Analyst*

Great. And 1 other 1, can you remind us on just how comps look like May and June compared to April as we think about the rest of the quarter on a year-over-year basis?

Matthias Tillmann - *trivago N.V. - MD of Finance, Marketing & Product, CFO and Management Board Member*

Yes. So I think the way to think about it is if you look at the first half then comps for us were toughest in March and in particular, April, and then will be slightly easier in May and June.

Operator

We have no further questions. I'll now hand back to Axel for any closing comments.

Axel Hefer - *trivago N.V. - MD of Legal, Marketplace, People & Culture and Technology, CEO and Management Board Member*

Thanks for taking the time to participate in today's earnings call. The next quarters and years will be decisive for the metasearch industry as we believe that a clear value proposition and its communication will be key to succeed. Many thanks, and have a good day.

Operator

Thank you. This now concludes today's call. Thank you so much for joining. You may now disconnect your lines.
