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EXPE.OQ - Q1 2023 Expedia Group Inc Earnings Call

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OVERVIEW:

EXPE reported 1Q23 revenue of $2.7b.

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PRESENTATION

Operator

Good day, everyone, and welcome to the Expedia Group Q1 2023 Financial Results Teleconference. My name is Emily, and I'll be the operator for today's call. (Operator Instructions)

For opening remarks, I will turn the call over to Senior Vice President, Corporate Development, Strategy and Investor Relations, Harshit Vaish. Please go ahead.

Harshit Vaish - *Expedia Group, Inc. - SVP of Corporate Development, Strategy & IR*

Good afternoon. Welcome to Expedia Group's earnings call for the first quarter of 2023 that ended March 31st. I'm pleased to be joined on the call today by our CEO, Peter Kern; and our CFO, Julie Whalen.

The following discussion, including responses to your questions, reflects management's view as of today, May 4, 2023, only. We do not undertake any obligation to update or revise this information. As always, some of the statements made on today's call are forward-looking, typically preceded by words such as we plan, we expect, we believe, we anticipate, we are optimistic or confident that or similar statements.

Please refer to today's earnings release and the company's filings with the SEC for information about factors which could cause our actual results to differ materially from these forward-looking statements. You will find reconciliation of non-GAAP measures to the most comparable GAAP measures discussed today in our earnings release, which is posted on the company's Investor Relations website at ir.expediagroup.com. And I encourage you to consistently visit our IR website for other important information. Unless otherwise stated, any reference to expenses exclude stock-based compensation.

And with that, let me turn the call over to Peter.

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Thank you, Harshit, and good afternoon, and thank you all for joining us today. As I mentioned last quarter, this year marks the final phase in our major platform transformation journey, and I'm pleased to have started the year with strong performance. We posted our highest ever quarter for lodging gross bookings and free cash flow and our best first quarter for revenue.

Throughout the quarter, we saw strong consumer demand with acceleration in international and big city travel and more of Asia reopening. The reemergence of major international cities has meant increased hotel demand, offset in part by flattening demand in vacation rentals as travel demand mixed to shorter stay urban destinations over extended beach and mountain trips. Similarly, air has continued to mix towards international travel and away from COVID era concentration in domestic.

By and large, prices have held up quite well after several years of inflation. We've seen lodging ADRs hold fairly steady across geos. Air ticket prices, however, continued to increase as strong demand continues to outstrip capacity. The only area where we have seen any meaningful decline in average daily rate is in the car rental space, where larger inventories have allowed rental companies to drive more volume at the expense of price.

Overall, we are pleased to see broad travel demand remain strong in what appears to be a more structural post-pandemic environment of people prioritizing travel above most other categories of spend. This has held up despite inflation and recession worries and even more recently, bank system concerns. While economists continue to debate potential recession outcomes and clearly, many unknowns are still out there, consumers have so far shaken it off and continue to travel.

Against this backdrop in our consumer business, we continue to invest in our strategy of acquiring and retaining high value loyalty members and app users across our 3 leading brands. As I have explained before, these cohorts drive higher production and repeat rates versus other customers, ultimately leading to higher lifetime value.

Q1 '23 was another step in this journey as we saw our active loyalty member base for our Core OTA brands grow over 25% year-over-year and the percentage of gross bookings coming through our app roughly double what it was in 2019. This continued growth in our base of valuable customer cohorts, obviously, bodes very well for our future.

I've also talked for a number of quarters about our platform journey and in particular, about the drag we had last year on our business resulting from the migration of Hotels.com to the Brand Expedia stack. I'm pleased to say that with that migration fully behind us, Hotels.com is now back in growth mode. We are already seeing higher conversion, increased feature velocity and higher bookings. In fact, year-over-year bookings growth for Hotels.com was nearly 20% in Q1 '23, which is beginning to approach the almost 30% we saw in Brand Expedia. This inflection back towards growth was exactly what we had expected, and we were pleased to see the pivot come so quickly.

As you may recall, we are following the same migration path with Vrbo, which has now started taking some traffic on the Expedia stack in our largest markets. Just as we saw last year with Hotels.com, this work has slowed conversion and feature work on Vrbo for the past few quarters. And as we cut over, we expect some inevitable degradation in conversion due to the switch. But as we get this migration finished in the coming months, Vrbo too will be in prime position to benefit from the Expedia platform and just like Hotels.com will benefit from reaccelerating testing, conversion, and feature improvements.

Our tech journey hasn't been easy, but we had to have conviction to give up some short-term gratification to get to the promised land. With a couple of last big lifts finishing this year, we will finally be in position for all of our business to accelerate their velocity of innovation and deploy more traveler features as widely as possible. In particular, I'm excited about the power to deploy AI and machine learning to all corners of our product to enhance the customer experience and move towards our North Star of true personalization. To that end, you probably noticed our launch of the Expedia plug-in for ChatGPT and the launch of ChatGPT in our own Expedia iOS app. This would not have been possible at this speed or with this efficacy in our prior world, and it's just a small piece of what the future will hold. It is yet to be seen how impactful large language models will be in facilitating travel shopping. But for us, this is just one step in a journey to bring the best technology to our members and partners at an accelerated pace.

And to be clear, we have already been at the cutting edge of deploying AI and ML across almost all experiences for our consumers. When they land on our site, we use AI to customize the sorting and filtering options and the images we render to make the shopping experience most relevant to them. AI allows us to deliver price predictions and enable comparison shopping so they can book the right product with confidence. Then post-booking, we use AI and our service stack to help consumers self-serve their problems, and it even helps our customer service agents more quickly address issues. While we have been using AI and ML for some time to make the experience better for consumers, we will go much further this year to continue to deliver the best technology in online travel.

Another exciting milestone ahead of us is our unified loyalty program, One Key, which will be released in July in the United States. It reflects the culmination of years of work on the technology side to get to a solution that enables earn and burn across multiple products and brands in our portfolio. We've been busy testing this program and sourcing preferred deals for our members, all with great results to date, and we cannot wait to launch it this summer.

I discussed many times how our broad investment in technology not only benefits the B2C traveler experience, but how it also enhances our B2B partner experience. This includes the over 400 million loyalty members we serve through our template partners and more than 35,000 offline travel agencies we power across more than 30 countries, all the way to our numerous API partners who take our inventory and certain debt capabilities to build their own experiences.

On the back of this, demand in our B2B business continues to accelerate worldwide. We had yet another quarter of impressive growth with revenue growing approximately 55% year-over-year. We continue to sign new business, including SoFi, who has launched our full template product to their customer base. And as we look to enhance our partnerships with our biggest suppliers, we went live with both Hilton and Accor who will use our capabilities to sell packages on their sites. These are just a few examples, and we have many more wins coming this year.

We continue to innovate for our supply partners and equip them with highly differentiated solutions. Last year, we spoke about our optimized distribution product that gives our lodging partners greater control of their wholesale business. This product has helped some of the biggest hoteliers in the world, and over the past 2 years, we have tripled the number of participating chains using this capability. There are significant innovations coming this year to give more control to our partners and allow smaller partners to participate in the product. I'm particularly proud of this product as it truly represents a winning technology for the entire industry and allows us to provide much more than just the marketplace for our partners.

Finally, though somewhat more nascent, we have talked about our ambitions to externalize our tech in the form of microservices to help any kind of travel company use our tech to enhance their business. Our first pilot of our fraud capability started late last year, and I'm proud to say we now have our first paying customer on the service. We also have other products in beta testing with a number of partners, including our best-in-class service technology and our revenue management API. While still early days, we believe that by delivering our technology as microservices, we are greatly expanding the addressable market for our tech and cementing our technology as the core operating system for the travel industry. Next week, we will host our EXPLORE partner event at our Seattle campus, where we are excited to showcase what we've been working on for our partners and how we are helping our partners sell more, operate more efficiently, and ultimately better serve travelers around the world.

Overall, I'm really pleased with our progress. I'm excited that we're in the final innings of our tech transformation, and I'm encouraged by the incremental momentum we achieved with every step. We've been willing to take some short-term lumps in order to get these moves finished, but the rewards are now clearly becoming visible in the Hotels.com reacceleration and the sheer velocity of our tech delivery. And in our B2B business, where we have not had disruption, and have only enriched our offerings, our growth has been phenomenal. No company is doing more to move travel tech forward and make the entire experience better for travelers. And ultimately, that is how we will win.

And with that, let me hand it over to Julie.

Julie P. Whalen - *Expedia Group, Inc. - Executive VP, CFO & Director*

Thanks, Peter, and hello, everyone. I am pleased with our performance in the first quarter with record lodging levels driving gross bookings up 20% year-over-year, revenue up 18% to its highest ever first quarter levels and record free cash flow. Our robust top line performance reflects the success we're seeing from our strategic growth initiatives as well as the continued health of the travel industry. And it's this strength in the business that gives us the confidence to continue to buy back our stock at accelerated levels at $600 million, one of the largest buybacks we have done year-to-date.

Before I jump into more of the details, I wanted to remind you that effective this quarter and going forward, all financial comparisons will be on a year-over-year basis. As a result, we no longer need to refer to like-for-like growth rates as the Egencia transaction and associated Amex GBT supply agreement closed in 2021. Additionally, to provide more clarity and transparency, we have removed less relevant disclosures and discussions within the press release, while at the same time, added new disclosures such as lodging gross bookings. Of course, we will continue to evaluate whether any additional disclosures may be helpful over time, and we'll update you accordingly.

It is also important to note that our first quarter 2023 growth rates as compared to 2022 were negatively impacted by FX headwinds of approximately 200 basis points to gross bookings, 300 basis points to revenue and 1,600 basis points to EBITDA. We also saw an approximately 80 basis point headwind to the EBITDA margin.

Now let's discuss more of the financial details regarding our performance this quarter, beginning with our gross booking trends. Total gross bookings of $29.4 billion were up 20% versus the first quarter of 2022 and saw a sequential acceleration in the year-over-year growth rate from the fourth quarter. Growth was driven primarily by total lodging gross bookings, which grew 19% versus last year and reached a record quarterly level of $21.1 billion.

In our hotel business, we saw significant growth from our B2B segment, driven by strong demand in EMEA and APAC. In our B2C business, Brand Expedia maintained strong growth and our Hotels.com brand showed impressive recovery post its migration to the Brand Expedia platform. These results are also aided to some extent by shifting demand patterns. For instance, as more and more businesses return to hybrid work policies, we've seen increased demand in urban markets and a reduction in length of stay. So while these trends are helping our hotels business, the same trends are also putting some pressure on our Vrbo business. Yet this pressure was far outweighed by our hotel strength, enabling us to maintain total lodging bookings at record levels.

We also saw strong growth in our air bookings this quarter, especially in international travel, which was more impacted by the Omicron variant during the first quarter last year. This air strength was both in the number of tickets sold and an air ticket price increases as demand continues to outstrip capacity. It is great to see that air continues to gain momentum despite higher prices and international air has recovered to close to 2019 levels.

Moving to the key financial metrics in the P&L, starting with total revenue. Revenue was the highest first quarter on record at $2.7 billion, up 18% versus the first quarter of 2022. The revenue margin at 9.1% was down slightly versus last year, driven mostly by the strong recovery in our lower-margin air business. Cost of sales was $411 million for the quarter, which is up about $43 million or 12% with approximately 100 basis points of leverage as a percentage of revenue versus the first quarter of 2022, driven by ongoing efficiencies primarily across our customer support operations. We benefited from lower customer support call volume as well as the continued efficiency from the various automation initiatives we have implemented over the past few years, and we expect to continue to find even more efficiencies as we finish our migration onto one platform in areas such as cloud and license and maintenance costs as we eliminate redundant systems.

Direct sales and marketing expense in the first quarter was $1.5 billion, which was up $311 million or 26% versus last year. There were 2 main drivers of the spend increase. First, in our B2C business, we leaned into marketing to take advantage of the strong demand environment and to accelerate gross bookings growth. And we also maintained our marketing spend mix towards longer-term payback channels to drive loyalty members and app users, which given the longer-term return profile of the spend is less closely correlated to demand within any given quarter.

The second reason for the increase in marketing spend is an increase in commissions to support the accelerating growth in our B2B business, which fall into our direct sales and marketing line. These commissions are generally paid on a stayed basis and to a contractually agreed percentage. And therefore, the returns against marketing spend are more guaranteed and immediate. Given these factors and the fact that we underinvested last year due to Omicron, we did see marketing deleverage.

Overhead expenses were $588 million, an increase of $56 million or 11% versus the first quarter of 2022, growing slower than revenue growth, resulting in leverage of approximately 160 basis points. While we remain disciplined on our overall cost structure, we continue to invest in talent across our product and technology teams in support of our platform initiatives to drive growth.

EBITDA was $185 million, up $12 million or 7% versus the first quarter of 2022, which includes the 1,600 basis point negative impact to growth from FX. Excluding this year-over-year negative FX impact, EBITDA grew 23% and ahead of revenue growth, resulting in an EBITDA margin, excluding FX, 10 basis points above last year.

Free cash flow for the quarter was at record levels, at a positive $2.9 billion or up 3% versus 2022, primarily driven by higher working capital from the outperformance in our gross bookings. On the balance sheet, we ended the quarter with over $5.9 billion in unrestricted cash and our undrawn revolving line of credit of $2.5 billion, which provides us with ample liquidity of $8.4 billion to operate the business.

From a debt perspective, our debt level remains at approximately $6.3 billion with a leverage ratio of 2.7x. However, in order to further fortify our investment-grade rating, we are targeting a leverage ratio of approximately 2x. And through EBITDA growth and potentially some early retirement of debt, we expect to make progress towards this goal by the end of the year. The great news is we have recently received upgraded ratings or outlooks from all 3 rating agencies, demonstrating the actions we have taken to improve the financial strength of the business are being well received.

As far as capital allocation, given our strong free cash flow levels and a stock price that we believe remains undervalued relative to our expected long-term performance, we have been opportunistically buying back our stock on an accelerated basis. Year-to-date, this is one of our largest levels of buybacks of $600 million or nearly 6 million shares. Post these buybacks, we have ample levels of shares remaining under our existing authorization for future repurchases at approximately 12.1 million shares. And considering our ongoing strong liquidity and free cash flow, as long as we continue to believe that our stock remains undervalued and does not reflect our confidence in the long-term strength of the business, we plan to continue buying back our stock opportunistically throughout 2023.

Looking ahead, given the strength we continue to see in our business, we are reiterating our full year outlook of double-digit top line growth with margin expansion. As it pertains to the second quarter, it is important to remember that although we continue to see strong travel demand, we expect year-over-year top line growth to moderate in the short term to mid-single digits, primarily driven by a tougher compare given the strength in the business last year from the immediate rebound we saw post Omicron as well as some short-term disruption to Vrbo resulting from its migration to the core Expedia stack.

In addition, similar to the first quarter, we expect to lean into marketing in the second quarter as we invest to drive gross bookings and increase loyalty membership and app usage ahead of the busy summer season, all of which has set us up for a stronger back half. Overall, we expect to see EBITDA margins in the second quarter to be relatively in line with last year.

In closing, 2023 is off to a great start, with record revenue and cash flow. The travel industry appears to be strong and growing, and our growth initiatives are gaining momentum. And all of this, we believe positions us well to drive long-term growth and shareholder returns.

And with that, I would now like to open the call for questions. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question today comes from Lee Horowitz with Deutsche Bank.

Lee Horowitz - *Deutsche Bank AG, Research Division - Research Analyst*

Great. So you talked a lot about continued improvement in loyalty and app usage. But can you maybe help us sort of clarify sort of all indirect bookings and how that's trending and how that informs the way you view advertising leverage, particularly in the second half of the year and you look out to next year? And I have one follow-up after if I could.

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Sure. Thanks, Lee. It's a little hard to hear you, but I think I got it. The -- so basically, the way we think about it is, our business, we said it last quarter, it's running at a similar level. About 2/3 of the business comes from direct. That continues to grow as a nominal number, but as a percentage, it's fairly similar to where it was a quarter ago. And basically, yes, we are investing in app and these longer -- and loyalty and these longer-term payback products. But remember, we're only taking a portion of our quarterly spend, if you will, and putting it into these channels.

So it's not like we reversed the model, and it's all into these long-term channels. We are peeling off a portion of it, a fairly modest but sizable portion, and putting it into these longer channels. It means we give up some short-term payback and it means we stack up these customers over time. But given that it's not our full spend, it takes a while for this to stack up. Then you add to that, that we are now getting back to the conversion levels we used to have and accelerating through them as we get HCOM on BEX stack, as we get Vrbo on the new stack and we're accelerating BEX itself because -- Brand Expedia itself because we are just upping the velocity of testing massively.

So we're getting a lot of improvement. A lot of it is coming through this year and coming even as we speak. And so the reason we have confidence in the leverage that will come in the back half of this year and the future is we're both stacking up the loyalty and the app usage and all these more direct channels. That's what we're doing with the money that we can tactically spend differently, but we're also changing and improving the product and the conversion in the product so that every dollar will work harder in the future.

So all of that's coming and then One Key launches in July, which is yet again another sticky product feature that will add millions of people from Vrbo, customers from Vrbo into the mix and allow more of our loyalty members to spend across more products. So all of that is coming kind of at the same time, not that it's going to be a moment in time inflection, but it's building on itself. And that's why we said second half of this year will be stronger. And obviously, going forward beyond that once we get past the One Key rollout, et cetera, would be stronger. So that's what gives us confidence in the marketing leverage. It's not like one tactical change in spend changes at all. It's a combination of building that up over time, plus adding the product benefits and getting all the technical work behind us.

Lee Horowitz - *Deutsche Bank AG, Research Division - Research Analyst*

Great. And then one more. With travel seemingly shifting back towards areas where you guys are incredibly strong, urban, international and the like, can you give us an update on how you think U.S. hotel share progressed in the quarter? And what your expectations are here for the rest of the year, particularly with HCOM accelerating at this point?

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Yes. I think broadly, we feel like -- from a share perspective in hotels in North America, we essentially held share, maybe slightly better. We're not overinvesting the problem again. It's a balance -- this journey is a balance of how you spend versus how the technology comes online. We could have spent a lot more on Hotels.com last year, but it wouldn't have been as effective as Hotel.com gets better, we can spend more.

So all of these capabilities give us more weapons to fight better in the fight. And so we feel like we've held maybe slightly better, and we should see acceleration from that. And equally importantly, we did pull back, as you know, in the past few years from some international spots where we were not as effective and as efficient, but as we now feel like the products improved, we have a marketing model that we believe in, we feel like we'll be in a position to start rolling out more aggressively. Not a North America story, it has been for a while, but this is really how do we grow beyond that as we get past these technical hurdles and are in a position to roll more quickly across the world.

Operator

Our next question comes from Kevin Kopelman with Cowen.

Jacob Seed - *TD Cowen - Research Analyst*

This is Jacob Seed in for Kevin Kopelman. Just a question on One Key launch. So with the launch in July, how are you thinking about some of the smaller brands that are not going to be included in the launch? And how are you thinking about managing them going forward?

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Yes. Thanks, Jacob. I think we've talked about it a couple of times before. But by and large, we have somewhat deemphasized and not invested as strongly in the smaller brands as we continue to put more heft behind the big 3 brands. One Key will envelop the big 3. And we certainly aren't going to take our brands away from people right away or anything, but we do believe that, that over time, people will migrate to our big 3 brands where the latest product features are, where One Key is, et cetera.

So essentially, the way to think about it, and that's why we've talked about how Brand Expedia is doing, how Hotel.com is accelerating is we've got a drag on the business, which is sort of our other brands going sideways to slightly down as against the businesses that are growing more quickly, where we're investing and where the product is accelerating faster. So it's essentially -- there's a little bit of the big brands have to eat the sideways or slightly slow degradation of the other brands, but that's something we've planned for in terms of the guidance we've given this year and certainly something we plan for long term.

Operator

Our next question comes from Anthony Post with Bank of America Merrill Lynch.

Anthony Post - *Bank of America Merrill Lynch - Analyst*

I guess a couple of things. When I see the B2B growth versus outpacing the core retail, how do you think about that business as a margin versus your core business? And should we expect to see more the retail accelerate as you kind of fix the platforms at Expedia and Hotels.com? And then secondly, as you think about the overall use of cash, anything to stop you from deploying cash flow to buybacks, anything on the debt side we should be thinking about?

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Yes. I'll take the first part and then leave the capital side to Julie. But -- so I think the B2B business has been growing terrifically, as I mentioned in my prepared remarks, we haven't had to do any big technical migrations. In fact, we've added to the capabilities over the last couple of years and we've seen the benefits of that in many of our business lines. That business saw great growth in part because it is more exposed to some of the geographies that came back last quarter. So the opening of Asia is more impactful for our B2B business, Latin America, et cetera.

So some of it is geographical mix that you're seeing there. But definitely, we expect our B2B business to continue to grow. I think I said a few years ago, this was an area we saw lots of opportunity that we were going to push into. So we expect and we'll be driving as much growth there as we can, again, to fill in the pockets of demand that we would not otherwise reach through our B2C business. But absolutely, we expect our B2C business to accelerate as we get through this major surgery we've done over the last few years, which has taken a long time and is painful.

But as we get across, we are in a better and better position every day to accelerate. We've got a few of these last lift to get through for sure. But hopefully, we're on the back 9, and we're close to the end of that, and we can put all our resource, technical product design resource against accelerating growth once we are across these things. So we do expect -- I'm not going to say I expect B2B to slow down to B2C. I expect B2C to accelerate, and I expect both businesses to grow well in the coming period.

Julie P. Whalen - *Expedia Group, Inc. - Executive VP, CFO & Director*

And from a capital allocation perspective, our approach hasn't changed. We did sort of lay out the targeted leverage ratio this time just to sort of give disclosure to what we internally are striving for, and we will make progress towards that this year and going forward. And we can make progress towards that with EBITDA growth and potentially some small paydown of debt. And it won't take much given how much you already reduced our debt level.

So all that to say with strong EBITDA and strong free cash flow, we have a lot of cash available to be able to deploy to buybacks. As we have done with our largest one to date -- one of our largest ones to date that we've done about $600 million this year. So there's still ample room and availability to be able to buy back. And as long as our stock is trading at the levels it is relative to what we know the long-term performance company is going to do, we will continue to do that opportunistically.

Operator

Our next question comes from Eric Sheridan with Goldman Sachs.

Eric James Sheridan - *Goldman Sachs Group, Inc., Research Division - Research Analyst*

So much of the focus for investors tends to be in the North America market. And you made some interesting comments about some of the international markets on this call so far. Can you give us an update on your view on where you sit competitively and how you think about the investment cycle to drive growth away from North America, maybe through the lens of some of the B2B and B2C initiatives and some of the refocused brand initiatives, so we have a better understanding of that?

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Sure. Let me kind of work backwards. I think B2B is a great business, a great tool for us to reach pockets of demand. As I said, that we don't otherwise reach or reach well. That might be geographical like China, for example, where we have -- where we expect a good rebound there, and we have a nice book of business with partners in China and -- or it might be a loyalty program in a market we're already in, but that has a captive audience that's burning points in a bank credit card program or something.

So that business definitely gives us ways to participate in travel economies that we are not otherwise sort of going head-to-head in the B2C side. But as we talk about the B2C side, we've had presence in many markets around the world, some of which we are just leaned into as we've ever been, and some of which we -- as we talked about in the prior periods, we pulled out of because the economics just weren't worth it. We were losing money and not gaining retainable share, I would say, without having to continue to spend than lose money.

We believe what we had to do and what we've been doing is building a better model, a better product, a better go-to-market marketing strategy that helps us acquire the right kinds of customers who value what we have, which is the best product, the best loyalty program, the best service in the category and that may or may not be every customer in the world, but we believe we can target those customers in lots of geographies. There are big pockets of them that we don't touch right now that are opportunities, and there are also pockets of them that we used to touch less efficiently that we think we can go back to with strength.

So I think you'll see us -- it's not going to be a huge story in the numbers this year, although we have seen a great comeback in EMEA, in Asia, in Latin America, where we do participate. But that's a bigger story over time as we get our One Key launch done, as we get our product complete and as we can start to move our strategy more holistically into new markets and target the right customers for us.

Operator

Our next question comes from Lloyd Walmsley with UBS.

Chris Kuntarich - *UBS - Research Analyst*

This is Chris on for Lloyd. Maybe the first question on just as we think about the '23 double-digit growth guide on both the top and bottom line. Just philosophically, how are you -- how do you think about potentially showing letting upside flow through on either the top line or bottom line for this year? And then second, just going -- it sounds like things are turning around in the air product. Just can you talk a bit about how you think about air as a separate funnel potentially for driving room night growth from here?

Julie P. Whalen - *Expedia Group, Inc. - Executive VP, CFO & Director*

So as far as the guidance, I didn't hear all of what you said, but I think basically the question is, what gives you the confidence to be able to hit the top line and the bottom line guidance, which does include margin expansion. I mean it's several things. Peter alluded to many of them. But I mean, obviously, it starts with the travel industry -- strength of travel industry is really strong. Everyone is reporting great numbers. And so clearly, the consumer is prioritizing their spend on travel.

We're seeing it in our own business with the success we're seeing with the Brand Expedia business with a 30% growth in gross bookings and then Hotels.com getting on that platform and at post-migration now driving 20% increase in gross bookings. We have a B2B business that's growing 55%, which is a halo for the rest of the business. We have Q2, we're at the moment where we've got to address this tougher year-over-year compare, and we're going through the Vrbo migration. But when we come out the other side, Vrbo will be on the platform that is delivering that same sort of double-digit growth. And so we're excited to see that. And then on top of everything else we're doing with the growing loyalty member base, the growing app user base and all of the goodness that, that will drive in the back half, along with all of our tech and product initiatives, that's what gives us the confidence that we're going to be able to hit this guidance on the full year.

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Yes. And I'll just take the second part on air. We've been innovating a lot on air. Now it's important to remember, since if you go back pre-COVID, we sold Egencia, our corporate business to Amex GBT, and we got out of the air business with our partner, Chase. So there's some weird comps if you go back in history. But if you look at the air product, I think we've made huge progress on it as a product. You'll find we have price tracking and predictions now in most of the world. That's been a great engagement product. It's helped with conversion. It's helped with attached sales of hotels and other things.

We've increased our speed. We've got smart shopping, which is a new capability of comparison shopping -- or looking at the best seats and the different economy -- basic economy, et cetera, and comparing more easily. We used AI to suggest the best option for each customer. So all of these things are in the works. We've improved our search speed considerably recently. So there's a bunch of work going in to make that product, the preeminent product in the space again. And I think we definitely look at it as an opportunity. It's a unique capability, something we've always been strong in, something we can drive traffic through. We have a lot of opportunity to improve our attach rates and our packaging, if you will. We have terrific package rates for many of our partners, and we've just started deploying as part of the run-up to One Key member flight member discounts, which we've never had before, which is a great opportunity for airlines to use their pricing to help get the best customers out of our marketplace.

So I think there's a lot of things that have been in the works and coming. And again, this is just one of the areas where I say the technology has been evolving through this period and it's all getting to a place where it can be much more effective. And we haven't spent much time on it. But obviously, once everything is on the same stack, we start to have a unique capability to start moving more products across brands. So things we've talked about before, like better selling, our Vrbo content, on our OTA brands and through those points of sales becomes a reality. Selling Vrbo content through our B2B partners, there's some vacation rental content in our OTA brands that isn't on our Vrbo stack. So we will have that consolidated. So there's lots of opportunities that come from this migration that are all in sort -- air is one of them, and we've done a lot there, but there are many.

Operator

Our next question comes from John Colantuoni with Jefferies.

Chris Suchecki - *Jefferies - Research Analyst*

This is Chris on for John. Can you double click on the commentary from last quarter around delivering margin expansion throughout the year? And maybe just give us a sense for kind of what line items we should expect that to come from and then help us size the (inaudible) you're anticipating as well?

Julie P. Whalen - *Expedia Group, Inc. - Executive VP, CFO & Director*

Yes. I mean as far as margin expansion as we move throughout the year. I mean, certainly, as we deliver more top line growth. And right now, we're sort of more of a mode of driving gross bookings where we don't get the benefit of that to revenue -- into earnings until the stay. And so in the back half with this outperformance that we're seeing today, we expect to have that benefit the P&L. And of course, we're expecting marketing leverage as we move throughout the year based on all the things we talked about that we're going to benefit from.

So it's really those two lines. We're going to be obviously working on efficiencies across the company as we deliver on our tech stack and start to be able to repurpose individuals and cut costs and things like that, and that will also drive some efficiencies, but it's really the top line revenue growth and the marketing efficiencies in the back half.

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Yes. And I'd just add one thing, which is the shape of the curve this year is we have a lot of work to get done, and that involves a lot of people being dedicated to these big lifts. But as we get towards the end of the year, a lot of that work subsides so that we can stick those people and that great talent on growth initiatives that are more near-term generative.

So that's part of what happens is every time we put something to bed, we get more resource available to drive conversion growth, to drive improvement in the customer experience that turns into money. So that the efficiency we get going forward once we're over these big lifts is much bigger. How much of it hits this year versus future years, TBD. But that's the journey we're on is we've got to get over these big humps and then we start -- we've seen it already when we did the Hotels.com conversion, the migration. We freed up a lot of talent to work on near-term conversion wins, and it's been hugely productive for us. Again, every time we do one of these, we get more capability back to put against more near-term uplift in the business. And so that's where we start to get more separation relative to the cost base, and that's partially this year, but it's obviously more going forward.

Operator

Our next question comes from Tom Champion with Piper Sandler.

Thomas Steven Champion - *Piper Sandler & Co., Research Division - Director & Senior Research Analyst*

Peter, just any interesting observations behaviorally on the GPT plug-in, maybe too early, but just curious any comments. And then I think this is self-evident in your implication, but the tech replatforming will be ostensibly complete in the U.S. in July with the launch of One Key. Just curious if that's the case. And then maybe just a final one for Julie. I was a little surprised by the outsized impact of FX on EBITDA in 1Q. Curious if you could elaborate on that or add any details.

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Thanks, Tom. I'll try the first couple. So you said the GPT -- the ChatGPT plug-in, which is that is where we have made a plug-in for their environment so that when people are searching, thinking about travel and their environment and want to see if there are hotels near the Eiffel Tower or what flight flew from L.A. to New York on Tuesday, if they have our plug-in, we can provide that. That is still only available in the paid and the developer environment. So it's not like out in the wild. So it's small still, but interesting to see how people behave. People are using it. And obviously, it's not materially changing our numbers, but it's definitely a lot of interesting learnings for us.

We've also deployed it, which may have been what meant into our own iOS app, and that's to allow people to essentially use the capability in our app to do a similar thing, what hotels are near the Eiffel Tower or whatever they might be searching for. And what we do then is if ChatGPT provides answers and it's a series of hotels, we will take those hotels, save those hotels for people so that they can then go shop, comparison shop, look at images, do whatever they want.

Again, early days, but people have engaged with it. It's been interesting to people, not a huge driver yet. And that's why I say we don't know how big a driver is going to be in behavior, but it's definitely interesting. And I'll just add, we wouldn't be the only company in the world, but we are on the forefront of looking at other ways that large language models can help other parts of our experience, whether it's with our partners, whether it's turning descriptions into property descriptions, making that easier for people. There's a lot of ways we think we can look at using AI in this construct, but we use AI and machine learning a lot of other constructs as I talked about, whether it's optimizing pictures or anything else.

So it's interesting, it's early, and we'll see and we'll see when the plug-in is available to a wider audience, what it drives, and we'll see what ChatGPT does to the search environment. We'd love to see more competition in global search. So we're rooting for a more competitive search environment, and we think we're staying on the absolute front of what anyone is doing in travel with large language models.

As far as the tech replatforming goes, yes, the answer to your question is, yes. The last of the big things in the U.S. is really to launch One Key. Now a launch is a launch. And sometimes it takes a little time to harden that and make sure everything is working perfectly. But yes, essentially, once One Key is done in the U.S., that's the last of the sort of big boulder lifts we've had. Now we want to launch One Key in more places. There's work to do to complete the set, if you will, as we complete the geographical set of capabilities and so forth. But in terms of the really big lift on the biggest piece of our business, that would be the last of the lifts, and that's why I say, I think we'll have a lot more talent available to drive other things once we're over that hump.

Julie P. Whalen - *Expedia Group, Inc. - Executive VP, CFO & Director*

And as far as FX, obviously, it just really depends on which currencies we are transacting in and their relativity to the strength of the U.S. dollar. And the difference between the delta on the top and the bottom line is really just a function of Q1 is our lower earnings quarter. And so it has a more pronounced impact on the lower level of earnings relative to the top line. It's obviously a much bigger number. So it's just -- it's a function of math.

Operator

The next question comes from Mario Lu with Barclays.

X. Lu - *Barclays Bank PLC, Research Division - Research Analyst*

So the first one, a follow-up on One Key. You mentioned it's rolling out in July. Just -- is that a global rollout? Or just U.S? And then is there like a rough time frame we should think about in terms of when we should see the benefits of the joint loyalty program? I understand that take rates will take hit initially once points are redeemed. But just curious how we should think about the expected payback period?

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Sure. Thanks, Mario. So yes, the -- we are rolling on the U.S. first. We will roll out in the rest of the world more later in the year and next year. And then just keep in mind, there are differences in the rest of the world where, in some cases, not all brands are present. In some cases, we have a different brand in lieu of one of our brands. So they will take on slightly different flavors across the world. But the U.S. obviously is the biggest proof point and the biggest place in which we think the installed base gets the biggest lift.

And as far as that payback goes, obviously, loyalty is a thing which drives future repeat, future loyalty, future engagement. And as you know, we've been focused on signing up as many -- even before One Key, on getting way more of our customer base signed in, signed up and engaged with our products, not least of all because they see the best prices that way, they get rewarded for their travel, and they have reasons to come back. So we've modeled it a lot of different ways. It's difficult to say how quickly it pays back given that travel for most people is a 1.5x a year kind of endeavor on average. Now obviously, there are people who go 20x a year, like everybody on this call probably.

But -- so we will see, we've modeled it a series of ways, but we don't expect a huge payback in this year. We think some of it will come back this year and some of it will come back in the future, but we'll keep building on itself. And as we've said before, our intent is between all of the levers we have of spend, be it direct sales and marketing, paid search, discounting, loyalty and everything else. We view that as one pool of capital, and we intend to balance between those pools.

So as we as we provide more loyalty, which will drive, again, some longer-term payback than the short-term paid search stuff. We will pull it out of other spots to accommodate that and live within an envelope of spend that we think is right in terms of what we should be spending all up against buying that future business. So again, it's a little bit a timing dislocation compared to that quick twitch muscle of performance marketing, but we think well worth it. And again, we are going to envelope a whole millions of customers in Vrbo that used to live outside our loyalty plan that will all of a sudden be able to spend into our loyalty plan whether it's for a different kind of trip or something else. And likewise, all of our existing loyalty members in Expedia and Hotels.com will be able to use their points against vacation rental. So there's a lot of things that could be shorter to it, so a lot of things that will be longer and we've modeled it a bunch of ways, but we'll see. We don't have too much of the benefit coming in this year.

X. Lu - *Barclays Bank PLC, Research Division - Research Analyst*

Got it. And just one for Julie, in terms of the 2Q commentary on the top line to mid-single digit, any color in terms of the drivers to get to that in terms of what level of bookings growth or take rate we should expect?

Julie P. Whalen - *Expedia Group, Inc. - Executive VP, CFO & Director*

No, we didn't go into that level of detail. I mean, obviously, it's a tough compare, I think, for a lot of companies for next quarter given the immediate rebound in travel post Omicron. So that's the biggest driver. That's bringing us down to the single digits. And of course, as we've been talking about, we're doing the Vrbo migration during the same time period. So those are the 2 real big drivers. And so I wouldn't think about anything else that's a big at play there.

Operator

Our final question today comes from Jed Kelly with Oppenheimer.

Jed Kelly - *Oppenheimer & Co. Inc., Research Division - Director & Senior Analyst*

Great. Just 2 questions. Just on the Vrbo migration you called out. Are you seeing any pressures from sort of the vacation rental markets having call it, 3 record years and now people being able to travel to other destinations? And then just my second question related to supply. Can you just give us a sense how your Vrbo supply is trending? And then your supply in some of the international markets where we are in supply?

Peter Maxwell Kern - *Expedia Group, Inc. - Vice Chairman & CEO*

Yes. Thanks for the question, Jed. So if you missed it, I mentioned it. But yes, we have seen a little bit of flattening in demand in VR, and that is largely because the length of stays have shortened, people are going to cities more than they're going to long extended beach -- COVID-era beach vacations or mountain vacations where they took a month and went wherever. So that's definitely changed, hybrid work has changed. So all of those things are impacting macro demand slightly.

Now much of it is going back to cities. In our VR business, we don't participate as much in the urban market, though we do have good product there. I mentioned it before, but we actually have good urban market product in our OTA brands, but it's not in our Vrbo brand. So one of the things that the Vrbo migration brings us is the ability to get all that content together. And that actually will help a lot. And as you think about supply because we've had it kind of in pockets as opposed to all available everywhere. And that makes a big difference in supply.

Having said that, we've grown supply well in our Vrbo. And again, in our core product, which is whole home or apartment, and is focused not on shared spaces or any of that. But we've had good solid growth throughout the period, and we continue to add product that are principally focused on places where we've seen the most compression overall in the world. We're not trying to break brand-new ground where we don't have demand. But we have seen solid growth in supply. We'll continue to push into that. But I think the biggest unlock for us will actually come when we get the Vrbo migration done and all of our supply can move really to any point of sale and any endpoint in our brand system. And that's -- it will take us a little while to optimize. So I don't think that's like a moment in time inflection point. But that's the biggest opportunity for us to amp up our supply and reveal it better to the demand in the market.

Thank you. And with that, thank you, everybody. I think that was our last question. Thanks for joining us. We'll see you next quarter. Take care.

Operator

This concludes today's call. You may now disconnect your lines. Have a nice day.