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# TripAdvisor, Inc. *(TRIP)*

Q2 2012 Earnings Call

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*Senior Director, Investor Relations, TripAdvisor, Inc.*

### Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

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### Julie M. B. Bradley

*Chief Financial Officer, Treasurer & Senior VP, TripAdvisor, Inc.*

## OTHER PARTICIPANTS

### Nathaniel Schindler

*Analyst, Bank of America Merrill Lynch*

### Heath Patrick Terry

*Analyst, Goldman Sachs & Co.*

### Tom Cauthorn White

*Analyst, Macquarie Capital (USA), Inc.*

### Herman Leung

*Analyst, Susquehanna Financial Group LLP*

### Mike J. Olson

*Analyst, Piper Jaffray, Inc.*

### Anthony Joseph DiClemente

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### Scott W. Devitt

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## MANAGEMENT DISCUSSION SECTION

**Operator:** Good day, ladies and gentlemen. Welcome to TripAdvisor Second Quarter 2012 Conference Call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session with instructions following at that time. [Operator Instructions] As a reminder, this conference call is being recorded.

Now I'll turn the conference over to Will Lyons, Senior Director of Investor Relations. Please begin.

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### Will Lyons

*Senior Director, Investor Relations, TripAdvisor, Inc.*

Thank you, Tyrone. Good afternoon, everyone, and welcome to TripAdvisor's second quarter 2012 earnings conference call. We appreciate your joining us today. I'm Will Lyons, Senior Director of Investor Relations for TripAdvisor. And joining me on the call today are CEO, Steve Kaufer; and our CFO, Julie Bradley.

Before we begin, I'd like to remind you that today's presentation contains estimates and other statements that are forward-looking under the Private Securities Litigation Reform Act of 1995. These forward-looking statements are subject to risks and uncertainties and involve a number of factors that could cause actual results to differ materially from those expressed or implied by such statements.

Additional information concerning these factors is contained in TripAdvisor's filing with the SEC, including our Annual Report filed on Form 10-K, which is available on [www.sec.gov](http://www.sec.gov). The forward-looking statements included in this call represent the company's views on July 24, 2012. TripAdvisor disclaims any obligation to update these statements to reflect future events or circumstances.

During this call, we will refer to non-GAAP financial measures that are not prepared in accordance with Generally Accepted Accounting Principles, including adjusted EBITDA, adjusted EBITDA margin, non-GAAP operating expenses, non-GAAP net income, non-GAAP net income per diluted share and free cash flow. A reconciliation of these non-GAAP financial measures to the most directly comparable GAAP financial measure is available in the press release announcing our second quarter 2012 financial results. This press release as well as other important content is available in the Investor Relations section of our website, [www.tripadvisor.com](http://www.tripadvisor.com).

And with that, I'll now turn the call over to Steve.

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### Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

Thank you, Will, and welcome, everyone, to today's conference call. The second quarter completed a great first half of 2012 for TripAdvisor. We generated record quarterly revenue of \$197 million and adjusted EBITDA of \$97 million, continued to grow traffic in hotel shoppers while taking important steps to optimize traffic quality, and continued growing and leveraging our social and mobile initiatives to drive user adoption.

We're making tremendous headway on content collection, membership and traffic. At the end of Q2, we passed the 75 million reviews and opinions milestone and our travel community continues to add content at 50 contributions per minute, which translates to an accelerated pace of more than 25 million contributions for 2012. Marketable number growth, travelers whom we have permission to email on a regular basis, also accelerated during the quarter, growing over 25% to more than 32 million, up over 60% year-over-year.

At the top of our funnel, total traffic growth also remained strong as Q2 comScore data reflects an average of more than 54 million worldwide unique visitors at TripAdvisor sites, up more than 31% year-over-year. Further down the funnel, hotel shoppers, the key metric for our quick base revenue line, was up approximately 30% year-over-year and would have been higher were it not for a strategy change that we'll discuss in a minute.

User engagement on the site was up as well, as we saw growth in time spent per session and page views per session according to our internal log files. We attribute this growth in user engagement to our robust email campaigns and continued efforts to personalize the site experience.

In social, we are finding great ways to leverage the building blocks we've put in place on the Facebook platform. In April, we emerged our TripAdvisor in Cities I've Visited apps into one application, better integrating Facebook's users' activities within TripAdvisor and allowing friends to find TripAdvisor more easily on Facebook.

In the first half of the year, TripAdvisor published more than 300 million actions generated from member activity on our website or using our app into Facebook's Open Graph. In June alone, we had over 32 million logged in Facebook users use a TripAdvisor app or be instantly personalized on the site. This traffic level makes TripAdvisor the second most popular Facebook app according to app data. These efforts have been very successful in terms of brand awareness, content and community building, and growing our friend connected member base.

In addition to social, our mobile initiatives continued to thrive as we continue to invest in and innovate on this fast growing platform. During the quarter, we rolled out our new iPad app and introduced Facebook login functionality. We also launched 30 new free city guides across iOS and Android, bringing our coverage to 50 cities. As of June 30, we reached over 22 million cumulative mobile app downloads of our TripAdvisor, City Guides and SeatGuru apps on smartphones and tablets, up more than 200% year-over-year. We also grew to more than 27 million monthly unique visitors of TripAdvisor on mobile devices in May.

Further, tablet continues to be our fastest grower in terms of mobile page views, sessions and unique users, and accounts for more than three-quarters of our mobile revenue. We're obviously pleased with our mobile growth and we are focused on creating more complete user experience on mobile, which will lead to an even more loyal and engaged user community.

One of the more interesting developments this quarter was our traffic quality improvement initiative, which spanned the quarter and affected all geographies. We leveraged our massive amount of user click and traffic conversion data to identify traffic that converted well on TripAdvisor but didn't convert as well on partner sites. In other words, these are visitors who browsed the TripAdvisor site, clicked on a paid link to visit one of our clients but ultimately didn't make a booking. While we get paid for that click, we know we aren't ultimately helping our clients make money.

Using this information, we reduced our SEM spend on lower performing traffic, as we believe this will increase the conversion rate for our clients. Rather than reinvest these cost savings in search marketing, we chose to reallocate some of it towards our traffic diversification efforts, including our marketing campaigns on Facebook. This initiative lowered our hotel shopper growth, which translated into lower top line revenue growth but also drove our improved Q2 EBITDA performance. Absent the strategy change, we would have seen higher Q2 hotel shopper growth, perhaps even accelerated growth from Q1, and revenue could have been approximately \$5 million to \$10 million higher.

This traffic quality improvement strategy is another example of us doing what's right for the business longer term even at the expense of near-term growth. Whereas our site redesign last year helped improved user experience for

our community, this initiative targets improved downstream conversion for our clients. We view this as a new steady state for our business as we strive to optimize and diversify our traffic sources where we can easily increase SEM spend if the opportunity arises.

Despite this optimization, it's important to note that we continue to expect revenue growth in the high teens for 2012. However, our strong Q2 adjusted EBITDA margin performance should not be taken as a new run rate. We have captured just a fraction of the global travel market online and we remain firmly within an investment cycle focused on capturing worldwide market share.

In other key investment areas we are pleased with the progress that we made during the first half of the year. Our rest of world growth remained strong, and notably, our APAC sales team was pleased to add Ctrip to our growing list of partners in that region. In our subscription businesses, our business listing team has progressed nicely on their sales force hiring plan and rolled out a new mobile upgrade product as a value-add for hoteliers and property owners.

Finally, we are also executing nicely in our vacation rental business on TripAdvisor and on HolidayLettings and FlipKey. In summary, we're tracking very well to our 2012 goals.

I'll now turn the call over to Julie, who will provide some color on the Q2 results and our financial outlook.

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## Julie M. B. Bradley

*Chief Financial Officer, Treasurer & Senior VP, TripAdvisor, Inc.*

Thanks, Steve, and good afternoon, everyone. Second quarter revenue increased 16% to \$197.1 million, in line with our expectations. In constant currency, revenue was up 19% year-over-year. Click-based revenue was up 13% year-over-year to \$151.1 million. The 7 percentage point sequential deceleration in year-over-year growth rate can be explained by three main factors: We benefited from increased conversion, more than offset by year-over-year decline in pricing and the traffic quality improvement strategy.

We saw increased hotel shopper conversion in Q2 relative to Q1 albeit on a slightly lower hotel shopper growth rate. Even with the unfavorable trend in foreign exchange rates, overall CPCs were stable in Q2 as compared to Q1. We did see CPCs increase in the US, but this was offset by CPC decreases internationally. However, when looking at the year-over-year growth rates sequentially, we had a tough pricing comp this past quarter compared to an easy pricing comp in the first quarter of this year. This accounted for 4 percentage points of the sequential year-over-year growth rate decline.

Finally, as Steve just described, we estimate that our traffic quality improvement strategy accounted for an additional 4 to 7 percentage points on the sequential year-over-year growth rate decline. Lots of moving parts, but the core fundamentals remain strong.

Display-based advertising revenue grew 14% year-over-year in Q2 to \$26.6 million. The sequential deceleration was due in part to specific timing of ad purchases, including a unique customer buy during Q2 2011. Overall, our CPM prices increased slightly as compared to Q2 of last year. We continue to maintain a premium price in the CPM market and stable click-through rates given our rich travel specific content.

Subscription, transaction and other revenue, which includes business listings, vacation rentals and our transaction businesses had a good Q2 growing 59% to \$19.4 million, just slightly behind our expectations. In business listings, we continue to see a huge opportunity to diversify our customer base and develop a channel to distribute value-added products over the long-term.

Our near-term challenge is ramping sales execution on a global basis such as connecting with a B&B in Vermont while also building a relationship with a large independent hotel in Cancun and concurrently determining the top domestic properties in Thailand. To that end, we are catching up to our aggressive sales force hiring plan and have seen encouraging productivity metrics. We remain focused on capturing the huge opportunity we have for business listings as well as growing our vacation rentals product in 2012 and beyond.

As it relates to geographic mix, despite macroeconomic challenges and unfavorable foreign exchange movement, non-US revenue was 49% of total revenue during the second quarter compared to 48% in Q1 and 44% in the second quarter of 2011.

On the expense side, non-GAAP sales and marketing expenses were \$63.3 million or 32% of revenue for the quarter, which is down sequentially in both absolute value and as a percentage of revenue. This was primarily due to lower SEM spend related to our strategy to increase traffic quality to our customers. We remain committed to making investments in our strategic growth opportunities and traffic diversification efforts. Given our year-to-date results, however, we expect non-GAAP sales and marketing spend to remain under 40% as a percentage of revenue for full year 2012.

Non-GAAP tech and content expenses were \$19.1 million or 10% of revenue for the quarter, which is up 17% sequentially, driven by additional head count costs and in line with our expectations. We expect this expense line to stay relatively constant on a dollar basis for the balance of the year.

Non-GAAP G&A expenses were \$14.8 million or 8% of revenue, in line with our expectations. Investment in our public company infrastructure is essentially complete and we expect quarterly G&A expenses to be relatively stable on a dollar basis through the balance of the year.

Depreciation and amortization totaled \$6.5 million or 3% of revenue and stock-based compensation expenses were \$6.8 million or 3% of revenue in the quarter. For 2012, we continue to expect depreciation and amortization to be approximately 3% of revenue and stock-based compensation to be approximately 4% of revenue.

Our effective tax rate was approximately 31.5% for the quarter. For the balance of 2012, we expect our effective tax rate to remain relatively unchanged.

In terms of liquidity, we ended the quarter with \$478.2 million of cash and cash equivalents. In early May, the warrants we inherited from the spin-off were exercised for approximately \$213 million. The warrant exercises were the primary driver of the uptick in our basic and fully diluted weighted average share count for the period.

Cash flow from operations was \$61.8 million or 31% of revenue for the quarter. We continue to expect full year 2012 cash flow from operations to track with adjusted EBITDA after providing for interest and taxes or low 30s as a percent of revenue.

Q2 CapEx was 3% of revenue. Given our capital efficient business model, we continue to expect this line item to remain in the low-single digit as a percent of revenue for 2012. As a result, we generated \$55.8 million of free cash flow during the quarter.

In terms of head count, we ended Q2 with just over 1,400 employees, up from just over 1,300 employees at the end of Q1. Hiring efforts for the balance of 2012 are global in scale and are focused on engineering and sales.

Also I'd like to provide a brief comment on foreign exchange impacts given the prevailing macroeconomic challenges overseas. As we've mentioned in the past, we forecast FX neutral based on current rates and do not try to anticipate movements in foreign exchange rates. Just over 20% of our revenue was denominated in euros and less than 10% in the British pound. A significant move in FX would have the greatest impact on revenue, as we have natural hedges to help mitigate bottom line exposure.

With that, let me turn to our outlook for the balance of the year. We continue to expect 2012 total revenue growth in the high teens. On the click-based revenue line, we are factoring in the Olympics and the continuation of our traffic quality improvement strategy as headwinds in Q3. We are also planning to roll out enhanced analytics to some of our large OTA partners on a test basis. Many of these customers have asked for more transparency in order to better understand the bid landscape and in turn increase their spend. We recognize the uncertainty this may present to our revenue results. While more transparency allows them to bid higher on their more profitable properties, it does come with a risk that clients will choose to optimize their spend without increasing revenue to TripAdvisor.

In addition, we saw strong pricing in the second half of 2011 prior to the rollout of lower Expedia pricing at the end of the year. However, we expect continued strength in hotel shoppers and lapping of last year's site redesign to more than offset the potential headwinds I just described. Given all these dynamics, we currently expect click-based revenue growth in the mid-to-high teens for the full year.

Display-based revenue faces a tough comp in Q4 based on an unusually strong demand in Q4 2011, which may not recur. Given this and our year-to-date performance, we now expect low double-digit annual revenue growth for display. We expect that full year subscription, transaction and other revenue growth will be consistent with our year-to-date results.

Importantly, early indicators for all these revenue lines are healthy as we continue to leverage our leadership position in the market. We continue to expect 2012 adjusted EBITDA to be higher than 2011 in terms of absolute dollars based on the better than expected results during the first half of the year. Given the strength in our core CPC business and reduced spend on SEM, we seek to reinvest all excess profits into our strategic growth opportunities and our traffic diversification efforts. We are committed to driving long-term user growth and engagement in the business.

In closing, the second quarter closed out a great first half of 2012 for TripAdvisor.

We will now open the call up to your questions.

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## Will Lyons

*Senior Director, Investor Relations, TripAdvisor, Inc.*

Tyrone can you please give the instructions.

## QUESTION AND ANSWER SECTION

**Operator:** Thank you. [Operator Instructions] First question is from Nat Schindler of Bank of America. Your line is open.

**Nathaniel Schindler**

*Analyst, Bank of America Merrill Lynch*

Q

Yes. Hi, thank you. Whenever Google makes quality improvements similar to you what you suggested you did and improves the conversion rates for its clients, they see an almost near instantaneous improvement in CPCs because they have a very dynamic auction. Your auction is a little slower. Usually it takes a couple weeks for things to flow through. Have you seen an impact from your quality improvements hitting CPCs with your clients now willing to spend more for higher quality clicks yet?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Hi, thanks very much for the question. We have seen – since we've been rolling out the quality improvements over the course of the quarter – we have seen some initial results from some of our clients saying that the effort has been working. As you point out, since we don't have a lot of ability for our clients to take quick action for the properties that it's working for, it is much delayed in terms of us seeing an increase in CPCs, which is certainly what we would expect. All of our tracking metrics, again with the clients with whom we can get all the way down to conversion improvements, have shown distinct benefits from the strategy that we've undertaken and I presume we've seen a modest increase or less – I mean, a modest increase in the prices that they paid per their profitability metrics.

**Nathaniel Schindler**

*Analyst, Bank of America Merrill Lynch*

Q

Okay. And just on – the second question is related – as you cut off some of this lower quality SEM, where do you think you'll reinvest those marketing dollars going forward?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

So as I indicated, we've disclosed that we've reinvested some of those marketing dollars into our Facebook campaigns. We may going forward choose to invest some of the dollars into some of the search engine marketing in our newer markets where the total dollar impact is less but we're more intent on gaining trial. And I'd also add it was a meaningful shift in the way we're conducting our SEM business, and SEM is a meaningful source of traffic for us. So, as the teams have now built in the new formulas, if you will, into their model, now we get to move forward and optimize on those. So, you could well see, we would hope to see, us just getting better at finding the right traffic that wants to not only convert on Trip but convert all the way downstream. So I don't think we'll be seeing a substantial additional cutback in the SEM versus – now that we know the best spots to grow, we'll be able to reinvest some of those dollars in SEM itself.

**Operator:** Thank you. [Operator Instructions] Our next question is from Heath Terry of Goldman Sachs. Your line is open.

**Heath Patrick Terry**

*Analyst, Goldman Sachs & Co.*

Q

Great, thank you. As you move to add to transparency within the bidding market, I was wondering if you could give us a sense of how far you think ultimately you want this to go and what kind of impact you see it having on the number of participants, either the number of participants in the market or overall potentially the impact that it could have on pricing or even volatility of pricing? Do we ultimately see over time kind of a real-time bidding market model the way you have with things like Google AdWords?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Yes. Thanks, Heath. An excellent question. We're not sure yet if it will evolve all the way to a real-time. Our customers aren't even necessarily asking for that level of information yet. But they do naturally want to know at a granular level, a property level, how the conversion rate, how the clicks on TripAdvisor share the market and various bidding strategies that they can use to buy the traffic that works the best from their end. So we're going from every couple of weeks you can update a set of properties and looking to test out – and we really have to learn how to do this effectively – test out over time a model where we are providing our clients a lot more information.

And I can absolutely appreciate how from the client perspective we're an extremely valuable channel to them and they would like to know how they can effectively spend more by buying the type of traffic that they want and that our current system is just too primitive frankly for them to be able to do so. We're approaching it gingerly in the sense that we don't have as many potential clients as someone like Google has that could bid for words. It's harder still on our system. And the dynamic is, on TripAdvisor, you're essentially mostly bidding for a dated search, it's not keyword match and it involves the specific availability question that our users are asking, show prices box. So, while everyone, of course, compares us to the Google auction that they have, ours is in one way more complicated because we have to have the date information and in one way simpler, we don't have to deal with broad matching or exact phrase or anything like that because you're bidding at the property level not the keyword level. Hope that helps.

**Heath Patrick Terry**

*Analyst, Goldman Sachs & Co.*

Q

Great. Thank you.

**Operator:** Thank you. Our next question is from Tom White of Macquarie. Your line is open.

**Tom Cauthorn White**

*Analyst, Macquarie Capital (USA), Inc.*

Q

Great. Thanks, guys. Two quick questions. One, with regard to the comments about traffic diversification, should I – I mean, should we be reading that if in the US you're sort of investing in Facebook, but maybe the bulk of the reallocation is going to be sort of outside the US to more search, that you guys are benefiting in terms of getting more direct navigation traffic here is in the US, thanks to the branding efforts that you guys are doing, the other widgets and all the third-party distribution? And then secondly, on business listings, on the push there, should we be concerned about the reactions from your core OTA partners and your other show prices customers from the push here, particularly if you guys start to evolve the business listing product to stuff beyond kind of the base phone number and web URL to perhaps other types of advertising across tripadvisor.com? Thanks.

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Sure, thanks. Thanks, Tom. I – First let me offer some perspectives on how we look at Facebook. For us, Facebook is – it's an excellent branding effort, it brings in lots of members, it is extremely global for us. So that's really not at all a US-type initiative and search overseas. We think of Facebook as very global. We think of search in terms of brand new markets are relatively low penetration for TripAdvisor versus mature markets. So we'll tend to lump Europe, UK, US, Canada and several others as more mature markets and Thailand and Poland and Brazil as newer markets. So we tend to treat the ROI we expect on search at a different level depending on if it's mature or new. For Facebook, similarly the advertising on Facebook, the pricing varies depending on the type of market that we're advertising in, but in general, we go very global on that platform.

To the second question on reaction from them on travel agencies to business listings, no, we are not detecting frankly any feedback worth mentioning from the OTAs on having business listings on the site, a website link and e-mail, or phone number. That's something that I think they are very used to doing in their channels. They are always offering their benefits over the supplier direct. I know – I shouldn't say I know – I presume all of the OTAs would not be very happy if TripAdvisor DotStar turns into a booking engine where we started actually taking the booking for hotel room and that's really not – that's not the media model that we're looking after. So we view BL as fantastic additional channel, marketing services or independent or chain hoteliers around the globe and response and attractions and other owners for whom we literally – were just offering marketing services. So that is a long answer to a simple question, saying no – no negative reaction to OTAs for BL.

**Operator:** Thank you. Our next question is from Herman Leung of Susquehanna. Your line is open.

## Herman Leung

*Analyst, Susquehanna Financial Group LLP*

Q

Great. Thanks. Two quick questions for you. I guess – I know that seemed like there was – investors are a bit surprised at the whole strategy change, but I understand that it's basically more for a long-term diversification. I guess, can you kind of explain to us sort of the thought process, when the decision was made to change the allocation of spend more towards Facebook against Google and what are sort of some of the metrics you're seeing away from SEM-type traffic against a Facebook traffic? And I have a quick follow-up.

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Sure. So we've been talking for a while about diversifying our traffic sources. So search engines, as you know, are a significant source. Thank God, they are wonderful. We get a ton of free traffic, we buy a bunch of paid traffic, but we like to have other sources and it was viewed as – we view it as – key to our long-term success to generate our own domain direct – higher rate of domain direct traffic and other sources by which people are learning about TripAdvisor.

From the SEM decision to kind of cut back, it – you can look at the revenue – you can look at the extra dollars, the millions of dollars that we delivered on the bottom line that was above our own expectations and make the simple case that says, hey, we just should have spent it at even 50% ROI, spending a dollar to make \$0.50 and we could have bumped the top line up by millions of dollars. And that's a perfectly reasonable strategy. It's not the one we took because in that case I'm actually spending a chunk of money and losing it on search. And we decided that we would rather in our mature markets spend those dollars on – some of those dollars on – the more branding and membership acquisition channels and Facebook is one that we're calling out because we're finding it's working for us. So the working is little more harder to quantify. It's not a direct ROI spend, but we're getting the content.

We're getting the Facebook connected members, which is really driving in our Wisdom of Friends strategy, to build the value proposition beyond just a click, hey, let me check, rate a hotel review and move on.

So I can appreciate how some of this may be a bit of a surprise, but I hope everyone can appreciate the balance of – we have a lot of profit to spend. We will – we could have chosen to invest it, in my view, unwisely in search, which would have generated more hotel shoppers and would have generated more top line revenue, but less of the type of revenue that we're looking for, less of the longer-term, we have you as a valuable customer going forward. So, proof will be in the pudding over the next couple of years as the membership base grows and we continue to knock it out of the park in the content collection space. But you can see in the quarter where we've spent. And I guess the final part of my long-winded answer would be, we would have spent more in the second quarter had we had enough of the campaigns set up on channels like Facebook because we are pleased that we have found some things that, to our metrics, are working for us.

**Herman Leung**

*Analyst, Susquehanna Financial Group LLP*

Q

Great, thanks. And just a very quick follow-up, If you could – is there a way, I guess, as we head into the travel seasonality of the third quarter, I guess, have you seen linearity of the quarter kind of continue to progress higher and accelerate from a traffic standpoint? Thanks.

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

The early indicators in July have been stronger in most markets than where we were finishing out Q2. I'm not sharing any surprises. We absolutely see what we believe to be the macroeconomic conditions in Europe being a drag on our revenue growth and our overall conversion growth. Hotel shoppers, interestingly enough, are doing okay in UK and Europe, not as strong as the US, but still frankly pretty strong, but the conversion of those shoppers to folks that are clicking to our clients is weaker than the US. And then on our client side, we're still seeing a pretty big hit there in terms of that traffic actually booking, and presumably if they're booking, maybe it's on cheaper property. So, we see it as CPCs that come back to TripAdvisor and UK and EU is distinctly hurting compared to prior year. Frankly, we have no reason not to believe it's macroeconomic in nature as people are taking less expensive vacations and shopping around more as opposed to buying more.

**Herman Leung**

*Analyst, Susquehanna Financial Group LLP*

Q

Great. Thank you very much, Steve.

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Surely.

**Operator:** Thank you. Our next question is from Mike Olson of Piper Jaffray. Your line is open.

**Mike J. Olson**

*Analyst, Piper Jaffray, Inc.*

Q

Hey, good afternoon. Sorry to beat a dead horse here, but you talked about the significant uptick in the usage of the app on Facebook and the increased spending there while certainly, like you said, that improves brand awareness. Are you able to determine what it means for conversion? I guess what you're seeing is SEM spend

drives kind of instantaneous traffic flow, but it may not be as higher quality. So, maybe what's the lag in the traffic growth and conversion from lower quality SEM-type traffic versus Facebook traffic that may be higher quality?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Yes, hard for us to know, I – the long-term answer to that question, certainly, most of the SEM traffic that we buy in most markets come, interacts with the site depending on the type of keyword. They have a nice long session and read tons of reviews. Other times they just do a quick price compare and depart. When they read the long reviews, we love it. We feel we've got the great brand impression and we presume that customer comes back more frequently than the one that just did a quick price compare and out the door. In most cases, we don't have a member at that point. We had a visit and that's great from trial but less good from a long-term perspective.

What we're doing on Facebook by – it's almost the reverse. It really is not generating immediate revenue at all for us. It's not generating a lot of traffic to the site immediately, at least from the Facebook side of things, but it is generating a member that is interacting with our site or our app our Cities I've Visited app who is generating content for us. We have an email and we know who their friends are. So, we're sharing those ratings, the reviews, the tips, the whatever across the broader set of people. So, again, it's building up that set of Facebook connected members that now hear from us every week in whatever language they speak, almost. And we're able to tell them what their friends are doing and we believe, and it will take a while to prove out, that those members upon seeing their friends interacting with TripAdvisor when they are ready to plan their next trip, come on back and do it on the site that they've been hearing about and that their friends are using, TripAdvisor.

**Mike J. Olson**

*Analyst, Piper Jaffray, Inc.*

Q

All right. Thanks. And then from a geographic perspective, would you say you saw any weakness in any particular market, like any headwinds from the broader challenges in your macro environment that we're hearing so much about or not really?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

We distinctly hear – see – our numbers demonstrate our challenges specifically in Europe and UK. And again, we see people still being interested in travel, but even on our site, they are converting less in two clicks. And when they get to our client site in general, they are converting, we believe, at a lower rate perhaps in some combination of buying cheaper stuff, all of which we see back as lower CPCs. So again, really happy with what we're doing in the US and in some of our newer markets, Australia. But we do derive a fair chunk of business in Europe, UK, and folks are suffering there.

**Mike J. Olson**

*Analyst, Piper Jaffray, Inc.*

Q

All right, thanks.

**Operator:** Thank you. Our next question is from Anthony DiClemente of Barclays. Your line is open.

**Anthony Joseph DiClemente**

*Analyst, Barclays Capital, Inc.*

Q

Hi, thank you very much. A few quick questions. First one is, can you give us a sense of when timing-wise you began some of these quality improvements in the quarter? Has it been a constant rollout or was there a discrete time when you started those?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Yes, I'd say pretty early on in the quarter. I'd say at this point, it's kind of getting better. We've tested early on and we found that the conversion rates we got from some of our clients was demonstrating what we had known. And so we continued to roll it out. At this point, I think if it has fully rolled out and we didn't really know – it was – at the end of Q2, it was a theory, and as we tested it maybe by the end of April, at that point we had a pretty good idea that it was working.

**Anthony Joseph DiClemente**

*Analyst, Barclays Capital, Inc.*

Q

Okay. That's helpful. Second one is, just wondering to what extent – and maybe this is more relevant to Julie's comments about CPC trending – but to what extent is mobile having an impact on CPC dynamics?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

To the extent that we do believe some of our traffic is just – I can't prove it – but we believe that some of our desktop traffic is moving over to mobile and our customers are not behaving the same on mobile. Mobile being phone. Then, that we're losing some clicks, it's hard for us to know whether the amount extra that we're gaining in all of the user engagement, all those millions of users that are picking up the phone and using TripAdvisor are then coming back to the desktop and doing their bookings there. We've just started to roll out functionality that allows you to save something on desktop and see it on mobile and vice versa, but the percentage of our audience that uses those features isn't enough to do a decent job tracking the follow-through.

**Anthony Joseph DiClemente**

*Analyst, Barclays Capital, Inc.*

Q

Okay, great. And then last one from me, Steve, the quality initiative that you articulated in your remarks and on the call, it seems like very well thought out intelligent strategy to me. I think one question investors might have is, at this early stage life cycle, I think folks have been measuring your success and evaluating your progress by looking at revenue. And so, to us, it now seems like profitability is becoming incrementally of greater importance. And so when I look at your guidance and your targets there, they are mostly revenue based, and so I'm just wondering if – should investors really start to weight profitability and margins a little bit greater in looking at TripAdvisor? And if so, do you expect to be giving more granular, more detailed profitability or EBITDA targets for us with respect to guidance?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

A fair question. I just – I don't quite look at it that way because I say, hey, as I look at the bottom line numbers, if we came in \$5 million above what you thought on the bottom line, you know that we could have bought an extra \$5 million to \$10 million on the top line. A monkey could have done that, just not that challenging because you know we know SEM. So, you can adjust the top line, bottom line. I'm looking at it from a long-term. I need to get better at SEM so that I'm spending efficiently buying the traffic that not only converts on TripAdvisor but it really helps my clients. So, we embarked on that program to a degree we had more success with the front-end piece of getting the right traffic to our site than we had on the spending piece to diversify the traffic. So, it's – you should

still – I'd urge you to still look at, hey, what's the top line, how is the growth of the company, how our hotel shoppers doing, what's the conversion rate, factors frankly because our margins in our view are already outstanding. And then when there is a lower than you might have thought on the top but higher on the bottom, hey, you can do the math and put it in reverse. In a similar way, if we blow out the top and I'm coming in below what I might have said on the bottom, you get the right to ask saying hey, did you find some great investment vehicle that you're taking the bottom line hit on in order to grow top. And if I'm one of those, I'm more than happy to explain it after the fact.

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**Anthony Joseph DiClemente**

*Analyst, Barclays Capital, Inc.*

Q

Okay. I understand. Thanks.

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**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Sure thing.

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**Operator:** Thank you. Our next question is from Scott Devitt of Morgan Stanley. Your line is open.

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**Scott W. Devitt**

*Analyst, Morgan Stanley & Co. LLC*

Q

Hi. Thanks for taking my question. I had a follow-up on mobile and you've done a great job with the app downloads. I was just wondering if you do have a specific monetization strategy for mobile or if you view it long-term more as an engagement mechanism as you had kind of highlighted in the answer previously. And then secondly, I was wondering if you think the improvement in traffic quality and the transparency that you're providing the partners in terms of how they should bid, if that's going to require just an incremental tech platform spend, and if so, if you could quantify that? Thanks.

---

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Sure. So, dealing with the second one first, yes, we're putting a couple of additional – I'm not sure yet how many – engineers against that particular project but we're talking a small handful. So it's nothing that would be noticeable in any of our lines in terms of building out that bidding system. Again, most of our clients primarily just want the information in order to be able to bid in a smarter way. So that's – it's a small resource allocation from my perspective.

To your mobile question, we absolutely do look at mobile as a revenue stream down the road. We continue to stay focused first on engagement, but we see the in-market opportunity as being potentially meaningful down the road as we get to offer better marketing services to the restaurants and attractions that are in-market versus the hotel purchase, which is the absolute lion's share of our revenue stream now.

There is some internal debate as to how much online booking TripAdvisor is going to be a part of, in the very, front-end hotel research experience. Just because on the phone, the screen is so darn small, are people going to want to review the information that TripAdvisor has versus their tablet. And so, to the tablet point, hey, we think tablet will mimic desktop and, our – most of the strategies we have on desktop will be just as applicable on tablet and tablet could even become better as the user demographics. So, folks using tablets probably spend more than on desktop in general. So short answer is at the moment, its more engagement and functionality, but we do believe

that mobile will become – a phone – will become a much more interesting revenue stream for us in the outgoing years.

**Operator:** Thank you. Our next question is from Chad Bartley of Pacific Crest. Your line is open.

**Chad Bartley**

*Analyst, Pacific Crest Securities LLC*

Q

Hi, thanks very much for taking the question. Looking at the year-over-year growth trends in your non-Expedia revenue, we saw a slowdown of about 10 points. And I wanted to ask, is that really a function of the traffic quality initiative that we've talked a lot about and then the tough pricing comparisons, or is there anything incremental or different going on that contributed to that slowdown?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Let's see. I suspect it's mostly around the geographic mix. So, as we already talked about sort of Europe is a bit of a challenge and we're just very global in terms of where our revenue is coming from. So, don't know a crisp answer to you, but I think I'd point you in that direction with some combination of their traffic quality piece, I'm sure.

**Chad Bartley**

*Analyst, Pacific Crest Securities LLC*

Q

I was probably wondering if there is any sort of update that you can provide as it relates to other advertisers, other OTAs, now that we're one quarter further away from TRIP becoming a standalone public company and potentially increasing their spend. So, is there any update around that?

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Yes. I mean it's – absolutely. The update is I've met with – met personally, met with many of the big clients, all our account managers have met with all of our big clients, and the message is just loud and clear to us. Hey, we would like to be able to spend more on your platform, nothing to do with corporate ownership stuff. Just give us the information so that we can optimize our bid strategy so that it can be a win-win. And we've heard some stories from our clients that talk about, hey, we tried to spend more in the test but it didn't work and we don't know why.

And the answer in these sorts of environments is always, well, in this part, you did make more money, but that part you didn't, and our system isn't transparent enough to let them optimize on the plus side and revert on the negative side. And we've recognized that. We told some of our major clients that this is coming. We're not secret about it. We just haven't gone to everyone necessarily. And it's in sort of what we will be rolling it out in test mode because we do believe – how do I phrase this – our clients are – many of our clients are adamant that if we provide them more visibility, they are absolutely ready to increase their spend. And that's why we call it in test mode as opposed to full mode because we haven't done it before, but we do think that there is more dollars there.

**Chad Bartley**

*Analyst, Pacific Crest Securities LLC*

Q

Great. Thank you very much for that.

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Sure thing.

**Operator:** Thank you. Our next question is from Douglas Anmuth of JPMorgan. Your line is open.

**Douglas Anmuth**

*Analyst, JPMorgan Securities LLC*

Q

Great. Thanks for taking the question. Just want to ask about two things. First on CPCs. Can you just talk about the overall outlook for 2012 relative to the flattish that you previously have stated and just thinking there about the potential lift from quality changes and sort of offsetting the macro pressures that you're seeing. And then also if you could characterize how you are thinking about the environment as it relates to algorithmic search results for you guys, would you say that things are sort of fairly stable in terms of what's happening on the natural results of Google pages? Thanks.

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Sure. Thanks, Doug. Two good questions. So the CPC outlook, I would say, we did have some tougher comps, though when you look Q1 to Q2, it was basically flat if I'm not mistaken. Even though we had the CPC declines in Europe offset by CPC growth, pricing increased in the US. So, we look at that and say, we think what we're doing, were it not for the macroeconomic climate in Europe, would be sending CPC prices higher across the board. And again, they're strong in many regions.

We think that that does have to do with our site redesign changes from last year, the quality improvements that we made on our SEM traffic this past quarter certainly contributing, and just some other pieces of the site personalization efforts that we feel are driving higher qualified traffic to our clients. So going forward, I'm not going to be able to offer any prediction on the travel climate in Europe. We generally – when we forecast – we take the position of, all right, next quarter is going to have the same mood, the same FX, the same everything as what we have today. And so if you guys are betting things are going to get better, then that will help us. If they're going to get worse, that will hurt us. We're – we believe ourselves to be reasonably sensitive to on the overall economic climate.

To your second question, algorithmic search results, we haven't seen much change by way of what Google has done in the past quarter. We don't think anything has affected us in a meaningful way. Certainly, we're pleased that we continue to have growth in our SEO channel across I got to believe all major markets. But we would absolutely expect that as the cycle of content creation, has grown in all languages. So, again, we get more content, more freshness, better results for the user. Google favors sites that offer better results. We're one of those, so we tend to rise in the rankings. I haven't seen – to give a follow-up to your question, haven't seen Google Places or Local, whatever they're calling it now, come out with any particularly interesting new features that we think are pulling traffic away from TripAdvisor. So again, stable. The integration they have with Zagats does appear more in the search results, again, more on restaurants than hotels, so less meaningful to our business. Yes.

**Operator:** Thank you. Our next question is from Mark Mahaney of Citigroup. Your line is open.

**Mark Stephen Mahaney**

*Analyst, Citigroup Global Markets (United States)*

Q

Hey, thanks. Just one quick follow-up question on the attempt to the goal of improving the quality of the traffic to the clients, the customers, that seems very straightforward, but what's driving that and to what extent have you – has there been a decline in the conversion and a decline in the quality of those leads that you've been delivering? Is this something that clients have noticed, OTAs had noticed and have brought up to you, or is it that you just looked across your marketing channels and discovered just a better mousetrap? Thanks.

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

We did see some indications from some of our clients about a decline in traffic – I mean, a decline, I'm sorry – in conversion of our traffic. Where we get good data from clients on conversion, of course, we like to act upon it and make a intelligent conclusion. When we sliced and diced and said, hey, why is this conversion going down in certain markets, it's understandable, but in other markets, it wasn't. And we've seen good growth in our SEM traffic year-over-year sort of 2011 over 2010 and 2012 over 2011.

And so one of the things that we found when we sliced and diced is that some of the traffic that we were buying on SEM, and as I've said before, sometimes we will buy on a barely profitable basis in the mature market. We can appreciate how if I'm buying a word at \$0.50 and someone comes to the site and they click around, visit pages and then we sell a qualified user to our partner for \$0.49, and then I've brought a profitable visitor. I'm happy to do that all day long. The profit isn't much, but it got me trial, and that was a successful event for us. If it turns out that, that visitor upon going to our client actually bought something at only half the rate of our normal traffic, then it turns out that that click to the client wasn't really worth \$0.49 on average, it was only worth \$0.25. But wait a minute, I paid – I think I might have said that wrong, but I paid -

## Julie M. B. Bradley

*Chief Financial Officer, Treasurer & Senior VP, TripAdvisor, Inc.*

A

\$0.48.

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Yes. If I had bought the traffic at \$0.49 and sold it to my clients at \$0.50, but it was really only worth \$0.25 because it converted at half the rate, then I ended up buying it at \$0.49, selling it at \$0.25 and I actually lost money on that SEM transaction. And so that was part of the dimension that we discovered, and it's not like it was a bad thing for the business in general because we got someone to give TripAdvisor a try. They had a successful experience, they read a review presumably, they went off and clicked on a client site, but they didn't convert as much. And maybe it's because of this particular keyword that we were buying or the experience that we put them through as they landed on TripAdvisor. So our Q2 efforts, and I'm sure this is way more detailed than you're looking for, but the Q2 effort was really, hey, let's not buy as much of that traffic because that's not really meeting our objective of being – for that mature market – being profitable on every click that we're buying. So we let go some of that traffic and are choosing to reinvest it elsewhere.

## Mark Stephen Mahaney

*Analyst, Citigroup Global Markets (United States)*

Q

Thank you, Steve. Thank you, Julie.

**Operator:** Thank you. Our next question is from Peter Stabler of Wells Fargo Securities. Your line is open.

## Peter C. Stabler

*Analyst, Wells Fargo Securities LLC*

Q

Thanks for taking the questions. Just a couple of quick ones. I think you told us that the comScore data was up 31% and that your hotel shoppers was tracking with that at about 30% year-on-year growth. I'm wondering if you could give us some regional color there and maybe compare and contrast mature markets with international growth markets and specifically Asia. And I have one quick follow-up. Thank you.

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Good, fair questions. I'm not sure how much of those numbers I have at my fingertips. I can give you the – hotel shoppers were growing between UK, Europe, US, US kind of grew the fastest in terms of shoppers and revenue in fact. UK and Europe were kind of tied in terms of hotel shopper growth, but meaningfully less than what the US was growing at. So from that, you can absolutely – I haven't told you rest of world. I don't have that handy here. But I can tell you that US grew faster than the 31% – than the 30% that approximate number, and that the UK and EU was less. The – a bit more important than the actual hotel shopper growth is how those shoppers turned into revenue, which was a much more dramatic shift. So the US was significantly above our year-on-year growth numbers compared to the average and EU and UK was significantly below.

## Peter C. Stabler

*Analyst, Wells Fargo Securities LLC*

Q

Any color on China?

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

China, from a sort of overall CPC number, still isn't meaningful enough to substantially color the overall averages. I look at China less from a, hey, are CPCs up or down in that part of the world, than how are we doing on overall reach, how are we doing on the site engagement metrics, are people sticking around longer. And we've cut back on some of our spend, as we've done a few things to improve the product. Adding CTrip, hey, that's a big win in that market. They're not on Qunar, they don't play in too many other channels, but we've got them on board and that's probably with most if not all of their inventory, and that helps our user experience. And it adds to our bottom line or top line, but at the end of the day, it just delivers the visitor to Daodao more choice, and that's the most important piece of it for us right now.

**Operator:** Thank you. Our next question is from Brian Nowak of Nomura. Your line is open.

## Brian T. Nowak

*Analyst, Nomura Securities International, Inc.*

Q

Thanks. I have two. First one is on kind of going back to Europe for a second, I was wondering if you can talk about kind of the European conversion and how it's kind of trended throughout the quarter, and now because you head into July and August, I mean, does it get any materially worse or is it kind of it's been a steady just lower rate of conversion since the beginning of the year?

## Stephen Kaufer

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

A

Let's see. I see the conversion – in Europe, I'd color it as mostly steady in terms of it wasn't good in Q1 and it may have fallen a bit in Q2. I'm hesitating only because I'm not sure if I'm looking at kind of all of the numbers synthesized. So I don't want to convey a misimpression for you. Sorry about that. So because of our onsite efforts with personalization, I think that Europe actually converted to clicks outbound a little bit better, but probably got hit worse on the pricing side as prices went down more in the second quarter.

## Julie M. B. Bradley

*Chief Financial Officer, Treasurer & Senior VP, TripAdvisor, Inc.*

A

Yes, we saw a steady decline in pricing in EMEA throughout the quarter.

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

There we go, a definitive answer.

A

**Brian T. Nowak**

*Analyst, Nomura Securities International, Inc.*

Okay. All right, great. And the other question I wanted to ask is on the hotel shopper growth. Can you help us a little bit just kind of – in 2011, what was the 2Q 2011 hotel shopper growth and then how did that trend through 3Q and 4Q of last year?

Q

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

I don't have those numbers with me. So I'm sorry, I just don't think I can answer that. I'm trying just to think back to what was happening in the second half of last year and I don't think there were any surprising growth shoots. So I don't think on the hotel shopper side we'll be facing any tough comps in terms of the shoppers. The comps will all be around pricing to the Expedia stuff and a strong pricing before that, and then the conversion, which will help things along because we'll have lapped that in Q4.

A

**Julie M. B. Bradley**

*Chief Financial Officer, Treasurer & Senior VP, TripAdvisor, Inc.*

Lapping of the site redesign.

A

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

Yes, the site redesign, sorry.

A

**Brian T. Nowak**

*Analyst, Nomura Securities International, Inc.*

Okay. So, no changes at all as Google changed its strategy in kind of the back part of the summer last year with Places?

Q

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

Yeah. I'm just not – I don't recall having a big Places impact in the back half of the year. There is always something, but I don't think that – well – I can say we haven't modeled a increase, a meaningful increase in hotel shoppers in the back half of the year based upon a particular weakness in the second half of last year.

A

**Operator:** Thank you. This ends the Q&A portion of today's conference. I'd like to turn the call over to the CEO, Steve Kaufer, for any closing remarks.

**Stephen Kaufer**

*President, Chief Executive Officer & Director, TripAdvisor, Inc.*

Great. Well, I just want to thank everyone for joining our call today as well all TripAdvisor employees around the globe for their hard work this quarter. And of course, we look forward to talking with everyone next quarter. Thanks very much.

**Operator:** Ladies and gentlemen, thank you for your participation in today's conference. This concludes the program. You may now disconnect. Have a wonderful day.

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