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Siena Market Line
2nd Week of May 2016

Expedia, Inc.

NASDAQ: EXPE

Analyst: Austin Bitzas
Sector: Internet Retail

BUY

Price Target: $126

Key Statistics as of 5/6/2016

Market Price:	$112.63
Industry:	Online Travel Agency
Market Cap:	$16.781B
52-Week Range:	$88.40 – 140.51
Levered Beta:	0.76

Thesis Points:

- Best in class, and increasing its market share through organic and inorganic growth
- Recently acquired HomeAway. Adding to their high revenue growth expectation
- Primarily industry leader for cheap pricing

Company Description:

Expedia Inc. (NASDAQ: EXPE) is an online travel agency that operates in the United States as well as worldwide. It is headquartered in Bellevue, Washington and was founded in 1996. The company assists the booking of airline seats, hotel rooms, car rentals, and destination services from its travel suppliers. Expedia works as an agent in facilitating these bookings treating a broad range of customers. Their customer base ranges from corporate to leisure travelers, offline retail travel agents and a variety of travel service providers. Expedia operates through the segments of Trivago, Egencia, Core OTA, HomeAway, and Core OTA.

Thesis

Expedia, Inc. (NASDAQ: EXPE) is best in class for online travel agencies. The company has shown impressive year-by-year growth over the past ten years, and has a positive outlook for the coming years. Through investing highly in their own themselves Expedia is projected to continue their organic and inorganic growth. Their partnership capabilities although remain highly strategic for Expedia allowing them to grow inorganically as well. Expedia has been active with its merger and acquisition strategy in investing in high growth businesses. The acquisition with HomeAway in mid-December of 2015 has added 1.24 million lodging alternatives to its existing 270,000 alternatives. Expedia's largest acquisition to date. Expedia will make HomeAway better with their expertise in online booking. Expedia covers all bases of the travel industry while growing at twice the rate if the industry. HomeAway acquisition also gives a competitive advantage over Priceline for pricing. The travel industry has been suffered until recently leading me to believe that it is a good entry point to buy Expedia for a medium to long position.

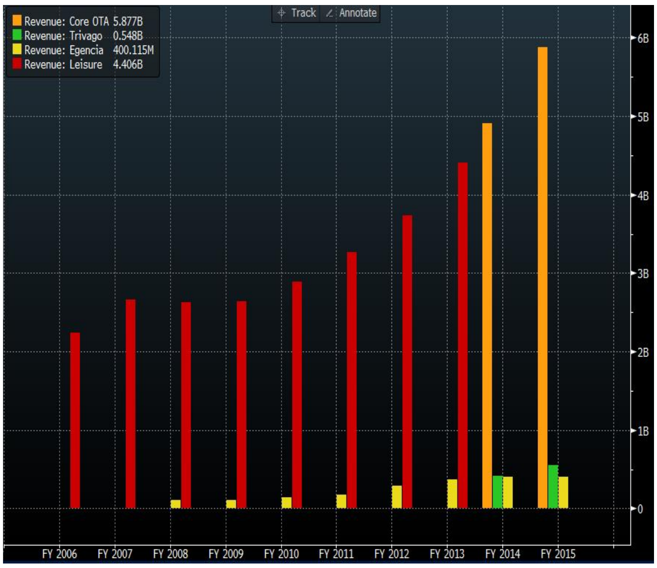
Industry Outlook

The online travel market is growing in the online booking sector. There has also been a shift in booking patterns towards mobile devices. Although, the US and some European markets are relatively saturated reaching a mature state. Online travel agency have to focus on the untouched newer markets of countries that already have a developed tourism industry with an emergent digital equipped middle class. Thus, those online travel agencies main market drivers are higher digitization, international expansion, and mobile implementation. New starts ups such as Airbnb are beginning to steal market shares from weaker online travel agencies. However, large companies such as industry leaders such as Expedia and Priceline are able to put substantial amounts of spending in advertising and media. As a result, they still remain at the top of their market for loyal customers. The strong dollar hit the travel industry in 2015 and early 2016. This caused the online travel industry to weaken due to significant revenue in international markets. Resulting in lower dollar revenues for both Priceline and Expedia; ultimately, effecting short-term revenues. However, the dollar is weakening only recently, it is now favoring the online travel industry once again. It can be argued that the market has not yet adjusted for this weakening in the US dollar.

Mergers and Acquisitions

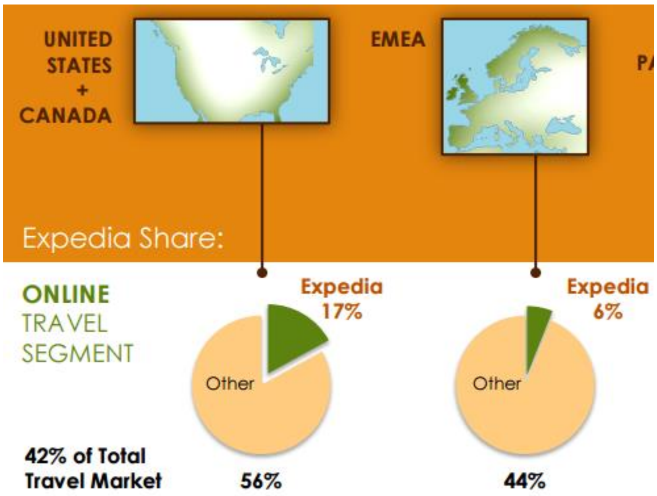
On December 15th, 2015 Expedia acquired HomeAway for $3.9 billion in cash and stock. This was Expedia's largest acquisition to date. By acquiring HomeAway Expedia is able to grab a share of the $100 billion and growing rental industry. HomeAway is leading the rental industry with about $15 billion books in 2015. When compared to HomeAway's close competitors Bookings.com and Airbnb has significant more bookings. HomeAway will also increase Expedia's propriety listings by 1.3 million. This is also greater than Airbnb and Bookings.com. Incorporating HomeAway into Expedia business plan will not be difficult since they have already been working with each other for two years now. HomeAway will serve as a vacation rental and a home sharing platform for Expedia. Although, Expedia's plan to be highly involved in HomeAway it will operate mostly as its own business. Through Expedia's expertise in online booking and converting page views to bookings it will help HomeAway expand aggressively moving it to a fully online transaction model by 2017. Expedia will be able to drive traffic to HomeAway's listings through their expansive advertising and marketing. This gives HomeAway a substantial advantage over its competitors being part of Expedia. HomeAway is beginning to introduce a service fee to travelers, which is ahead of schedule. This process will be monitored very closely, and be pared with a confidence guarantee. Thanks to Airbnb and TripAdvisor already implementing booking fees the transition should go smoothly. This can be advantageous to expanding Expedia's revenue significantly. Also the successful integration of HomeAway within Expedia could eliminate the need for people to use Airbnb to compare hotel prices. The subscription will work by matching HomeAway's unique travel preferences with the right listings while driving book volume for owner and manager communities. According to the most recent earnings call booked transactional revenue is up 170% year-over-year in Q1. Meanwhile in early 2015 Expedia sold a 62.4% stake in eLong for a profit. The company focused on majority travel products and services in China. Removing eLong from Expedia's business would allow them to better focus on its core online travel agency business. In response to selling eLong proved to have significant positive results in boosting Expedia's online travel business revenue. Thus becoming a key driver in Expedia's return to profitability in later 2015. This positive revenue results is still continued to be felt by the company today. Expedia has also been working to integrated Orbitz.com and CheapTickets onto the brand Expedia platform. As of the latest earnings call the results have been promising with positive growth in Q1 of 2016. This integration should be smoother, then Travelocity and Wotif, according to management since Orbitz already has a strong online marketing team. Strong growth for Trivago have continued through 2016 with 176 million in revenue, up 48% year-over-year. And management projects to achieve aa healthy bottom-line growth through 2016 and global growth rate continues to be substantial. Expedia's merger and acquisition strategy in investments in high growth businesses has been key in their success of inorganic growth. Chart 1 below shows the trend in increased revenue of Expedia's core online travel agency (Core OTA), Trivago, Egencia, and leisure year-over-year.

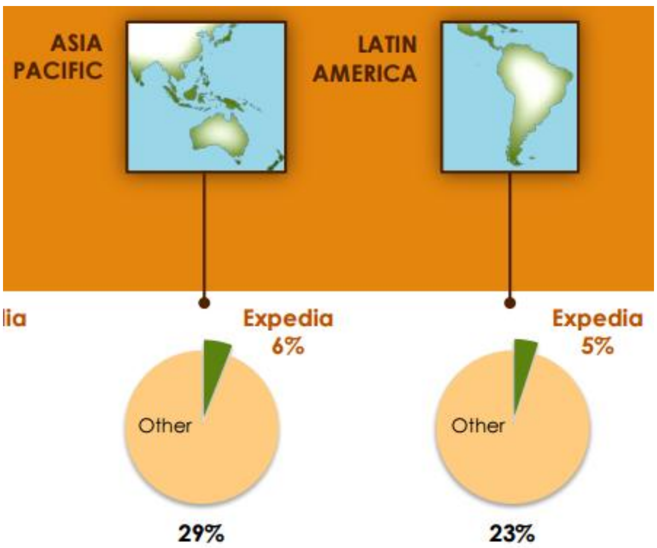
Chart 1:



Organic Growth

Besides connecting customers with online travel brands that are part of Expedia's business platform their organic growth continues to grow at a healthy rate. Hotel revenue grew 25% on room night growth of 37% for quarter 1 of 2016. Air revenue was up 61% on ticket growth of 70%. Expedia has positive growth outlooks for ticket volume organically in addition to significant contributions from their recently acquired companies. With a current growth rate of 6% for air revenue and 22% for ticket growth. There is strong momentum in the unit growth with global room nights up 37%, air tickets up 52%, car days up 48%, and advertising and media revenue growing 44%. Expedia plans to continue this growth while increasing to grow additional travel product. Expedia is ahead of their business model in growing additional travel products. Expedia's business model is to achieve healthy growth in the near and mid-term by reinvesting a portion of their outperformance back into the business to grow year-over-year. Thus, supporting mid to long term growth for the company with their outlook towards the future. According to their most recent earnings call management expects adjusted EBITDA to grow between 35 to 45% year-over-year. Expedia has also repurchased 2.9 million shares for $312 million this year showing a balance between capital allocation between M&A, share repurchases, and their dividend. Also with Expedia being able to offer an abundance of the travel market it gives it an advantage over the competition. With Expedia being a leader in the travel booking industry with 42% of the total travel market since mid-2015. This is only growing with the acquisition of HomeAway. This allows Expedia to supply lower prices for the 200 plus countries they have a presence in.





Valuation

Using Expedia's most recent acquisitions, as scene in their last 10-k report, the amount of goodwill that attributed operating synergies had to be calculated for each segment. Using a weighted-average approach 10 percent of good will was deemed invested on future revenues and the rest counted for sunk cost. HomeAway was acquired for $3.6 billion in cash and Expedia common stocks. It was recorded that $2.6 billion out of the total $3.6 billion was considering operating. The Travelocity brand and other associated assets from Sabre for $280 million in cash on January 23, 2015. Of that $196 million was attributable to operating synergies and $82 million is expected to be deductible for tax purposes. Wotif Group, an Australian based online travel company, was acquired in November 2014, for $612 million. Of that $350 million was attributable to operating synergies. In 2014 another three acquisitions, one for a leading car rental reservation company in Europe were completed. There was $70 million in goodwill recorded, and of that $51 million was intangible assets. Adjustments for goodwill was the leading driver which affected Expedia's price. The nature of Expedia's business model made the proportion of intangible assets deemed operating or non-operating. Expedia evaluates goodwill for impairment in two ways. First, a qualitative assessment to check if the fair value of the reporting unit is less than the carrying value. Thus, if this is true than the goodwill of the reporting unit is impaired. The impairment loss is recorded as equal to the excess of the carrying value of the reporting unit's goodwill. Fair value of indefinite-lived intangible assets are primarily trade name and trademarks. It is assumed that trade name and trademarks have extended value. It requires Expedia to estimate future revenue for related brands, to determine the appropriate royalty rate. The carrying value of definite-lived intangible assets is looked over when changes in circumstances indicate that the carrying amount of the assets might not be recoverable. Thus, if it indicates potential impairment the recoverability of an asset group is assessed. An assumption for proportion of intangible assets deemed operating of 10 percent was determined as follows. This is a positive for Expedia because high sunk costs make it difficult for a competitor to enter the new market, since they have to commit money upfront with no guarantee of returns in the end.

Porters Five Forces

<u>Barriers to Entry: Moderate</u>

The online travel agency is capital intensive thus making it hard for startups to quickly enter the market. The more capital available for large travel agencies allows them to buy in bulk resulting in cheaper overall prices. However, there are low level of proprietary travel knowledge and asset specificity. This makes it relatively easy for new players to enter the industry.

<u>Bargaining power of suppliers: HIGH</u>

Expedia is getting its prices by a diverse group of suppliers. Suppliers mainly consist of airlines and hotels. These suppliers are affected by commodity products making the global market a large factor in prices. Also concentration and ability to sell direct gives power to suppliers like airlines, which cannot always be bought out. Whereas, hotels can often be bought out in bulk giving some power back to travel agencies like Expedia.

Bargaining power of customers: HIGH

In order, to stay top of class Expedia needs the cheapest prices. With brand loyalty low and the ability to switch gives buyers reasonable buying power. Strong competitors like Priceline make it crucial to have the lowest prices to keep customers coming back.

Threat of substitute: LOW

It's difficult for substitutes to come to be since it is challenging to build scale due to lack of ready distribution. Although, there are minimum efficient level to allow small startups to do so at a significant scale is necessary to negotiate profitable deals.

Existing Rivalry: HIGH

Competitors such as Priceline and Airbnb are Expedia's largest rivals. And with brand loyalty, in some sectors, making the ability to switch easy it comes down to the cheapest and best product. Improving the customer experience, while cutting operating cost is a big factor. Expedia has done this well and has produced best in class prices allowing it to be competitive.

Conclusion

Expedia, Inc. is best in class for online travel agencies. The company has shown impressive year-by-year growth over the past ten years, and has a positive outlook for the coming years. It recently experienced a better than expected earnings call. Its acquisition with HomeAway is already showing to be a highly favorable revenue producer to the company along with its other segments. HomeAway acquisition also gives a competitive advantage over Priceline and Airbnb for pricing. Expedia is also working on improving efficiency for a solely e-commerce experience in their other segments. The travel industry has been suffered until recently leading me to believe that it is a good entry point to buy Expedia for a medium to long position. After its most recent earnings call the price went up to $115. With an intrinsic price of $111.68 according to my DCF, I would recommend to buy once the price spike from the latest earnings call settles to my intrinsic value. Thus, I recommend Expedia for a medium to long position at this price or lower with a one target of about $126.

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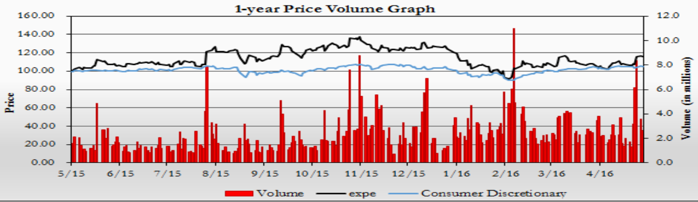
Analysis by Austin Bitzas	Current Price:	$112.63	Intrinsic Value	$111.68	Target 1 year Return: 12.64%
5/6/2016	Divident Yield:	1.0%	Target Price	$125.80	Probability of Price Increase: 85.7%



Description

Expedia, Inc., together with its subsidiaries, operates as an online travel company in the United States and internationally.

General Information

Sector	Consumer Discretionary
Industry	Internet and Catalog Retail
Last Guidance	November 3, 2015
Next earnings date	July 28, 2016
Estimated Country Risk Premium	7.60%
Effective Tax rate	33%
Effective Operating Tax rate	28%

Market Data

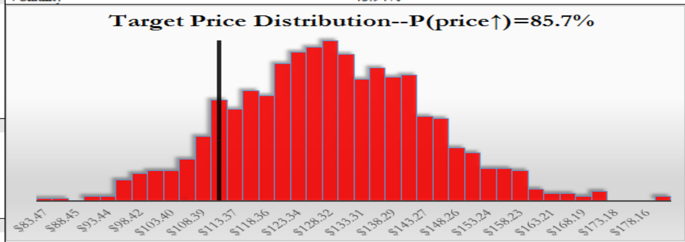
Market Capitalization	$16,781.61
Daily volume (mil)	0.44
Shares outstanding (mil)	149.10
Diluted shares outstanding (mil)	138.93
% shares held by institutions	80%
% shares held by investments Managers	58%
% shares held by hedge funds	16%
% shares held by insiders	4.31%
Short interest	9.36%
Days to cover short interest	4.63
52 week high	$140.51
52-week low	$88.40
Levered Beta	0.76
Volatility	45.94%

Past Earning Surprises

Quarter ending	Revenue	EBITDA
3/31/2015	-4.20%	-74.71%
6/30/2015	-2.81%	-26.20%
9/30/2015	-11.76%	-12.01%
12/31/2015	-7.05%	-27.96%
3/31/2016	-1.18%	-18.78%
Mean	-5.40%	-31.93%
Standard error	1.9%	11.1%

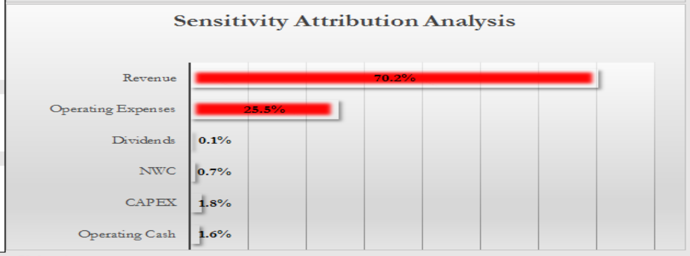
Peers

The Priceline Group Inc.
Netflix, Inc.
Yahoo! Inc.
TripAdvisor Inc.
Groupon, Inc.
Amazon.com, Inc.
Alphabet Inc.
Ctrip.com International Ltd.

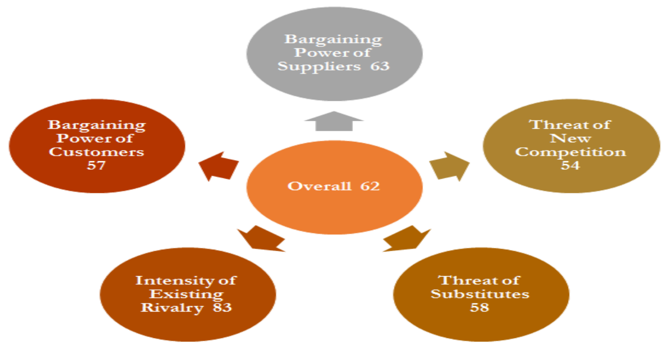


Management	Position	Total compensations growth	Total return to shareholders
Diller, Barry	Executive Chairman, Senior E	18.1% per annum over 5y	-5.88% per annum over 5y
Khosrowshahi, Dara	Chief Executive Officer, Pre	78.83% per annum over 5y	-5.88% per annum over 5y
Okerstrom, Mark	Chief Financial Officer and	24.86% per annum over 4y	25.27% per annum over 4y
Dzielak, Robert	Executive Vice President, Ge	32.95% per annum over 3y	15.48% per annum over 3y
Soliday, Lance	Chief Accounting Officer, Co	N/M	N/M
Holtz, Bill	Chief Information Officer	N/M	N/M

Profitability	expe (LTM)	expe (5 years historical average)	Industry (LTM)
ROIC	-72.8%	-129.19%	7.23%
NOPAT Margin	11%	12.38%	9.0%
Revenue/Invested Capital	-6.55	-10.43	0.80
ROE	9.3%	17.64%	7.57%
Adjusted net margin	10%	10.88%	8.1%
Revenue/Adjusted Book Value	0.97	1.62	0.93
Invested Funds	**expe (LTM)**	**expe (5 years historical average)**	**Industry (LTM)**
Total Cash/Total Capital	22.3%	26.9%	37%
Estimated Operating Cash/Total Capital	22.0%	22.6%	N/A
Non-cash working Capital/Total Capital	-55.7%	-52.3%	-23%
Invested Capital/Total Capital	-10.7%	-10.7%	67%
Capital Structure	**expe (LTM)**	**expe (5 years historical average)**	**Industry (LTM)**
Total Debt/Common Equity (LTM)	0.25	0.19	0.09
Cost of Existing Debt	4.53%	6.37%	4.79%
Estimated Cost of new Borrowing	4.81%	4.49%	4.79%
CGFS Risk Rating	CC	CCC	B
Unlevered Beta (LTM)	0.67	0.96	1.42
WACC	8.71%	11.54%	14.65%



Porter's 5 forces (scores are out of 100)



Valuation

Period	Revenue growth	NOPAT margin	ROIC/WACC
Base Year	21.3%	11.1%	-8.35
3/31/2017	22.2%	11.7%	-11.75
3/31/2018	10.7%	13.0%	36.96
3/31/2019	9.1%	14.0%	11.41
3/31/2020	13.8%	14.2%	7.29
3/31/2021	6.9%	14.6%	7.52
3/31/2022	6.7%	15.3%	7.89
3/31/2023	6.2%	16.1%	8.46
3/31/2024	5.2%	16.3%	8.55
3/31/2025	4.8%	17.3%	9.00
3/31/2026	-20.2%	17.5%	6.83
Continuing Period	2.1%	19.9%	9.21

Period	Invested Capital	Net Claims	Price per share
Base Year	-$561.48	$5,051.84	$111.87
3/31/2017	-$402.09	$5,189.03	$126.41
3/31/2018	-$509.35	$5,272.52	$138.86
3/31/2019	-$519.54	$5,161.93	$152.93
3/31/2020	-$1,099.53	$3,791.47	$168.95
3/31/2021	-$1,005.50	$1,748.26	$189.30
3/31/2022	$384.15	$46.24	$206.27
3/31/2023	$1,438.08	-$1,860.92	$223.98
3/31/2024	$2,543.44	-$3,881.73	$242.28
3/31/2025	$2,670.03	-$6,136.98	$261.14
3/31/2026	$2,775.92	-$8,284.51	$279.58
Continuing Period			