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GRPN.OQ - Groupon Inc at Barclays Global Technology, Media and Telecommunications Conference (Virtual)

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CORPORATE PARTICIPANTS

Aaron Z. Cooper *Groupon, Inc. - Interim CEO*

CONFERENCE CALL PARTICIPANTS

Deepak Mathivanan *Barclays Bank PLC, Research Division - Research Analyst*

PRESENTATION

Deepak Mathivanan - *Barclays Bank PLC, Research Division - Research Analyst*

Great. Good morning, everybody. My name is Deepak Mathivanan, and I'm the intent analyst here at Barclays. And we're super excited to have Aaron Cooper from Groupon joining us today. Aaron, thanks for joining us.

Aaron Z. Cooper - *Groupon, Inc. - Interim CEO*

Thanks so much for having me.

Deepak Mathivanan - *Barclays Bank PLC, Research Division - Research Analyst*

Great. So yes, we have about 25 minutes. I'll go ahead and get started with a list of questions, and we'll go right into it.

QUESTIONS AND ANSWERS

Deepak Mathivanan - *Barclays Bank PLC, Research Division - Research Analyst*

Great. So the first topic, which obviously is in everybody's mind, is about 2021. Local was one of the categories that struggled a little bit during COVID and there has been some uneven recovery since then. Obviously, the news of vaccine is a huge development, particularly for companies in travel or hospitality, Local side of the things. So how are you thinking about 2021?

Clearly, it feels like Local could be one of the categories that comes back pretty swiftly once we have consumer adoption of vaccine in place.

Aaron Z. Cooper - *Groupon, Inc. - Interim CEO*

Thanks. And you're absolutely right. This is absolutely on everybody's mind. And obviously, you can only imagine that the Groupon community, our employees, our customers and merchants are energized by the momentum here towards a vaccine.

What we've seen demonstrates to us that Local commerce is really resilient. And we already observed that earlier during this year, even in the spring, where we saw customers already coming back throughout the spring and summer. A couple of the examples that I'll point to where we saw a recovery happen really quickly was in beauty and wellness, which recovered to north of 70% by the end of Q3. And also, our home and auto vertical, which recovered to north of 80% into the summer. And what we see is, we see things playing out differently by geo and by vertical. I mentioned health, beauty, wellness and home and auto, which are recovering on the faster side.

And of course, we believe things like live events, big concerts and sporting events, that might take a little bit more time. For us, because of the diverse supply we have, we have the ability to pivot and surface relevant supply to our customers, which is a strength of ours and what they count on us for.

So overall, we see customers and merchants are adapting during the pandemic based on what's safe and comfortable and I expect that to happen in a recovery and into people starting to get vaccinated. But for me, I can tell you, for example, last night, I bought a Groupon for takeout and delivery for a local restaurant when maybe before I would have dined in.

And a week or 2 ago, I went on a scavenger hunt with my family. We were out in Chicago, down by the bean. It was a great COVID-friendly activity. We did for a couple of hours, incredibly numerable. I also got a car wash. All things that we see our customers adapting to over this period of time.

For the team over this period of time, we've been executing on our strategy that's designed to improve the customer, merchant value proposition. So that when customers come back into this recovery, they're coming back to a new experience with more breadth and depth of inventory than ever before.

And as we think about how Groupon shows up for local merchants into this recovery, this is really important because Groupon is a no risk option. There's no CPC, there's no CPM. Merchants only pay Groupon for performance which when you're watching your financials like any small business should, that's really important.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. I was going to ask a little bit more about that as well. So you obviously have launched a pretty big initiative and have been doing it in some of the test markets already. Maybe share a little bit of thoughts on how you think about the milestones for those initiatives in 2021?

Are there specific goals in terms of how you want to expand supply? And then are there any KPIs like conversion that you track that gives you inputs on, what to expect for 2021?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

Thanks for asking me. I mean, this is exactly the team's obsession, and we're really energized to continue executing on our growth strategy in 2021. Our priorities next year remain laser-focused on our 2 strategic initiatives: number one, and this is in order, expanding inventory; and number two, modernizing our market place.

We've removed all distractions, and we're extremely focused organization now and we have been all year. And you should expect that to continue in 2021. The most important work we're doing right now is getting signal our inventory test. And I think what might just be helpful, and so, I'll take a step back for one, second because for folks newer to the Groupon name and story, the context I find here really helps folks come along quickly.

What Groupon has been known for, for years is inspiration. When Groupons suggests something, just like Groupon suggested this scavenger hunt to me a week ago, people buy it. We see so many times where people aren't even thinking about the category or the specific item for this specific merchant until Groupon suggested it.

This inspiration has -- is led to billions of dollars of Local commerce. Now if you look at other businesses, a lot of them are destination. You think of something and then you go to a site or app to fulfill that. What we're doing now is we are complementing our inspiration business with a destination business. And let me explain you why that's so important.

Our inspiration business cost merchants as much as \$0.70 on the dollar. And that limits our value proposition. It limits our access to the \$1 trillion TAM in the local marketplace that we compete in. And so we want to expand that. The way it works is if a merchant pays 35% to us and then a 35% discount, that's a \$0.70 all-in cost on every dollar. Other marketplaces in the way you've seen them grow and add platforms start with very low take rates.

They achieve supply density on these low take rates. And then they worry about growing monetization after they've achieved a certain level of commerce and tipping point threshold. So for Groupon, in this sense, from a destination standpoint, we kind of built our marketplace backwards.

So that's what we're getting after right now. We're adding this. Customers tell us they want more supply that they can buy repeatedly, which means there's no more new customer restrictions. And for merchants to add that, to add all of their items, not just the manicure, but the pedicure, the facial, the eyebrows, and for have customers come back and come back repeatedly, they want a lower price.

So what we've done is we've taken our core deals product which is this product that has done billions of dollars of local commerce, and we've complemented it with our offers product, which is lower cost to the merchant, a much lower all-in cost. So that merchants can put their full catalog of inventory on our site and feel great when customers buy and buy again, which then makes the -- our catalog fuller so that when customers are searching, they always have something to buy.

And only a third-party marketplace supply that fills out the store. To our inventory test, we had 2 goals. Goal #1 was to increase supply by 25% to 50%. And we exceeded the high end of that range, as we said about a month ago. So over the 50% range.

Now we're focused on the customer value proposition and getting the signal there. The goal that we set at the end of our 6-month test is low single-digit percentage point improvements in units and billings.

We're going to share more about the next steps in what we think scaling it looks like when we report in February. But I can tell you, we're already moving on things that we see as no brainers. For example, removing those restrictions on deals that means customers can only buy them once. And so while expanding inventory is absolutely priority one, we've also, over this period of time, made good progress on priority 2, which is modernizing our marketplace for customers and merchants. And happy to answer any questions about that as well.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

No, makes sense. Okay. From a category standpoint, obviously, Local is crucial to your business. Goods also makes a lot of sense. What about things like travel? Do you think there's opportunities to kind of optimize the right category or even by vertical from a product standpoint, mix over the next maybe 6 to 12 months?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

Absolutely. And just so we always name it, and any time I talk about any other category, I'm going to punctuate it with winning for Groupon is on the other side of winning in Local. But I'll ask you, like what other marketplace can you buy (inaudible) and scavenger hunts in sizes that we can get away in physical goods? I mean, that is Groupon. And our diverse supply has helped us over the pandemic as we see a role for our each vertical. And cross category, merchandising opportunities have been important over this period of time to bring a full Groupon experience for our customers.

You asked specifically about Travel. Now this is a business that has a soft spot in my heart, since I work in the travel industry earlier in my career. And what I'll tell you is, is that when customers want to travel and they know where they want to go, there's a lot of places they can go to find that. What we do is we inspire them.

And we see in the data, upwards of 80% of our customers weren't thinking about the location, and upwards of 90% weren't thinking about the exact property. Similar statistics that I gave you before about our local deals. That is a big deal for our hoteliers they use us as a core part of their revenue management throughout the year.

Now that said, I'll say it again, we're most focused on Local. And within Local, local experiences, which for us, we're really focus on things to do in beauty and wellness, this supply is the most differentiated and fragmented and where we believe we're best positioned for growth.

So you'll see us take advantage of all of our supply, but this is where we're investing, where our strategy is focused. And again, I'll punctuate again for Groupon, it's all about winning in Local.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. Got it. No. Okay. Maybe I'll just ask one near-term obligatory questions about 4Q. Clearly, in the last month or so, many states in the U.S. and even in some other international markets have pushed for aggressive shutdowns to control the second wave.

How are the inputs to your business responding to these? I mean, clearly, there is demand side, but there's also a supply side, which probably is now, of course, to stop servicing. So can you talk a little bit about that?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

Absolutely. Within the United States, there is different trends state by state, market by market. We're watching them closely. And I mean daily by vertical, by market, by customer segment and merchant segment. And I'll tell you, at the highest level, there's nothing I can tell you here that's going to be overly surprising or really all that new.

Markets where there's little to no government restrictions are behaving very differently than markets that have more restrictions. And where the culture is responding differently to COVID.

Now what we're seeing in our model is that our model gives us some resiliency here based on our geographic diversity. Now into the holiday season, I'll tell you that we felt really well prepared. And one thing that we saw that was encouraging is that while we were flexible using our inventory mix across all of our categories, our local categories led by health, beauty wellness, actually still made up 7 out of the 10 most search core terms in our marketplace over Black Friday and Cyber Monday.

So while their short-term is certainly going to be volatile and it has been, what we're seeing gives us confidence. And we're really focused on this strategy that I talked about, so that when customers and merchants really start to come back into this recovery, they're coming back to this improved Groupon that has this expanded value prop on both sides of our marketplace. And that's, again, just our absolute obsession.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. No, that makes a lot of sense. Okay. Yes. I mean, I think certainly, 4Q is going to be a very uneven quarter for a lot of businesses. And it will be interesting to see how the early part of next year also response.

Okay. And switching gears a little bit. You talked a little bit on this initially. As you kind of onboard more supply and as you unlock some of the frequency. How should we think about the monetization model for Groupon evolve? Do you think there should be -- there could be potential volatility in take rate? Or there are any other variables where you expect it to affect the P&L?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

So overall, when we look at monetization, we -- are you asking specific about our inventory strategy? Was that your question number?

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Yes. Yes.

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

Yes. So with our inventory strategy and take rate overall, what's most important here is that this offers product is designed to complement our deal product. And that has really got to be the key here in the way that merchants adopt and use it and the way that we've seen it show up in our model.

Deals get this preferential treatment in our marketplace where they're showing up in e-mail, they come with that high discount, they're used for inspiration. Merchants know how to use them again to drive billion-dollar of commerce. Offer's still out the store. Let me give you an example of -- and this is just a great example of this merchant that I talked to.

She had 3 items on our site that were deals. She then adding over 70 items that included a ton of offers because she could now do that and she couldn't do that before. She also unrestricted everything so customers could buy and buy again, which she couldn't do before, and added our booking technology to make it easier for her and for the customers to book.

So really, the [tri] effective things that we want to see to improve our marketplace on the merchant side and for the customer value proposition. Now when I talked to her about 2 weeks after she launched this expanded offering. And what we saw was about 1/3 of our sales came in on things that she never would have been able to put on the site before. And the things that weren't necessarily showing up in our email, things that customers had to search for.

So complementary to our overall deals product. So what we think about as we see offers as complementary to deals. And then in addition, just like I mentioned, what we've seen from other marketplaces and ad platforms, we can now offer a products such as sponsored listings.

What sponsored listings does, is it allows the supply to compete, just like you see on every other ad platform. And so if you and I both run a salon and you run a better salon than me, you can engage in sponsored listings and you could get a preferential placement and take advantage and get more traffic than I can.

I've talked to so many merchants over the years, and they say, how can I get more, and we have not had a way to say yes. And now we can say, yes. Yes, you can put all your inventory on our site at a price that works for you. Yes, you can pay to get more. Yes, customers, when you're coming to our site to click there's tough for you to buy.

And you clicked on it and we actually let you buy it is opposed to saying, sorry, that's just the first time customers. Yes, yes, yes, across the board. And all in a way that we see as complementary to inspiration business that we've been leading in for years.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. And I believe these efforts are still in limited test markets. When should we expect you to kind of push this more broadly? Is there a time line that you're thinking for that?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

The real key for us is to talk about what we -- and what we were going to -- obviously going to talk more about this in February, but that we should think about this in 2 ways. One, there's some things that we're just going to roll out where we don't have to wait. We found in our test markets just as part of the inventory part, where we really focus on getting supply over those first 3 months that we could remove restrictions a lot faster and easier than we ever expected.

And so we're going to move the fact. That's going to roll out across our business on deals specifically. Also, we are rolling out campaign builder, which is our growing self-service offering. For years, merchants have -- every time they have to make a change with the deal and to add a deal, to add an offer, they have to call the rep, have the e-mail them and go through multiples of -- almost churn on both sides. It's really just -- it makes things difficult. With self-service technology, they can do that themselves. We put the power in the hands of the merchants, we allow our sales team to work on higher leverage activities. And then merchants will invent more ways to do things on our platform.

Also sponsored listings will launch as part of self service. So there's a lot of things that we're just going to go with that are absolutely no brainers to get greater leverage out of this business model because, one, the merchants respond so quickly and as customers respond so quickly, but also they're just complete no brainers for the value proposition of the business we're driving to.

As it relates to scaling all the components of the test, I said we'll share more in February. But based on what we can see right now, there's absolutely nothing to suggest that we can scale quickly.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

That's great. Okay. On the goods side of the business, clearly, you've been migrating into the third-party model. Is the migration now fully done in North America? What are you seeing during the holiday season in terms of both inventory and kind of consumer behavior opposed to migration?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

So I'm going to stick to what I told you earlier, when you asked about Goods, and I tell you, winning for Groupon is on the other side of winning in Local. Now there's a role for Goods on our platform. And as Local recovers and we grow Local, Local is what the business is all about. Now we did say -- we made a decision to stay in the Goods category because we recognize we have the opportunity to significantly reduce that cost structure and simplify this business.

And then at the height of COVID, it's been an important category to keep customers engaged. Now as it relates to third party, we exited the third quarter with 55% of the North American Goods business migrated to third-party and expect to be substantially migrated in North America by the end of the year, kicking off our international transition in 2021.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. Okay. On the cost savings side, obviously, you made some pretty big changes over the past few months, and it sounds like majority of them are kind of fixed costs, which you expect to sustain in 2021, even during periods when demand rebounds. But maybe more specifically, how should we think about the sales force requirements of the business as there's a couple of pieces here, right?

One is demand is expected to rebound and more merchants are likely to come out on the platform, but you're also exploring the new initiatives, which you're likely to expand into new markets. So between these moving pieces, what do you think is the right level of investment on sales force and maybe tie it in with the total fixed cost levels for the business.

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

Absolutely. We're executing on our multiphase restructuring plan, as you noted, which will take \$225 million of fixed costs out of the business by 2022, (inaudible) by 2022. And we've rebuilt our organization with fewer layers. That allow us to be nimble and more productive. So which means we're moving faster and we're getting the leverage.

This reduced cost structure not only allows for greater EBITDA flow through, but it's especially powerful with success in our strategy because that flow through in EBITDA happens in our base case. Whereas success in our strategy is over and above our base case. So let me give you a little bit of the way to think about that from a math standpoint. A Just -- a recovery to the 80% range of gross profit. And again, I already told you about verticals that recovered 80% this summer, but just a recovery to 80% with the cost takeout has it set EBITDA that's greater than we did in 2019. And a recovery to 90% with the cost takeout, which is on track, would have this business at record EBITDA. Over and above that, our growth strategy is laser-focused on increasing customer share of wallet and expanding purchase frequency. And we believe, based on what we're seeing so far, that we're going to be successful in this effort. So we have 2 ways to grow. It's attracting new customers and driving frequency of our existing customers. And then on the merchant side and what's so important for this value proposition that we've talked about is leverage within the sales team. And there's a couple of things here that you can just kind of do the mental math to suggest, how we get that leverage as we go forward? One, we're ramping self-service, we're wrapping self-service from a pretty low base.

That puts our sales team in a position of a lot higher leverage activities. And two, with our offers product, we're also reducing a barrier to merchants by lowering the cost for some of them to come on the platform to make it easier.

Both of these things help us see a path to getting a lot more engagement on the merchant side, as we've already seen in our test markets. And then more engagement on the customer side, again, over and above our base case, which, again, starts off the business at already EBITDA levels higher than 2019, adjacent 80% recovery.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. No, that makes a lot of sense. Okay. On the capital allocation front, I mean, I think clearly, when demand recovers, to your point, there will be pretty significant EBITDA on free cash flow generation. Are you thinking about the priorities primarily in terms of shareholder returns? Or are you looking at any M&As? How would you kind of rank all of those priorities?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

We have a balanced capital allocation strategy that includes investing in the business, M&A, returning value to shareholders via buybacks. And we're just an open mind in management team that are always looking for ways to create that shareholder value. Now I'll tell you is that there is -- I mean, and you've heard from our -- almost every -- no matter what you asked me, we are just so focused on this strategy they we have been. We see that as our greatest opportunity to create value. And with the \$1 trillion total addressable market. And our small share of that, there's just so much potential out there that we (inaudible) ability to unlock and to drive growth for this group.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. Okay. On the partnership's front, I mean, clearly, many companies are now exploring subscription offerings. We've seen subscription offerings to be coming in food delivery space now, and we had TripAdvisor CFO talk about subscription offerings, they're exploring.

Do you think it makes sense to kind of explore partnerships offering with some of the other players in the category and maybe launch a holistic subscription offering? Or is that something that you would consider doing by yourself?

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

So again, the key for us is our inventory strategy. Let me explain you why. Our -- there are a lot of different businesses adapting subscription offerings. What's so special about Groupon is the uniqueness of our inventory. That is special, it's special to our customers and it's especially to any strategic partnership we can look forward to.

And so that is really priority 1 far and away. From a partnership standpoint our customers love great brands, and we have a lot of partnerships that bring brands to our platform. And that's something that we've always been appreciative of and enabled to send these partners a lot of demand.

But we're always looking for opportunities to use our partnerships to accelerate growth. There's lots of potentials out there. You name some examples. There's a lot of other examples out there, but growth achieved strategically and now can be a organic means are both things that we're always considering.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

Got it. Great. With that, we're out of time. Thank you so much, Aaron, for joining us today, and looking forward to talk to you soon.

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Aaron Z. Cooper - Groupon, Inc. - Interim CEO

Thank you very much. I appreciate it.

Deepak Mathivanan - Barclays Bank PLC, Research Division - Research Analyst

All right. Have a great holiday.

Aaron Z. Cooper - Groupon, Inc. - Interim CEO

You too.

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