

05-Nov-2019

Groupon, Inc. (GRPN)

Q3 2019 Earnings Call

CORPORATE PARTICIPANTS

Jennifer Beugelmans

Vice President-Investor Relations, Groupon, Inc.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

OTHER PARTICIPANTS

Elliot Alper

Analyst, D.A. Davidson Companies

Tom Champion

Analyst, Cowen and Company

Michael Ng

Analyst, Goldman Sachs & Co. LLC

Deepak Mathivanan

Analyst, Barclays Capital, Inc.

Eric J. Sheridan

Analyst, UBS Securities LLC

Ygal Arounian

Analyst, Wedbush Securities, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good day, everyone; and welcome to Groupon's Third Quarter 2019 Financial Results Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the company's formal remarks. [Operator Instructions] Today's conference call is being recorded.

For opening remarks, I would like to turn the call over to the Vice President of Investor Relations, Jennifer Beugelmans. Please go ahead.

Jennifer Beugelmans

Vice President-Investor Relations, Groupon, Inc.

Good morning, and welcome to Groupon's Third Quarter 2019 Financial Results Conference Call. On the call today are our CEO, Rich Williams; and Interim CFO, Melissa Thomas.

The following discussion and responses to your questions reflect management's views as of today November 5, 2019 only and will include forward-looking statements. Actual results may differ materially from those expressed or implied in our forward-looking statements. Additional information about risks and other factors that could potentially impact our financial results is included in our earnings press release and in our filings with the SEC, including our annual report on Form 10-K for the year ended December 31, 2018 and subsequent quarterly reports on Form 10-Q.

We encourage investors to use our Investor Relations website at investor.groupon.com as a way of easily finding information about the company. Groupon promptly makes available on this website the reports that the company files or furnishes with the SEC, corporate governance information, our quarterly stockholder letter, and select press releases and social media postings.

On the call today, we will also discuss the following non-GAAP financial measures, adjusted EBITDA, free cash flow and FX-neutral results. In our press release and our filings with the SEC, each of which is posted on our Investor Relations website, you'll find additional disclosures regarding the non-GAAP measures, including reconciliations of these measures to the most comparable measures under U.S. GAAP. All references to SG&A in 2018 exclude the charges for the IBM patent litigation.

As we discuss our results during this call, note that all comparisons unless otherwise stated, refer to year-over-year growth as-reported. All gross profit comparisons are FX-neutral including gross profit per customer.

And with that, I'm happy to turn the call over to Rich.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

Thanks, Jennifer; and thanks to everyone for joining the call as we discuss our third quarter results. As usual, we also released our quarterly letter to stockholders yesterday alongside our earnings announcement, which goes into more detail about the things we'll discuss today. I encourage you to take the time to read it.

I'm pleased to speak today about our strategic progress in the third quarter, which delivered adjusted EBITDA of \$50 million and free cash flow of \$126 million on a trailing 12-month basis. These results underscore the tremendous opportunity Groupon is best positioned to capture. Local commerce is a vast addressable market in few, if any, can boast our unique combination of customer and merchant scale. To fully realize this opportunity, we remain focused on four strategic priorities: improving the customer experience; expanding our open platform; investing in our International business; and continuing our history of operational rigor.

I'm pleased to report that we made progress in all four areas even as we faced challenges in the form of continued traffic declines as well as in International business dealing with broad macroeconomic issues in Europe, particularly in the UK. Those factors contributed to lower-than-expected gross profit in the quarter. In spite of some near-term challenges, the team also delivered on some key initiatives in the quarter as we continue to scale Groupon Select, our new membership product and launched important product enhancements, including significant improvements to our mobile web experience, focused squarely on reducing friction and improving conversion.

We also continued to add high-quality partners which will bring even more great inventory and offers to our site. Over the last quarter, we've made a concerted effort to meet with many of you and the feedback was clear. We can be crisper in describing our vision and in helping you identify the metrics that will matter most and tracking our progress going forward, particularly where we are most differentiated in Local. Expect to hear more from us moving into 2020, as we further refine our communications approach and strategy.

Before I hand to call over, I'd like to introduce Melissa Thomas, our Interim CFO. For those of you who have not yet spoken with Melissa, she is a veteran finance professional who was been with Groupon for three years. In that time, she's overseen our commercial finance teams and currently also serves as our Chief Accounting Officer.

With that, I'll turn the call over to Melissa to walk you through the financial highlights for the third quarter.

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

Thanks, Rich. I'm excited to be in the CFO role during this important time at Groupon. During my last few years at the company, I've been motivated by the opportunity we have in front of us and the incredible team that's helping us get there. I'll use my time today to walk you through our key financial highlights, including gross profit and adjusted EBITDA, provide you with a few insights on unit trends which we believe is an important metric to measure our success, update you on our progress with Groupon Select; and after that, we'll open up the call for questions.

Let's start with gross profit. In the third quarter, we delivered gross profit of \$278 million. We are making progress against our key strategic priorities, particularly removing friction from the customer experience, growing membership in our Select program and expanding our open platform. Ultimately, we believe success in these areas will help us drive higher purchase frequency, conversion and gross profit growth over the long run.

As we discussed with you last quarter, we expected to face persistent traffic headwinds, customer losses in North America and challenging macroeconomic conditions that would impact our European business, particularly the UK. In fact, during the third quarter the European economy performed even more poorly than we anticipated, causing these challenges to impact the International Local category, as well as Goods. In addition, the competition in our Goods category was tougher than we expected.

In North America, gross profit was \$192 million, down \$12 million or 6% year-over-year. Q3 North America Local gross profit was \$155 million, down \$4 million or 3%. Q3 North America Goods gross profit was \$26 million, down \$5 million or 15%. Gross profit per customer on a trailing 12-month basis was \$30.56, up 6% year-over-year. North America net customers declined by 870,000. This decline was expected, but it's important to note that active customers is not the only metric to measure our progress.

Those of you close to the Groupon story know that we're uniquely positioned within Local, given our scaled two-sided marketplace with millions of customers and hundreds of thousands of local merchants. And our strategic initiatives are closely tied to driving this part of our business. We know that we can improve the customer experience by making our websites and mobile applications more engaging and easier to use, launching new products such as voucherless offerings and Groupon Select and adding more high-quality supply to the marketplace.

As we transition our customer base to higher quality, more engaged customers, we believe that unit growth, particularly Local, will be a leading indicator of improving purchase frequency and conversion. Naturally, billings and gross profit per customer all remain important, but we believe unit growth will speak even more broadly to the health of our evolving marketplace.

In Q3, year-over-year Local unit performance for North America improved for the third (sic) [second] sequential quarter and our expectation is for this trend to continue into Q4. In fact, within the third quarter Local unit year-over-year trends strengthened in each month. We are encouraged by these trends which we believe are an early indicator that our strategic initiatives are beginning to deliver.

We're excited about our Select membership program and are already seeing encouraging results. To-date, we have over 260,000 members despite a total third quarter investment that came in slightly lower than the \$10 million expectation. It's still early days, but we're seeing member acquisition costs payback within six months; and payback has been driven by both the recurring revenue from membership fees as well as incremental gross profit generated on membership-related transactions.

For modeling purposes, it's important to remember that historically we routinely offered order discounts and some of our merchants participate with us on these discounts. As a result, the discounts associated with Select memberships are not entirely incremental. We are really excited about the early impact we're seeing on purchase behavior. On average, in the first six months post-enrollment, Select members increased purchase frequency by about 60% and average order values by about 20%.

We believe these early positive results illustrate our ability to monetize the member-like behavior of our customers and demonstrate the power of our massive Local two-sided marketplace. By making progress on these fronts, we believe we can unlock the potential of our financial model and deliver long-term gross profit growth and significant adjusted EBITDA.

Turning to International, gross profit was \$86 million, down \$12 million or 12%. Q3 International Local gross profit was \$61 million, down \$8 million or 11%, despite Local unit growth. Local gross profit performance was impacted by higher-than-expected purchases of lower-priced and lower-margin deals. While it can be difficult to predict consumer shopping behavior, we believe one way to offset the impact of this in the future is to continue focusing on enhancing the quality of our supply.

International Goods gross profit was \$17 million, down \$3 million or 16%. International gross profit per customer on a trailing 12-month basis was \$22.51, down 5%. While net customers declined slightly in the quarter, excluding the UK, net customers would have been up. Notwithstanding the transitory challenges created by the instability of the economies in Western Europe, particularly the UK, we remain confident in our international strategy and believe we are taking the steps necessary to drive long-term growth outside of North America.

We view the progress we're making in the Asia-Pacific geography, which includes double-digit billings growth, as a proof point that our international growth strategy remains solid. In the third quarter, on a consolidated basis, marketing expense was \$74 million or 27% of gross profit. Historically, our marketing expense has trended closer to 30% of gross profit. We've spoken in the past about our focus on driving marketing efficiency and our focus hasn't changed. We are also deploying marketing strategies that allow us to leverage data to better segment our customer base and personalize the overall Groupon experience.

Our goal is to drive purchase frequency, particularly within the first 90 days post purchase. We know that this metric is highly correlated to customer lifetime value and we're looking at opportunities to drive it higher. To complement these efforts, we're also in the process of adapting our brand strategy to support our evolving marketplace. As part of this process, we're pragmatically evaluating our spend across the marketing funnel.

SG&A for the third quarter was \$198 million, an improvement of \$2 million or 1% year-over-year, driven by our ongoing efficiency efforts. We delivered adjusted EBITDA of \$50 million during the third quarter. We purchased a little more than 5 million shares for \$15 million in the third quarter. On a trailing 12-month basis, share repurchases represented over 44% of our free cash flow. And to date, we've returned more than \$900 million to shareholders through repurchases.

We have a strong balance sheet and ended the third quarter with \$567 million of cash and \$400 million available on our undrawn revolver. This strength provides us with important financial flexibility to support a balanced approach to capital allocation. That includes our track record of share buybacks, strategic investments and product launches like Groupon Select and opportunistic M&A that can accelerate our core strategy.

As we move into the fourth quarter, a very important time for us, we expect positive contribution from our conversion initiatives, which include our recent guest checkout and universal cart product launches. In addition,

we expect marketing leverage to increase modestly from what we delivered in Q3. These factors, along with a continued momentum in North America Local including improved performance in units, give us confidence that we can drive sequential improvement in year-over-year gross profit trends and deliver approximately \$270 million in adjusted EBITDA for full-year 2019.

Thank you for your time today. We appreciate the support of our investors and look forward to chatting with you about our progress. With that, let's open up the call for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And your first question comes from the line of Elliot Alper with D.A. Davidson. Your line is open.

Elliot Alper

Analyst, D.A. Davidson Companies

Q

Great. Thank you. I was wondering if you could expand more on the deceleration of active customers, particularly in the US. Maybe the puts and takes that you're seeing in the marketplace and your marketing planned spending for the holiday season? Thanks.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Thanks for that, Elliot. I'll start and just give an overview of where we are on the marketing side, and then I'll hand it over to Melissa to give a little bit of color on active customers. But it's probably just helpful going into holiday season in particular to have just a broad view of how we're thinking about our marketing strategy. As Melissa mentioned in prepared remarks, we are being thoughtful as we're starting to think more deeply about our brand path in particular as we scale the marketplace, as we refactor the product and improve the customer experience overall.

As you probably know, we have a new CMO and he's conducting an overall strategic review of the brand. And you're seeing that play itself out on our marketing allocations. And I think it's important there to lock in on that allocations point, because if you think about Q3, the way we think about it from a marketing point of view, you'll see our total marketing investment which includes our working spend, traditional marketing and order discounts, it's actually changed very little.

And so, we're seeing more of a reallocation and a reapplication of dollars in the funnel to improve efficiency overall and to make sure we're spending in areas that are aligned with our strategy going forward. And that's what I would expect to see us doing as we move into Q4, to be more thoughtful about the application and allocation there and align that to where we are and how we're viewing the brand and the opportunities to recast the brand that better align with the product and the marketplace we're building. And so, you can see that in general play itself out over the course of the next couple of months and frankly the quarters to passed.

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

A

And a word out on the decline we saw in active customers in North America. This was something that we expected. If you think about the drivers, the key areas there, traffic headwinds which – those are ongoing traffic

headwinds that impact customer accounts in North America in particular, as well as the marketing efficiencies that Rich mentioned. Those are really the two large drivers of the decline in active customer accounts.

What I would mention is, in our prepared remarks we did – let folks know that while active customer accounts are an important metric for us, right now where we're really focused is units and purchase frequency. Ultimately, we believe that that's really the unlock – unlocking the leverage in our model and will position us to drive long-term sustainable gross profit growth. So that's where really going forward, you'll see us focused. And as we mentioned, what we're seeing in North America in particular is some improving year-over-year sequential trends in Local unit performance and we're definitely encouraged by that.

Elliot Alper

Analyst, D.A. Davidson Companies

Great. Appreciate it.

Q

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

Thanks, Elliot.

A

Operator: Your next question comes from the line of Tom Champion with Cowen. Your line is open.

Tom Champion

Analyst, Cowen and Company

Hi. Good morning. Looks like North American Local billings grew quarter-over-quarter and there were some constructive comments around units. And I'm just curious, Rich, if you could provide any more thoughts on the driver there. It sounds encouraging. And whether it's Select or inventory or maybe new features like guest checkout. Maybe just any comments there would be really helpful.

Q

And maybe just one more if I could. The letter talks about fighting traffic headwinds with purchase frequency and product enhancements. Can you just talk about what you're doing to ramp product development and speed up implementation? And just, I guess lastly, any thoughts on the traffic headwinds and whether that might moderate over the next couple quarters? Thank you.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

Awesome. Thanks for that, Tom. I'll start and Melissa add color as I work through here. But I think it's actually a similar answer to both questions, Tom, in a bunch of ways there. People were excited about what we're seeing that's really encouraging, as Melissa mentioned, is that you're starting to see our strategy around the product and the investments that we've been making and it's just a better customer experience started to play its way through the local consumer.

A

And I think [ph] in that place (00:19:23) you're seeing things like guest checkout, like universal cart start to make an impact, and we talked about it before. Those aren't [ph] whiz-bang (00:19:32), those are e-commerce standards that people are well familiar with and accustomed to seeing in checkout that they hadn't seen on Groupon. It's making that experience easier, higher converting and just generally better. And the same goes for the other things that we're doing on the convenience side. And so, our mobile web experience is just a better experience. If you've not used it, I'd recommend to try it. It'll give you a window into where we're headed with things like personalization, the more intelligent use of data and really harnessing all that we know about

customers. So, you're starting to see some of those pieces really work their way through that local customer experience, and we're seeing the impacts of that.

Select as well is in there. Melissa mentioned, a 60% increase in purchase frequency is pretty significant, especially over the course of the first six months of membership. So, that's a piece that's absolutely helping as we grow that customer base as well, as small as it is today. So you're really starting to see those pieces through. And as a team what we're most focused on, to your point, is how do we go faster, how do we do more, how do we start to ramp up the productivity and production of our software development pipeline and really get more software and more great enhancements in front of customers?

And a big piece of what we're doing there, one, has been team. So we've made investments in team and leadership on that side. We're really pleased with how that team has come up to speed under the leadership of our Chief Product Officer, Sarah Butterfass. She's doing a great job. And a lot of the work that she's doing is kind of good old-fashioned [ph] Agile (00:21:08) development and really adding ownership decision-making rights and agility to the team and just freeing them up to do great work.

So, that's going to be a real key piece of what we do alongside some of the infrastructure investments that we're making just to enable that more rapid development and rapid deployment of software. So there is a lot of work happening in our technology teams to just enable that raw speed, because we already have a lot of quality in our production processes. It's really we've been lacking I think that core speed and you're starting to see the acceleration of that over the last couple of months as you've seeing big pieces of enhancement moved out into the market. Melissa, do you have other things you want to add?

.....
Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

A

Yeah, just on the traffic headwinds. I think you had asked whether that would moderate over the next few quarters. So, let me just give you a little bit of context on the traffic headwinds, what we saw in terms of the third quarter. So North America was broadly in line with our expectations. However, internationally – from an international standpoint, traffic did worsen given the transitory macroeconomic conditions in Europe that we mentioned, particularly in the UK. When you think about the go forward, we'll look to provide more color on our 2020 outlook in our Q4 call. But traffic headwinds we do expect to persist.

.....
Tom Champion

Analyst, Cowen and Company

Q

Okay. Thank you, both.

.....
Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Thanks, Tom.

.....
Operator: Your next question comes from the line of Michael Ng with Goldman Sachs. Your line is open.

.....
Michael Ng

Analyst, Goldman Sachs & Co. LLC

Q

Hi. Good morning. Thanks for the question. I just have two. The first is just on the guidance. Could you just talk about some of the key drivers of the, I guess, implied EBITDA inflection in the fourth quarter? And as a follow-up

to that, how much was the EBITDA contribution or, I guess, headwind from Groupon Select in 3Q? And what's your expectation for how Groupon Select affects 4Q? Thank you very much.

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

A

Sure. I'll start off with your question on guidance. So if you think about the key drivers for our full-year guide, I'll point to really few key items. So first, starting with – as Rich mentioned, we've been accelerating our progress on the product front and we have recently launched two key conversion driving initiatives, including guest checkout and universal cart. We are expecting meaningful contribution from these in the fourth quarter. I mean, I can tell you that early results, particularly with guest checkout, are very encouraging. We're definitely pleased with what we're seeing on both of these. But as we continue to improve the customer experience, we certainly see that to manifest itself in a more meaningful way in the fourth quarter.

In addition to that, I would point to the continued improvement that we've been seeing in sequential year-over-year North America Local trends that we do expect that momentum to carry forward into Q4 and to see continued sequential improvements there. Also the next point that I would make is really on the marketing side. We do expect, as I mentioned in my prepared remarks, to have marketing leverage that is modestly up versus what we saw in Q3 into fourth quarter.

The one thing that I would point out here is not just related to the efficiencies that Rich mentioned earlier on the call, but it's also the result of – I mean, as you think about how conversion initiatives manifests itself in the P&L. As we see improving year-over-year sequential trends in GP in the quarter, that does improve our marketing leverage. So, those are really the key drivers that I point out there.

And then on your question on Select and the headwinds that we saw in Q3 and what we expect to see in Q4, what I'd say there is we've been really pleased with the trajectory in terms of our ability to improve member accounts and what we're seeing on the customer side from a frequency standpoint as well as average order values improving. I'm not going to give specific impacts on Q3, but just to give you a flavor for Q4 what we're expecting to see, we are expecting to continue to invest in acquiring members within the program. But we expect overall the program to be net neutral impact on GP in Q4.

Michael Ng

Analyst, Goldman Sachs & Co. LLC

Q

Great. Thank you very much. That's very helpful.

Operator: Your next question comes from the line of Deepak Mathivanan with Barclays. Your line is open.

Deepak Mathivanan

Analyst, Barclays Capital, Inc.

Q

Hey, guys. Thanks for taking the question. Yeah, I just wanted to ask a little bit more about that. Slightly a big picture question in terms of how we think about customers versus gross profit. With all these product initiatives that's going on and also some of the way you are optimizing the marketing investments, clearly there is some drag in terms of the net active customers. But as we fast-forward say two to three years down the line, where do you think are pockets of customers that you can capture incrementally from here, specifically if you look at US as a proxy market?

Are there any other categories where you think your customers are still not in the platform? Any color there will be helpful. And then from a gross profit per customer standpoint, clearly it's been hogged by a number product tweaks recently. But from a unit economic standpoint, as you think about these customers that are coming in, is there enough run way to kind of sustain that over the next few years as you think about it? Thank you very much.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Thanks for that, Deepak. I'll start and Melissa, please, add color as well. I think you'd point out I think an important piece here, Deepak, and it's that we of course care and pay a lot of attention to our active customer accounts. But as we've mentioned, I think right now we're – and we continue to be focused on driving purchase frequency, unit growth and unit volume and total demand on the platform. And the reason that we're focused there is really a simple one.

If you think about it in a really simple way, with our roughly 45 million customers that are purchasing call it 3.5 times a year, one incremental purchase is massive, right? You're talking about 45 million extra units every year. It would take an additional 10 million active customers or more, almost 11 million or 12 million customers, buying at the same rate as our average customer to just replace – or to compensate for that one extra unit. And again, we're not talking about taking someone or an average customer from 3.5 units to 10 units; we're talking about going from 3.5 units to 4.5 units.

So, that unlock is really, really significant. And adding 10 million or 12 million customers is a big guess. But I think the biggest opportunity for us is really going from 3.5 units to 4.5 units and from 4.5 units to 6 units and 8 units and 10 units and so on. So that's where you'll see us continue to focus, less so where do we become the next incremental customer, but more so how do we deepen our relationships with our customers, how do we give more value to our customers through our improvement in our customer journey by removing friction, launching new products like booking and moving to a voucherless environment, continuing to enhance the basics of how we work with things like guest checkout and universal cart. That enrichment in getting wallet share with our existing customer is the biggest opportunity for us at this point, which also then unlocks additional capacity to go acquire more.

And again, the areas that we work in were the biggest which is really in dining and health and beauty and activities and things to do. We're a very small percentage of a very big market there. So we have a lot of room just to gain wallet share and we have a lot of room to continue to address that market and pull new customers in. But in the immediate term and as you see us move through our strategy to improve the total experience on the platform and to open it up, you're going to see us focusing intently on unlocking that purchase frequency component that's really – that's the really big growth driver for us over time.

And I don't know, Melissa, if you have any thoughts on GP per customer?

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

A

Yeah. I think I'd tie it in to exactly to what Rich said. I mean, really when you think about the run way to improve gross profit per customer, the unlock of purchase frequency, that's really what gets that number to continue to grow.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Yeah. The only other thing I'll add, Deepak, that makes me think of it is, when you think about runway, outside of just the basics of what we do which tends to be at least the history of Groupon, right, we tend to be the platform that helps you discover something new and find that place that we hope you love and then most of our customers end up repeat visiting. Where we've historically sat out and not participated is on one of our big opportunities when we think about frequency, and it's participating in that repeat visit. And there's already pieces of our product strategy that you're seeing going in the market.

We have a cashback loyalty reward for those repeat visits. We're starting to participate in that part of the relationship between the customer and merchant because it's extraordinarily valuable for the merchant side of our marketplace to do that. So in terms of runway, I think we have really significant runway to improve our connectivity between consumers and merchants in that space. Now, the unit economics of those at full price versus discounted and promoted versus not, those will play themselves out over time. But we see, really just from a pure addressability perspective, the runway is significant.

Operator: Your next question comes from the line of Eric Sheridan with UBS. Your line is open.

Eric J. Sheridan
Analyst, UBS Securities LLC

Q

Thanks so much for taking the question. Maybe two if I can. On International, are there ways to provide some examples on a country-by-country basis of where you either see supply dynamics or traffic dynamics or marketing dynamics to drive velocity of shopping, and what you're trying to solve for some of the individual country levels?

And then, along those same lines, on the headwinds you've called out from a traffic basis, are those more pronounced overseas or are those more pronounced domestically on the traffic side? And maybe if you can give us a little bit of granularity on the skew between that? Thank you.

Richard Williams
Chief Executive Officer & Director, Groupon, Inc.

A

Sure, Eric. I'll start and – we don't provide detail on a country basis in International. But what we have provided is – I think you'll get a little bit of color on how our businesses are performing in International and that's where there really is a tale of two cities happening here, arguably maybe three. You have the UK, you have Europe and then you have Asia. And for us, our fastest-growing businesses are actually – in our International markets in they're in Asia and they're growing in double digits.

So, there is a lot happening in those markets that is really just the fundamentals of running a good Groupon business, which is focused on great supply, great merchant relationships, high-quality national brands. And then good efficient marketing to support it to acquire customers and also some product enhancements and different ways of engaging our customers, which are starting to make their way into some of our other larger markets as well.

So we've done a lot of refactoring of our e-mail programs in our International markets. We've done a lot of refactoring of our onboarding for new customers, et cetera. So we're using a lot of those markets in our footprint as an advantage to learn and to experiment in ways that doesn't require really having the entirety of the US exposed to something. So we have more agility that way.

So we're learning a lot in those markets. We're seeing that the fundamentals drive good solid results and performance. And you are seeing the differentiation between those markets and some of the – those markets

specifically where we don't see those macroeconomic issues where things like Brexit and uncertainty around the Eurozone haven't really crept in to our APAC market. So, I think that's probably the best color I can give you on how we're approaching that. I don't know if you have other thoughts on headwinds?

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

A

Yeah. I think covers it. I think the only thing I would call out is, and you can tell it from our prepared remarks, that UK is certainly a standout and is a meaningful portion of our International business so we do see that, but it varies across Europe [ph] back there (00:34:20).

Eric J. Sheridan

Analyst, UBS Securities LLC

Q

Thanks everyone for the color.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Thanks, Eric.

Operator: [Operator Instructions] Your next question comes from the line of Ygal Arounian with Wedbush Securities. Your line is open.

Ygal Arounian

Analyst, Wedbush Securities, Inc.

Q

Hey, good morning. A couple questions. I'll start with marketing. And I guess, I'll just ask why not step into marketing a little bit more in the near term? Your initiatives to drive frequency are starting to work. All of them are pretty new. You've got Select and universal cart and guest checkout. So, I get that frequency should beget marketing leverage over time. But if you've got these things that are starting to work and are driving the thing that is ultimately the difference maker which is the increased frequency why not, especially in the fourth quarter, kind of push on it a little bit more. That's the first question.

And then second, just maybe looking for a little bit more details in Select and how to think about why it's gross profit neutral through the end of the year or, I guess, in fourth quarter. If you think about the amount of subscribers that have joined that kind of basic – just doing the basic math of the \$5, \$6 a month and how that flows through to gross profit. Is the offset there just continued investment? Are there churn elements that we should be thinking about? Maybe just a little bit more detail there. Thanks.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Sure. Thanks for that, Ygal. I'll start on the marketing side. Yes, it's a great question and fair question; one I'm not accustomed to hearing all that much frankly of why not spend more on marketing. But look, I think that – I guess, I'll go back to what I said earlier on, I think it's important to remember. We haven't made really significant changes for our total marketing investments that we're making. You've seen some significant shifting and how we're allocating to improve performance and efficacy. But I think we're still investing at a pretty aggressive level.

Now, I think that however the biggest gating factor on that side is, is really where we are in terms of rethinking our brand's proposition and how we go to market on some of these pieces. And while we sort those out, we're

reallocating a lot of our investment to drive adoption in our promotional calendar and get people in some of these new experiences at a higher rate, because I think again that's where we're going to get the biggest total leverage is getting more of our existing buyers, those existing 3.5- to 4.5-time a year buyers in these new experiences, enjoying a new version of Groupon that is far more rewarding as a customer.

So you're going to see us do some of that, while we're working on the total brand piece and thinking about how we go to market with these new products in a much broader way. But I think that's really the big gating factor is on really making sure and feeling strongly about our refresh brand proposition and how it's going to play through the funnel and how we use that strategically as we move forward.

Melissa Thomas

Senior Vice President, Chief Accounting Officer & Interim Chief Financial Officer, Groupon, Inc.

A

And then on the Select side there, just to give you a little bit of color on why essentially Select is – we expect it to be net neutral in the fourth quarter. There is a few elements I laid out in my prepared remarks that you need to take into consideration when we think about Select. So, we are making investments in Select and those do show up in terms of GP, whether it be opportunity, costs, et cetera. However, those are offset by subscription fees that we are collecting. And then the important part to remember is that we are also earning incremental GP on the transactions and we're seeing a purchase frequency lift at 60% higher in that 180-day post-enrollment in the program.

And the third piece I'd call out is that the entire discount is not incremental. So when you take into account what we're earning on the overall program for the members we have in it versus the caps which I mentioned on the call – on my prepared remarks as well, are very reasonable. We don't see it as being a meaningful headwind for us.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

A

Right. I think within that you're seeing us in that net neutrality pushing for continued investments, while we're harvesting the benefits that we see. So we're not going to stop investing in the quarter; we're going to continue it. We see opportunity to increase enrollment and participation in the program. We like what we see in this early stage of development with purchase frequency and that just engagement behavior overall. We're going to continue to lean into that. If not at any cost, because we're – as I mentioned before and we mentioned a couple of times, we still have some investments to make there on this core infrastructure. And when I say that, it's really integrating it into the core of the Groupon experience.

It's important to remember, Select was an experiment, was a trial that we've iterated on and we continue to develop over time and we are excited by it. But we're excited about it in a way that we're feeling it needs to be part of Groupon. It can't just be the side; the side test for a group of people really needs to be – needs to permeate the Groupon customer experience, which we're starting to see. You're starting to see, if you go to the desktop as an example, you're seeing Select pricing frontend center as a promotional item and as a reminder to our members that they get a unique benefit.

But it needs to be deeper in our onboarding processes, it needs to be much more integrated in our merchandising, it needs to be much more targeted. And so, it really needs to start to leverage the core of our infrastructure and systems, and really be a deeper part of what we do. So, you're seeing us balance our investment and scaling on that side in both ways, both in terms of the number of folks we're bringing in as well as the amount that we're investing in product development to really make it a core part of what we do moving forward.

Ygal Arounian

Analyst, Wedbush Securities, Inc.

Great. That's helpful. Thank you.

Q

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

Thanks, Ygal.

A

Operator: And there are no further questions at this time. I turn the call back over to our presenters for any closing remarks.

Richard Williams

Chief Executive Officer & Director, Groupon, Inc.

Thanks, everyone, for making time on the call and we appreciate it. We look forward to speaking with many of you soon.

Operator: Ladies and gentlemen, this concludes today's conference call. You may now disconnect.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2019 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.