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EDITED TRANSCRIPT

CTRP - Q2 2017 Ctrip.Com International Ltd Earnings Call

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OVERVIEW:

Co. reported 2Q17 net revenues of CNY6.4b or \$946m, net income attributable to Co.'s shareholders of CNY327m or \$48m, and diluted earnings per ADS of CNY0.59 or \$0.09.



AUGUST 31, 2017 / 12:00AM, CTRP - Q2 2017 Ctrip.Com International Ltd Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and thank you very much for joining today's Ctrip.com International, Ltd. Earnings Conference Call for Q2 2017. (Operator Instructions) And then next, I will turn the call over to Ms. Michelle Qi, IR Director of Ctrip.com. Please proceed.

Michelle Qi

Thank you, Bart. Good morning, and welcome to Ctrip's second quarter of 2017 earnings conference call. Joining me today on the call, we have Mr. James Liang, Chief Executive Chairman of the Board; Ms. Jane Sun, Chief Executive Officer; and Ms. Cindy Wang, Chief Financial Officer.

During this call, we will discuss our future outlook and performance, which are forward-looking statements made under safe harbor provisions of U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements involve inherent risks and uncertainties.

As such, our results may be materially different from the views expressed today. A number of potential risks and uncertainties are outlined in Ctrip's public filings with the Securities and Exchange Commission. Ctrip does not undertake any obligation to update any forward-looking statements, except as required under applicable law.

James, Jane and Cindy will share our strategy and business updates, operating highlights and financial performance for the second quarter as well as outlook for the third quarter of 2017. After the prepared remarks, we will have a Q&A session.



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With that, I will turn the call over to James for our business update. James, please.

Jianzhang Liang - *Ctrip.com International, Ltd. - Co-Founder and Executive Chairman*

Thank you, Michelle, and thanks to everyone for joining us on the call today. Ctrip group reported a solid growth in the second quarter. Net revenue was up 45% year-over-year in the second quarter. The strong performance was mainly driven by healthy organic growth and the addition of Skyscanner. Non-GAAP operating margin reached 18% for the quarter, improving from 4% a year ago and 15% last quarter.

In the following discussion, I would like to share updates on our progress in expanding into lower-tier cities and increasing presence in international markets.

Lower-tier cities are becoming a key driver of the growth of China's travel industry for the coming decade. Ctrip is well-positioned to benefit from both the increasing online penetration as well as consumption of growth trends in lower-tier cities. We have expanded our product offering in these markets and a further streamlined user experience by offering multiproduct reservation and order changing services. We also offer more personalized services through our franchised top line retail stores.

To promote such a strong value proposition to consumers in lower-tier cities, we have launched a series of effective marketing campaigns. Our dedicated efforts have led to market share gains for all our brands. New customer acquisition and the user engagement have improved significantly across [post] brands. In the second quarter, user traffic in second-tier cities increased about 50% year-over-year.

As part of our -- next, I would like to comment on our international business development. As part of globalization, the growth of international service trade has been accelerating around the world. China service trade as a percentage of total international trade has increased approximately 600 basis points in the last 2 years.

Travel is the largest part of service trade and will continue to be critical in driving this future growth. In the next several years, China's outbound tourism will continue to deliver robust growth. The growing scale of our outbound business allows us to capture more and more local inventories in popular international destinations.

We continue to enhance our one-stop shopping experience by adding new services to existing accommodation, transportation, local activities, food reviews, shopping and tour guide offerings on our platform to serve both packaged tour and DIY customers. As a result, we are well prepared to benefit from the growth of outbound tourism.

We're still in the early stage of the international expansion. The Ctrip international website and mobile apps are only available in 12 languages, so we are expanding into more markets. We are also strengthening our presence in many product verticals. For example, we have started working with Skyscanner via direct booking model to reach more international customers. Skyscanner has officially launched the direct booking model, which introduces travelers to a seamless booking experience. This is a more efficient way to convert Skyscanner's user traffic while helping their business partners retain customer relationship and ability to upsell ancillary services. The new model accounts for a very small part of Skyscanner's business at this point. Some earlier partners, including Ctrip, saw an approximate 50% boost in conversion rates of mobile traffic. We are very confident in this future potential.

Investing in lower-tier cities in international markets will continue to be our priority as we are progressing into the second half of 2017. The group will keep improving comprehensive product offering, enhancing best-in-class services and driving effective marketing. We have made good progress in these areas and are confident that the group can continue to deliver long-term sustainable growth.

With that, I will turn the call over to Jane for business highlights.



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Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Thanks, James. I'm very pleased to share updates on Ctrip's main businesses with you. First, on hotels and other accommodations. The total hotel revenue grew by 30% compared with the same period last year, mainly driven by volume growth. This quarter's growth rate reflected some negative impact due to the adoption of the VAT tax. At the end of the second quarter, Ctrip's domestic hotel coverage reached 570,000 hotels, increasing by approximately 25% over a year ago.

In addition to traditional hotels, both Ctrip's and Qunar's accommodation booking engines now offer 450,000 vacation rental properties from Tujia, the largest platform of its own kind in China. This segment is -- has significantly strengthened our overall accommodation inventory.

In the second quarter, vacation rental bookings grew at a triple digit from the previous year. The group continues to strengthen its presence in the lower-tier cities. Hotel bookings in these markets have achieved accelerated growth across brand. In July, the total number of room nights in the lower-tier cities reached approximately 20 million.

Second, transportation and ticketing services. Total transportation revenue grew by 49% year-over-year in the second quarter, supported by strong volume growth and inclusion of Skyscanner's financials. The air ticketing business delivered solid performance, led by strong international air ticketing growth.

Ctrip has been making meaningful improvements in the price competitiveness in the international markets and enhancing our technology platform to support functions such as search for complex, multi-destination itineraries. Now, approximately 50% of international air tickets booked on Ctrip are for flights originated from airports outside of China. In addition, Ctrip and Skyscanner has been sharing best practices and creating strong synergies, which should further drive our international air ticket growth. We are greatly encouraged by the progress and confidence in the potential of our international air ticketing business.

Our focus on technology and services have enabled us to optimize our customer experience while strengthening our support to suppliers. For example, our AI customer service checkbox now handles over 40% for air ticketing customer service inquiries. With such improvements in service quality and operating efficiency, our air ticketing business continues to create value for both our customers and suppliers.

Ground transportation maintained triple digit year-over-year growth in the second quarter. Our multimodal transportation offerings currently provide different combinations of air, train, bus and car rental services. Such transportation solution are well received by young and tech savvy travelers. We are continuing to invest in adding domestic and international routes and developing technology to integrate these services.

Ctrip's intracity bus ticketing platform is now the largest in China, effectively expanding our transportation services to the lower-tier cities. We have also helped bus operators develop coach services for private hires and shuttle services connecting hotels, tourist attractions, airports and train station. [Bus plus x] has become an important part of Ctrip's multimodal transportation framework.

Third, on packaged tour. Packaged tour revenue increased by 29% year-over-year, driven by healthy volume growth. In the past 2 quarters, we have opened over 400 Ctrip and Qunar franchise retail stores, with approximately 200 more in the pipeline. Market feedback in the past several months was encouraging. Some stores have reached a monthly sales of RMB 2 million. Including the 5,500 stores under Travel Bestone brand, we plan to have at least 6,500 stores in operations by the end of this year.

The Ctrip team is dedicated to make tour easier by offering personalized choices. Following the success of our tailor-made tours, we have launched the first global market phase for tour guides in China travel industry. Travelers can choose from more than 8,000 local tour guides over 800 destinations. We have carefully designed and implemented the processes to verify the qualification of these tour guides and ensure service quality on our platform. So far, 98% of our customers have given favorable feedback after trying these services.

Fourth, on corporate travel. Corporate travel business growth accelerated in the second quarter to 36% year-over-year. Our corporate travel team works hard to build an integrated end-to-end travel and expense solution. We have expanded our product offering, enhanced our mobile application functions and collaborated with leading players to integrate new features such as reporting solutions and traveler location functions. In July, Ctrip's corporate travel management was awarded the 2017 Most Influential Corporate Travel Brand in China Financial Summit.



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Overall, we are pleased with the strong operating and financial results in the second quarter. I would like to thank our employees for their hard work and dedication. We will remain focused on operating fundamentals that create value for our customers and suppliers. We are confident in generating long-term value for our shareholders in the years to come.

With that, I will turn the call over to Cindy for financial highlights.

Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

Thanks, Jane. Thanks, everyone. For the second quarter of 2017, Ctrip reported net revenue of RMB 6.4 billion or USD 946 million, representing a 45% increase from the same period of 2016. Net revenue for the second quarter of 2017 increased 5% from the previous quarter.

Accommodation reservation revenue for the second quarter of 2017 were RMB 2.3 billion or USD 341 million, representing a 30% increase from the same period of 2016, primarily driven by an increase in accommodation reservation volume. Accommodation reservation revenue from the second quarter of 2017 increased 12% from the previous quarter, primarily due to seasonality.

Transportation ticketing revenue for the second quarter of 2017 were RMB 3 billion or USD 441 million, representing a 49% increase from the same period of last year, primarily driven by an increase in ticketing volume and the consolidation of Skyscanner's financial results since December 31, 2016. Transportation ticketing revenue increased 4% from the previous quarter, primarily due to seasonality.

Packaged tour revenue for the second quarter of 2017 were RMB 612 million or USD 90 million, representing a 29% increase from the same period of 2016, primarily driven by an increase in volume growth of organized tours and self-guided tours. Packaged tour revenue for the second quarter of 2017 decreased 13% from the previous quarter, primarily due to seasonality for Chinese New Year in the first quarter.

Corporate travel revenue for the second quarter of 2017 were RMB 199 million or USD 29 million, representing a 36% increase from the same period of 2016, primarily driven by expansion in travel product coverage. Corporate travel revenue for the second quarter of 2017 increased 38% from the previous quarter, primarily due to seasonality.

Gross margin was 82% for the second quarter of 2017 compared to 72% for the same period of 2016 and 80% for the previous quarter.

Product development expenses for the second quarter of 2017 increased by 18% to RMB 2 billion or USD 300 million from the same period of 2016, primarily due to an increase in product development personnel-related expenses. Product development expenses for the second quarter of 2017 increased 4% from the previous quarter. Product development expenses for the second quarter of 2017 accounted for 32% of the net revenue. Excluding share-based compensation charges, non-GAAP product development expenses for the second quarter of 2017 accounted for 27% of the net revenue, which decreased from 31% for the same period of 2016 and decreased from 28% for the previous quarter.

Sales and marketing expenses for the second quarter of 2017 increased by 49% to RMB 2 billion or USD 295 million from the same period of 2016, primarily due to an increase in sales and marketing-related activities. Sales and marketing expenses for the second quarter of 2017 increased 6% from the previous quarter. Sales and marketing expenses for the second quarter of 2017 accounted for 31% of the net revenue. Excluding share-based compensation charges, non-GAAP sales and marketing expenses for the second quarter of 2017 accounted for 30% of the net revenue, which increased from 29% for the same period of 2016 and remained consistent with the previous quarter.

General and -- G&A expenses for the second quarter of 2017 increased by 19% to RMB 608 million or USD 90 million from the same period of 2016, primarily due to an increase in G&A personnel-related expenses and consulting expenses. G&A expenses for the second quarter of 2017 decreased 5% from the previous quarter. G&A expenses for the second quarter of 2017 accounted for 9% of the net revenue. Excluding share-based compensation charges, non-GAAP G&A expenses accounted for 7% of the net revenue, which decreased from 8% for the same period of 2016 and remained consistent with the previous quarter.

Income from operations for the second quarter of 2017 was RMB 645 million or USD 95 million compared to loss of RMB 396 million for the same period of 2016 and income of RMB 414 million for the previous quarter. Excluding share-based compensation charges, non-GAAP income from



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operations was RMB 1.2 billion or USD 173 million compared to RMB 182 million for the same period of 2016 and RMB 936 million for the previous quarter.

Operating margin was 10% for the second quarter of 2017 compared to negative 9% for the same period of 2016 and 7% for the previous quarter. Excluding share-based compensation charges, non-GAAP operating margin was 18% compared to 4% for the same period of last year and 15% for the previous quarter.

Income tax expenses for the second quarter of 2017 were RMB 529 million or USD 78 million compared to RMB 53 million for the same period of 2016 and RMB 148 million for the previous quarter. The change in group's effective tax rate is primarily due to the change in profitability in the subsidiaries with different tax rates and certain non-tax-deductible losses, including share-based compensation charges.

Net income attributable to Ctrip's shareholders for the second quarter of 2017 were RMB 327 million or USD 48 million compared to net loss of RMB 521 million for the same period of last year and net income of RMB 82 million for the previous quarter, primarily due to the net gain recognized from a number of investing activities.

Diluted earnings per ADS were RMB 0.59 or USD 0.09 for the second quarter of 2017. Excluding share-based compensation charges, non-GAAP diluted earnings per ADS were RMB 1.49 or USD 0.22 for the second quarter of 2017.

With that, operator, we are opening the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Binnie Wong from Merrill Lynch.

Wai Yan Wong - BofA Merrill Lynch, Research Division - Research Analyst

Congrats on the strong quarter with top line and margins coming above expectation. James highlighted in the opening remarks that on Ctrip's long-term strategy in international market and lower-tier cities expansion. Can you provide us more update on the progress and your long-term vision on this front? And also, I would like to ask management about the potential impact from the cross-selling under the recent new requirements by CAAC is contribution and margin profile and also whether has reflected in our 3Q revenue guidance.

Jane Jie Sun - Ctrip.com International, Ltd. - CEO and Director

Thanks, Binnie. James will take the first question. Cindy will take the second.

Jianzhang Liang - Ctrip.com International, Ltd. - Co-Founder and Executive Chairman

Yes, I think we've made great progress in the international expansion. Our integration with Skyscanner have been executing very well, and it's already bearing some fruit. For example, in the direct booking feature we built for -- with Skyscanner, our direct booking question on the Skyscanner website has been received very well at very high conversion rates and a better customer experience. Also on the hotel front, we've expanded our hotel supply network in Asia, and we are generating higher than -- much higher growth than the average -- the market growth. So I think, overall, our international expansion has been well executed according to our plan. Thank you.



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Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

And regarding the new CAAC guideline, in the short term, especially the second half of this year, it will have a negative impact on the revenues for our air ticketing business, and the impact on the following quarter will be reflected in our quarterly guidance, including Q3. However, cross-selling products are designed to facilitate one-stop shopping experience and meet customers' travel demand, many customers will still purchase those products even under an opt-in model. And furthermore, in the second quarter, international air ticket, which will be much less impacted by the new CAAC guideline, contributed close to 40% of Ctrip's total air ticket revenue and has already become a key growth driver, thanks to the heavy investment we made in the last few years by building the best international air ticket platform, not only just for the China market but also is now becoming very competitive in the international market. In the long term, as long as Ctrip continues to provide the best-in-class products and services in the air distribution industry, we create value for both our customers and suppliers. Therefore, Ctrip shall be fairly rewarded for the products and services we offered. And service charge has already become an industry practice in rest of the world. Even in China, many Internet companies, for example, the online video companies, have already started to charge membership fees for the programs that customers subscribe to. In summary, although there will be some short-term headwinds that we are facing, Ctrip will continue to invest and provide superior product and service, which creates tremendous value for our customers and suppliers. Therefore, we are very confident to achieve our original 2020 growth target. And given the largest scale Ctrip achieved and continuous improvement in the operational efficiency in terms of earning ability, Ctrip is also very confident to bring our non-GAAP operating margin back to the 20% to 30% level in the next 1 to 2 years.

Operator

Our next question coming from Alvin Jiang from Deutsche Bank.

Alvin Jiang - *Deutsche Bank AG, Research Division - Research Analyst*

Could you provide us more color on your revenue guidance for next quarter based on different business lines? And is there any color on the margin outlook?

Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

Sure. For each business line items, accommodation reservation revenues will grow at around 25% to 30% in the Q3, and transportation ticketing revenue will grow 40% to 45%. Packaged tour business will grow about 25% to 30%, and corporate travel business will grow 15% to 25%. And our total net revenue will grow at about 35% to 40%. Regarding the earnings ability, our non-GAAP operating profit, we estimated we will generate about RMB 1.5 billion to RMB 1.6 billion non-GAAP operating profit in the next quarter.

Operator

Next question coming from Alicia Yap from Citigroup.

Alicia Yap - *Citigroup Inc, Research Division - MD and Head of Pan-Asia Internet Research*

I actually have questions on your lower-tier offline penetration progress. Are these 400 stores that you opened recently, is it under the Ctrip and Qunar branded store? Or is this a Bestone store? And I think you mentioned about RMB 2 million store revenue. Can you clarify? I might have missed it. Is this revenue coming out from a single store? And then following that related to this is that, as the customer walk into the store, are we helping them to make reservation just like the traditional agents? Or do we have the intention to help them to download the mobile app so that we also aim to grow our app penetration into the lower-tier cities? And as we continue to grow this offline store, what would be the margin profile look like, especially on the gross margin front?



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Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Thanks, Alicia. First of all, the 400 stores we have already established, these are representing Ctrip and Qunar's offline stores. Traditionally, Qunar and the Ctrip brand was only presented on the online platform. But now, we are quite aggressive in penetrating into the lower-tier cities. So, so far, the feedback on Qunar brand and the Ctrip brand has been very positive, and the revenue per store also stands out at RMB 2 million per store, which is significant, considering we only opened the store for a few months. In the overall offline stores, Bestone already have about 5,500 stores. So going forward, by the end of the year, we will aggressively grow that number into 6,500. And these stores are on franchise model. So hopefully, within one year, they will be already in a breakeven stage. So, so far, I think that our movement, not only on the online platform but also penetrating into the lower-tier cities through offline platform, and the feedback is very positive.

Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

And, Alicia, regarding your question about the RMB 2 million, it's just the GMVs. And since it's a franchise model, we don't take any inventory risk. So in the accounting, we only recognize the net commissions that we earned for the transaction. So it won't have impact on our gross margin.

Operator

Next question coming from Natalie Wu from CICC.

Yue Wu - *China International Capital Corporation Limited, Research Division - Analyst*

And congratulations on the result quarter. For this quarter, your gross profit margin actually increased quite steadily, which is quite impressive. Just curious, how much is contributed by those AI robots replacement of customer service employees and how much by Skyscanner contribution? And what's the change going forward? And about Skyscanner, can I get an update about the contribution from Skyscanner this quarter? Is it mainly recognized on the transportation revenue? And what do you expect the contribution going forward?

Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

Yes, regarding the gross margin, there's a couple of reasons this year, our gross margin increased quite significantly compared with last year. First reason is our Baby Tiger program, the small business unit. They are contributing much more revenues than last year. And in terms of the gross margin, those business units comparatively have higher margins than our hotel and air ticket business. And the second reason is because of Skyscanner. They don't -- because they are not a search model, they don't have the cost associated with each transaction, so they have a very high gross margin. And last and most important reason is, even for the air ticket and hotel business, we continuously improve our operational efficiency. For example, we introduced a lot of new technology, including AI-assisted transport, now to handle more than 40% of our booking inquiries, significantly improved our operational efficiency and, at the same time, improved our user satisfaction rate. And regarding Skyscanner, Skyscanner contribute mid-to high single digits of our total revenue. And we believe Skyscanner will continue to have a very healthy growth momentum. And overall, their growth rate is comparable with Ctrip's total growth percentage.

Yue Wu - *China International Capital Corporation Limited, Research Division - Analyst*

Great. Just to clarify, do you mean that the gross profit margin improvement channel will be continued in the following quarters?

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

I think the majority, for example, the Skyscanner impact has already reflected in the last 2 quarters. So, of course, internally, we will do our best to continue to improve our operational efficiency and slightly improve our gross margin in the next couple of quarters, a few years.

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Operator

Next, we have Kevin Kopelman from Cowen and Company.

Kevin Campbell Kopelman - *Cowen and Company, LLC, Research Division - Director and Senior Research Analyst*

I had a question on the statistic that you gave on lower-tier city room nights. You noted 20 million nights in July. That's an impressive number. Can you give us any more context around that number in terms of both growth and how large that is within the overall Ctrip business and, also, where you see that going as you noted lower-tier being -- lower-tier cities being a key growth driver going forward?

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Yes. So Ctrip has put lots of efforts to aggressively penetrate into the lower-tier cities. First of all, we strengthened our branding power. In the lower-tier cities, we have increased our branding efforts. And so far, it has been very positive in increasing our [DAUs]. Secondly, on the product coverage, we have developed comprehensive products, not only in the hotel but also in air ticket, bus, train, rental car, et cetera. So with that comprehensive products into these cities, customers can use Ctrip services very conveniently. That also helps us to increase our brand as well as our volume. Thirdly, we want to make sure our pricing is very comprehensive, and our open platform enables us to attract the best price on these cities, and that is very suitable for the price-sensitive customers and young users. And thirdly, as we discussed before, we also were very aggressive opening the offline shops. By the end of this year, our target is to open 6,500 stores. And these stores are also going to be in the center of the cities, which will help us to expand Ctrip and Qunar and our brand and product exposure. With all these efforts, we are confident that Ctrip's brand as a group will be able to attract the customers who start to travel to the other cities and even abroad.

Operator

(Operator Instructions) And our next question coming from Wendy Huang from Macquarie.

Wendy Huang - *Macquarie Research - Head of Asian Internet and Media*

Your international business actually -- is growing very nicely. Can you provide the retail number for the international ticketing growth, especially given that the market growth was actually only 2% this quarter? So how should we actually expect your market share in the international to grow going forward? And also housekeeping regarding the 600 offline stores, how many people actually will you put in those 600 self-operated store? And also, what's the CapEx for that?

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Yes, international expansion is our main focus. In the past and going forward, we will continuously invest in our technology. So multi-destination tickets is our focus, and we make it seamless for our customers when they use our services. And also, our 24 hours global service is also very helpful. Whenever our customer travels around the world, Ctrip team is behind them to support them. That gives them lots of confidence and peace of mind when they travel abroad. So going forward, international travel still is our main focus to lead the new wave of the growth. Regarding your question on the lower-tier offline stores, it's a franchise model. So the shops where owners will pay a franchise fee, and we give them guidance as to the quality and we provide the product linkage to them. So they have to access Ctrip's brand, quality guidance as well as the product coverage. We do not incur labor cost. The labor cost is on the shop owners. So for us, it's a very light model, but it's a win-win model because Ctrip is strong in its technology, branding, service and product coverage, and we make it accessible for the shop owners. And the shop owners, their strength is the knowledge in a local market. So by combining our strength on both side, we're able to penetrate in the lower-tier cities very well.



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Wendy Huang - *Macquarie Research - Head of Asian Internet and Media*

Sorry, Jane, but I thought the franchise model you mentioned were mainly referring to the 6,000 or 5,500 Bestone stores, not really for the 400 -- the Ctrip and Qunar stores. When you say you target to open another 200 more in the pipeline, is it referring to the franchising store as well?

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Yes. All 3 brands are franchise models.

Operator

Our next question coming from Justin Patterson from Raymond James.

Justin Tyler Patterson - *Raymond James & Associates, Inc., Research Division - Internet Analyst*

I wanted to revisit the operating margin guidance, which looks like it's coming in at around 20%. That looks like one of the more modest sequential upticks we've seen on operating margin for some time. So just curious if there's any incremental investment you're making, if there's a change in the competitive environment that's reflecting cross-selling a little bit, just a partial quarter there from that impact. Just what's behind the operating margin guidance?

Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

Yes. Ctrip -- although we are quite strong in the China market, but compared with the total market share, we are still in the very early stage, even for the China domestic market. So the first priority for Ctrip as a group is to continuously gaining market share. For example, in the first half of this year, we put a lot of investment branding campaigns in the second, third tier cities, and also, we have planned to open more markets outside of China. So the strategy, current strategy for Ctrip group is to continuously gaining more market share in China market, in the international markets but, at the same time, maintain a very healthy margin.

Operator

Next question coming from Tian Hou from T.H. Capital.

Tianxiao Hou - *T.H. Capital, LLC - Founder, CEO, and Senior Analyst*

I have a question relate -- okay. I have a question related to the Marriott Hotel recently announced they formed a partnership with Alibaba's Fliggy to enable the users use Marriott Hotel much more convenient. So what kind of impact could that be to Ctrip? And also a much bigger picture issue. So Ctrip used to say that travel is a low-frequency business, but I figure -- we did some research. I feel like recently, I think that pricing has been changed from a low frequency to relatively higher frequency. So I wonder, what's your data say? What's your corporate analysis? Tell us about it. That's my 2 questions.

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Yes. So for Marriott, the alliance with Alitrip, we have historically developed very solid relationship with all hotel chains, and our partnership has always been very innovative. So our team continuously work with all hotel chains to develop a very strong synergy, including the cooperation on the technology brand, including the branding, co-marketing. So that is the reason why Ctrip in overall market is way ahead of the other players. Secondly, on your question high frequency versus low frequency, yes, Ctrip's platform is -- offers not only the low-frequency items such as air tickets and hotel but also offers comprehensive products. So we included our travel journal, very similar to TripAdvisor's model in it. So when people want



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to go somewhere, they can scan through pictures, read through their travel journals from other travelers. And also, we include bus, train, cars, all these high-frequency products into our platform. And once the customers feels that they can find anything that is associated with travel at our app, then it's a very loyal customer base. So internally, we increased the customer loyalties through offering a comprehensive product to increase stickiness and loyalty from our customers. So increasing the frequency by our customer is one of our focuses when we develop new products.

Operator

Next question coming from John Choi from Daiwa.

Hyungwook Choi - *Daiwa Securities Co. Ltd., Research Division - Head of Hong Kong and China Internet & Regional Head of Small/Mid Cap*
(technical difficulty)

get more color. You said there could be a negative impact on the airline revenue in the second half. Can you give us a bit more color on how you guys are trying to fix the situation? And also, secondly, on the vacation rental contribution, it seems like in the second quarter, there has been a very strong uptick in this business. Can you give us more metric on how important vacation rental is in the accommodation business?

Jianzhang Liang - *Ctrip.com International, Ltd. - Co-Founder and Executive Chairman*

Yes, I think vacation rental is a very promising way of -- alternative way of traveling, will be increasingly popular in China. But, of course, this is still early stage of the development, and we are still making sure the product is -- meets the customer needs in terms of service, in terms of coverage. But Ctrip's customers are very -- from our initial testing, very willing to experiment with these new products. So the opportunity definitely is very, very interesting for us. It will be increasingly a very viable alternative way of travel for our customers.

Xiaofan Wang - *Ctrip.com International, Ltd. - CFO and EVP*

Regarding the impact, negative impact on the revenue for the air ticket business, as I said, cross-selling those product, we always provide or we always recommend the most useful product to facilitate our customers' one-stop shopping experience. Therefore, even under an opt-in model, we believe there -- still a lot of customers will purchase those useful product coupons. And secondly, with the more contribution from our international air ticket, naturally, it will mitigate the negative impact from the new guideline. And also, in the long run -- and also, internally, we are testing different product, new product and different new ways to mitigate the potential impact. But in the long run, we believe as long as we provide the best product, most comprehensive international air ticket services in the air distribution industries we created for both our customers and our suppliers, Ctrip sure has a very reasonable premium -- create -- shall charge a reasonable premium on the services that we offer.

Operator

Next, we have Juan Lin from 86Research.

Juan Lin - *86Research Limited - Research Analyst*

So my question is related to cross-selling. I'm wondering, do you think that with such low commissions and restriction on cross-selling, CAAC will eventually allow OTAs to directly charge service fees from consumers? And also wondering whether there's any potential regulatory risk related to cross-selling for business lines other than air ticket booking.



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Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Yes, I -- we believe that Ctrip needs to be very resilient in order to provide a very good services to the customer in a most efficient manner. So the key for Ctrip's team is continuously improve our IT platform and also services to make sure the service and technology compared to the other players stands out as the best service provider in the market. And with that, we have already seen that the international business has increased to approximately 40%. And going forward, that number will continuously to grow, which is very promising in terms of increasing both volume as well as the revenue. Secondly, with our strong investment into the service and technology, more customers will come to use our platform. So that will be very positive in our business going forward as well. Thirdly, there are many new alternatives our team is exploring. And in the market, we have already seen -- Amazon has a very good Prime membership platform, et cetera. So going forward, we believe service has value and service contributed greatly into China's GDP growth, and service needs to be rewarded. So as long as we offer the best technology product and service to our customer, we should be very well rewarded for what we have invested.

Operator

Next, we have Jed Kelly from Oppenheimer.

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

On the competitive side, Alitrip signed a deal with Marriott, (inaudible) [talked up] some of the room night growth as well, and then Airbnb appears to be putting meaningful resources behind its Chinese expansion. Can you just speak to how the competitive environment is evolving versus 12 months ago and some of the different competitive dynamics between Tier 1 and the lower-tier cities?

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Yes. I think because travel industry is so promising, over the past 18 years, many players come into the market, many come, many withdraw and new generation will come. So our team is very well trained to monitor the market and move aggressively into different segments. If you look at our development throughout the past 18 years, we started with hotel business. And then 2 years later, we added air ticketing business. After 2 years, we added packaged tour and then corporate travel. And now we have Baby Tiger programs covering more than 30 products. So our team is very well trained to be very sensitive into the market and develop product and technology, which will satisfy our customers' needs. And going forward, we'll keep up with this innovative spirit to make sure wherever our customers are, whatever they need, Ctrip is the first mover into the market to give them the product and the services. In terms of the alternative accommodation, I think James is extremely positive in this segment. Do you want to add?

Jianzhang Liang - *Ctrip.com International, Ltd. - Co-Founder and Executive Chairman*

Yes, I think we are very confident of our product coverage and our service and our cross-selling ability as Ctrip or Qunar. The largest hotel platform will be much more likely to win this race, to make Ctrip a much likelier winner in this race compared to even Airbnb, at least in the domestic market.

Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

So yes. Yes, we will continuously work diligently to be very sensitive and quick to market to develop new products and move into these new verticals in the first place.

Operator

Next, we have Ming Xu from UBS.



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Ming Xu - UBS Investment Bank, Research Division - Director and Research Analyst

So I have two questions. Firstly, you mentioned that in July, the room night from lower-tier cities or lower-tier hotels are 20 million. I'm just wondering, firstly is, what's the volume or revenue contribution in the total hotel business? Secondly is, how much of that 20 million is booked through your app, your offline stores and also the Bestone stores, respectively? And secondly, very quickly on the CAAC announcement. So I understand CAAC is a regulator for airlines and airports, but I just want to confirm, does CAAC have direct regulatory power over OTAs? And also, how should we -- when we try to understand the impact on this and that, how is it different from the last time the Consumer Rights Association (sic) [China Consumers' Association] investigation into the cross-selling practice?

Jane Jie Sun - Ctrip.com International, Ltd. - CEO and Director

Yes, so the first question regarding the lower-tier cities innovation, I think, yes, as we discussed, we put tremendous efforts in our branding into the second-tier and third-tier, fourth-tier cities. We also put tremendous efforts to develop comprehensive products, which will serve our customers well in these areas. And third thing is we make sure we have the lowest price for all products that is available on our platform. That is the reason why the growth in the second-tier, third-tier cities have been very significant. In terms of revenue contribution, as we highlighted in the -- our financials, it's close to be a RMB 2 billion revenue. So it's a very significant revenue contribution from hotel business view. And the CAAC regulation, I think we always respect government's guidance, rules and regulations, and we will, again, work very closely to make sure we are in compliance with all the guidance, rules and regulations. And Ctrip team also want to make sure that the product we offer to the customers satisfy their need. So a lot of cross-sell product we're offering is very well welcomed by the customers when they are traveling within China or outside of China. So we will work very closely to listen to the customers to make sure our product satisfy their need and also work very closely with all the government agencies to make sure we are in compliance with their guidance and their requirement. But, again, I think as long as we have the best technology and services, we will add value through our platform.

Ming Xu - UBS Investment Bank, Research Division - Director and Research Analyst

A very quick follow-up, Jane. So I want to understand. So within the hotel business itself, so in terms of revenue and volume contribution from these lower-tier cities, so what's the contribution now?

Jane Jie Sun - Ctrip.com International, Ltd. - CEO and Director

Yes, so we have -- in China hotel business, we have 2 brands. One is Ctrip brand, one is the Qunar brand. Ctrip brand is more positioned toward the mid-to-high end of the market. So still, first-tier, second-tier cities contribute a significant portion of our total revenues and almost 100% of our profit. But Qunar brand, we have -- this year, we made the investment, increased our marketing budgeting to use the Qunar brand to penetrate into the lower-tier cities, which has been very successful. And the lower-tier cities contribution to the total (inaudible) improved significantly.

Operator

Thank you, ladies and gentlemen. Miss Qi, back to you.

Michelle Qi

Thanks for everyone who joined us today. You can find the transcript and webcast of today's call on ir.ctrip.com. We look forward to speaking with you on our third quarter 2017 earnings call. Thank you, and have a good day.

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Jane Jie Sun - *Ctrip.com International, Ltd. - CEO and Director*

Thank you very much. See you next quarter.

Operator

Thank you. Ladies and gentlemen, you may now disconnect.

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