
ETSY, INC. (ETSY – LONG; TARGET: \$15.39)

JAMES CAFFREY, ANDREW LEE, NATHAN LIN, BRIAN MURRAY

MII POINT72 STOCK PITCH COMPETITION

February 21, 2017



Etsy

Agenda

MII Point72 Stock Competition (ETSY - L)

- I. Thesis Points**
- II. Industry Analysis**
- III. Business Model & Value Proposition**
- IV. Data Analytics**
- V. Valuation/Investment Recommendation**

Thesis Points

1. Etsy will continue to invest in and roll out various **Seller Services** which will add meaningfully to its top-line and could trickle down to Etsy's bottom line sooner than investors anticipate.
2. The **Etsy Studio initiative will help Etsy broaden its user and seller base** and will allow the company to better serve the \$44 billion U.S. crafts supply market compared to traditional retailers.
3. **Etsy's marketplace business model lacks the overhead and inventory costs of its traditional retail competitors** which should aid Etsy in its pursuit of profitability and could eventually contribute to industry-leading margins.
4. **Etsy maintains a wide network of buyers and sellers with concentrated buying in affluent cities and suburban areas.** The typical cart totals per user confirm Etsy's value proposition to the consumer of delivering middle-price, vintage goods to consumers.
5. **Sellers truly respect Etsy's commitment to sustainability and community,** will remain loyal to Etsy and its platform and will be key players in helping Etsy improve its marketplace and keep the firm one step ahead of Amazon and eBay.

- Etsy inhabits the arts, crafts and accessory niche of the ecommerce industry.
- Primary Competitors: Amazon, Ebay, “Brick and Click Retailers,” Folksy.com, Online Wholesalers
- Large number of suppliers with dominance from a small number of companies.
- Low threat from substitutes
- Low startup costs but high costs to scale
- **Focus on fostering inspiring creativity and personality among suppliers rather than mass production for reduced prices.**

Etsy's Business Model: It's Not a Fad

- Etsy operates a marketplace where people all over the world connect, both online and offline, to make, sell, and buy unique goods.

Reimagining Commerce

- Etsy generates revenue by charging a \$0.20 fee on each product listing and a 3.5% transaction fee for completed product sales on its platform and selling a variety of services to its sellers.
- Etsy's aim is to be a mindful, humane, transparent business that supports global craftsmanship and is build for the long-term.
- Etsy's seller-aligned business model is based on partnering with entrepreneurs and sharing success.
- The more Etsy invests in and improves its platform, the easier it is for Etsy sellers to pursue their craft and grow their businesses and for Etsy buyers to find unique goods.
- By expanding its active user base, Etsy is able to grow its revenue from increased listings and sales as well as cross-selling its convenient services to its sellers. Ease of doing business on Etsy attracts more users.
- Etsy is uniquely positioning itself to profit from the long-term transition to personalized DIY e-commerce by investing in its mobile, search and machine learning capabilities.

Adding to Etsy's Value Proposition I: Moving Beyond First-Mover

Etsy's aggressive investment spending is beginning to trickle down to the bottom-line in 2017

Expanding Seller Services

- Seller Services (**55% of Q3 revenue**) helps Etsy attract sellers, support sellers beyond its core marketplace, reinforce seller loyalty, enhance Etsy's brand and ecosystem and further monetize its platform through cross-selling and closer seller integration.
- Seller Services revenue includes the fees sellers pay Etsy for services such as Promoted Listings, prominent advertisement placements on in-site search results, Direct Checkout (Paypal integration), payment processing, and Shipping Labels.
- One of Etsy's relatively new seller services is Pattern which allows sellers to quickly create their own custom websites to highlight their own brands and leverage the hard work they've already put into their Etsy shops. With Pattern, Etsy will now compete more with Shopify's lucrative website services platform.

Adding to Etsy's Value Proposition II: Moving Beyond First-Mover



Etsy's aggressive investment spending is beginning to trickle down to the bottom-line in 2017

Improving Search

- The search function on Etsy.com is a crucial part of any user's experience simply because buyers come to Etsy for unique items they can't find anywhere else.
- In order to help buyers discover exactly what they want among Etsy's 40 million unique listings, Etsy recently **acquired Blackbird Technologies, Inc.**, a developer of proprietary machine learning technology that delivers superior search relevance and recommendations.
- Blackbird's novel technology combines images and text using advanced Deep Learning Artificial Intelligence techniques to power a range of search capabilities, including personalized search, ranking, spelling correction and predictive typeahead, to deliver a personalized shopping experience.

Brand New Initiative: **Etsy Studio**

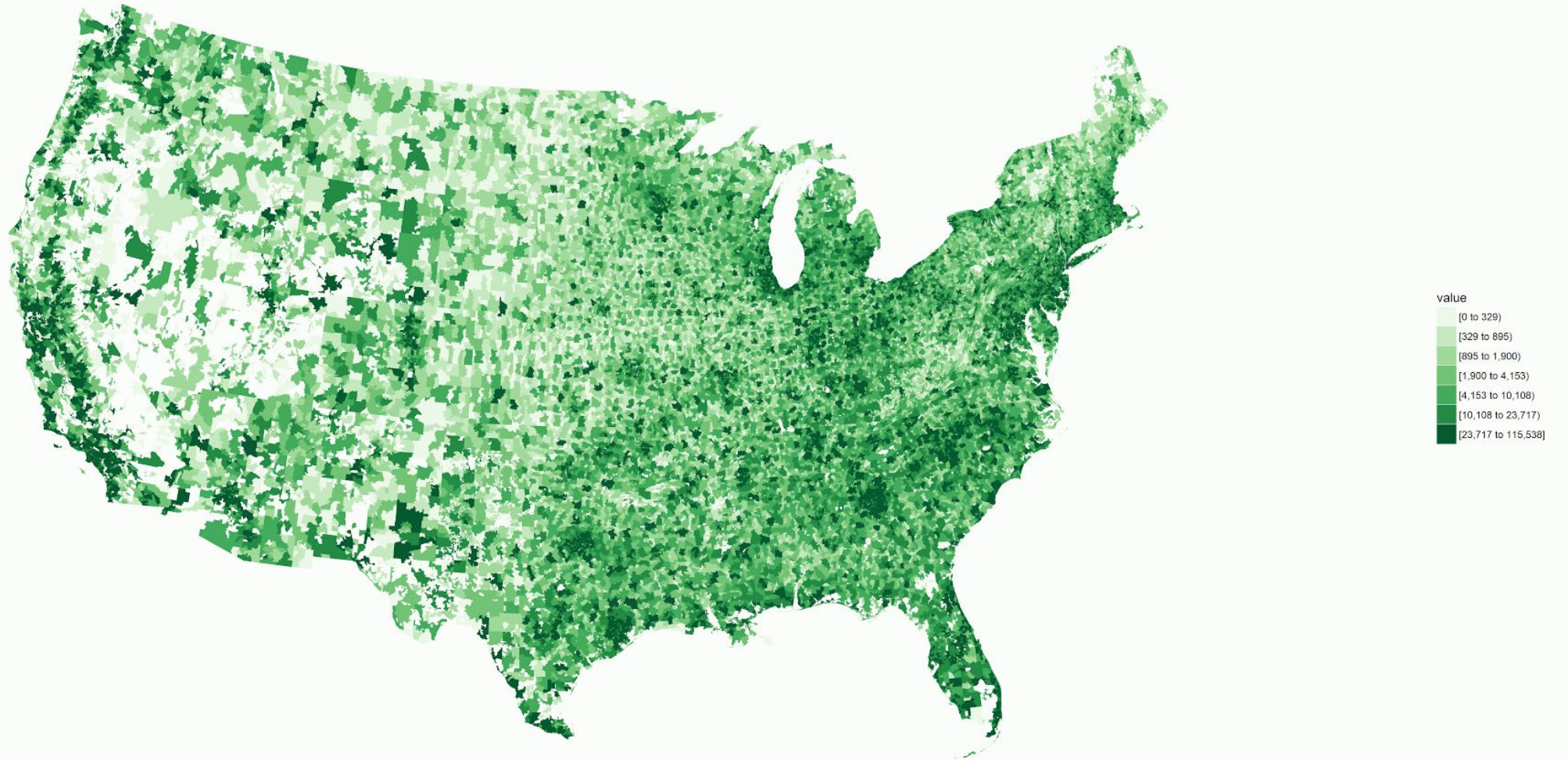
Bringing Joy to Craft Supplies

- Etsy Studio will be a global marketplace dedicated to craft supplies, a **\$44 billion opportunity** in the U.S. alone. Launch in April 2017.
- Initiated after Etsy heard about the unique challenges of selling and shopping for craft supplies from its sellers and buyers.
- The DIY e-commerce site is already onboarding sellers to the marketplace and plans to launch with **at least 8 million products**, including things like paintbrushes and mosaic tiles.
- Additional features of Studio will include extended search filters, video tutorials, inventory management, order tracking, and shop analytics to assist Etsy's sellers in growing their business. When sellers grow, so does Etsy.
- Etsy Studio will solidify Etsy's strong leadership in the artisan segment of e-commerce, broaden the number of potential Etsy buyers and sellers, bolster Etsy's ecosystem, and accelerate user growth on its platform.

DATA ANALYSIS

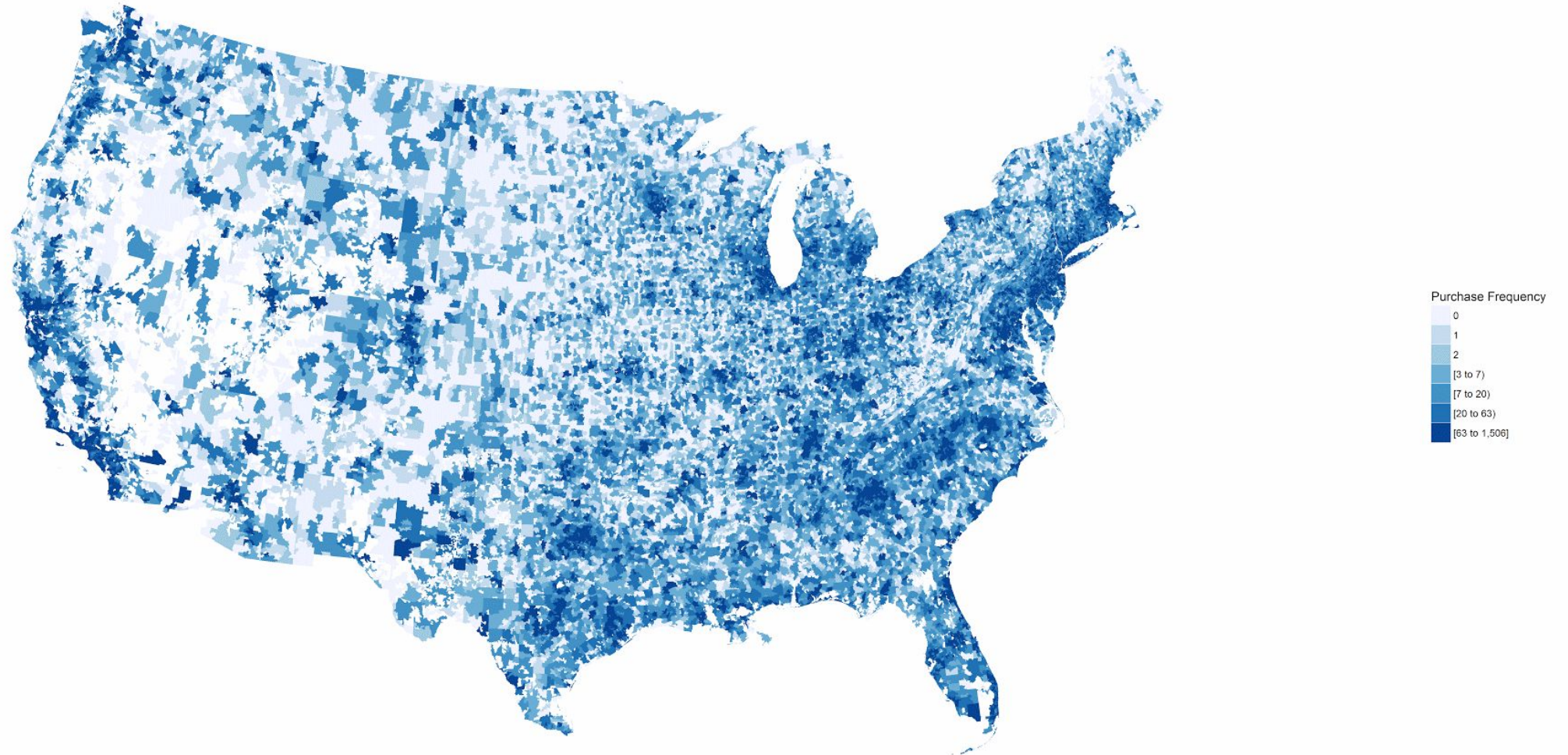
US Population Density (US Census Bureau, 2012)

US Population Density
Data for Zip Code Tabulated Areas in 2012



Etsy's Reach in the US - Etsy Purchase Frequency (Sample, 2013-2016)

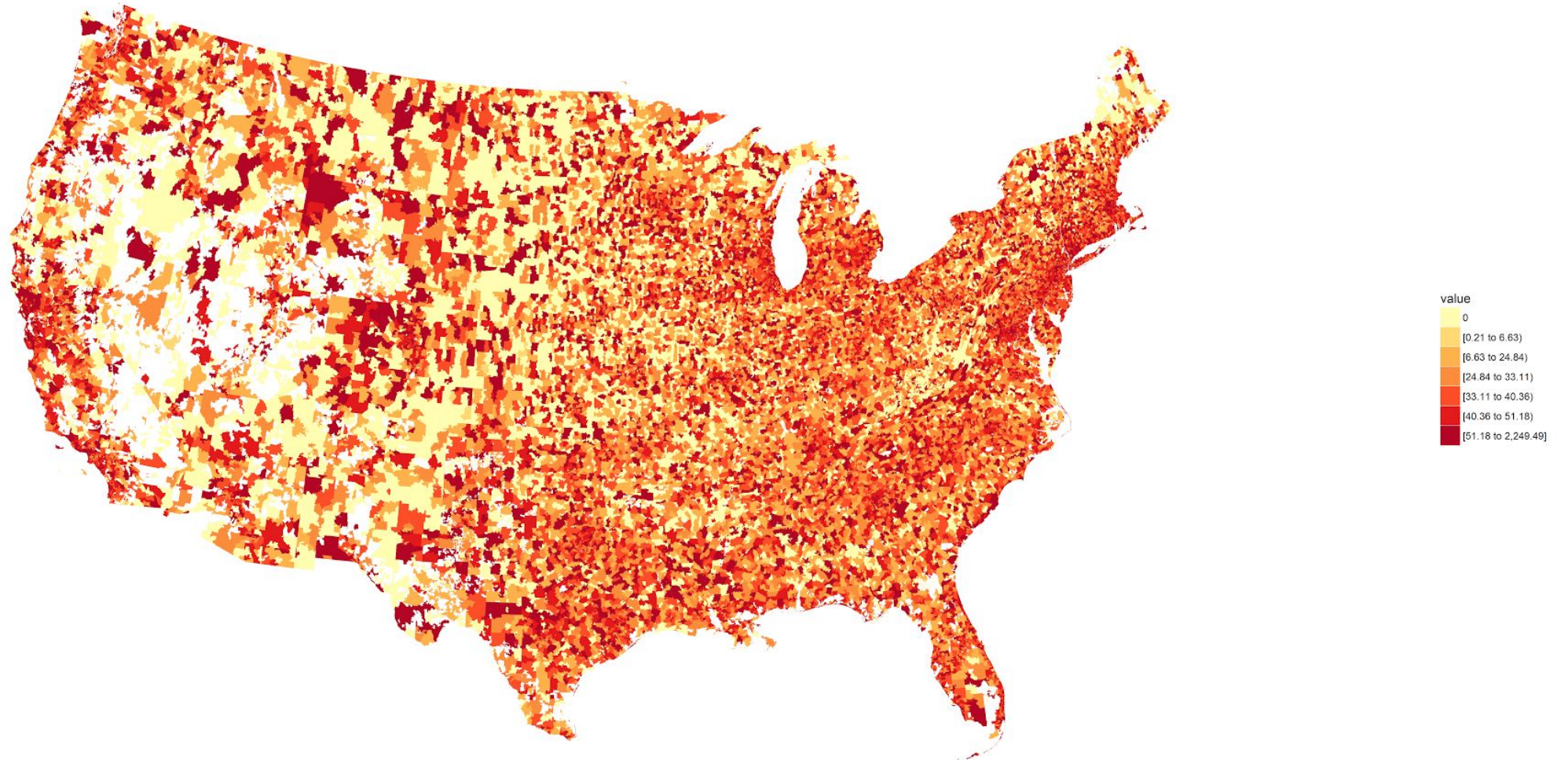
ETSY Purchases by Zip Code Frequency
Transaction data from January 2013 to October 2016



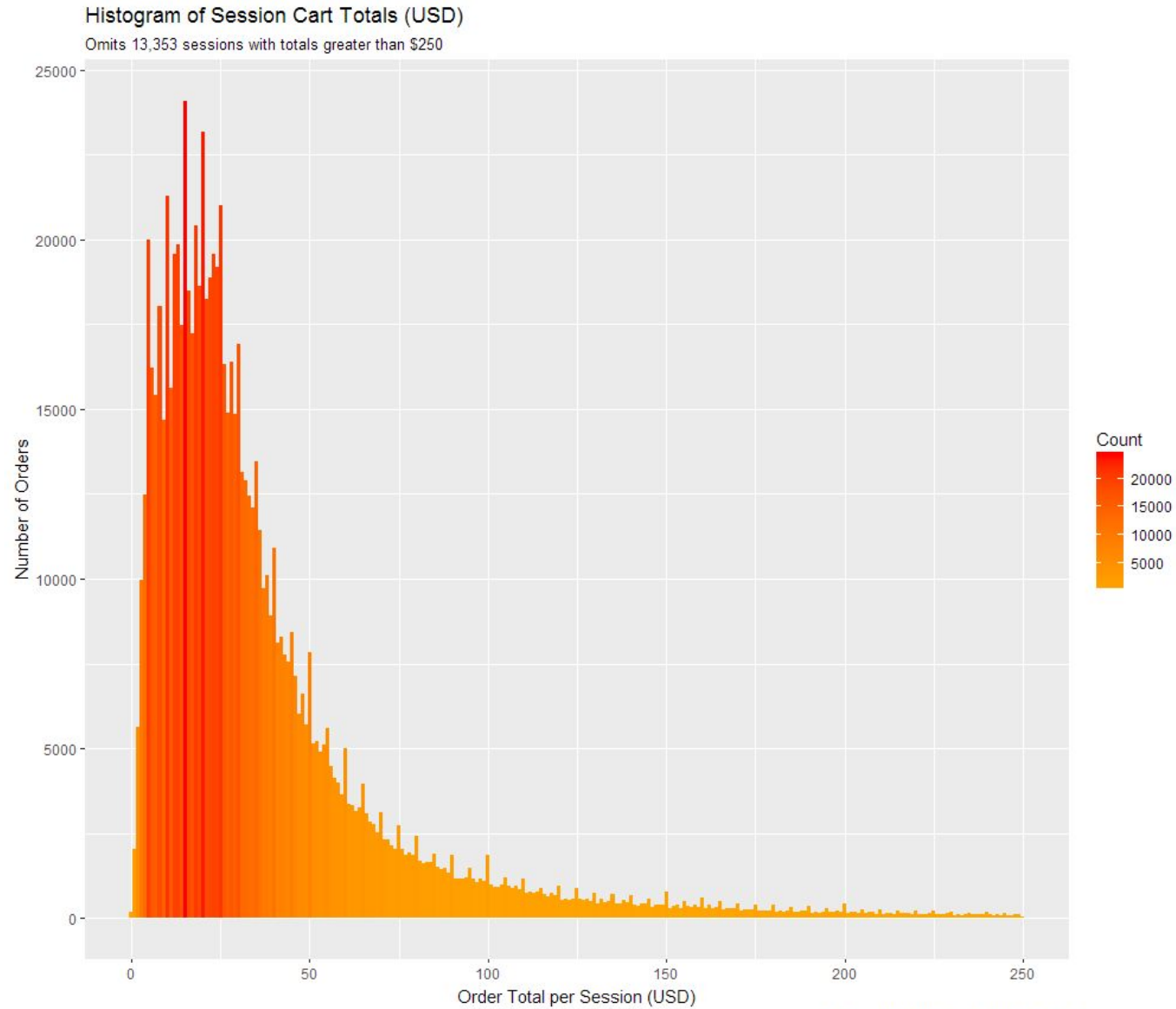
Concentrated Purchasing - Average Purchase Size by Zip (Sample, 2013-2016)

ETSY Average Purchase by Zip Code

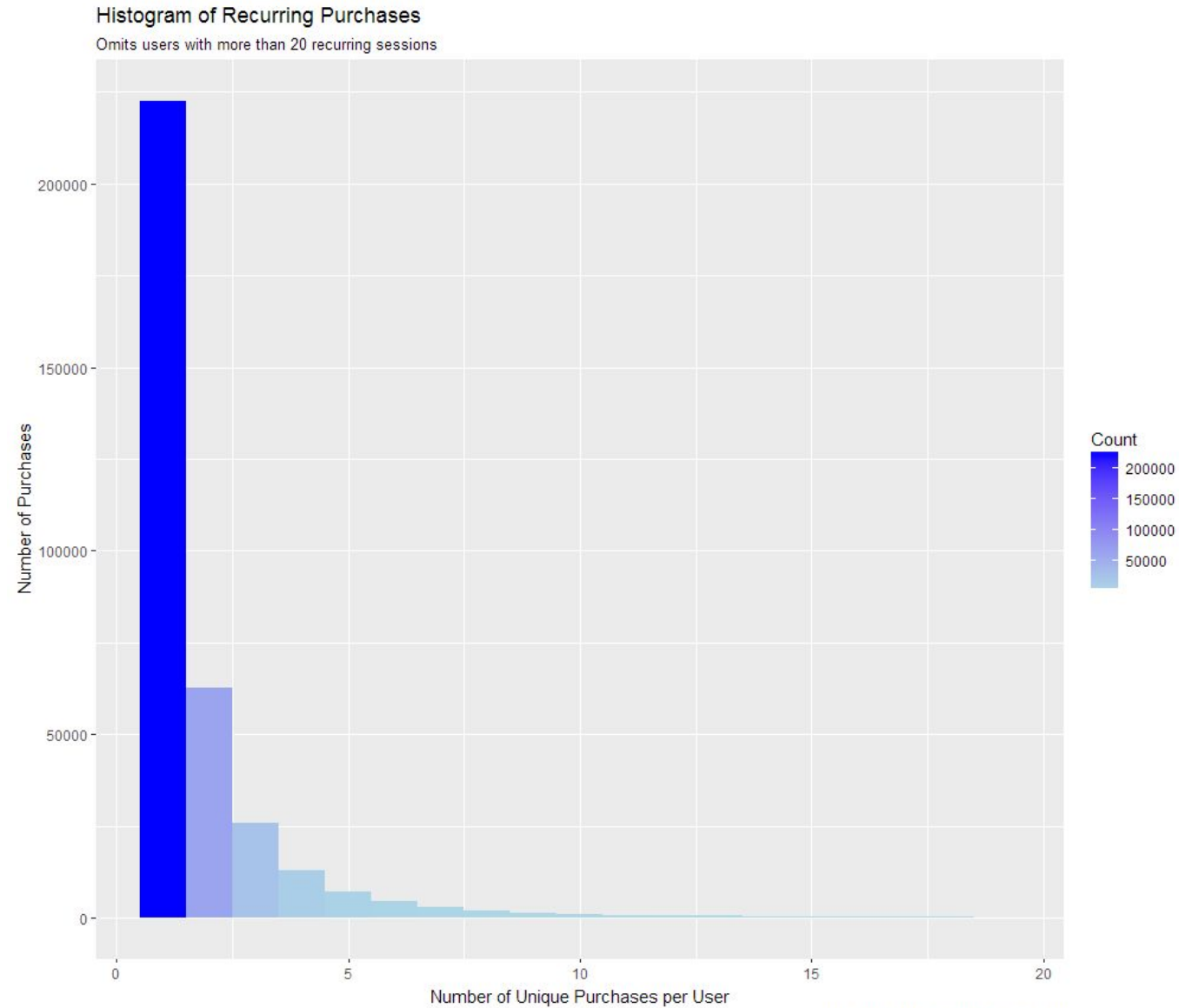
Transaction data in U.S. Dollars from January 2013 to October 2016



Average Order Totals (USD) by Frequency (Sample, 2013-2016)



Recurring User Frequency and Dataset Shortcomings (Sample, 2013-2016)



Comparable Analysis Confirms Undervaluation

Since Etsy doesn't have positive FCF, Comparables Analysis is the most appropriate method of valuation.

Results of Comparables Analysis

- Used similar e-commerce and e-retailers including \$EBAY, \$AMZN, \$SHOP, and \$BABA and the median EV/Sales multiple to quantify the appropriate value of Etsy's business.
 - Yields a price target of **\$15.39 per share**.
 - Therefore, at the current price of roughly \$13.00/share, our quantitative analysis projects at least **~18% upside** by buying \$ETSY.
 - A near-term catalyst for the realization of Etsy's appropriate valuation is likely to come on Feb 28th when Etsy releases its Q4 2016 earnings.
 - When Q3 '16 earnings were announced, Etsy raised its '16 guidance to at least 30% revenue growth, GMS growth of at least 17% and Adj. EBITDA Margin of at least 14%.

1. **Etsy's growth potential can be limited due to possible competitions with other e-commerce giants, such as Amazon and Ebay.**
 - a. Specialization in craft goods and vintage items; Etsy's craft goods selection is 100 times that of Amazon
 - b. Cheaper selling fees than Ebay
2. **Etsy's operational model is ineffective, as shown by its negative earnings.**
 - a. Large cash outflow due to its purchase of PPE and marketable securities (PPE: 9 million to 34 million, Marketable Securities: 18 million to 108 million)
 - b. Operational margin rose from -5% to +5%; still negative earnings due to tax expenses. Also, dramatic drop in net loss in 2016 from 49 million to 8 million
 - c. Rise of current ratio from 4.4 to 4.5 despite significant cash outflow

Thesis Points

1. Etsy will continue to invest in and roll out various **Seller Services** which will add meaningfully to its top-line and could trickle down to Etsy's bottom line sooner than investors anticipate.
2. The **Etsy Studio initiative will help Etsy broaden its user and seller base** and will allow the company to better serve the \$44 billion U.S. crafts supply market compared to traditional retailers.
3. **Etsy's marketplace business model lacks the overhead and inventory costs of its traditional retail competitors** which should aid Etsy in its pursuit of profitability and could eventually contribute to industry-leading margins.
4. **Etsy maintains a wide network of buyers and sellers with concentrated buying in affluent cities and suburban areas.** The typical cart totals per user confirm Etsy's value proposition to the consumer of delivering middle-price, vintage goods to consumers.
5. **Sellers truly respect Etsy's commitment to sustainability and community,** will remain loyal to Etsy and its platform and will be key players in helping Etsy improve its marketplace and keep the firm one step ahead of Amazon and eBay.

QUESTIONS

APPENDICES

Company Comparables Analysis

Company Name	Ticker	Share Price	Market Cap	Enterprise Value	TTM	EV/Revenue	
						FY1	FY2
eBay Inc.	EBAY	\$34.01	\$36,557.2	\$38,368.2	4.3x	4.1x	3.9x
Amazon.com, Inc.	AMZN	840.45	399,100.7	393,532.7	2.9x	2.4x	2.0x
Alibaba Group Holding Limited	BABA	101.83	253,975.0	252,730.1	12.2x	11.1x	8.5x
Target Corporation	TGT	65.64	36,875.3	48,470.3	0.7x	0.7x	0.7x
Shopify Inc.	SHOP	60.43	5,043.6	4,643.3	11.9x	12.2x	8.2x
Low			\$5,043.6	\$4,643.3	0.7x	0.7x	0.7x
Median			36,875.3	48,470.3	4.3x	4.1x	3.9x
Mean			146,310.4	147,548.9	6.4x	6.1x	4.7x
High			\$399,100.7	\$393,532.7	12.2x	12.2x	8.5x
Etsy, Inc.	ETSY	13.20	1,486.2	1,227.7	3.6x	3.4x	2.8x