

## BCP Research: Mercado Libre (MELI -/-/-) 1Q20 Earnings- Improved, But (More Than) Reflected in Price

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*Summary: LatAm e-commerce company, MELI, reported improved 1Q20 earnings. Revenue increased by 38% y/y in USD terms (71% in LC), driven primarily by Argentina and Mexico from strong marketplace and fintech revenue growth. Although Brazil revenues did increase by 31% y/y in USD terms (55% in LC), there was a deceleration vs previous quarters primarily in marketplace revenue. EBITDA improved on a sequential basis, yet it remained negative as the marketing expense cuts were offset by bad debt expenses in part ASC adoption. On an LTM FCF burn reached US\$213 mm, as the favorable WK dynamics are offset by negative EBITDA and higher capex. MELI's liquidity remains solid with strong cash position and large short-term UST holdings, which together exceed total debt. MELI's target of developing its logistic network remains unchanged per covid-19, as the issuer mentioning to be focusing on being able to absorb the additional volumes. Operations are functioning normally with no significant disruptions, as well as mentioning strong activity rebound in LatAm through April 2020, with the exception of Brazil.*

*On a consolidated basis, USD revenue growth decelerated to 38% vs 58% last quarter, missing our revenue estimate by 9%. This was due to LC depreciation in the three major countries, as well as lower revenue growth rates in Brazil. At the current FX, our estimated revenue growth rate decreases to 25%, vs our 50% for the prior quarter. MELI's TEV/sales multiple has increased to 14.8x, which is well above the historical 9.5x. Under our new 25% growth rate estimate, we see MELI's TEV/Revenue multiple expanding well above its historical average while revenue growth is decelerating. As such, we remain neutral on MELI 28s on an outright basis and see the convert as a deep in-the-money option.*

	Amt Out (US\$ MM)	Mid Price	Mid YTW	IVOL	Cheapness (par)	Delta (par)	Conv. Price	MELI Price (USD)
MELI 2% 08/15/2028	880	198.13	(6.75%)	30.11%	5.00%	96.21%	443.40	\$834.17

\* Source: Equity information sourced from Bloomberg. Convertible pricing as of May 26<sup>th</sup> 2020.

### 1Q20 Earnings Highlights:

- 1Q20 Revenue increased by 38% y/y to US\$652 mm, managing to beat the BBG consensus by 4%
  - Active users were 31% higher y/y at 43 million, with a 45% y/y increase in items shipped through MELI's network
  - On FX neutral basis, revenue grew by 71% y/y driven by Argentina and Mexico, partially offset by a slowdown in Brazil
  - Brazil sales were 31% higher y/y at US\$397 mm, mainly from fintech non-marketplace revenue and lower shipping subsidies
  - Argentina sales were 42% higher y/y at US\$133 mm (123% growth y/y in LC), due to strong marketplace and non-marketplace growth
- EBITDA was negative US\$8 mm, yet improving vs last quarter and beating the estimated BBG consensus as well
  - EBITDA remained negative as the lower marketing expenses were offset by higher bad-debt provisioning
  - Direct costs continued to outpace revenue in all three major countries
- FCF burn was US\$180 mm, driven by higher capex and WK expansion from lower A/P and accrued expenses

- Net loan portfolio was 21% lower q/q at US\$148 mm, primarily from lower loans to online merchants as the issuer tightened origination
- Total debt was US\$1,125 mm, with cash decreasing to US\$1,072 mm
  - Total debt incl. US\$192 mm lease liabilities, we note MELI has US\$1.8 bn in sovereign debt securities, mostly UST
  - As such, total cash stood at US\$2.9 bn
- Covid-19:
  - MELI continues to focus capex on developing its own logistics delivery network, focusing on covering the increased volume demand
  - The managed logistics and warehouse operations are operating normally, with no significant disruptions
  - The issuer mentioned that most business impact was felt during the initial lockdown weeks, yet rebounding through April 2020
    - April 2020 revenue growth rates were higher pre-covid in most countries, with the exception of Brazil
  - Essential and packaged food items have shown strong volume growth, with non-essential high-price declining the most
- [Link to results here](#)

#### **EV Multiples & Growth Rates:**

- MELI's current market cap is US\$41.5 bn, with the estimated 2020 revenue at US\$2.8 bn
  - An implied EV/sales trading multiple of 14.8x – well above the historical EV/sales multiple
- Brazil accounts for about 2/3 of sales, with Argentina accounting for 1/4 of sales, both showing revenue growth in both LC and USD despite the macro headwinds

Recent revenue growth rates in USD and Local Currency (“LC”) are detailed in the table below:

MERCADO LIBRE	1Q20	4Q19	3Q19	2Q19	1Q19	4Q18	3Q18	2Q18	1Q18
<b>Revenue (US\$ MM)</b>									
Brazil	397	428	390	341	302	265	221	196	184
Argentina	133	132	116	114	94	91	84	100	102
Mexico	95	85	71	64	55	46	29	18	17
<b>Consolidated</b>	<b>652</b>	<b>674</b>	<b>603</b>	<b>545</b>	<b>474</b>	<b>428</b>	<b>355</b>	<b>335</b>	<b>321</b>
<b>Y/Y Revenue Growth Rates (US\$)</b>									
Brazil	31%	61%	77%	74%	64%	34%	25%	25%	15%
Argentina	42%	46%	39%	14%	(8%)	(16%)	(8%)	14%	43%
Mexico	74%	86%	146%	267%	220%	157%	152%	62%	51%
<b>Consolidated</b>	<b>38%</b>	<b>58%</b>	<b>70%</b>	<b>63%</b>	<b>48%</b>	<b>20%</b>	<b>17%</b>	<b>18%</b>	<b>19%</b>
<b>Y/Y Revenue Growth Rates (LC\$)</b>									
Brazil	55%	74%	77%	89%	91%	58%	56%	40%	19%
Argentina	123%	133%	119%	115%	83%	77%	68%	68%	80%
Mexico	81%	80%	153%	261%	227%	170%	168%	71%	39%
<b>Consolidated</b>	<b>71%</b>	<b>84%</b>	<b>91%</b>	<b>102%</b>	<b>93%</b>	<b>62%</b>	<b>58%</b>	<b>44%</b>	<b>30%</b>

### Convertible Risk / Reward:

- MELI's EBITDA remains negative due to free shipping initiatives as the company builds market share and a defendable position against future market entrants
- LTM FCF burn is US\$213 mm, as the favorable WK dynamics are offset by negative EBITDA and higher capex
- The 2020 BBG consensus revenue estimate has been reduced to US\$2.8 bn, an implied 22% y/y growth vs 2019
- Assuming the current ARS and BRL FX, with the current LC revenue growth rates:
  - Our estimated revenue growth acceleration would be 25% in USD terms (as shown below), a contraction vs last quarter's 50% estimate
- Using the 9.5x historic revenue multiple, the implied market cap would be US\$29.0 bn (assuming steady undiluted share count of 50 mm)
- Based on the above, MELI could trade to \$584/share over a one-year time horizon, implying a **30% decrease vs the current market cap**

MERCADO LIBRE (US\$ MM)		MERCADO LIBRE (MM)						
Est. y/y revenue growth	25%		Act. US\$ Rev	BCP Est. US\$ Rev	Act. Y/Y Rev. Growth (LC)	Act. LC Rev	Current LC FX	Estimated US\$ Rev
Est. Total Sales	2,867		<u>1Q20</u>	<u>1Q20</u>	<u>1Q20</u>	<u>2Q19</u>		<u>2Q20</u>
EV/Sales multiple	9.5x	Brazil	397	452	55%	1,336	5.35	387
Total EV	27,236	Argentina	133	137	123%	5,013	68.26	163
Net Debt	(1,775)	Mexico	95	99	81%	1,230	22.23	100
Est. Market Cap	29,010	Others	27	25	17%	26		31
# shares out	50	<b>Total Revenue</b>	<b>652</b>	<b>713</b>				<b>681</b>
Est. Stock Price	\$ 584	% Dif vs Est.	(9%)			2Q19 US\$ Act. Rev		545
						<b>Est. US\$ Growth Rate</b>		<b>25%</b>
<b>% Vs Current Mkt. Cap</b>	<b>(30%)</b>							

Source: Equity information sourced from Bloomberg. Convertible pricing as of May 26<sup>th</sup>, 2020.

MERCADO LIBRE (US MM)	1Q20	BBG consensus	% dif	4Q19	1Q19	q/q	y/y
Total Revenue	652	629	4%	674	474	(3%)	38%
EBITDA	(8)	(25)	67%	(48)	26	83%	-
EBITDA margin	-	-	-	-	5%	-	-

MERCADO LIBRE (US MM)	1Q20	4Q19	1Q19	q/q	y/y
Total Debt	1,125	1,017	899	11%	25%
Cash & Equivalents	2,899	3,246	3,220	(11%)	(10%)
Net Debt	(1,775)	(2,229)	(2,321)	-	-
Total Debt / LQA EBITDA	n/a	n/a	8.7x	-	-
Net Debt / LQA EBITDA	n/a	n/a	n/a	-	-

MERCADO LIBRE (US MM)	1Q20	4Q19	1Q19	q/q	y/y
EBITDA	(8)	(48)	26	83%	-
Interest expense	(24)	(22)	(16)	(11%)	(49%)
Capex	(45)	(36)	(33)	(25%)	(37%)
Working capital	(98)	120	116	-	-
Tax expense	(4)	9	(3)	-	(27%)
<b>FCF</b>	<b>(180)</b>	<b>24</b>	<b>89</b>	<b>-</b>	<b>-</b>

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