09/19/2020: Space Market (4487.JP) - Japan's WeWork, Only Profitable

Business Description: SpaceMarket operates an online platform for space sharing in Japan. It provides a marketplace of unused or idle venues for on-demand rental use. The company offers a space market app, which allows customers to search and reserve rental space. Its platform allows searching for rental space for parties, business, shooting and recording, hobbies/play, sports/fitness, study group, lessons/courses, music, beauty, office, pop-up store, baggage, and other events.

Facts & Figures

- Shares Outstanding: 11M
- Market Cap: $108M
- EV: $100M
- Founder/CEO owns 40% of company
- EV/Sales: 9.63x
- EV/EBIT: 68x
- Current (2018) TAM: $18B
- Estimated 2030 TAM: $48B - $105B

How Space Market Makes Money:

- 5% guest fee (usage fee for renting space)
- 30% host fee (also incentives to give money back to hosts that have high guest volumes)

The Elevator Pitch: Space Market is a founder-led real estate sharing company sitting at the forefront of the fast-growing sharing economy movement. As the industry leader in space offerings, the company benefits from network effects that its competitors can't rival. As the company grows, it will attract more listings, which will attract more users to its platform. This flywheel effect will help Space Market capture most of its addressable market and maintain its industry leading status. The company's capital-light business model will shine as they leverage their fixed costs and grow EBITDA margins to upwards of 30% on a run-rate basis. The balance sheet is strong with $8M in net cash. You can buy Space Market for <5x our estimate of 2023 sales.

Founder-Led Company Solving a Real Japanese Problem

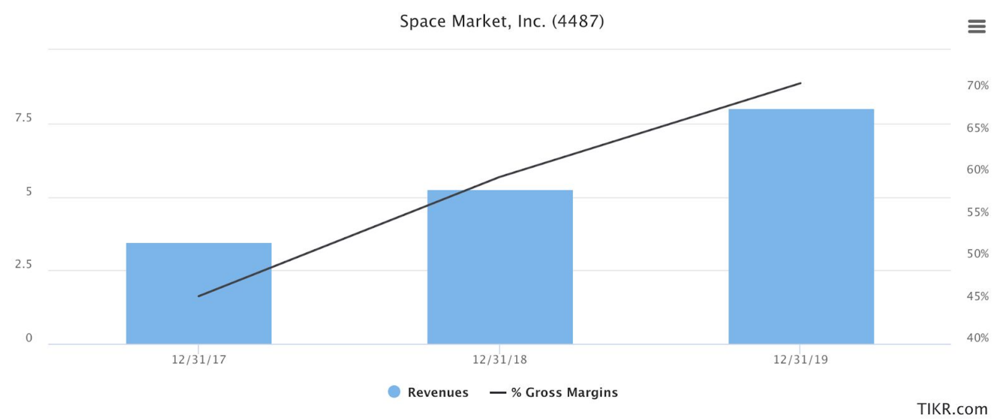
Space Market solves the rising vacancy problem in Japan. Between declining birth rates and an elderly population, vacancies should continue to rise over the next two decades. The company creates value in places where home/office owners thought there was none. In turn, it's a win-win for both the guest and the host. The guest can reserve a cool spot for a company meeting or team bonding session. And the host can make more money than they pay in rent.

The company's led by founder Daisuke Shigematsu. Daisuke owns 40% of the company between individual shares and via his asset management company, KK Double Pines. He started the company in 2014 and won Best Company in Japan's Cyber Expo event.

Unit Economics of Listings

- 2019 Listings: 12,200
- 2019 Revenue: $8.03M
- Revenue/Listing: $680.32/listing
- Company's Stated Listings Goal: 80,000
- Revenue at 80K Listings (assuming 2019 Rev/Listing Figures): $54M (1.85x current EV)
    - 70% GM: $38M in GP
    - 36% Steady-State EBIT Margin: $20M (5x current EV)

I'm not sure this is the right way to think about 4487's revenue trajectory. On one hand, I assume more listings would drag average revenue per listing down. But on the other hand, if more people engage with Space Market, we could see higher total revenues per listing as more people rent out spaces on an annual basis. Shoot me an email if you have better thoughts on this framework -- much appreciated!



Our 2024 revenue estimate is $25.8M. If we divide that figure by 2019 revenue/listing ratio we get roughly 38K listings. That's a 3x increase in listings in five years. Is that doable? Yes, if COVID clears up. If COVID hangs around like a storm cloud for the next year or two, there's no way they meet that target.

Now, if they reach $25.8M in revenue by 2024, what does their EBIT look like? After growing to 38K listings, the company wouldn't need to spend on advertising and marketing. This greatly increases operating margins to an estimated 36%. In this scenario, Space Market would generate ~$9.3M in operating income. That puts it at roughly 10.75x our 2024 EBIT estimate. A high-growth, space sharing company with 70% GM and 30%+ EBIT margins should trade roughly double that.

How To Get From 12K To 80K Listings

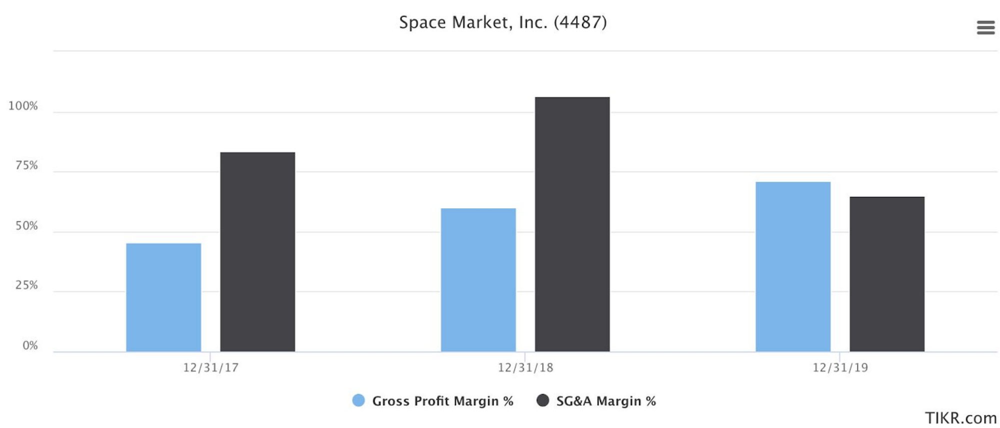
Space Market will have to spend a lot of money on marketing and advertising to reach 80K listings. If they maintain their industry-leading status, the natural network effects should take over and make their job easier. The issue is we don't know when that will happen. Will it start at 20K listings? 30K? Who knows.

What we do know is they'll have to do things that don't scale. This means local community events. Higher incentives for (to steal Airbnb's monicker) "super hosts". Anything to expand their reach and grow that network.

The company will also need a continued shift away from ownership to sharing mentality. That's not easy in Japanese culture where status matters. Yet as the population ages/dies out, the younger generation will prefer the latter.

Why The Opportunity Exists

There's a few reasons why this opportunity exists. First, Space Market is a micro-cap company trading on Japan's Mother's Index. For those unfamiliar, the Mother's Index is closer to a venture-capital space than a public market. There's zero Japanese analyst coverage, let alone US-based interest. It's one of the last remaining un-fished ponds in the public equity market.



Second, shares are illiquid. The stock trades roughly 125K shares on a 10 day average. This is 0.00113% of the company's overall shares outstanding. But makes sense given the stock's low float.

Third, COVID-19 makes the most recent quarters numbers look downright awful. Revenue dropped 60%+, gross margins shrank 20% and the company lost money during the most recent quarter.

Risks

The Space Market thesis hinges on the company reaching critical mass before its competitors. Sharing economy companies have virtually zero barriers to entry and low operating costs. It's the perfect industry for start-ups to compete.

First-mover advantage is key here. Luckily Space Market is the first and (as of writing this) only publicly traded space sharing company. Listing on the Mother's Exchange should provide the company with enough capital to acquire more customers and entrench its network effect.

Finally, you can't write about a space sharing company without mentioning COVID-19. We saw what COVID did to the company's most recent quarterly numbers. If the virus hangs around another year or two, the company will need to either a) issue equity to raise cash, or b) issue debt to pay their expenses.

