MO Weekly Equity Note: 10-02-2021

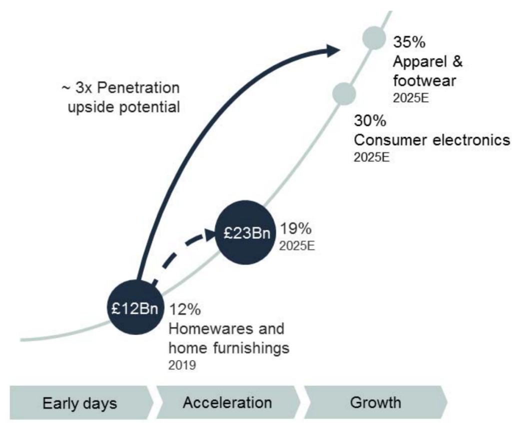
MADE.com (MADE) & 1stDibs.com (DIBS): Two Cash-Rich, Broken-IPO Online Marketplaces

One thematic we love researching at Macro Ops is *The Great Digital Transition,* where consumers go from buying products mostly offline to primarily online.

No better industry exemplifies this theme than **home decor, furniture, and luxury design items**. This theme was the driving force behind our Westwing (WEW) bull thesis, which you can read [here].

For example, online penetration rates in WEW's core markets stood at only 5%. This compares to 13% for consumer appliances, 14% for fashion, and 24% for consumer electronics.

Online penetration rates by industry in MADE's markets[5]



There are two legitimate reasons for this slow adoption.

First, people that buy home & decor products are *usually* older than those purchasing consumer electronics. This means it takes a home & decor customer longer to adopt new ways of purchasing a couch than, say, a new gadget for a teenager.

Second, home & decor products aren't economically friendly for most e-commerce platform business models. Cliff Sosin of CAS Investment Partners calls these items "un-Amazonable." Large-sized furniture products need specialized logistics operations while margins compress as shipping costs eat away a traditional e-commerce platform's profits.

There are two companies well-positioned to capture significant portions of this *massive* shift from offline to online spending: **MADE.com (MADE)** and **1stDibs.com (DIBS).**

Together, these companies serve a highly fragmented, $247B addressable market with a unique and differentiated value proposition to its customers.

Both companies stumbled out of the IPO gate. MADE has seen its share price decline ~28% since listing while DIBS has endured a 42% price decline.

Suppose we had to guess the reason for the IPO decline. In that case, we'd assume it has to do with investors' understandable skepticism of the durability of COVID-related consumer shopping trends.

That said, both companies trade at attractive prices looking out a few years. For example, you can buy *both* businesses for a total of $814 Enterprise Value (MADE at $514M and DIBS at $298M). Currently, you can buy MADE for less than 1x current sales. To compare, other leading high-end home decor/fashion marketplaces like FarFetch (FTCH) trade for over 5x current revenues.

Finally, today's prices make both companies ideal acquisition targets for giant conglomerates like an IAC or LVMH.

This week, we'll discuss the first of the pair, MADE.com.

MADE: UK's Leading Digitally Native Home Decor Brand

MADE is the only pure-play digitally native lifestyle brand in the furniture and homeware category operating at scale in the UK. MADE offers an exclusive, well-designed, ever-changing product assortment at affordable prices as an online home lifestyle destination.

The company offers over 6,000 SKUs through its website sourced by a network of 150 in-house designers and external independent designers.

MADE sells sofas, chairs, tables, beds, storage, lighting, home furnishings, and garden furniture and accessories.

Each design is a standalone piece specifically curated for MADE's aesthetic and target consumer (affluent millennials). Additionally, MADE is vertically integrated, giving the company *complete* control over product development and design, sourcing, manufacturing, and distributing.

This vertical integration allows MADE to command lower prices from its raw material suppliers (which it directly sources 95% of the time). Low raw materials prices allow MADE to charge less for higher-quality pieces, creating a sustainable moat its competitors can't match.

Finally, MADE operates a "Just-in-Time" supply chain. Its supply chain software allows MADE to test new design pieces rapidly without spending loads of cash on "hopeful" future sales. If a test product doesn't work, they don't ship more. This short batch system ensures the company maintains a negative working capital cycle.

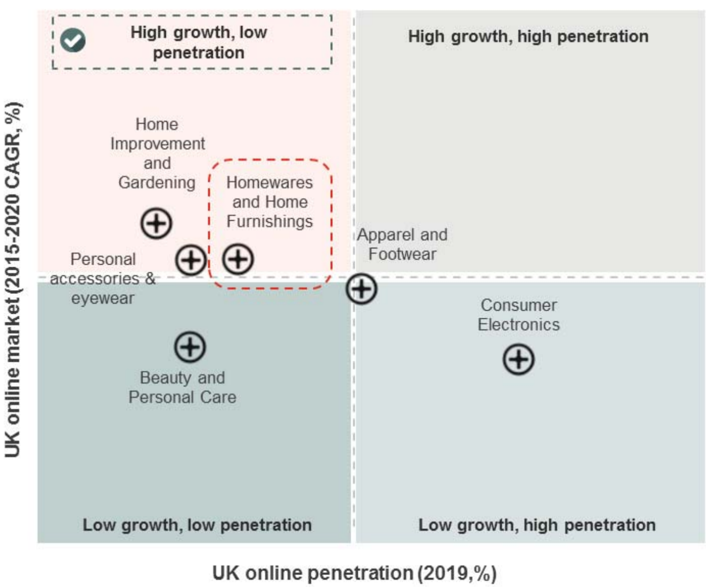
There are three main reasons we like MADE:

- It reminds us of Westwing (WEW)
- Attractive Customer Demographics
- Strong balance sheet and a cheap multiple

Let’s unpack each topic.

Why MADE Reminds Us of Westwing

MADE reminds us a lot of Westwing (WEW). For example, both companies generate similar EBITDA margins (low teens) and boast impressive top-line revenue CAGRs (28% 5YR in the UK, 48% in Continental Europe).



The second reason MADE reminds us of WEW is that it generates substantially higher EBITDA in its core UK market. In 2020, MADE generated 13% EBITDA margins in the UK. The company notes that its International segment generated only 1% during the same year.

The final reason MADE reminds us of WEW lies in the company's reinvestment strategy. Though MADE generates ~13% EBITDA margins in the UK, it ended 2020 with only 2% total EBITDA margins compared to its 53% gross margin print.

What explains the difference? The company spent nearly 24% of its sales on marketing for its Continental Europe business segment.

So while its UK business is highly profitable, MADE still needs to invest in Europe to get that business at the UK level.

Again, we saw this with WEW. The company generated mid-teens EBITDA margins in Germany and high single-digits in its other markets.

Attractive Customer Demographics

As we mentioned earlier, we're at the precipice of rapid online spending adoption in home decor and furniture. Who will lead that adoption? Millennials and Generation X, which bodes well for MADE.

MADE is the most popular home and living brand for UK millennials, with roughly 50% of its customers 35 years or younger. This allows MADE to capture most of the value of that demographic as it matures and buys more homes.

Currently, Average Order Values (AOVs) stand at ~EUR 235. This should increase as its core customer base switches from renting to buying homes, fueling the need for more home decor items.

Speaking of capturing value, let's see how much value MADE can generate over the next five years.

MADE's Strong Balance Sheet & Cheap Valuation

MADE's stock has been down ~30% since the IPO, with a current market cap of $734M. Here's the exciting part. The company has ~$166M in net cash on the balance sheet with no long-term debt, giving MADE a ~$567M Enterprise Value.

It's important to note that MADE is a run-rate profitable business generating mid-teens EBITDA multiple on revenue. So the cash isn't a melting ice cube.

Now, management has ambitious goals for the next five years. But ones they think they can hit. The company expects to reach $1.6 in revenue by the end of 2025. MADE's currently doing $431M for the LTM 2021. That's almost 3x in revenues over the next five years.

The company's already estimated $559M in revenue next year and nearly $700M in 2022. So you'd need a roughly 37% revenue CAGR to reach that $1.6B 2025 figure.

Usually, in this market, you'd pay ~10-20x revenues for this growth expectation. That's not true here. You can buy MADE for <1x next year's revenues.

And remember, the company is highly profitable in its core UK market. Should they expand that profitability to its Continental Europe segment, total EBITDA margins would expand to mid-teens (13-15%).

There's a scenario where MADE generates $1.6B in revenue while printing *at least* $160M in EBITDA.

And you get that scenario for <1x next year's sales estimates.

But, if the company generates over $1B in revenue with mid-teens EBITDA margins (or even low teens), what should it be worth? **A modest 10x mutliple on 2025E EBITDA gets us ~$1.6B in EV. That's almost a 200% upside from the current price.**

Here's the exciting part. If MADE generates those types of financials, what would a buyer pay on a sales multiple basis … 2-4x? That doesn't seem unreasonable. Assume a 2.5x multiple on 2025E (and management guided) sales, and you get roughly $4B in Enterprise Value, or **nearly 600% higher than the current price.**

How Does This End: Potential M&A

MADE's current CEO, Philippe Chainieux, has over two decades of experience in e-commerce businesses. Chainieux has a history of building great companies. For example, Chainieux was the former CEO of Barry Diller's IAC darling, Match.com.

Chainieux's connection with IAC makes me wonder if MADE becomes an ideal acquisition target for Diller's capital.

We don't know when that will happen. But suppose MADE can print a couple years of sustained revenue growth and EBITDA margin expansion. In that case, the current sub-1x sales multiple is ***far too low***.

Concluding Thoughts

Like WEW, investors assume that the COVID-sparked shopping trends will normalize to more of an offline experience. Our variant perception is that COVID catalyzed a **permanent** shift in the way consumers (specifically millennials and Gen X) shop for home decor and furniture.

MADE is a direct bet on that variant perception and can make at a cheap valuation. It boils down to one fundamental assumption. MADE becomes increasingly valuable in a world where more consumers shop for home decor items online than offline.

We have the mental model toolkit available from our work on WEW to opportunistically buy should the charts firm up.

