

## Etsy, Inc. (ETSY): Buy @ \$13.00

**Buy Thesis:** We upgrade our rating from a Hold to a Buy and our PT from \$11 to \$13. We believe Etsy’s Market Position in e-commerce is stable as 1Q17 y/y growth rates for both GMS (14%) and Revenue (18%) are projected to outperform estimated 1Q17 U.S. e-commerce growth (11% y/y). The slowdown in Seller Services revenue drove slower top-line growth but a review of Etsy’s Internals (Growth in Active Buyers/Sellers and Take Rate) shows stability in the e-commerce platform. Etsy is undergoing a Management re-shuffle and implementing cost savings measures. We’re confident that the introduction of *Etsy Studio* last month, a marketplace hub between arts & crafts suppliers and sellers, could add to incremental growth in Seller Services revenue in 3 to 4 quarters. Furthermore, the requirement by Etsy for all Active Sellers to use *Etsy Payments* platform later this month could also add to higher transaction fee revenues.

TABLE 1: Etsy 1Q17 Results

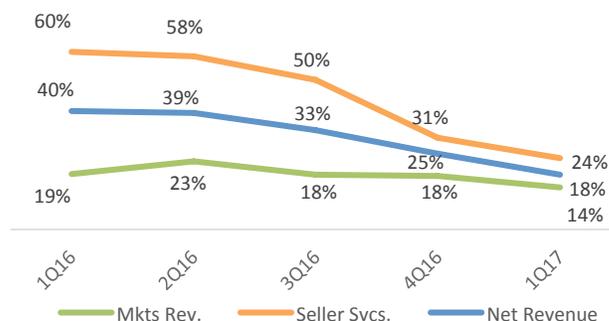
1Q17 Results			2Q17 Guidance			1Q17 Results			2Q17 Guidance		
EPS	Cons.	Result	EPS	Cons.	Result	Total Rev.	Cons.	Result	Total Rev.	Cons.	Result
0.00	0.01	miss	n/a	-0.01	n/a	96.89M	98.35M	miss	n/a	104.55M	n/a

Source: Etsy, Inc. and Estimize.com

### I. Slowdown in Seller Services Revenue Drove Slower Top-line Growth

Etsy’s drop in 1Q17 revenue growth to 18% y/y from 25% y/y last quarter was a result of a combination of macro weakness and internal factors. On the macro side, U.S. consumer spending growth slowed down in 1Q17 and political uncertainties in Europe – Brexit and the French elections – may have had an adverse impact. Etsy’s international GMS is now 13% of total GMS and grew 21% y/y in 1Q17.

FIGURE 1: Y/Y Revenue Growth, by Business Segment (%)



On the internal side, the steep decline in Seller Services revenue from ~60% y/y in 1Q16 to just 24% y/y in 1Q17 was a major factor in driving down 1Q17 net revenue growth (see Figure 1). Seller Services has become a greater part of the sales mix growing from 53% of total sales in 1Q16 to ~56% in 1Q17.

Source: Etsy, Inc.

Etsy is replacing their current CEO (Chad Dickerson) with a new CEO (Josh Silverman) who could be more capable in taking Etsy to the next level of growth. While it's still too early to gauge what the new growth strategy will be, management clearly hinted during the 1Q17 call that the company will increase marketing spend to acquire new customer traffic, drive higher conversion from site visits and encourage existing buyers to increase their average spend. Management reiterated that for the first 8 years in business, Etsy did not engage in any type of marketing campaign.

**II. Healthy Internals Indicate Stable E-commerce Market Position**

Etsy's internal metrics indicate a stable market position in e-commerce. For example, Active Buyers have grown steadily from 25M in 1Q16 to ~30M in 1Q17, an average of 19% y/y over the last 5 quarters (see Figure 2 left). Active Sellers have also posted a nice growth rate from 1.6M in 1Q16 to ~1.8M in 1Q17, for an average growth rate of ~12% y/y (see Figure 2 right).

**FIGURE 2: Active Buyer Growth (left) and Active Seller Growth (right) – in Million and Y/Y Change (%)**



Source: Etsy, Inc.

**FIGURE 3: Take Rate (%)**



Source: Etsy, Inc.

Etsy's take rate has also increased incrementally from 12.7% in 4Q16 to 13.5% in 1Q17, up 80 bps. Over a 5-quarter period, take rate grew by 50 bps from 13% in 1Q16 (see Figure 3). As management executes its strategic initiatives this year to increase conversion and average purchase size, it is likely conversion rates will grow incrementally as well.

## **Disclosure Information**

### **Analyst Certification**

The authors of this report, hereby declare that: (i) all of the views expressed in this report accurately reflect their personal views about any and all of the subject securities or issuers; (ii) no part of any of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this report; and (iii) no insider information/non-public price-sensitive information in relation to the subject securities or issuers which may influence the recommendations were being received by the authors.

### **Disclaimer**

By accepting this report (which includes any attachment hereto), the recipient hereof represents and warrants that he is entitled to receive such report in accordance with the restrictions set forth below and agrees to be bound by the limitations contained herein. Any failure to comply with these limitations may constitute a violation of law.

This report is strictly confidential and is for private circulation only to clients of Viola Advisory, LLC. This report is being supplied to you strictly on the basis that it will remain confidential. No part of this report may be (i) copied, photocopied, duplicated, stored or reproduced in any form by any means or (ii) redistributed or passed on, directly or indirectly, to any other person in whole or in part, for any purpose without the prior consent of Viola Advisory, LLC.

Viola Advisory, LLC, its affiliates and related companies, their directors, associates, connected parties and/or employees may own or have positions in securities of the company(ies) covered in this report or any securities related thereto and may from time to time add to or dispose of, or may be interested in, any such securities.

The information contained in this report is prepared from publicly available data and sources believed to be correct and reliable at the time of issue of this report. This report does not purport to contain all the information that a prospective investor may require and may be subject to late delivery, interruption and interception. Viola Advisory, LLC does not make any guarantee, representation or warranty, express or implied, as to the adequacy, accuracy, completeness, reliability or fairness of any such information and opinion contained in this report and accordingly, neither Viola Advisory, LLC nor any of its affiliates nor its related persons shall not be liable in any manner whatsoever for any consequences (including but not limited to any direct, indirect or consequential losses, loss of profits and damages) of any reliance thereon or usage thereof.

This report is general in nature and had been prepared for information purposes only. It is intended for circulation amongst Viola Advisory, LLC's clients generally and does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may receive this report. The information and opinions in this report are not and should not be construed or considered as an offer, recommendation or solicitation to buy or sell the subject securities, related investments or other financial instruments thereof.

The views, recommendations, advice and opinions in this report may not necessarily reflect those of Viola Advisory, LLC or any of its affiliates, and are subject to change without notice. Viola Advisory, LLC has no obligation to update its opinion or the information in this report.

Investors are advised to make their own independent evaluation of the information contained in this research report, consider their own individual investment objectives, financial situation and particular needs and consult their own professional and financial advisors as to the legal, business, financial, tax and other aspects before participating in any transaction in respect of the securities of company(ies) covered in this report. The securities of such company(ies) may not be eligible for sale in all jurisdictions or to all categories of investors.

### **Risk which may impede the achievement of our Price Target**

This report was prepared for general circulation and does not provide investment recommendations specific to individual investors. As such, the financial instruments discussed in this report may not be suitable for all investors and investors must make their own investment decisions based upon their specific investment objectives and financial situation utilizing their own financial advisors as they deem necessary. Past performance of the financial instruments recommended in this report should not be taken as an indication or guarantee of future results. The price, value of, and income from, any of the financial instruments mentioned in this report can rise as well as fall and may be affected by changes in economic, financial and political factors. If a financial instrument is denominated in a currency other than the investor's home currency, a change in exchange rates may adversely affect the price of, value of, or income derived from the financial instrument described in this report. In addition, investors in securities such as ADRs, whose values are affected by the currency of the underlying security, effectively assume currency risk.