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SABER CAPITAL
MANAGEMENT, LLC

ETSY:

EMPOWERING MILLIONS OF
“SHOPS AROUND THE CORNER”

DISCLOSURE

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SABER FIRM OVERVIEW

Saber Capital Management, LLC manages an investment partnership and separate accounts for high net worth individuals, families, and institutions.

Saber's philosophy stems from the simple observation that in the long run, the best investments come from the best companies.

Our investment approach is to carefully study and selectively invest in great businesses that we believe will compound value over time.

We align ourselves completely with our investors. John Huber has nearly all his personal net worth invested alongside clients. Investors in Saber Investment Fund, LP pay no management fees and only pay performance fees for returns above 6% per year.

WHAT IS ETSY?

Etsy provides a global platform that helps millions of talented individual entrepreneurs & DIYers make money from their labors of love.

WHAT IS ETSY?

- Highly profitable two-sided marketplace (33% FCF margins ttm)
 - 3.7 million active sellers
 - 80 million listings
 - 70 million active buyers
- ~\$10 billion in 2020 gross merchandise sales (GMS)
 - 117% growth (93% excluding masks)
- \$1.4 billion in revenue (ttm)
 - 95% growth
 - \$450 million free cash flow (ttm)
- Market Cap: \$21 billion (\$167 per share) as of 1/6/21

ETSY: A 5-TOOL PLAYER?

Desired business attributes:

1. Delighted Customers
2. Monopoly Magnets
3. Royalty on Work of Others
4. Tailwinds
5. Adaptable to Change



Willie Mays – maybe the greatest ever 5-tool player

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Delighted Customers

PEOPLE LOVE SUPPORTING LOCAL

Everyone wants the Shop
Around the Corner to have a
chance against the Fox Books.

Etsy is giving opportunities to
millions of Kathleen Kellys
(i.e. people of the “passion
economy”— artists, carpenters,
jewelers, bakers and many other
small but talented creators)



Everyone wants Kathleen Kelly to just have a chance

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PEOPLE LOVE ETSY

- Social followers are usually just vanity metrics, but one anecdotal takeaway I have is how much people love talking about Etsy

12/30/20	Engagement			\$ billions		\$ thousands
	Top FB Group (thousands)	Top Group Posts/Day	Twitter/ Instagram Followers	Sales (GMS)	Market Cap	GMS per Follower (how "monetized" are followers?)
<i>Retail</i>						
Etsy	63	1600	5.1	10	\$22	\$2
Amazon	59	20	6.4	475	\$1,596	\$74
Target	345	120	6.5	89	\$96	\$14
Ebay	88	1100	1.7	90	\$37	\$53
Walmart	473	1100	3.7	549	\$416	\$148
Shopify	106	10	1	110	\$141	\$110
Wayfair	3	1	2.4	13	\$25	\$5

Source: MBI Deep Dives and Saber's archives of interesting (if nothing else) stats

YOUR PERSONALIZED ETSY STORE

- A major advantage of ecommerce: personal catalogs
- Each Etsy shopper gets a unique shopping experience that becomes more personalized over time
- And the more customers Etsy gets, the better the experience gets for everyone else (“[data economics shared](#)”)

And the **quality of search results on Etsy is dramatically better than it was even just 2 years ago**. We're now just starting to not just close the semantic gap, meaning understand what you met, not just what you said. But now start to actually personalize search results, so that if Rachel and Shweta both ask – **both type in the same keyword on Etsy, they'll see very different results**

And then our ability to **understand each individual person and what their taste and style is. Are they shopping for themselves? Are they shopping for someone else? What else have they been interested in, in the past? We're getting much, much better** at that. And it's those 2 pillars that I think together make for a really amazing discovery experience. We are investing significantly in that now at Etsy. I think that's a relatively new track of investment for us, and I think it's going to yield tremendous gains.

- Josh Silverman, 9/15/20 and 11/17/20

MONOPOLY MAGNETS

**“A Business is either a monopoly
or a non-monopoly.”**

- [Peter Thiel](#)

ETSY'S NETWORK EFFECT

Two-sided marketplaces are not all monopolies, but they trend in that direction as they grow:

- ROIC's don't revert; they expand as network grows ([see link](#))
- The platform consolidates demand (buyers), leads to more sellers, who make products that bring in more buyers, etc...
- Customer acquisition costs decline
- Networks are the rare business where it becomes cheaper/easier to find the 101st customer than the 100th

COVID & ETSY'S NETWORK

Covid has accelerated two key trends that benefit Etsy:

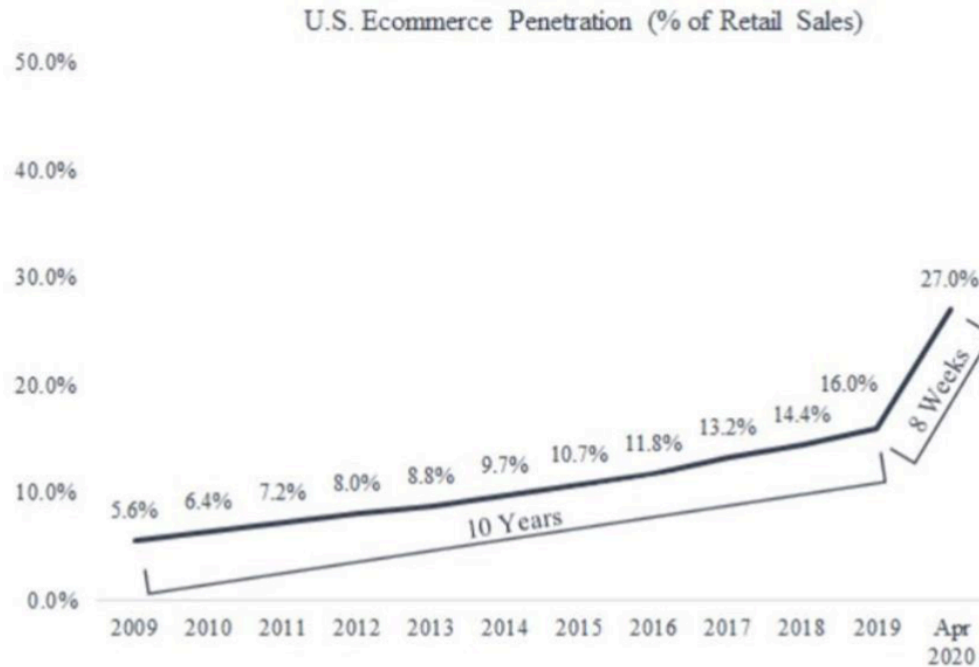
1. **Ecommerce adoption (buy side)**
2. **Individual entrepreneurship (sell side)**

Each trend fuels one side of Etsy's growing network.

This has had a game-changing impact: 23 million new buyers (+50% increase) and over 1 million new sellers in just 6 months.

COVID CATALYST

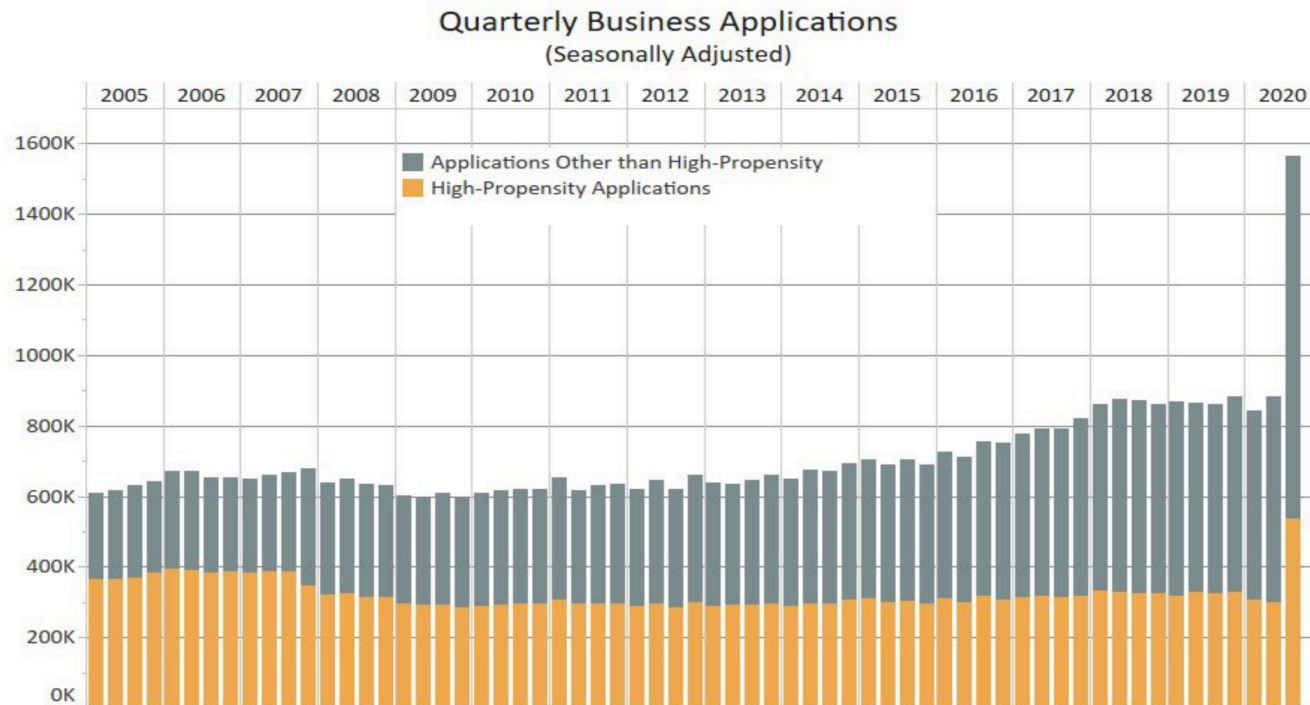
“It’s 2030 at Shopify” – Tobi Lutke



Source: Bank of America, U.S. Department of Commerce, ShawSpring Research

COVID CATALYST

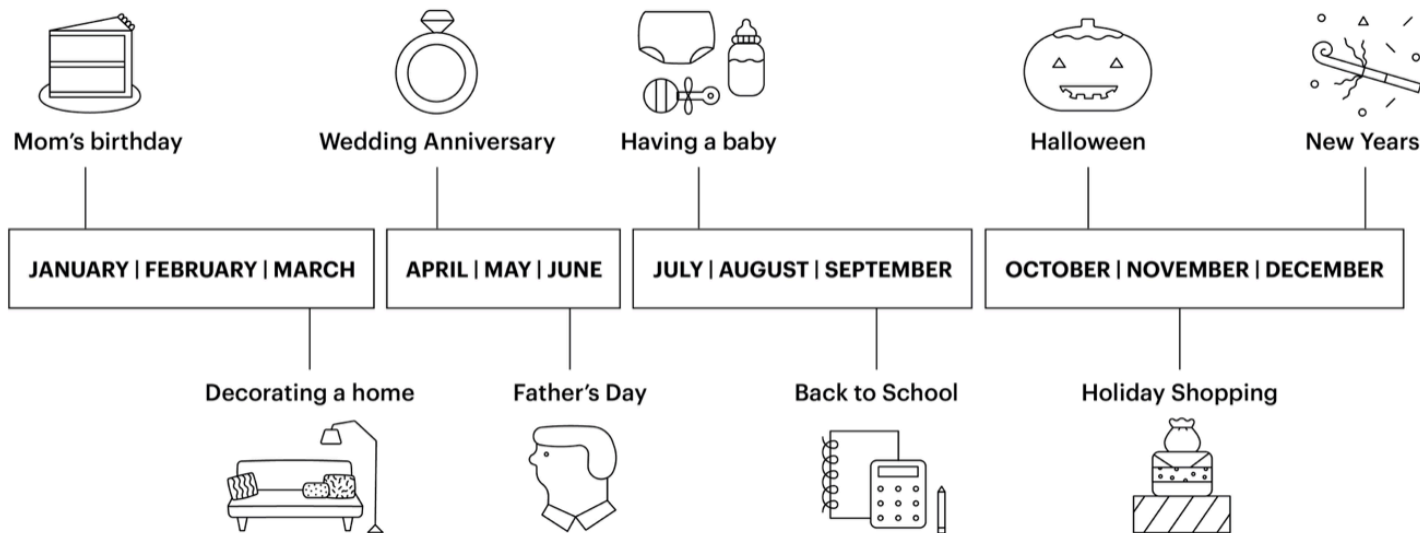
Covid unleashed a boom in entrepreneurship:



(and no, the boom in applications was not solely PPP)

GROWTH: NEW HABITS FORMING

- Think of all the last-minute gift shopping that gets done at Target, Kohl's, Amazon, Walmart, department stores
- Much of the purchases below can (and I think will) shift to Etsy over time:



Source: Etsy 10-k

**“The Best Business is a Royalty on the
Growth of Others”**

- Warren Buffett

HIGH RETURNS ON OPM

- Some of the greatest businesses in the world get a free ride on someone else's capital, effort, and risk: [\(see post\)](#)
- MSFT's growth was funded by IBM
- NVR profits on 3rd party land developers' risk
- AAPL, NFLX, FB, GOOG all boomed along with internet adoption, which was funded by telecoms' broadband investments
- TWLO gets a free ride on UBER and WhatsApp's growth

SELLERS FUND ETSY'S GROWTH

- Lots of capital is funding ecommerce market's rapid growth
- Lots of capital tied up in Etsy's 80 million listings
- Etsy benefits from both
- Without using any of their own money
- Etsy has no inventory, warehouses, trucks, etc...

ETSY'S ROYALTIES

Etsy's marketplace is asset-light, very profitable, and acts like recurring revenue on millions of annual transactions.

Main revenue sources:

- **Transaction fees:** 5% of order
- **Listing fees:** \$0.20/listing
- **Etsy Payments:** 3% of order + \$0.25 (varies outside US)
- **Etsy Ads:** profitable and rapidly growing; +95%

Adaptability to Change

ADAPTABLE TO CHANGING TRENDS

- Change is constant in retail
- Thousands of decentralized “manufacturers” can be mobilized **within hours**
- Etsy is best positioned to adapt to these inevitable changes

Yes. The first thing I would say on that is that, that was a very unique e-mail because we had such an unbelievable surge. And within 2 weeks, we had 20,000 sellers making and selling masks, and now we have many, many more than that. It's provided a really good income for tens of thousands of people this year when they've otherwise been so hard hit with the economy. But in general, **our seller community is so agile, they're paying so much attention to sales in their category that they typically pivot within hours or days to meet demand.**

And an example I would give is bread and bread-making in the month of May. **I never would have guessed that bread and bread-making products would be a big category on Etsy.** Never in a million years would it have occurred to me. But in the month of May, we started to see bread shortages in stores, and a lot of people stuck at home decided to take up bread-making as a hobby. And so they turned to Etsy, and **we started to see a surge in keywords, in demand, and literally within hours, bakers are coming on Etsy and starting to meet that demand.** And supply and demand met effortlessly and almost instantaneously because the communities are paying enough attention and bakers started to talk to bakers and word just got out. So we actually didn't need to do anything in that case, and we had enough supply.

- Josh Silverman, 9/15/20

Tailwinds & Growth

ETSY'S MARKETS

Six Major Markets

1. US
2. Canada
3. UK
4. Germany
5. France
6. Australia

Six Main Retail Categories:

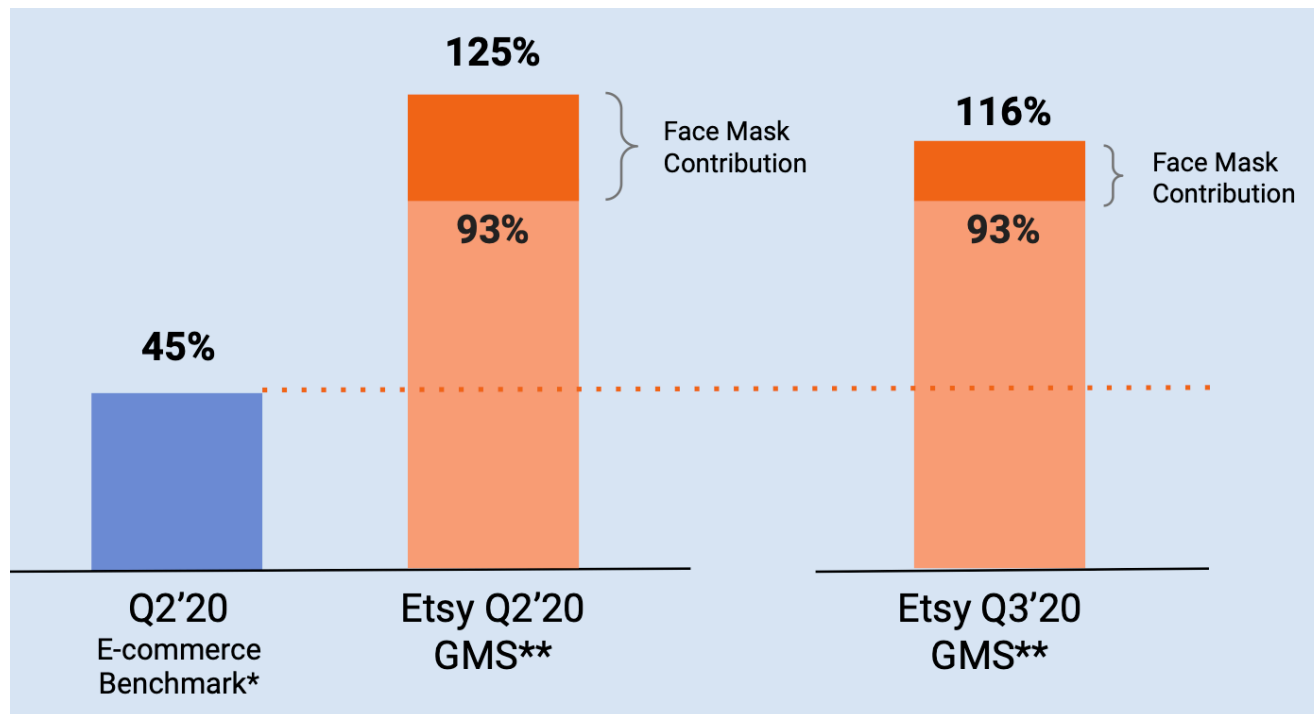
1. Home furnishings
2. Jewelry & accessories
3. Apparel
4. Craft supplies
5. Paper/party supplies
6. Beauty and personal care

I challenge you. Go back and look at the last 90 days of purchases you've made online. Look at everything you've bought online, and then spend a little bit of time and see how many of those things you could have bought on Etsy. I promise you, you'll be very pleased with what a high percentage of things you bought online, you could have bought on Etsy. And those items are going to be more unique. They're going to be more tailored to your taste, and they're going to be sold at a fair price.

Source: 2019 Etsy Investor Day

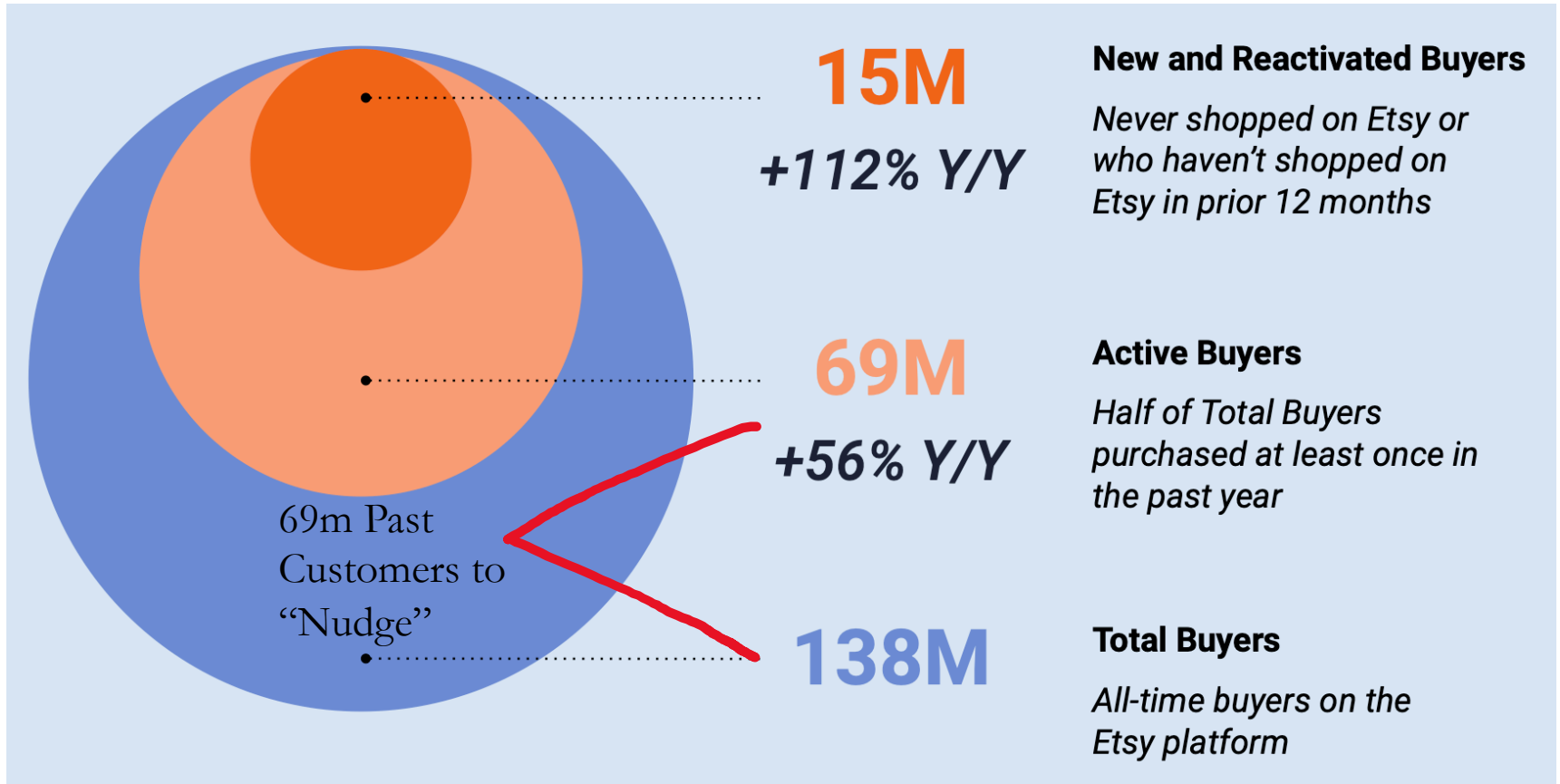
EXPLODING GROWTH

- Etsy's business (not including masks) is growing twice as fast as the ecommerce market



Source: Company Presentation; *US Census Bureau

OPPORTUNITY: 69M POTENTIAL BUYERS



Source: Company Presentation + Saber edits

ETSY'S GROWTH IS VERY VALUABLE

- Low marginal costs: each additional sale is very high margin
- This leads to widening profit margins (Q3 EBIT Margin: 26%)

Ratios	12/31/16	12/31/17	12/31/18	12/31/19	LTM
EBIT Margin %	5.1%	6.6%	13.8%	11.3%	21.1%

Chart: Ticker

- These GAAP margins include big investments in marketing & product development (38% of revenue in Q3), which is largely to fund growth
- I believe Etsy's "steady state" **current** profit margins are enormous

ETSY ADS

- Etsy Ads growing by 95%
- Saber Capital likes advertising business models ([See FB post](#))
- Internet advertising is a great business
- Highly profitable with strong economies of scale and data feedback loops
- Etsy's ad business will grow as the marketplace grows
- Pinterest isn't directly comparable, but worth noting:

	PINS	Etsy Ads (Services Segment)
Revenue (Annual Run Rate)	\$1,750	\$500
Current Growth Rate	58%	106%
Profitable	Not Yet	Yes
Market Cap	\$43b	N/A
Price/Sales	24x	?
<i>How much is Etsy Ads worth?</i>		

Valuation

ETSY'S MARKET: IT'S BIG

“You don't need to know a 350 lb man's weight to know he's fat”

– Ben Graham



MARKET OPPORTUNITY

- Etsy GMS = \$10b
- Management believes market is \$400b online and \$2 trillion total
- TAM estimates are sometimes wildly optimistic
- **But Etsy's market is like the 350lb man; we know he's fat**
- Home furnishings alone is \$120 billion in the US alone*
- Just 1 of 6 verticals in only 1 of Etsy's 6 major markets
- Kohl's, Macy's & Dillard's still did \$45 billion in sales last year!
- And Etsy is already expanding and growing in many other markets

* Source: Census Bureau, St. Louis Fed

IF YOU COME, THEY WILL BUILD IT

- A misunderstanding: Etsy's network is **not** limited by the number of potential sellers, or “hand-made” capacity
- **Buyers will determine the ultimate size of Etsy's business**
- Etsy sellers will create whatever is in demand and will shift rapidly to changing trends (e.g. masks, bread, etc...)
- If demand for quality, custom made products rises, Etsy sellers will create supply

MY VALUATION NAPKIN - 1

- So, the key questions:
 - Will demand for ecommerce rise over time?
 - Will demand for unique, quality products rise over time?
 - If so, will Etsy be one of the key places to shop?
- Marketplaces get stronger as they grow
- Etsy's network grew over 50% in 2020
- Much more likely that Etsy is a key retail destination in the future

MY VALUATION NAPKIN - 2

- Etsy turns 5% of its GMS into free cash flow (30% margin on revenue)
- GMS: \$10 billion this year
- GMS was growing at 25-30% per year pre-Covid
- Market is very big and growing

MY VALUATION NAPKIN - 3

- GMS can be \$50-\$75 billion in 10 years and still be just a fraction of Etsy's markets (17-22% CAGR)
- Take rate is 16%, but will rise over time (e.g. Etsy ads +95% yoy)
- At 20% take rate: \$10-\$15 billion in sales
- \$3-\$5 billion in free cash flow at current FCF margin levels
- At \$21 billion, I believe there is significant margin of safety

I think Etsy is a great business that could compound value for many years to come.

DURABILITY

“Silicon Valley focuses too much on growth and not enough on durability” - Peter Thiel

- In 2001, Thiel did a DCF on PYPL and realized most of the value came from cash earned after 2011
- Durability is what's most important
- The “TAM” is large enough
- Network effects get more durable as they grow
- **Etsy's network of 69m buyers and 3.7m sellers is 50% larger than a year ago, and getting more durable by the day**

VARIABLES TO WATCH

Two most important variables to watch concerning the strength of Etsy's long-term business:

- Strength of network (active buyers, listings)
- Handling of inevitable conflicts
 - Every business faces inherent conflicts between customers, users, suppliers, etc...
 - e.g. Google could maximize ads or maximize user experience; Amazon could maximize value in low prices at expense of third party merchants, etc...
 - Every business has to manage these tradeoffs as it grows, and I try to carefully watch the progression of these conflicts over time

IDEA IN A NUTSHELL

- Fast-growing marketplace (+117%)
- Network effects are one of the world's greatest moats
- 23 million new active buyers last 9 months (+50%)
- Habits formed are likely permanent
- Big trends: Ecommerce, “shop local”, and boom in small entrepreneurship
- Etsy takes a royalty on that growth (33% FCF margins ttm)
- \$10b GMS in a market that is hundreds of billions in size globally
- Future free cash flow could be 5-10x next decade

Etsy is a snowball rolling downhill; it gets stronger as it grows, and is almost certain to grow for a long time

THANK YOU!

John Huber

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