MEMO

To: Doctor Pratik Goel
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Subject: Grubhub (US GAAP) & Delivery Hero (IFRS) Financial Ratio Analysis

Grubhub is an online and mobile application based in Chicago that delivers restaurant orders across the United States. Grubhub's revenue model is based on charging restaurant partners on the platform a per-order commission primarily percentage-based. The percentage can be chosen by the restaurant where a higher fee will give the restaurant a superior exposure on the platform.

From the 2019 annual report, we can see that there are no R&D expenses and a constant increase in their gross food sales, they increased by 34% in 2018 and by 17% in 2019, leading us to conclude that Grubhub follows a cost leadership strategy. Moreover, under the competition section in the 2019 annual report, it is stated that they are offering the lowest overall pricing while trying to gain differentiation.

On the other hand, Delivery Hero is a European multinational online food delivery service based in Berlin. The company operates in more than 40 countries across Europe, Asia, Latin America, and the Middle East; their revenue model is based on charging an initial set-up fee and a monthly subscription fee for restaurants to have delivery orders placed through its marketplace and takes a commission on every order completed.

Delivery Hero is following a differentiation strategy. According to the 2019 Annual Report, the weight of COGS increased by 37 points compared to the base year (2017), and the R&D expense also increases from EUR 42.2 mm to EUR 65 mm, and the firm is also heavily investing in marketing. However, a drop in its gross margin from 62% to 25% compared to the base year indicates that the firm is trying to achieve a differentiation strategy.

Strategy analysis of the food delivery industry using Porter's Five Forces model:

- **The threat of new entrants - HIGH -** The global food delivery services industry was valued at USD 111.32 bn in 2020 and is expected to grow to USD 154.34 bn by 2023. The industry is growing fast, attracting many well-established industry giants like Amazon, Alibaba, and Google, who are proactively looking to expand their services in different industries. And since they already have the technology, infrastructure, and resources, it is relatively easy for them to enter and dominate the online food delivery business.

- **Rivalry among existing competitors - HIGH -** Given that price competition is tight, and the buyer's switching cost is very low, firms are aggressively offering discounts and coupons regularly to increase sales, gain a more significant market share and increase their brand popularity, which slashes their profit margin. Moreover, one of the main challenges is that the existing competitors could continue to grow in the market. Some may have superior resources and capabilities that could impact Grubhub and Delivery Hero's revenues.

<u>Financial Ratio Analysis: Measuring and Decomposing Profitability:</u>

<u>Grubhub Ratio Analysis:</u>

As shown in *appendix 1,* Grubhub's Return on Equity (ROE) declined from 5.4% in 2018 to -1.26% in 2019, this sharp drop is seen negatively by investors because it shows that managers are not doing a decent job of employing the funds invested by the shareholders to generate returns. However, investors may overlook this negative ROE if they believe that Grubhub is well-positioned for future growth.

To get a better understanding, we need to look at the different levels of ROE; after decomposing the ROE, we can notice that the decline in ROE is mainly caused by a decline in Return on Sales (ROS).

Since ROE is mainly driven by ROS, assets turnover and financial levarage, we can clearly see that ROS had the most significant decline from 7.79% in 2018 to -1.41% in 2019, while the increase in assets turnover and financial leverage were so small that they couldn't offset the effect of the ROS, this indicates mismanagement on an operational level.

The declining ROS also indicates that Grubhub had a financial loss during 2019. When we look at the income statement trend analysis in *appendix 2*, we can see that Grubhub was caught in a scissor effect. The costs are growing faster than the sales in both 2018 and 2019. This is mostly due to increased competition in the industry and the ease and non-existing switching cost between providers.

The continuous drop in the EBITDA margin from 20.73% to 16.97% to 8.32% in 2017,2018 and 2019, respectively, confirms our assessment of the low operational performance of Grubhub since EBITDA is a comprehensive indicator of the operating performance of a firm that eliminates the effects of financing strategy, taxes, and capital investment policy.

When it comes to investment management, we can see that Grubhub is also not doing well, as seen by the increase in its Cash Conversion Cycle (CCC), which increased from 28.74 in 2018 to 55.95 in 2019 mainly driven by the rise in their Day's Receivable which almost doubled from 35.42 in 2018 to 63.42 in 2019.

This jump in the Day's receivables is mainly due to restaurant partners' high bargaining power from the increased competition in the food delivery industry. According to the 2019 annual report, there are different contractual arrangements regarding payment frequency, which leads us to conclude that restaurants enforce the payment frequencies and tend to make them longer.

When it comes to financial management and, specifically, liquidity analysis, we can see an improvement in the current ratio, which measures Grubhub's ability to repay its current liabilities using its current assets. Since the current ratio is at 2.27, which is higher than 1, creditors have assurance about being paid in full and timely.

On the other hand, when it comes to solvency analysis, we can see a drop in interest coverage from 879.9 in 2017 to 24.07 in 2018 and -0.31 in 2019. This decrease is driven by the 19991% increase in interest expense between 2017 and 2019 from 0.102 mm to 20.49 mm. This increase was attributed to the increase in outstanding borrowings of long-term debt in the 2019 period primarily due to the issuance of $500 mm of the company's 5.500% Senior Notes.

Finally, the Net Debt to EBITDA ratio increased from -0.43 in 2017 to 0.76 in 2018 and reached 1.07 in 2019. And since the normal range is between 1.0x and 3.0x, we can conclude that Grubhub is doing reasonably well when it comes to financial management, given their current overall financial situation.

<u>Delivery Hero Ratio Analysis:</u>

As shown in *appendix 3,* Delivery Hero's ROE saw a significant increase from -2.53% in 2018 to 13.20% in 2019. To find the root cause of this profitability growth, we further analyzed the ROE's different levels. In 2019, we can see that the main driver behind the increase in ROE was the ROS.

Since ROE is mainly driven by ROS, assets turnover, and financial leverage, we can see that ROS had the most significant increase from -6.34% in 2018 to 18.6% in 2019 compared to the rise in assets turnover and financial leverage that was relatively small. This indicates that Delivery Hero has efficiently managed its operations.

Looking at the income statement trend analysis in *appendix 4,* we can see that revenues increased from EUR 453.7 mm in 2017 to EUR 1237.6 mm in 2019. Delivery Hero reported a 173% revenue growth in 2019 from the base year 2017, which was driven by the organic growth in the firm's commission across all its geographical markets. We can also see that the COGS almost tripled in 2019 primarily because of the market expansion strategy that Delivery Hero is following, including the launch of its dark stores. As stated in the annual report, to achieve differentiation, the firm is investing heavily in IT, marketing, and R&D.

Furthermore, even though the CCC is still a good indicator since its negative, we can see that it increased by 32 days. This was mainly caused by the decrease of 49 in the Day's paybales that were not offset by the smaller increase of 16 days in Day's receivables. The firm's cash converting cycle was 92 days in 2019. This helps the firm stay more liquid when it comes to cash.

This resulted in a negative EBIT Margin of -52% and an EBITDA margin of -44.51% despite having a positive gross profit. In fact, the firm reported a net profit of EUR 230.2 mm achieved by their divested German operations to Takeaway.com N.V.

Finally, based on the cash flow analysis in *appendix 5*, we can see that the firm boosted its net increase in cash by 237% (EUR -191.1 mm to EUR 262.3 mm) in 2019 compared to 2018. The firm can utilize this additional money to buy-back shares from the market or in order to attract investors, the firm also can repay its long-term financial liabilities and further decrease its already low Debt to Equity ratio of 0.10 and Net Debt to EBITDA of 0.92.

Comparaison and Conculsion:

Grubhub and Delivery Hero have a very different financial performance; the ROE for Grubhub is on a decreasing trend whereas Delivery Hero's is on an increasing trend.

The main driver in ROE for both firms is the ROS, leading us to conclude that this could be the main profitability driver for the food delivery industry.

Both EBIDTA margins declinded by experiencing a scissor effect in their income statement where the costs are increasing higher than the revenues. Grubhub's margin is still positive, while Delivery Hero's is a triple-digit negative ratio due to their strategy of expanding and acquiring small delivery companies in the regions where they operate. In contrast, Grubhub didn't acquire any new business in 2019.

Delivery Hero's CCC is significantly better than Grubhub's, even though they are both on a declining trend; this indicates that Delivery Hero has higher bargaining power and superior working capital management.

The Debt to equity ratio is 0.33 for Grubhub and 0.1 for Delivery Hero, which indicates that both companies don't depend on debt financing. Delivery Hero's is less dependant on Debt financing compare to Grubhub.

Finally, the most important ratio when analyzing a company's financial position is the Net Debt to EBITDA ratio. We can see that the ratio is within the normal range of 1x and 3x. Grubhub's Net Debt to EBITDA is 1.07, and Delivery Hero's is 0.92, which tells us that both companies are doing well overall since the low ratio implies that the companies can be paying off their Debt and increase earnings.

We can conclude that both companies have room to grow and become profitibale if they are adequately managed.

Appendix 1

GrubHub - Ratio analysis	2019	2018	2017
Profitability analysis			
ROE	-1,26%	5,44%	
ROA	-0,84%	4,35%	
Fin. Leverage	1,51	1,25	
ROS	-1,41%	7,79%	14,49%
Assets turnover	0,59	0,56	
ROE decomposition: Traditional approach			
ROE = ROA x Fin.Leverage	-1,26%	5,44%	
ROE = ROS x Assets turnover x Fin.Leverage	-1,26%	5,44%	
Operating management: Profit margins			
Gross margin	48,52%	54,90%	60,55%
EBITDA	$ 109 166,00	$ 170 903,00	$ 141 598,00
EBITDA margin	8,32%	16,97%	20,73%
EBIT margin	-0,48%	8,44%	13,14%
Net margin (ROS)	-1,41%	7,79%	14,49%
Investment management: Operating working capital management			
Days' receivables	63,24	35,42	
Days' inventories	N/A	N/A	
Days' payables	7,29	6,69	
CCC	55,95	28,74	
Investment management: Non-current asset management			
Non-current assets turnover	1,36	3,17	
PP&E turnover	8,98	3,17	
Financial management: Liquidity analysis			
Current ratio	2,27	1,63	2,07
Quick ratio	2,27	1,63	2,07
Days' receivables	63,24	35,42	
Days' inventories	N/A	N/A	
Financial management: Solvency analysis			
Debt-to-equity	0,33	0,24	0,12
Interest coverage	-0,31	24,07	879,90
Net debt-to-EBITDA	1,07	0,76	-0,43

Appendix 2

STATEMENTS OF OPERATIONS
(in thousands, except per share data)

	2019			*2018*			*2017*	
	2019	***Trend***	***% Change***	***2018***	***Trend***	***% Change***	***2017***	***Trend***
Revenues	$ 1 312 151,00	192,10	92,10	$ 1 007 257,00	147,46	47,46	$ 683 067,00	100,00
Costs and expenses:								
Operations and support	675 471,00	250,68	150,68	454 321,00	168,61	68,61	269 453,00	100,00
Sales and marketing	310 299,00	205,86	105,86	214 290,00	142,17	42,17	150 730,00	100,00
Technology (exclusive of amortization)	115 297,00	204,93	104,93	82 278,00	146,24	46,24	56 263,00	100,00
General and administrative	101 918,00	156,74	56,74	85 465,00	131,44	31,44	65 023,00	100,00
Depreciation and amortization	115 449,00	222,67	122,67	85 940,00	165,75	65,75	51 848,00	100,00
Total costs and expenses	1 318 434,00	222,21	122,21	922 294,00	155,45	55,45	593 317,00	100,00
Income (loss) from operations	-6 283,00	(7,00)	(107,00)	84 963,00	94,67	(5,33)	89 750,00	100,00
Interest expense - net	20 493,00	20 091,18	19 991,18	3 530,00	3 460,78	3 360,78	102,00	100,00
Income (loss) before provision for income taxes	-26 776,00	(29,87)	(129,87)	81 433,00	90,84	(9,16)	89 648,00	100,00
Income tax (benefit) expense	-8 210,00	87,95	(12,05)	2 952,00	(31,62)	(131,62)	-9 335,00	100,00
Net income (loss) attributable to common stockholders	$ -18 566,00	(18,76)	(118,76)	$ 78 481,00	79,29	(20,71)	$ 98 983,00	100,00
Net income (loss) per share attributable to common stockholders:								
Basic	$ -0,20	(17,39)	(117,39)	$ 0,88	76,52	(23,48)	$ 1,15	100,00
Diluted	$ -0,20	(17,86)	(117,86)	$ 0,85	75,89	(24,11)	$ 1,12	100,00
Weighted-average shares used to compute net income (loss) per share attributable to common stockholders:								
Basic	91 247,00	105,74	5,74	89 447,00	103,65	3,65	86 297,00	100,00
Diluted	91 247,00	103,48	3,48	92 354,00	104,73	4,73	88 182,00	100,00

GRUBHUB INC.
Consolidated Statements of Comprehensive Income (Loss)
(in thousands)

	2019			*2018*			*2017*	
	2019	***Trend***	***% Change***	***2018***	***Trend***	***% Change***	***2017***	***Trend***
Net income (loss)	$ -18 566,00	-18,76	-118,76	$ 78 481,00	-18,76	-118,76	$ 98 983,00	100
OTHER COMPREHENSIVE INCOME (LOSS)								
Foreign currency translation adjustments	263,00	30,94	-69,06	-663,00	30,94	-69,06	850,00	100
COMPREHENSIVE INCOME (LOSS)	$ -18 303,00	-18,33	-118,33	$ 77 818,00	-18,33	-118,33	$ 99 833,00	100

Appendix 3

Delivery Hero - Ratio analysis	Fiscal 2019	Fiscal 2018	Fiscal 2017
Profitability analysis			
ROE	13,20%	-2,53%	
ROA	9,84%	-2,08%	
Fin. Leverage	1,34	1,21	
ROS	18,60%	-6,34%	-76,72%
Assets turnover	0,53	0,33	
ROE decomposition: Traditional approach			
ROE = ROA x Fin.Leverage	13,20%	-2,53%	
ROE = ROS x Assets turnover x Fin.Leverage	13,20%	-2,53%	
Operating management: Profit margins			
Gross margin	25%	52%	62%
EBITDA (in £m)	-550,80	-194,01	-189,50
EBITDA margin	-44,51%	-29,17%	-41,77%
EBIT margin	-52%	-36%	-52%
Net margin (ROS)	18,60%	-6,34%	-76,72%
Investment management: Operating working capital management			
Days' receivables	31,20	47,06	
Days' inventories	2,23	3,11	
Days' payables	125,30	173,83	
CCC	-91,87	-123,66	
Investment management: Non-current asset management			
Non-current assets turnover	0,87	0,55	
PP&E turnover	10,66	21,39	
Financial management: Liquidity analysis			
Current ratio	**1,54**	**2,68**	**3,44**
Quick ratio	1,52	2,67	3,43
Days' receivables	31,20	47,06	
Days' inventories	2,23	3,11	
Financial management: Solvency analysis			
Debt-to-equity	0,10	0,01	0,02
Interest coverage	68,94	ns	13,06
Net debt-to-EBITDA	0,92	1,76	3,15

Appendix 4

DELIVERY HERO - 2017-2019									
CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME									
			2019			***2018***			***2017***
EUR MILLION	***NOTE***	***2019***	***Trend***	***%Change***	***2018***	***Trend***	***% Change***	***2017***	***Trend***
CONTINUING OPERATIONS									
REVENUE	G 01	1237,6	272,8	172,8	665,2	146,6	46,6	453,7	100,0
COST-OF-SALES	G02	-926,4	533,6	433,6	-318	183,2	83,2	-173,6	100,0
GROSS PROFIT		**311,2**	**111,1**	**11,1**	**347,2**	**124,0**	**24,0**	**280,1**	**100,0**
MARKETING EXPENSES	G03	-495,2	191,8	91,8	-313,9	121,6	21,6	-258,2	100,0
IT EXPENSES	G04	-94,8	230,7	130,7	-54,3	132,1	32,1	-41,1	100,0
GENERAL ADMINISTRATIVE EXPENSES	G05	-373,5	171,1	71,1	-217,2	99,5	-0,5	-218,3	100,0
OTHER OPERATING INCOME	G06	19,9	79,6	-20,4	10	40,0	-60,0	25	100,0
OTHER OPERATING EXPENSES	G07	-6,7	98,5	-1,5	-9,2	135,3	35,3	-6,8	100,0
IMPAIRMENT LOSSES ON TRADE RECEIVABLES AND OTHER ASSETS	G07	-8,8	60,3	-39,7	-4,3	29,5	-70,5	-14,6	100,0
OPERATING RESULTS		-648,0	277,2	177,2	-241,7	103,4	3,4	-233,8	100,0
NET INTEREST RESULT	G08	-9,4	52,5	-47,5	2,8	-15,4	-115,4	-17,9	100,0
OTHER FINANCIAL RESULT	G09	93,7	-126,6	-226,6	18,8	-25,4	-125,4	-74	100,0
SHARE OF THE PROFIT OR LOSS OF ASSOCIATION ACCOUNTED FOR USING THE EQUITY METHOD	D. 03. E)	-99,7	-11077,8	-11177,8	-38,6	-4288,9	-4388,9	0,9	100,0
EARNING BEFORE INCOME TAXES		**-663,4**	**-204,2**	**-304,2**	**-258,8**	**79,6**	**-20,4**	**-324,9**	**100,0**
INCOME TAXES	G.10	-26,5	353,3	253,3	-18,3	244,0	144,0	-7,5	100,0
NET LOSS FOR THE PERIOD FROM CONTINUING OPERATIONS		**-689,9**	**207,6**	**107,6**	**-277,1**	**83,4**	**-16,6**	**-332,4**	**100,0**
NET INCOME FOR THE PERIOD FROM DISCOUNTINUED OPERATIONS		920,2	-5861,1	-5961,1	234,8	-1495,5	-1595,5	-15,7	100,0
NET RESULT		**230,2**	**-66,1**	**-166,1**	**-42,2**	**12,1**	**-87,9**	**-348,1**	**100,0**

Appendix 5

CASH FLOW ANALYSIS	2019	2018	2017
Excess Cash flow :	-432,4	-193,5	-225,8
Available Cash flow :	262,5	-201,7	-328,1
Free Cash flow :	262,5	-201,7	-328,1
Other Financing CF	-0,2	10,6	748,8
Net increase in cash and cash equivalent	262,3	-191,1	420,7

References:

Delivery Hero 2019 Annual Report: *https://ir.deliveryhero.com/download/companies/delivery/Annual%20Reports/DE000A2E4K43-JA-2019-EQ-E-00.pdf*

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