

WESTPEAK RESEARCH ASSOCIATION

Fitbit – Target (NYSE:FIT)

Google/Alphabet – Acquirer (NasdaqGS:GOOG)

Technology Hardware and Equipment – Electronic Equipment and Instruments

Will Google be able to dominate wearables?

December 6, 2021

Google acquired Fitbit, a pioneer of the fitness tracking market, at \$2.1 billion in November 2019 for \$7.25 per share in cash which represented a 30% premium on their market cap. This acquisition move was to bolster their wearables portfolio competing with earlier players like Apple, Samsung, and Huawei while aiming to make health and wellness more accessible to more people.

Fitbit Strategic Objectives

Fitbit forsees that joining Google will propel them to "innovate faster, provide more choices, and make even better products" in support of consumers' health and wellness needs. They hope to push their innovative limits by gaining access to Google's vast resources, knowledge, and global platform.

Google Strategic Objectives

Google hopes that the Fitbit acquisition will drive its ambitions for Wear OS, its software for android smartwatches including Samsung, Huawei, and more. Not producing its own wearables hardware prior, Google plans to innovate Fitbit at a faster level, make health more accessible, and compete against the market leader, Apple.

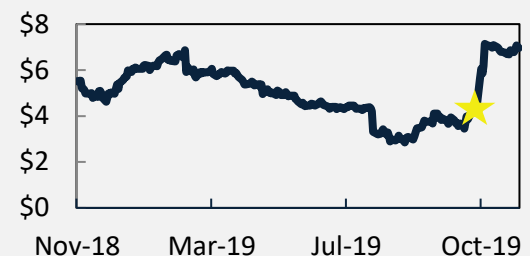
In midst of privacy and competition concerns, Google promised to protect Fitbit users' privacy and made a series of binding commitments with global regulators, confirming that health and wellness data will not be used for Google ads.

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Key Statistics - Fitbit

52 Week H/L	\$7.14/\$2.85
Market Capitalization	\$1,815M
Average Daily Trading Volume	N/A
Net Debt	-\$723M
Enterprise Value	\$1,407M
Net Debt/EBITDA	5.5x
Diluted Shares Outstanding	\$259.9M
Dividend Yield	N/A

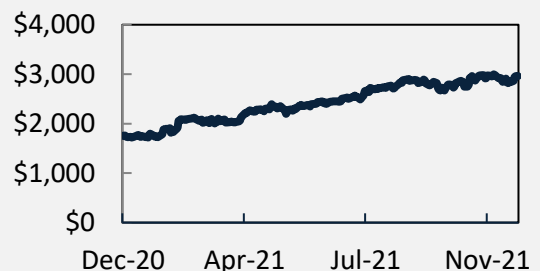
1-Year Price Performance



Key Statistics – Google

52 Week H/L	\$2966.80/\$1720.20
Market Capitalization	\$1,962,913M
Average Daily Trading Volume	1.2M
Net Debt	-\$109,251M
Enterprise Value	\$1,848,576M
Net Debt/EBITDA	-1.9x
Diluted Shares Outstanding	\$663.8M
Dividend Yield	N/A

1-Year Price Performance



Business Overview - Fitbit

Company History

In 2007, Fitbit, headquartered in San Francisco, California, was founded as a pioneer leading the American digital health and fitness wearables craze. Starting with little interest by James Park and Eric Friedman who self-raised \$0.4M from friends and family, Fitbit went on to secure \$66M in VC funding and IPO with a \$4bn valuation in 2015. They are continuing to grow with around 29M active users worldwide and selling more than 120M devices.

Revenue Breakdown

Fitbit sources revenue through their line of smartwatches, fitness bands, Fitbit Premium, smart scales, band accessories, and fitness gear. They offer a range of devices like Fitbit Charge (tracks basic health/fitness metrics), Fitbit Inspire (least expensive, only track workouts), Fitbit Ionic (smartwatch with fitness, music, payment features), and Fitbit Ace (tracks fitness/health for kids) from \$60 to over \$250 to capture diverse needs of their target consumers.



Figure 1: Fitbit Product Line

On the other hand, Fitbit also offers software and services (represented less than 2% of revenues in 2019) to engage users through the Fitbit online dashboard and mobile apps (visualize/sync data from devices), Fitbit Premium (paid subscription with coaching), and Fitbit Care (connected health platform for health plans, employers, and health systems).



Figure 2: Fitbit App

Past Acquisitions

Fitbit has made many acquisitions valued over \$48M into Twine Health, Coin, Vector Technologies, Vector Health, Switch2Health, Pebble and Fitstar. Notably, Fitbit leveraged Fitstar's fitness coaching features, Pebble/Vector Watch's smartwatch products, and Coin's wearable payment features to strategically grow and integrate technical offerings. This was fueled by market pressure from cheaper brands from China and consumers' preference of an all-encompassing smartwatch from Apple, Samsung, Xiaomi over Fitbit's focus on simpler health/fitness bands.

Google - Acquirer

Company History

Google was founded in 1998 by two Stanford University students, Larry Page and Sergey and is based in Mountain View, California. They are a subsidiary under the holdings company Alphabet Inc. Google mainly operates a search engine to help the public access organized information and have grown to be a world leader in online advertising, cloud computing, software, and hardware solutions. In 2004, Google went to IPO with a valuation of \$23bn. Today, Google is worth \$1978bn and employs 0.14M workers across the world.

Revenue Breakdown

Their numerous products/services include applications, such as Search, Maps, Translate, Chrome, YouTube Music, cloud platform, chromecast, google play movies and TV, YouTube, Pixel 3, Connect Home, Pixel Slate, Google Wifi, Android OS, Wear OS by Google, and Chromebook. Google also sell devices, including laptop, phone, speakers, and voice control multiple compatible devices. Moreover, it offers advertising services through Google Ads, AdSense, and Analytics.

Industry Analysis

According to Grandview Research, the global fitness tracker market size was valued at \$34.6bn in 2020 and is expected to grow at a compound annual growth rate (CAGR) of 18.9% from 2021 to 2028. The smartwatch segment accounted for 48% of revenue while the fitness band segment trailed behind but is estimated to grow the fastest due to its lower costs. Compared to fitness bands, smartwatches provide communication with smartphone notifications & calling features, acting as a phone on the wrist on top of basic fitness & health tracking features.

Key Trends

- **Rising health & fitness awareness**
 - With more time spent at home, COVID-19 prompted unexpected lifestyle changes along with unhealthy diet habits. This accelerated the health & fitness awareness among younger adults and working-class population, who are the target customers for fitness trackers.
- **Growing penetration of the internet & smartphones**

- Most of the world's population transitioned to remote work or schooling which further drove the adoption of the internet & smartphones. As more users became more aware of fitness devices, industry players fought to capture market share and growing demand through continuous development & innovation and providing a diverse range of price/type of devices.
- **Increased consumer disposable income levels**
 - In Canada, disposable income for the lowest-income households increased 36.8% over the first three quarters of 2020. This was due to the value of government COVID-19 support surpassing lost salaries.
 - Despite the US economy contracting 3.5% in 2020, disposable income grew rapidly due to unemployment insurance, stimulus checks, and support for small businesses. As well, lower interest rates fueled strong spending on new homes, vehicles, and recreational goods which offset some of the reduced spending on services and businesses.

Competitive Landscape

Apple

Since its 2015 launch, the Apple Watch immediately dominated the market with its brand power, collection of smartphone apps which were not available on traditional brands Fitbit/Pebble, and influential design collaborations with Hermes, Coach, and Nike. In February 2021, it was estimated that 10% of iPhone users also owned an Apple Watch which spoke to the power of Apple's ecosystem and the network effects it held. Moreover, Apple's brand power allows them to enjoy higher gross margins with one watch ranging from \$400 to over \$1,000 depending on options, case style, band style, and more. This is a stark contrast from a Fitbit retailing around \$300, Samsung from \$200-400, and Huawei and many smaller brands being cheaper.

Huawei

Huawei debuted its first Huawei Watch in 2015 utilizing Google's Wear operating system. It has strongly competed through its design and technological expertise (ultra-long battery life, customized features for over 100 sports). Huawei hopes to break into the Apple-dominated wearables market in the West but faces restrictions due to security concerns from the US government.

Samsung

The Samsung Watch prevailed in the wearables market when it was released in 2013 with few competitors at the time. However, they were quickly overtaken by the release of the Apple Watch. Samsung continues to fall behind Apple in the number of apps available on their watches, operating system, and design.

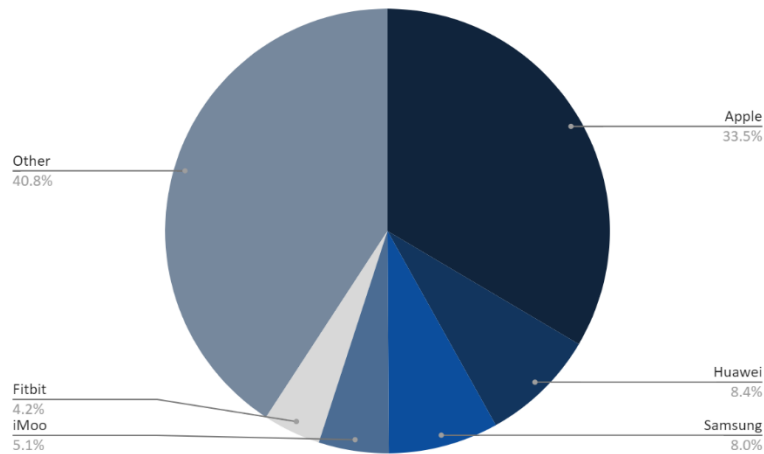


Figure 3: 2021 Smartwatch Market Share

M&A Rationale

Strategic Objectives

With Fitbit's struggle in the recent years to capture market share against the growing popularity of Apple Watch, Google can be the catalyst to attract consumers with next-level and affordable innovations. At the same time, Fitbit will provide Google access to an established brand with a solid product line, strong hardware foundation in wearables, and respectable market penetration to compete against Apple. Moreover, this 2.1bn deal was a great opportunity to use its cash balance of \$121bn towards the rapidly growing wearables and health technology space.

Synergies

When the deal was announced in Oct 31, 2019, Fitbit shares rose 14% and Alphabet were up roughly 3%. This spoke highly to positive investor expectations towards potential synergies derived from this merger. Prior to the deal, Alphabet did not have a clear competitive standing in consumer-facing health products compared to Apple (Apple Watch) and Amazon (prescription delivery, health clinics, and health information through Alexa). Fitbit's wearables will play on Google's strength in collecting and synthesizing data to deliver personalized Internet services. In addition, Fitbit can utilize Google's strong portfolio among AI, software, and hardware to spark innovation in wearables and build more products to benefit more people around the world. Furthermore, this deal will allow Google to expand their Wear OS software and introduce Made by Google wearable devices into the market. Google can also integrate features like Google Assistant and Wear OS into Fitbit models to reinforce their product ecosystem.

Valuation

The Nov 2019 acquisition by Google saw Fitbit valued at \$2.1 billion with shareholders receiving \$7.35 per share in cash. Fitbit's stock performance has been far from great, staying below \$7 from 2017 to 2019, even reaching as low as \$2.81 in

Aug 2019, despite previous highs of \$50 in summer 2015. In 2018, Fitbit reported \$1.51bn revenue which represented a YoY decrease of 6.7% and their third year of decline. Still, the user base grew 9% during the year to 27.6MM but not as fast as their competitors. With news of the acquisition, Fitbit's stock price reached \$7.14 per share on Nov. 1, 2019, and closed at \$6.51 per share on Jan. 13, 2020.

Comps

Referencing Figure 5 in the Appendix, six companies: Apple, Xiaomi, Garmin, Fossil, Zepp Health, and Nautilus were selected as competitors in the fitness tracker/smartwatch space. A range of larger players like Apple, Xiaomi, Garmin who operate in multiple industries and smaller players like Fossil, Nautilus, and Zepp Health with a focus on fitness trackers were chosen to reflect a balance for Fitbit's valuation. The LTM EV/Revenue multiple was adjusted to the Sep. 30, 2021 period before the announcement in November to remove any influence that could skew the data. The calculated median share price reflected a \$4.44 share price for Fitbit which was a 16.5% increase compared to their actual price of \$3.81. Google's acquisition placed Fitbit at a 92.9% premium paying \$7.35 per share.

Risks

Privacy

According to Internet Society and Consumers International, 69% of consumers are concerned about how personal data is collected in mobile apps with governmental bodies beginning to regulate this. During the 2019 acquisition, there were widespread concerns from existing Fitbit users on how their data would be utilized and backlash from the public and regulators. To mitigate this risk, Google promised that Fitbit data will not be used to sell ads and that users will be able to review, move or delete their health data. If Google were to go back on their words or new privacy regulations are introduced that would impede on their strategic objectives, there would be negative brand reputational and financial impacts.

Competition

Amazon, Apple, Facebook, Google, and Microsoft have a combined value of over \$8 trillion and are the five largest companies in the United States. Public scrutiny against Big Tech companies' strong influence raised antitrust concerns. At the time, Google/Fitbit deal raised concerns to competitors in the wearables market. Although the deal was eventually passed by the EU, new competition regulations might place Google on the map again to face reputational or financial damages.

Appendix

Comparable Company Analysis

As of Sept 30, 2019

Figures in MM USD

Company	Share Price	Diluted Shares Outstanding	Equity Value	Cash	Debt	Other EV Adjustments	Enterprise Value	LTM Revenue	LTM EV/Revenue
Apple Inc. (NasdaqGS:AAPL)	\$ 55.99	18,125.6	1,014,851.2	50,530.0	108,418.0	-	1,072,739.2	260,174.0	4.1 x
Xiaomi Corporation (SEHK:1810)	\$ 1.13	23,821.3	26,918.1	5,572.5	2,590.1	-	23,935.7	30,386.1	0.8 x
Garmin Ltd. (NYSE:GRMN)	\$ 84.69	190.1	16,099.6	976.4	56.3	-	15,179.5	3,587.4	4.2 x
Fossil Group, Inc. (NasdaqGS:FOSL)	\$ 12.51	50.5	631.4	147.5	621.1	-	1,105.0	2,293.1	0.5 x
Zepp Health Corporation (NYSE:ZEPP)	\$ 10.00	61.5	614.8	269.7	17.3	-	362.4	772.3	0.5 x
Nautilus, Inc. (NYSE:NLS)	\$ 1.35	29.7	40.1	5.8	43.9	-	78.2	366.3	0.2 x
Fitbit, Inc.	\$ 3.81	259.9	990.2	287.4	94.0	-	796.8	1,511.5	0.5 x
Median									0.6 x
Mean									1.7 x
High									4.2 x
Low									0.2 x
Median									\$4.44
Mean									\$10.73
High									\$25.35
Low									\$1.99

Figure 5: Fitbit Comparable Company Analysis

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