



MercadoLibre

David Gardner | February 18, 2009

CURRENT PRICE: [MELI](#) \$ 971.44 ↑ \$ 17.67 (1.9%) Cập nhật vào 18/02/2009

Why Buy:

- It held off eBay on its home turf, turning a potential rival into an ally.
- User fees bring in revenue at every step of the online shopping process, giving MercadoLibre many ways to benefit from growing Internet use.
- The formerly sky-high stock has returned to earth, and the market is now underestimating the growth potential ahead.

What It Does

The eBay of Latin America runs an auction site and online payment system.

Key Company Data

Headquarters: Buenos Aires, Argentina

Website: www.mercadolivre.com

CAPS Rating: 4 Stars (62.22 out of 100)

Sign of a Breaker: True Rule Breaker

Market Cap: \$711.0

Cash/Debt: \$30.9 / \$18.5

Revenue (TTM): \$130.5

Earnings (TTM): \$16.2

Revenue (2005-07): \$28.2 / \$52.1 / \$85.1

Earnings (2005-07): \$2.4 / \$1.1 / \$9.7

Recent Price: \$16.05

Data as of 2/13/09

Dollar amounts in millions except recent price.

If you want to buy a *bicicleta* in Brazil or unload some used *accesorios* in Argentina, you can find a good deal or make a little money online. But if you can control the marketplace that connects millions of buyers and sellers, you've got a great deal that can make a lot of money. Sellers want to go where the customers are, and buyers want to go where the goods are. Each new user adds value for every other user -- a network effect that magnifies the growth potential for customers and investors alike.

That's how **eBay** ([NASDAQ: EBAY](#)) rose to the top. By gaining scale early on, the world's premier online auction site became the place to be. And that's the story behind the success of **MercadoLibre** ([NASDAQ: MELI](#)). The eBay of Latin America, like its U.S. counterpart, offers online auctions as well as fixed-price sales (think Amazon.com), local classifieds (à la Craigslist), and a payment service (like eBay's PayPal). With a phenomenal track record of adding users, transactions, and revenue over the past decade, it's little surprise this company has smothered the competitors that have tried to challenge it.

Sniping eBay

What is perhaps surprising is that eBay itself was one of those challengers to admit defeat. As with **Gmarket** ([UNKNOWN: GMKT.DL](#)) in South Korea, eBay couldn't gain traction on MercadoLibre's home turf. Instead, it decided back in 2001 to sell its Brazilian subsidiary for a stake in MercadoLibre. It still owns 18% and acts like a mentor, letting MercadoLibre turn a possible rivalry into a competitive advantage. eBay learned the hard way that it needed a payment platform, so MercadoLibre knew to start MercadoPago; eBay recognized the threat of online classified ads, so last year MercadoLibre acquired a local version of Craigslist, TuCarro.

MercadoLibre makes money throughout the transaction cycle. It collects a fee when users list items for sale and another when each sale is made. Buyers and sellers who use MercadoPago, its PayPal-like online payment service, pay another fee. Altogether, about 70% of revenue comes from auction listings and sales, 18% from MercadoPago, and the rest from online ads.

There's still plenty of opportunity ahead: Only about 10% of users pay through MercadoPago. By comparison, eBay has reached 63% penetration with PayPal -- indeed, PayPal is consistently the bright spot in eBay's business. By gaining ground here, MercadoLibre can expand the top and bottom lines regardless of how fast the core auction business grows. Of course, that's growing rapidly as well. Moreover, the business is wonderfully scalable. Fixed costs don't change much as the market grows, so the operating margin stays high -- and the pesos, reals, and bolivars keep flowing to the bottom line.

Buy It Now

So is MercadoLibre cheap? Well, it's a lot cheaper than it was a year ago, when the stock traded close to \$80 a share, for a forward P/E of more than 200. Yet for the most part, despite the sinking economy, the company has lived up to those high expectations -- revenue was on track to grow an estimated 63% in 2008, about the same pace as in 2007. The number of registered users climbed 36% in 2008, also keeping up with the swift pace of growth.

MercadoLibre is young and has only been consistently profitable and cash-flow positive since 2005, so it still has a pretty steep P/E. Its prospects aren't much different from the high-flying optimism that ruled last year, but now you can invest for "only" about 28 times forward earnings.

Admittedly, that price assumes continued healthy growth. Internet use is still gaining ground in Latin America, and transactions are on the rise, so there's every reason to believe MercadoLibre will deliver. A relatively conservative discounted cash flow analysis -- assuming growth of a little more than half the heady 56% annual rate analysts expect over the next five years -- suggests MercadoLibre is about fairly priced at today's \$16. I think it can do better than that simply because its network effect business model can command extraordinary growth over a long period.

That same success shows up in the company's management team, which combines effective stewardship with a shareholder-friendly philosophy. CEO Marcos Galperin is a major owner, with 13% of the company he started a decade ago. Galperin takes a relatively modest salary and doesn't dole out many options to himself or to any of the top 10 execs, who have all been with the company since 2000.

Risks

MercadoLibre gives you exposure to Brazil, a nation fast emerging as a global economic force with above-average growth even in today's tough economy. That should keep real wages on the rise and help MercadoLibre's business. But we're still counting on growth from a less-proven region: About 59% of revenue came from Brazil in 2007, which, like Argentina (15%) and Mexico (12%), presents economic and currency risks. The company reports its results in dollars and houses the servers that are the backbone of its business here in the United States, but it's always worth watching the political and financial news abroad.

No high-P/E company can avoid valuation risk. MercadoLibre is priced for growth, which is to say it's priced for the future. If investors become even more pessimistic, they'll be inclined to bid the price down. But I think we're already pretty well weighted on the side of pessimism, and the market's expectations for MercadoLibre are realistic -- and probably understated.

Foolish Bottom Line

Latin America's eBay still has a long way to go to catch up to its U.S. counterpart. If you want to roll back the clock on one of the best investment opportunities of the past decade, here's your chance. For a price that represents relatively modest downside risk, you can buy into extraordinary growth protected by a strong network effect that has locked out major competition. Add exposure to Brazil's emerging economy and the fast-growing reach of the Internet in Latin America, and MercadoLibre is a growth story that will continue long after the auction clock hits zero.

David owns shares of Amazon.com.



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Market data provided by FactSet and Web Financial Group.