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Out of gas

Never mind sex, data breaches, intellectual-property jiggery-pokery, the sabotage of the competition, the harassment of the press, cultural-sensitivity deficits, the "Susan Fowler PR problem" or the disgraced, yet rich and now very liquid, founder Travis Kalanick himself: The trouble with Uber is that it has lost money, it is losing money and it will lose money. That's the nature of its business model.

So said we one year ago (Jan. 27, 2017). We return to Uber because our newfound interest in SoftBank Group Corp. (*Grant's*, Dec. 15, 2017) makes that topic timely again. Our contention, for which we gratefully acknowledge the inspiration of the independent airline guru Hubert Horan, is that Uber is unfixable. Under a new CEO—Dara Khosrowshahi, the former head of Expedia, Inc. (see page 4)—the ride-sharing unicorn is on a cost-cutting mission. It's not the answer.

For the complete analysis, read Horan's new monograph, "Will the Growth of Uber Increase Economic Welfare?," in volume 44 of the *Transportation Law Journal*. The short-form version begins with the proposition (so far unchallenged, the author reports) that Uber loses money because it has no cost advantage over the legacy taxi model it seeks to disrupt. From our year-ago story:

> The major costs to get a passenger from point A to point B are the same for both Uber and the legacy cabs, [Horan] says. Fuel and fees are the same, yellow cab or black sedan. Wages? Uber has to offer enough to attract new drivers. Car ownership and maintenance? Uber drivers bear those costs. And then there's corporate overhead. Though it grabs 20% to 25% of each fare, Uber Technologies is [still] losing money. In short, Horan argues, an Uber driver can never match the taxi companies' economies of scale: "Uber not only lacks the major cost advantage that a company seeking to drive incumbents out of business would be expected to have, but actually has higher costs than traditional car service operators in every category, except for fuel and fees where no operator can achieve a cost advantage.

As you've been reading, SoftBank last month paid $6.5 billion to acquire Uber shares from existing stockholders and employees at a $48 billion valuation, a 30% discount from the previously quoted $69 billion valuation. A stroke of value-investing genius? The insiders reportedly queued up to sell many more shares than SoftBank was prepared to buy.

You can't say that the new broom isn't trying to sweep clean. This is the year that Uber was planning to move into hip new headquarters in Oakland, Calif. (*Grant's*, Feb. 24, 2017). Khosrowshahi rather sold the 1929-vintage, Beaux Arts–style vanity tower for $180 million. Might he also raise fares? You'd need at least a 40% boost to generate net income, Horan speculates. Lyft, and the yellow cabs, too, would likely be the gainers by that radical gambit.

At the top of the 2019 Uber corporate agenda is an IPO, according to press speculation. What might entice a profit-seeking investor to buy is a question without an obvious answer. "True GAAP P&L losses have steadily increased from $2.5 bn. in 2015 to probably $4 bn. in '16 to likely $5 bn. in '17 (based on 2/3Q losses of $2.5 bn.)," Horan advises *Grant's* by email. "No VC startup in history lost $2.5 bn. in year 6 and then doubled those losses in year 8."

To stanch the red ink, Khosrowshahi sold Xchange Leasing, Uber's loss-making U.S. subprime auto-leasing business. He hired Barney Harford, the former CEO of Orbitz.com, as chief operating officer, with instructions to slash spending. He replaced the decorative video presentations of Uber's former 14 cultural values (e.g. "always be hustling") with photos of the drivers whom Uber used to say it couldn't wait to swap for autonomous vehicles.

"There are undoubtedly a bunch of short-term moves Uber could make to reduce the financial bleeding (sell off overseas operations, stop spending on long-term pipe dreams like driverless cars, cut back on operating subsidies)," Horan comments, "but these are incredibly unlikely to get the company anywhere near breakeven, and would destroy the remaining fantasies about long-term profitable growth that a future IPO would depend on. All steps to repair damaged driver relations in 2017 directly increased losses. Their strong customer support was entirely based on uneconomically low fares, and any moves to significantly increase prices would kill off this support."

According to a Dec. 21, 2017 report on CNET.com, Uber's self-employed drivers earn not much more than $15 an hour, hovering near the minimum wage, after the necessary deductions for the cost of oil and gas, insurance, maintenance and depreciation. According to an April survey by The Information, only 20% of 2.5 million Uber drivers across 75 countries said they planned to stick with the company for more than a year.

SoftBank invested not only the aforementioned \$6.5 billion at a \$48 billion valuation but also \$1.25 billion at the previous \$69 billion valuation. The \$7.7 billion grand total makes Uber the largest investment in SoftBank's nearly \$100 billion Vision Fund. A \$5 billion commitment to Didi Chuxing, the Chinese version of Uber, makes the structurally unprofitable ride-sharing business Vision's largest exposure to any single industry, at more than 10% of assets. Recall, please, that \$40.4 billion of the roughly \$100 billion committed to the Vision Fund takes the form of 7% preferred stock. How to pay that substantial dividend? Not with loss-making assets. Such facts make us no less bearish on SoftBank.

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