



Wealthpin **Pro**

SEPTEMBER 2023

Welcome to this month's edition of Wealthpin Pro!

Let's get right to the pick, shall we?

TRADE IDEA:

MERCADOLIBRE INC (NASDAQ: MELI)



mercado
libre

PRICE AT PUBLICATION: \$1381.69

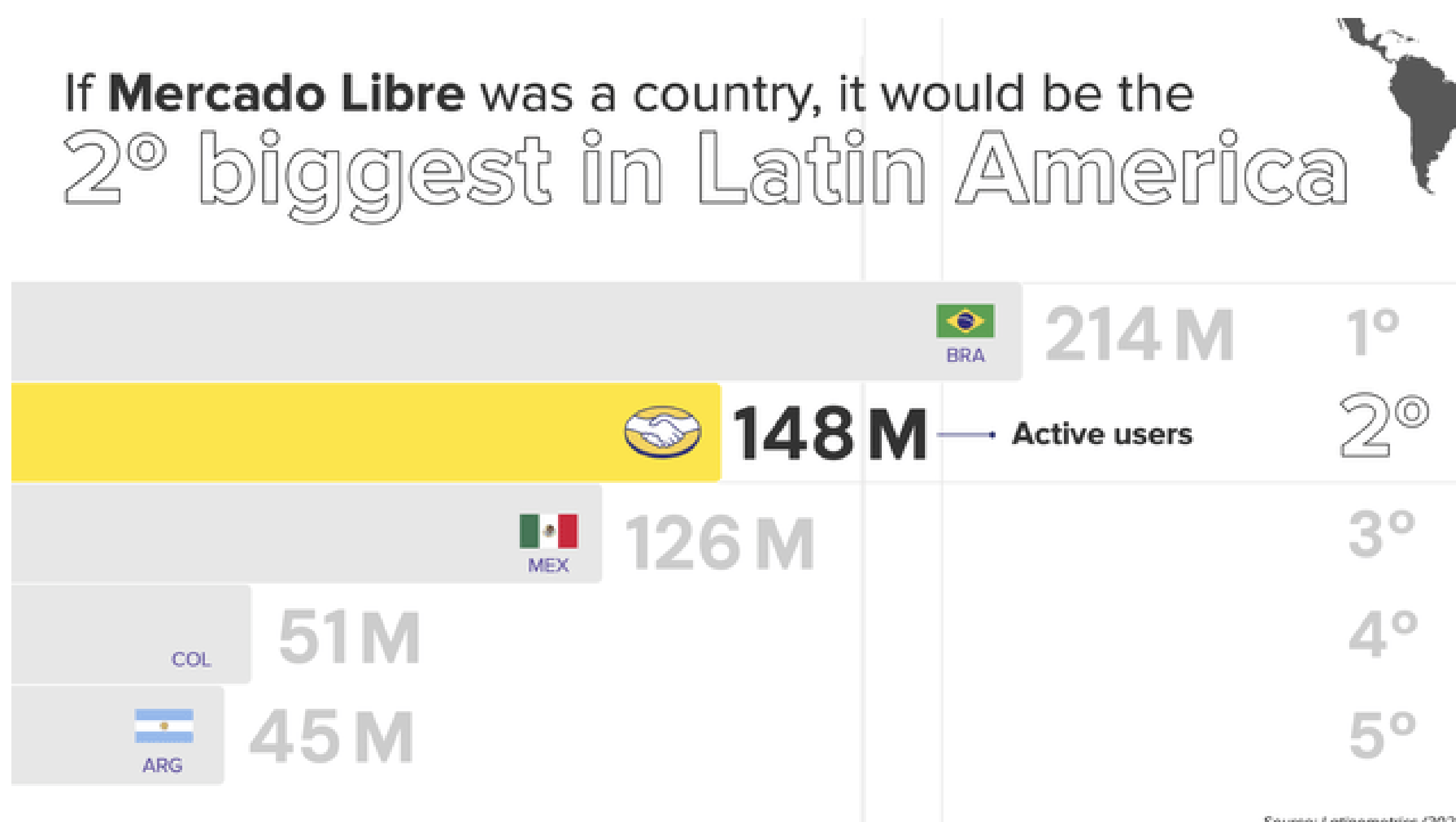
MARKET CAP AT PUBLICATION: \$69.2 BILLION

52-WEEK RANGE: \$754.56 - \$1,451.56

MercadoLibre (NASDAQ:MELI), often dubbed the "Amazon (AMZN) of Latin America" could be on the biggest growth prospects of the next decade. Let's dive in so I can show you why.

Mercado Libre's Business Overview

MELI's Scale in Perspective (MELI investor presentation).



Established in 1999 in Argentina, MercadoLibre has been a pivotal force in the e-commerce sector for over twenty years. In recent times, the firm has witnessed a remarkable expansion in its user base, amassing 148 million users as of 2023. To give you a sense of its magnitude, this user base would constitute the second largest nation in Latin America, as per the company's own analysis.

Fundamentally, MercadoLibre operates as an e-commerce behemoth. However, similar to Amazon, it has ventured beyond its original domain, branching into numerous related sectors such as logistics, advertising, financial services, insurance, and more, which we will delve into in subsequent sections. The diverse range of services provided, along with their rapid expansion, has catapulted MercadoLibre's revenue to soaring heights, mirroring the steep ascent of a hockey stick graph.

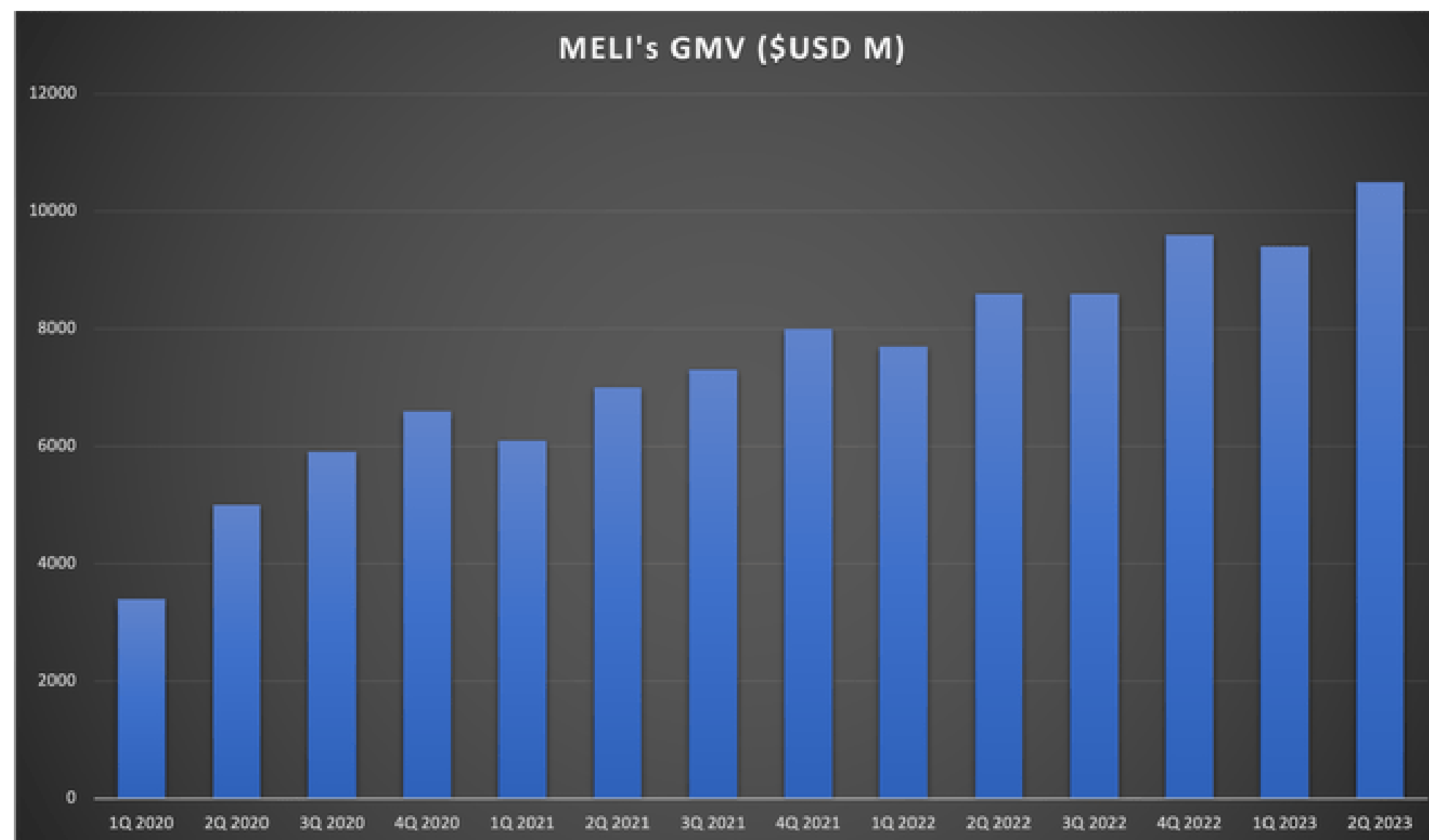
The decade-long revenue chart depicted above bears witness to its thriving trajectory. Indeed, this meteoric rise might render MercadoLibre's market valuation somewhat lofty by certain standards. Nonetheless, a significant segment contends that this valuation is warranted, even amidst signs of a slowing economic climate in Latin America.



Visualizing the Growth Trajectory

The surge in revenue is undeniably striking, but a more nuanced analysis of the income statement is necessary to fully grasp the underlying strength of this enterprise. Investors should keep a close eye on three pivotal areas that MercadoLibre identifies as their Key Performance Indicators (KPIs), a staple in their investor communications.

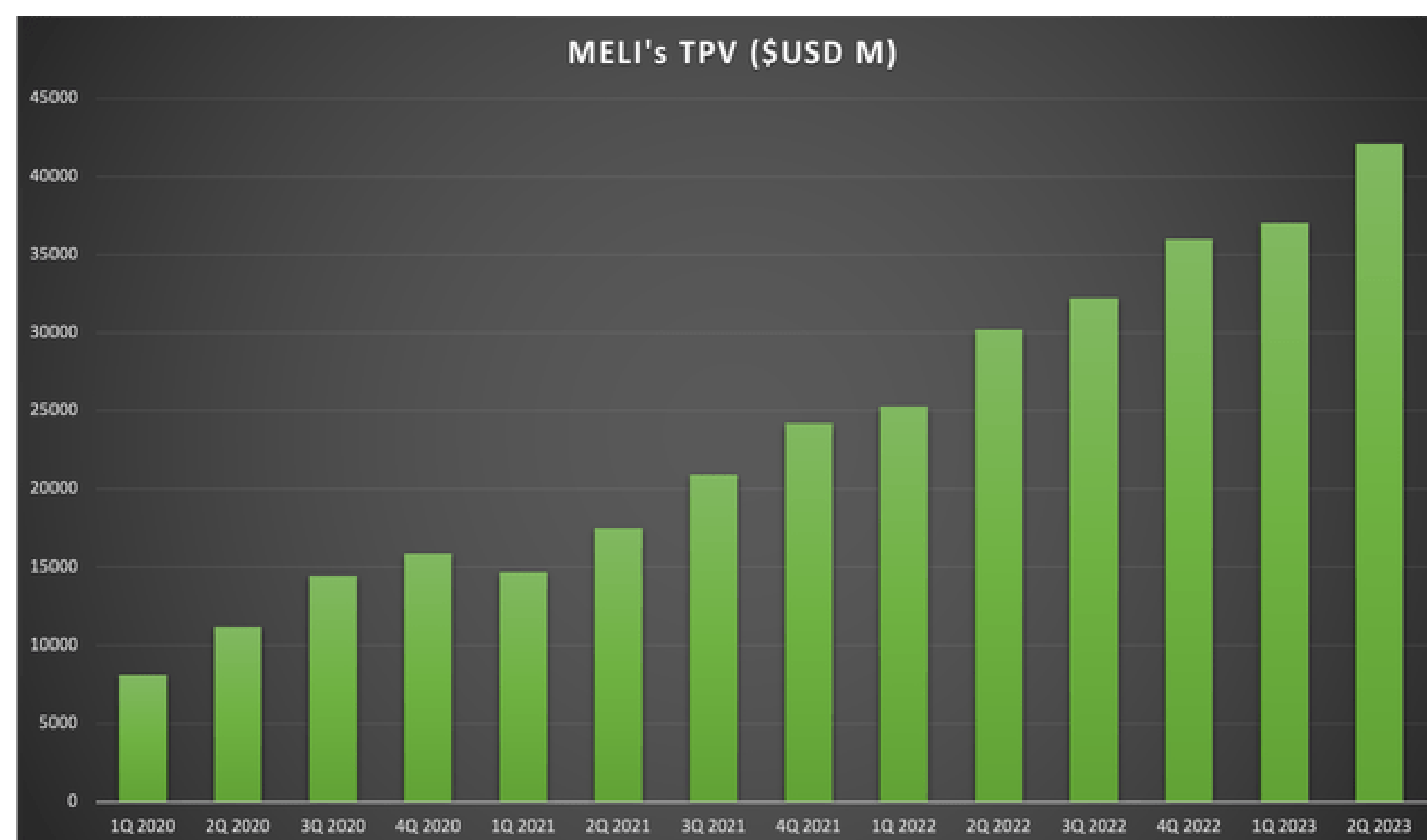
MELI GMV



(Image courtesy of Ash Anderson)

Topping the list is GMV, or Gross Merchandise Volume, denoting the cumulative value of goods transacted on the platform. A brief overview of its recent trends showcases an admirable growth trajectory.

MELI TPV

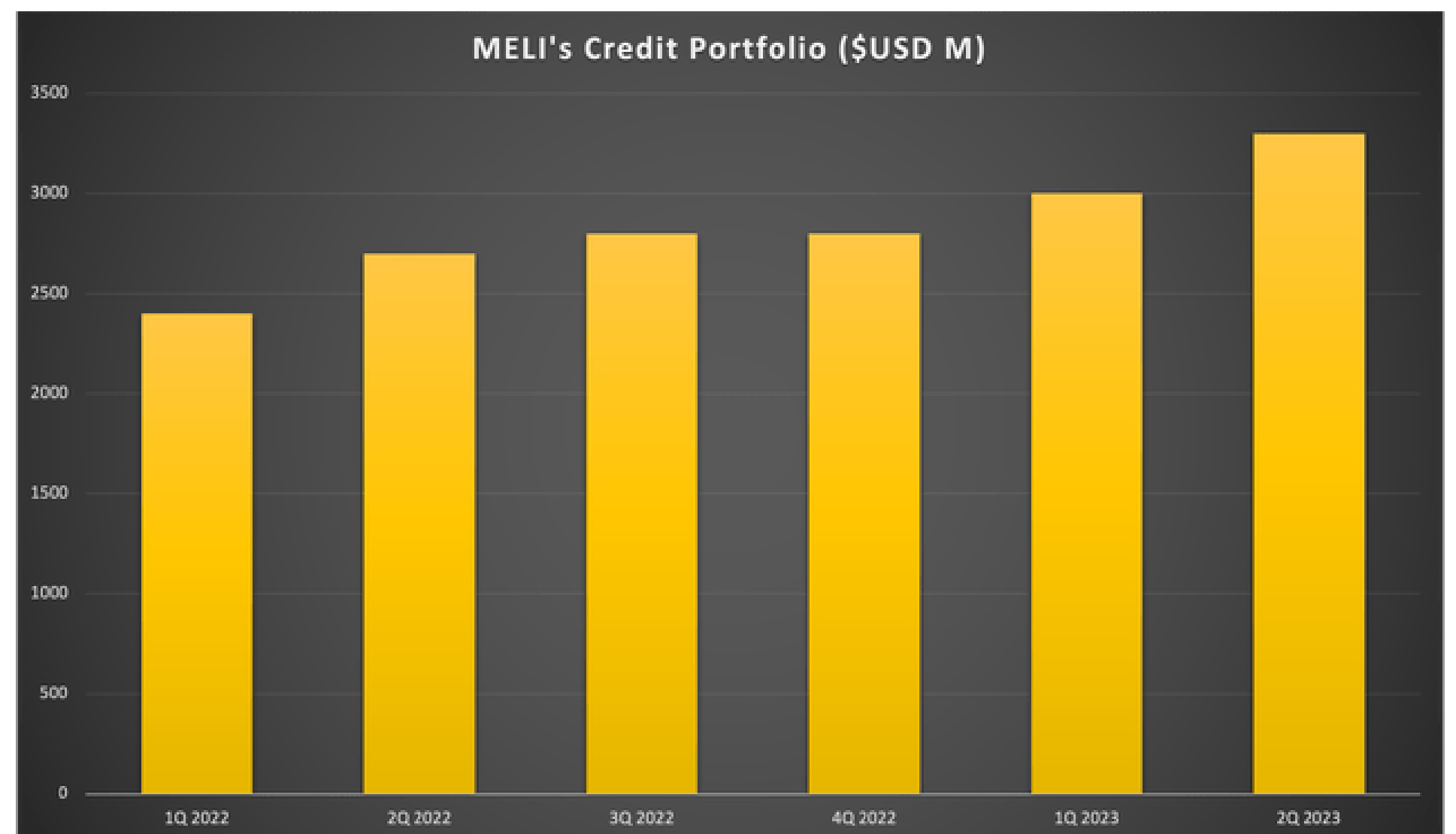


(Image courtesy of Ash Anderson)

Next, the TPV, or Total Payments Volume, graph sheds light on the expansion of Mercado Pago, the company's payment gateway. While the firm delineates this metric into on/off network transactions, a comprehensive perspective reveals a graph that is nothing short of astounding. Over a year, a 39.4% swell in volumes has been observed, hinting at an accelerating growth pace.

MELI's Credit Portfolio

Lastly, we turn our attention to the firm's credit portfolio. Although the data available is somewhat restricted, it still demonstrates a 22% annual growth. A closer examination indicates that this portfolio encompasses merchant credit (\$707M), consumer credit (\$1.795B), and credit cards (\$748M), with respective growth rates of 2.5%, 21.9%, and 42.5%.



(Image courtesy of Ash Anderson)

What implications does this hold? Merchant credit facilitates businesses on the platform, aiding them in inventory procurement, payroll management, and other vital functions. The "Consumer" segment operates akin to a deferred payment scheme, while the credit card segment is self-explanatory. Predominantly, MercadoLibre manages this credit portfolio, capitalizing on insights gleaned from its vast sales and transaction network.

Now that we've provided a panoramic view of the corporation, let's now delve into the finer details.

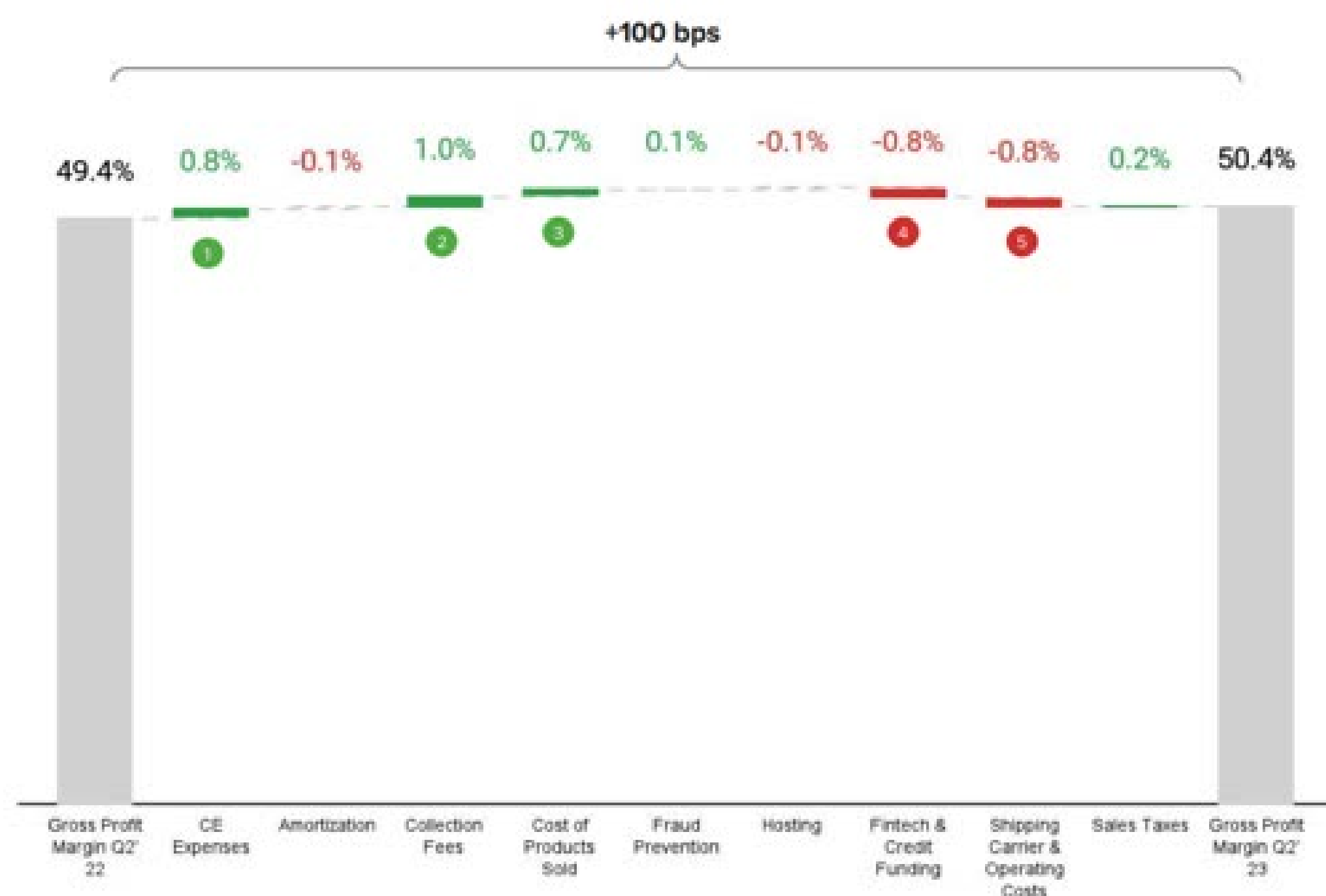
A Staggering Bottom-Line Performance In the Year's Second Quarter



MercadoLibre posted stellar financial outcomes, marked by vigorous revenue augmentation, adept cost stewardship, and a notable uptick in profitability. The firm announced a consolidated net revenue of \$3.4 billion, a 31.5% increase year-over-year, primarily fueled by the e-commerce division which registered a significant 37.9% growth year-over-year, spearheaded by strong showings in Mexico and Brazil.

2023' & 2022' USD M	Brazil		Argentina		Mexico		Others		Total	
	2023	2022	2023	2022	2023	2022	2023	2022	2023	2022
Commerce Services ⁽¹⁾	846	641	243	200	393	232	102	82	1,584	1,155
Commerce Products Sales ⁽¹⁾	203	111	59	70	82	58	8	10	352	249
Total Commerce Revenues	1,049	752	302	270	475	290	110	92	1,936	1,404
Fintech Services ⁽¹⁾	462	384	296	202	67	34	46	28	871	648
Credit Revenues ⁽¹⁾	263	307	172	120	159	101	2	1	596	529
Fintech Products Sales ⁽¹⁾	6	8	1	2	2	3	3	3	12	16
Total Fintech Revenues	731	699	469	324	228	138	51	32	1,479	1,193
Total Net Revenues	1,780	1,451	771	594	703	428	161	124	3,415	2,597

However, it is pertinent to acknowledge the increase in the cost of goods sold (COGS), amounting to \$1.7 billion, indicative of investments in fulfillment infrastructure and financing expenditures. Despite this, the company managed to secure a gross margin of 50.4%, surpassing revenue growth rates. Operational costs, encompassing SG&A and R&D, were adeptly handled, enhancing profitability.



Expenditure on provisions, notably the Provision for Doubtful Debts (PDD), has decelerated as the credit sector shows signs of recovery. However, lingering apprehensions remain about the 90-day Non-Performing Loans (NPL) figure and its prospective repercussions on forthcoming expenditures. MercadoLibre posted a notable EBIT margin of 11.2%, propelled by substantial gross margin advancements and judicious cost control.

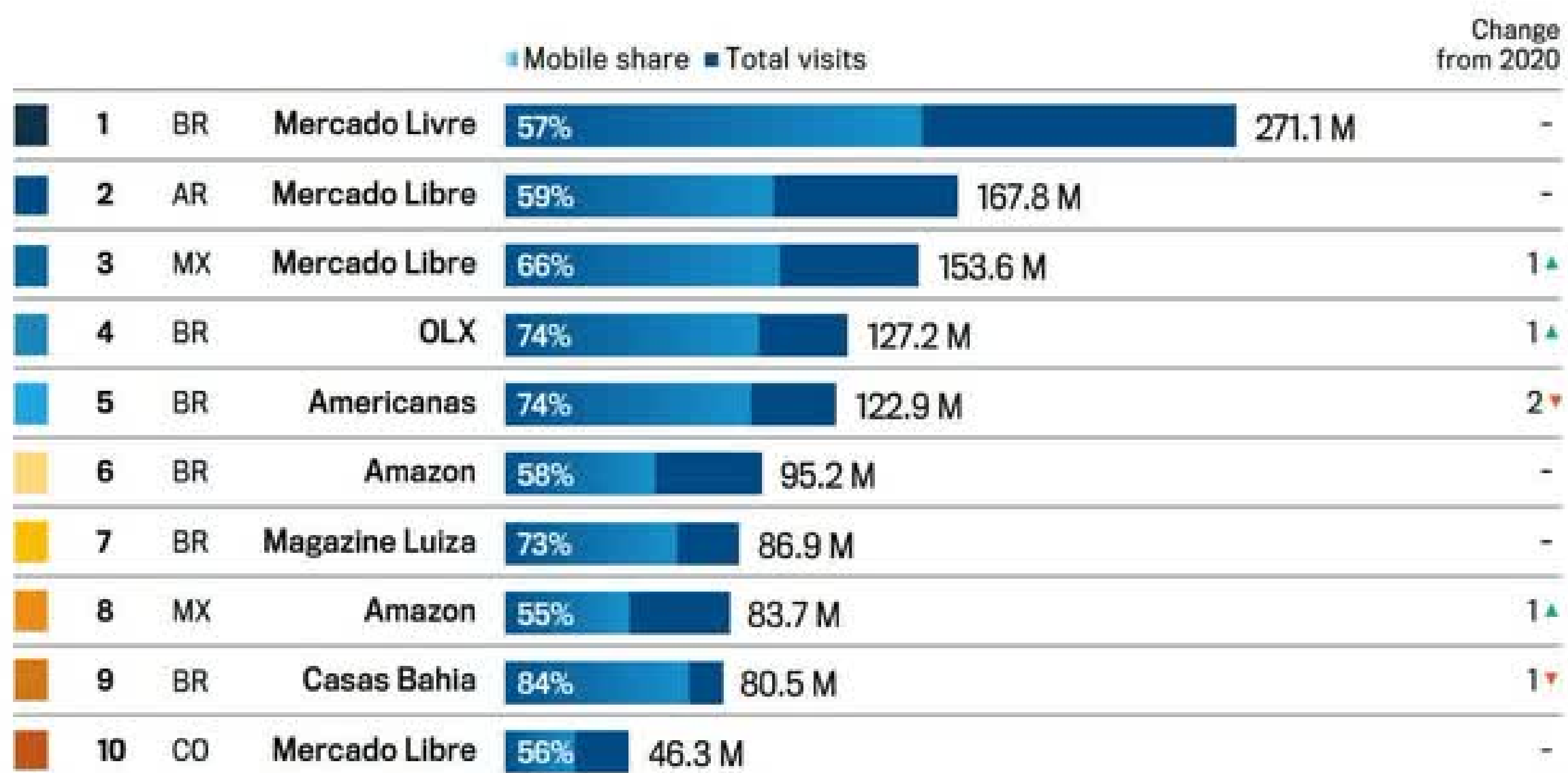
Yet, the economic climate in Argentina, chiefly characterized by foreign exchange setbacks, has somewhat mitigated these advancements. In spite of these hurdles, the firm announced an extraordinary 113% annual profit escalation, amounting to \$262 million. The Q2 outcomes of MercadoLibre illustrate its vigorous growth pattern, fiscal prudence, and operational supremacy, cementing its status as a frontrunner in the Latin American e-commerce sector.

Leading the Charge in Latin American E-commerce

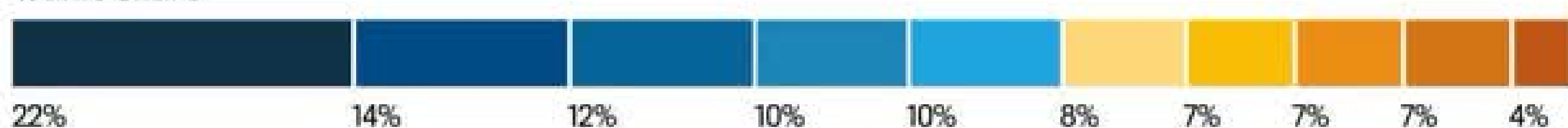
MercadoLibre reigns supreme in the Brazilian e-commerce sphere, accounting for roughly 33% of traffic across its digital platforms. It successfully seized market share from Americanas, a Brazilian retailer grappling with bankruptcy as of late 2022. Sea Limited's (SE) Shopee — another competitor — maintains a firm foothold with over 20% market share, demonstrating consistent stability. Meanwhile, Shein has been on an upward trajectory, securing over 15% of the market share.

Who is leading the race

The top 10 e-commerce websites in Latin America¹

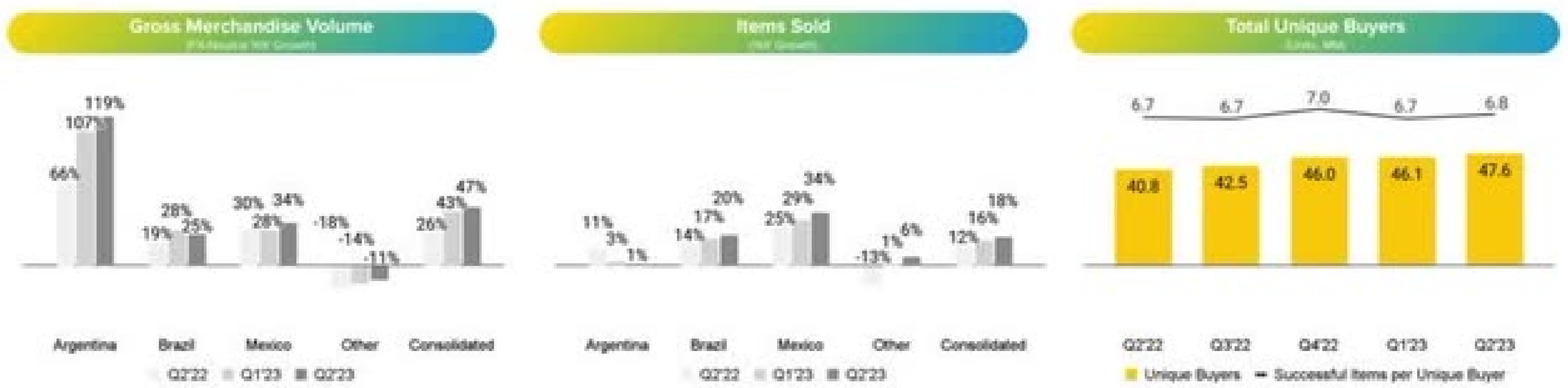


Traffic share



Source: Atlantic's recent LATAM State of Digital 2023 Report

MercadoLibre has exhibited stellar growth in its Gross Merchandise Volume (GMV), witnessing a significant 22.9% uplift compared to last year, amounting to \$10.5 billion. This potent e-commerce activity highlights the firm's ongoing expansion in its business verticals.



Mercado Livre (the Portuguese spelling, but same company) has fortified its commanding presence in Brazil's e-commerce domain, leveraging emerging opportunities earlier in the year to augment its market share. This strategy has culminated in a remarkable 59% surge in 1P GMV (first half) in the local currency, substantially bolstering the positive trajectory of the domestic operation.

Mexico has surfaced as a powerhouse for MercadoLibre, overtaking Argentina to become the second-largest market in terms of GMV. The Mexican branch is on a fast track to growth, with a 52.0% year-on-year escalation in local GMV. Moreover, this sector has marked the highest surge in both product sales and new customer acquisitions over the past two years.

Conversely, Argentina's macroeconomic climate continues to cast a shadow over the local operations, primarily due to inflationary pressures impacting GMV. The growth in sales volume and absolute values remains restrained, showcasing a nominal 1% growth in local currency GMV.

Despite these economic impediments, MercadoLibre managed to secure a substantial 38% increase in e-commerce revenue, spurred by a 23% growth in total GMV and a +200 basis points surge in the e-commerce take-rate, which settled at 18.4%. This acceleration was facilitated by heightened ad revenue penetration, revised marketplace fees, and a boost in first-party (1P) sales.



Flourishing Fintech Sector Despite Challenges

MercadoLibre's fintech arm witnessed a 45 basis points dip in its take-rate year-on-year, settling at 3.52%. This downturn is attributed to a tempered growth pace in the credit sector and reduced commission fees in other segments. However, the fintech division still managed to record a 24% annual revenue growth, accumulating \$1.5 billion, a prudent approach considering the prevailing macroeconomic circumstances and the focus on sustaining the credit business.



In essence, despite a reduced commission rate, the fintech sector of MercadoLibre has demonstrated robust revenue growth. Mercado Pago's Significant Transaction Volume Expansion Mercado Pago, the payment arm of MercadoLibre, showcased a stellar quarter with a 39.3% boost in Transaction Volume (TPV), amounting to \$42.0 billion. This expansion is largely credited to its focus on small and medium enterprises (SMEs), which significantly contributed to the massive 128.7% and 58.2% year-on-year growth in Off-platform TPV and digital accounts TPV, respectively.



Furthermore, the acquiring sector experienced substantial growth, amassing a total of US\$27.2 billion. This strategy, grounded in sustainability, adeptly caters to market needs while fostering a vibrant competitive environment.

Credit Sector Dynamics Amidst Rising Delinquency Worries

The credit sector maintained its upward trajectory, with the credit portfolio amassing a total of \$3.2 billion, denoting a significant 21.0% surge compared to last year. This uptick was chiefly fueled by the burgeoning consumer sector in Mexico and the steady growth of credit card ventures in Brazil. A standout aspect was the pronounced growth in credit card activities, registering a quarter-over-quarter growth rate of 12.8%.



Nonetheless, a word of caution is warranted concerning the delinquencies spanning less than 90 days, which saw an uptick for the first time in a year, hitting 9.9%. This trend is perceived to be a result of seasonal discrepancies and the augmented engagement of the In-store Merchant sector, which inherently bears a higher risk due to the absence of established user behavior patterns.

The issue of delinquency persists as a significant concern, particularly as the firm ramps up its credit card initiatives. It becomes imperative to strike a harmonious balance between growth and portfolio quality to safeguard the longevity of the credit operations. Disparities between these elements could potentially incur elevated costs in the forthcoming period, particularly as late payments accumulate within the portfolio.



While the second quarter of 2023 didn't witness a substantial discrepancy, forecasting the exact repercussions on new groups remains a complex endeavor, given the portfolio's nascent stage, and these groups are still in their infancy. Although the current dynamics pose certain apprehensions, the scenario remains well-managed at present.

My Evaluation

MercadoLibre has maintained a tradition of delivering stellar operational results, thereby validating its market valuation. Boasting an EV/EBIT ratio of 39.7x for the 2023 estimate and 25.7x for 2024, I am inclined to assert that MercadoLibre's history of excellence warrants the existing premium on its shares, positioning them as comparatively undervalued.

Especially due to the burgeoning size of the Latin American digital advertising market.



The Digital Ad & AI Revolution Advances Steadily

Mercado Libre is perfectly positioned to benefit from the enormous upcoming growth in digital ad spending over the next five years.

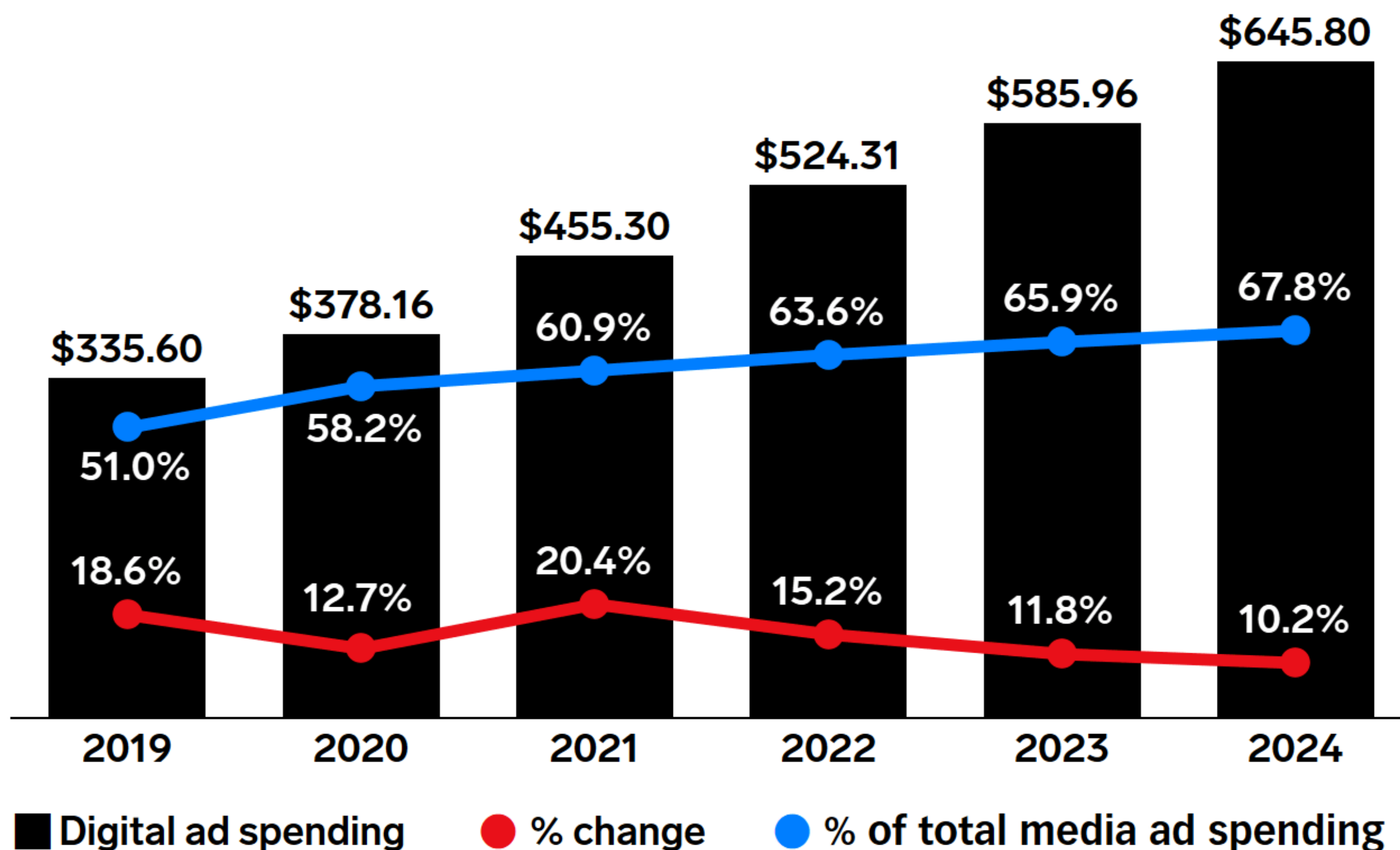
As you can see in the chart below, digital ad spending has only been heading in one direction:

Up.

Global Total Digital Ad Expenditure

Digital Ad Spending Worldwide, 2019-2024

billions, % change, and % of total media ad spending



Note: includes advertising that appears on desktop and laptop computers as well as mobile phones, tablets, and other internet-connected devices, and includes all the various formats of advertising on those platforms; excludes SMS, MMS, and P2P messaging-based advertising

Source: eMarketer, March 2021

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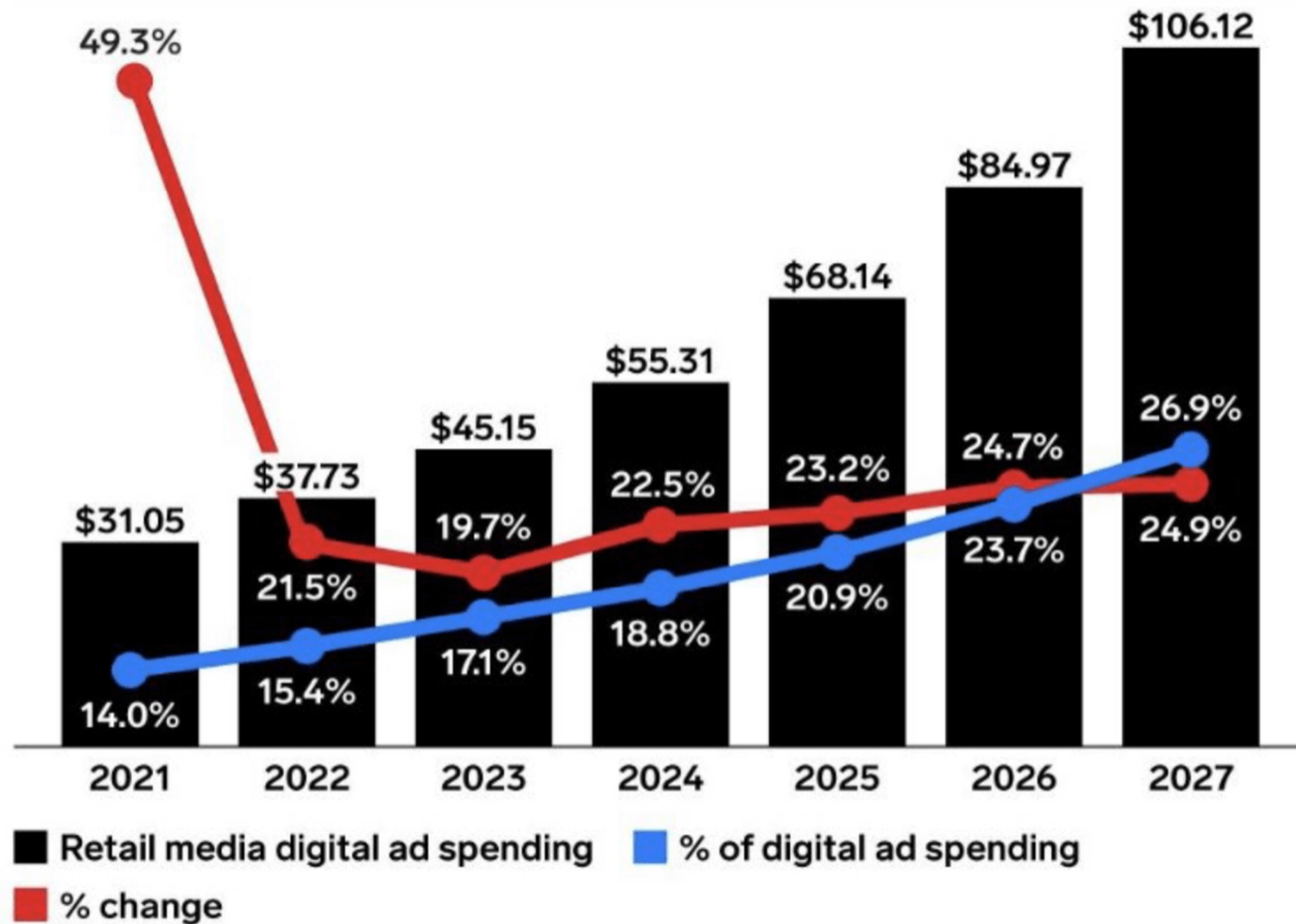
eMarketer | InsiderIntelligence.com

It's pertinent to note that this data is from 2021, and 2023 has emerged as a tumultuous year for the entire advertising sector, potentially seeing growth rates dip below 10%. However, the overarching trend is undeniably upward. Moreover, within this Total Addressable Market (TAM), the growth in e-commerce advertising spending is outpacing the broader digital ad TAM, as depicted below:

Investments in Digital Advertising on E-commerce Platforms

US Retail Media Digital Ad Spending, 2021-2027

billions, % change, and % of digital ad spending



Note: digital advertising that appears on websites or apps that are primarily engaged in retail ecommerce or is bought through a retailer's media network or demand-side platform (DSP); examples of websites or apps primarily engaged in retail ecommerce include Amazon, Walmart, and eBay; examples of retail media networks include Amazon's DSP and Etsy's Offsite Ads; includes ads purchased through retail media networks that may not appear on ecommerce sites or apps
 Source: eMarketer, March 2023

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This upward trend aligns seamlessly with the figures disclosed by global e-commerce platforms, including industry giants like Amazon (AMZN) and of course, MercadoLibre itself.

Finally Realizing Potential

As we delve deeper, it's clear that MercadoLibre has made substantial strides in its digital advertising sector. In 2021, it constituted a mere 0.4% of the GMV, a figure significantly smaller than its current standing. Currently, MercadoLibre has not only expanded its advertising division but also significantly augmented its GMV. At present, the advertising sector of MercadoLibre accounts for 1.6% of a quarterly GMV valued at \$10 billion, witnessing a growth rate exceeding 60% in Q1 2023.

This data suggests that MercadoLibre's advertising arm is generating approximately \$640 million in annualized sales with a gross margin of 80%, potentially growing at a rate well above 50%, even amidst an economic climate where advertising expenditures are relatively stagnant. As we navigate past this period of advertising expenditure stagnation, induced by the swiftest rate-hiking cycle witnessed in American history—a phenomenon that extends to Latin American nations as delineated by the "Trilemma"—this growth in advertising might potentially accelerate further



In essence, I posit that MercadoLibre's advertising sector is poised to generate multi-billion dollar revenues in high-margin sales for the conglomerate in the long run, indicating that we are merely at the inception of a promising journey for MercadoLibre's advertising division and its overall conglomerate growth.

Now, let's shift our focus to the other burgeoning sectors within MercadoLibre, which are also in the nascent stages of their growth trajectories.

Upholding Integrity Consistently: The Payments & E-commerce Sector

Americanas, a formidable rival of MercadoLibre in the coveted Brazilian commerce market, has been implicated in fraudulent activities, foreseeably leading to a gradual cessation of operations or, at the very least, a significant reduction in its competitive stance against MercadoLibre's innovative growth dynamics. The alleged fraudulent activities were notably severe:

Retail & Consumer

Brazil's Americanas accuses former executives, banks and auditors of aiding fraud

Simultaneously, DLocal (DLO), a contender in the payments sector (specifically the acquiring platform) against MercadoLibre's payment division (also an acquiring platform facilitating merchant transactions), faced fraud allegations. In DLocal's scenario, these remain as allegations, yet the public accusation of fraud, which precipitated a 50% decline in share value—a position it hasn't recovered from—is hardly conducive for business prosperity.

Keeping these developments in perspective, as I have reiterated, business success is less about rivalry and more about a customer-centric approach coupled with high-integrity operations. Predominantly, businesses that prioritize quality and integrity, offering consistent value to customers over extended periods, are destined to thrive, eventually rewarding their shareholders.



The exact timeline remains uncertain, and challenges, including competitive pressures, are inevitable. However, entities that maintain a relentless focus on delivering quality and integrity in their offerings are bound to attain success, metaphorically reaching the "kingdom of heaven." This philosophy seems to resonate with MercadoLibre's journey.



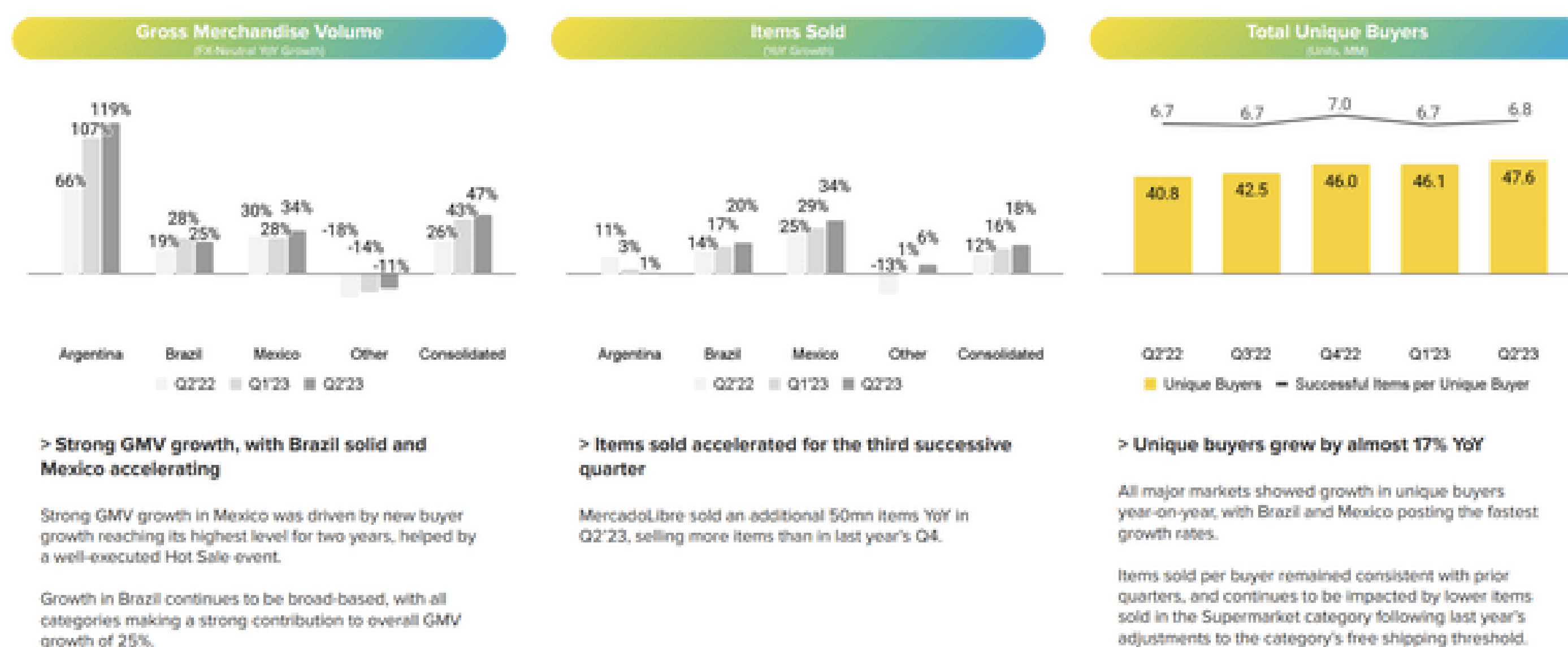
Despite facing competitive pressures from rivals, including Amazon (AMZN), it has persevered in serving the Latin American market with unwavering commitment to quality and integrity. Currently, the road ahead seems to be clearing: A major Brazilian competitor (Americanas) has succumbed, and a significant player in the payments sector is grappling with fraud allegations. It appears as though the turbulent times are subsiding, paving the way for sustained growth in the future, a path forged through consistent, high-quality, and integrous business practices, rather than complex, strategic maneuvers often witnessed in Silicon Valley.

Highlights of MercadoLibre's E-commerce Venture

The growth trajectory in Brazil and Mexico is noteworthy, with Mexico emerging as MercadoLibre's second-largest market, a development that mitigates the pressures stemming from political instability in Argentina. A significant increase in unique buyers is also evident.

Marketplace Highlights

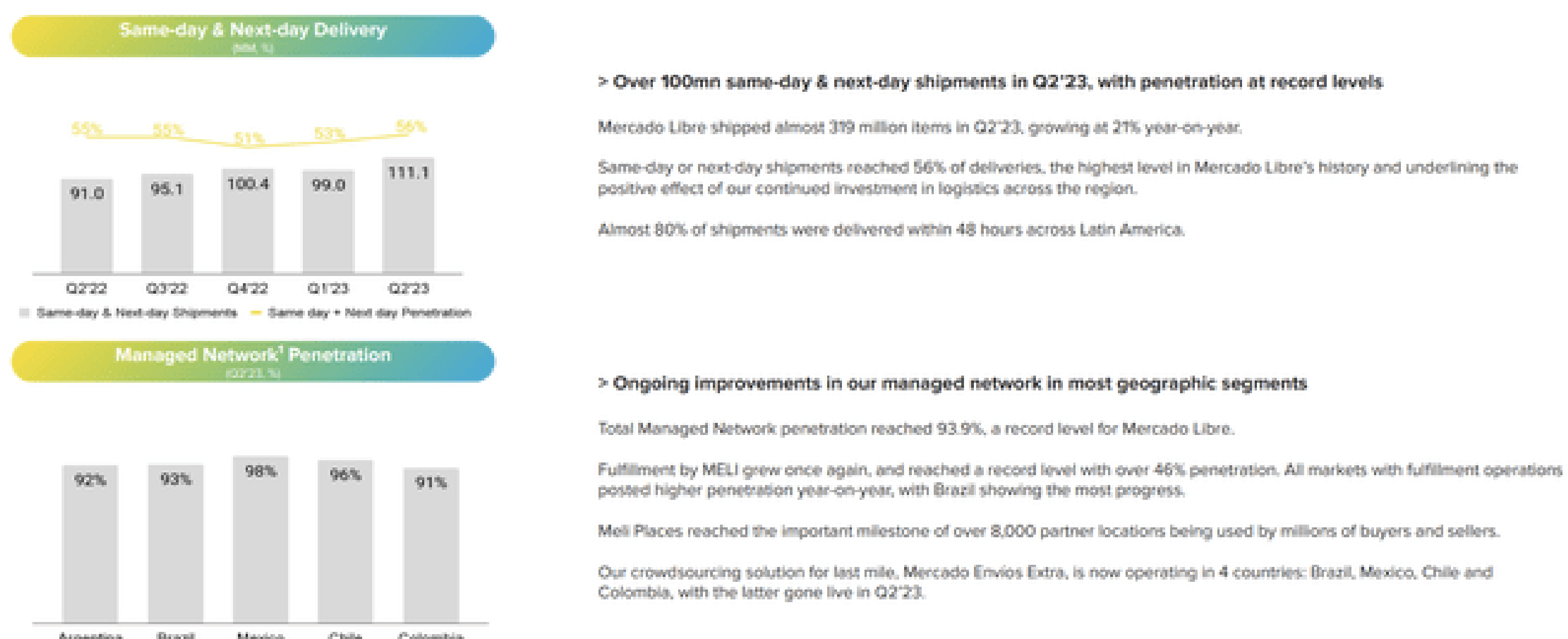
Momentum remains strong, with Mexico accelerating and Brazil continuing to stand out



This growth spurt is anchored on MercadoLibre's formidable logistics network, which serves as a protective moat for the business. I firmly believe that there exists substantial potential to revolutionize e-commerce logistics through AI and automation, further strengthening MercadoLibre's competitive edge in this domain.

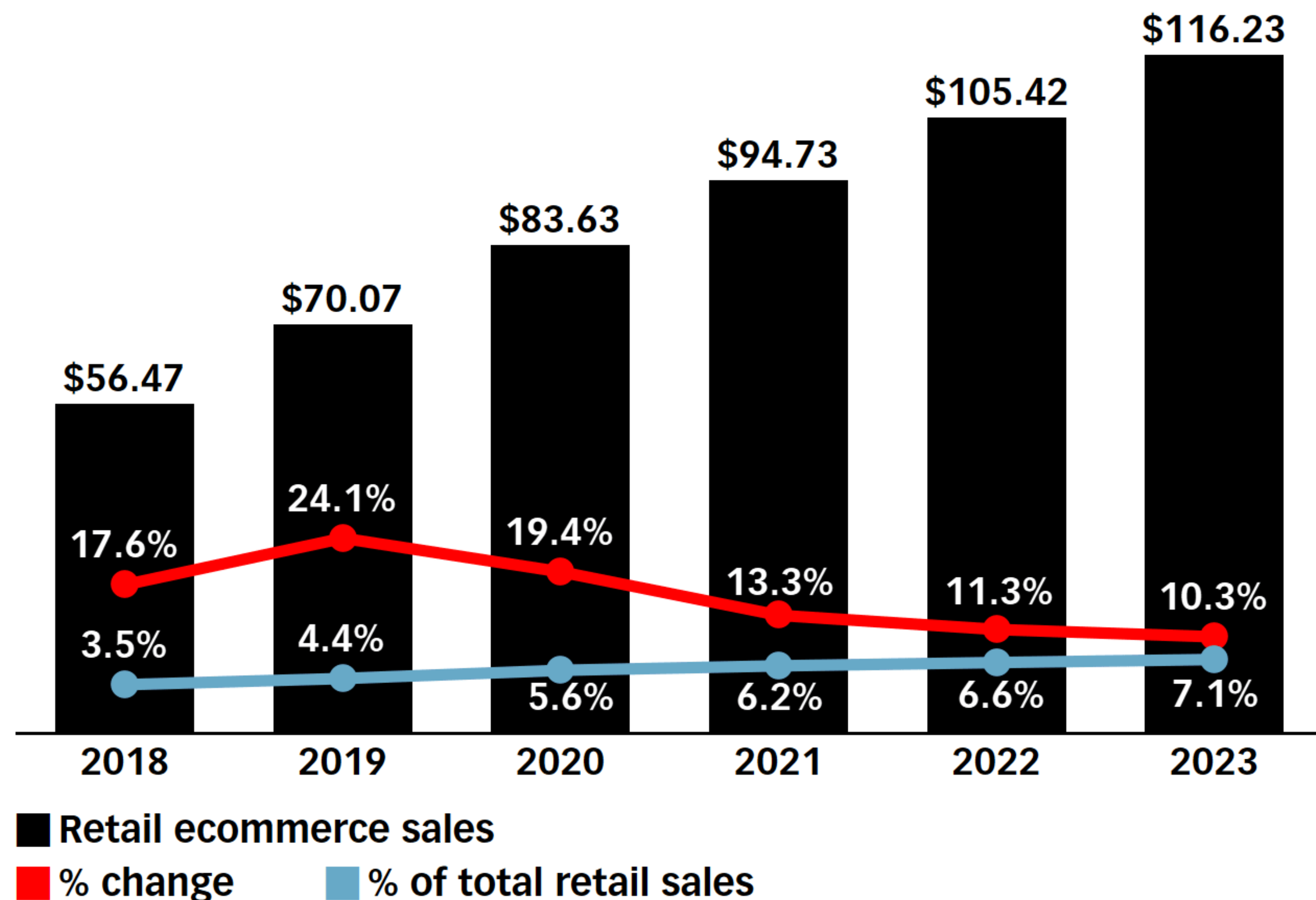
Logistics Highlights

A new record of same- and next-day deliveries as Fulfillment penetration continues to rise



I perceive a long and promising growth trajectory for MercadoLibre's e-commerce sector. While e-commerce sales penetration in the U.S. has reached 21.7%, in Latin America, it remains at a mere 7%.

Retail Ecommerce Sales in Latin America, 2018-2023 billions, % change and % of total retail sales



Note: includes products or services ordered using the internet via any device, regardless of the method of payment or fulfillment; excludes travel and event tickets, payments such as bill pay, taxes or money transfers, food services and drinking place sales, gambling and other vice goods sales
 Source: eMarketer, May 2020

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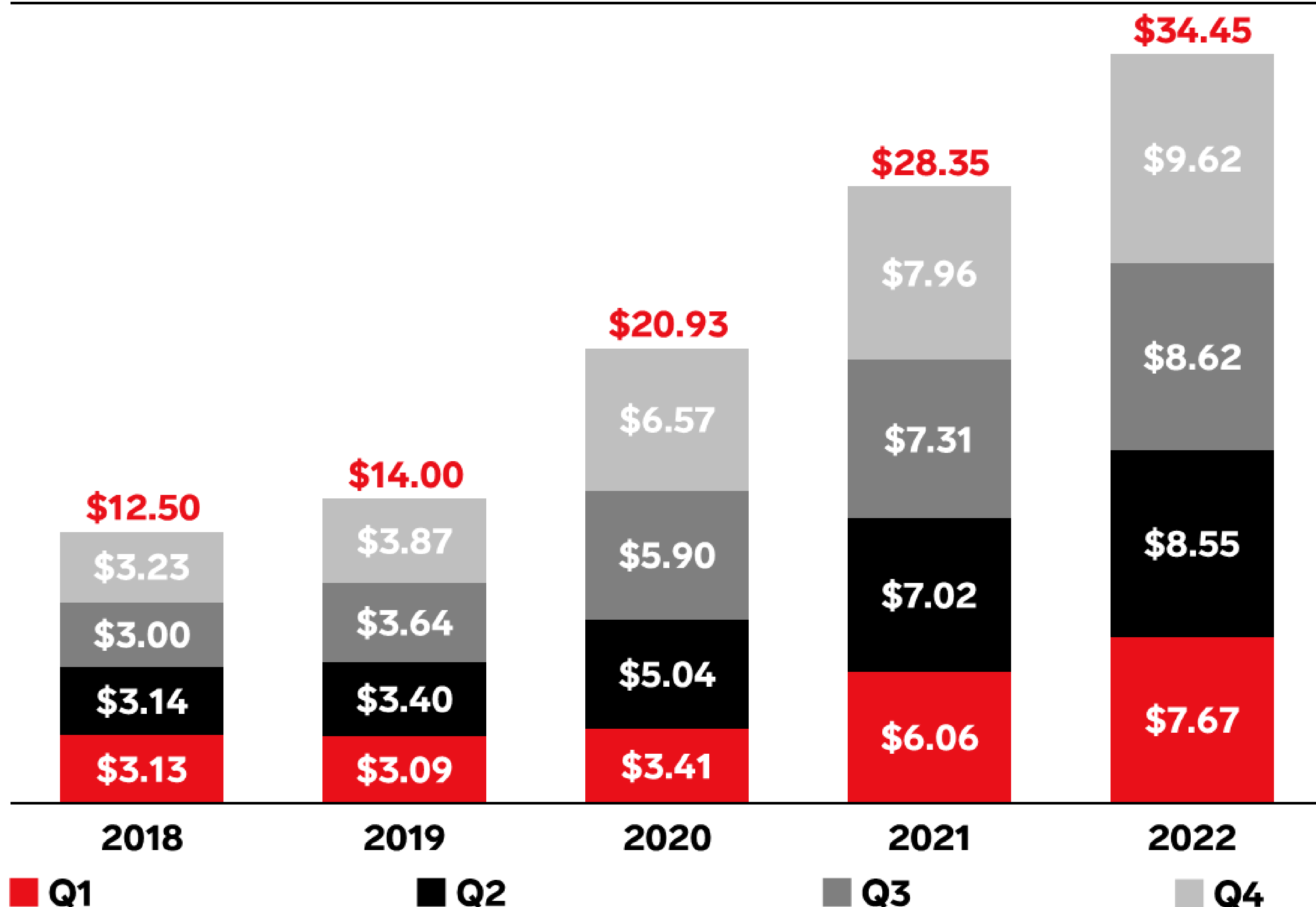
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MercadoLibre's e-commerce marketplace, advertising sector, payments division, and shipping & logistics arm are all poised for growth, leveraging the extensive growth runway that lies ahead. Turning our attention to MercadoLibre's payments sector, the recent period witnessed remarkable growth in its acquiring platform.

Acquiring Platform (Facilitating Merchants in Managing & Accepting Payments) and Consumer Platform (Comparable to Your Preferred Digital Banking Platform)

Mercado Libre Retail Ecommerce Sales in Latin America, by Quarter, 2018-2022

billions



Note: includes all transactions completed through the Mercado Libre marketplace; excludes classified items such as aircraft, motor vehicles, real estate sales, and vessels; numbers may not add up to 100% due to rounding

Source: Mercado Libre, "Investor Presentation: Fourth Quarter 2022 Results"; Feb 23, 2023

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As noted, DLocal is a competitor in this space, alongside other entities like Adyen (OTCPK:ADYEY). Both sectors—payments and e-commerce—represent excellent business opportunities, especially considering the anticipated growth in digital advertising.

Banking Penetration in Latin America



Image courtesy of Microsoft

Moreover, considering the significant portion of the population in Latin America still without banking facilities, MercadoLibre's consumer-oriented financial platform is poised for decades of growth. As digital banking becomes more accessible in Latin America, MercadoLibre's acquiring platform, which facilitates digital transactions for merchants, is set to witness increased adoption, fostering further growth for the company.

Conclusion

MercadoLibre is well-positioned to grow over the next few years. Booming demographics, increased internet adoption rates, and an increased market for payment and credit solutions will be strong tailwinds for this Latin American e-commerce giant. And yes, the price per share is expensive — but remember, you can always buy fractional shares!



To your wealth,
Alex Reid
Founder, Wealthpin Pro

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