

# FCL*Capital*

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## **A free “unicorn” in a defensive company with a widening moat.**

As long-term value investors, there are two possible situations of particular interest to us:

- 1) Huge discrepancies in valuation between similar assets of different asset classes, and;
- 2) Misunderstood and/or overlooked assets in a particular asset class.

We believe Match.com fits both of these criteria. Match.com filed for an IPO in late 2015, a particularly troubling time for the stock market in general and, more specifically, a bad time for tech IPOs. News sources were full of stories of failed tech IPOs at the time. Meanwhile, a Texas Law Firm quickly filed a class action lawsuit on totally baseless grounds (in our opinion) arguing the company's IPOs prospectus misled investors and that the shares were likely to fall because of that.

Due to this confluence of factors, it is safe to say Match.com did not have an auspicious start in the stock market and its valuation suffered consequently.

Many investors are blind to the huge opportunity it brings. Possibly, because the company is newly listed and many investors are still getting used to its numbers, and maybe, because of simple misunderstanding about its prospects amid huge societal and economic changes.

Match.com is a legitimate platform company. It has what Warren Buffet once described as a “moat”, a huge barrier to entry. Platform companies benefit from network effects. It is very hard to start a new online auction site because eBay is already where buyers and sellers are. In addition, the more buyers and sellers are attracted to the platform, the harder it is to start a new online auction website and wider its moat becomes. Likewise for car hailing apps (Uber and Didi Kuaidi), social Networking (Facebook, Twitter and LinkedIn), and so forth.

Match.com is exactly in this same category. The company owns four of the five largest dating platforms in the US and three of the five largest in the western hemisphere. The barrier to entry in online dating is exactly the same one as in, say, social networking: people tend to flock to platforms where other people already are, for obvious reasons. The only major difference in the business model is that while Facebook earns its revenue through third party advertisers

Match.com earns most of its revenue directly through its users that pay subscriptions for premium features of its services.

Furthermore, Match.com is a pioneer in the internet industry. Apart from Amazon, it is very hard to think of a company that was already a leader in its niche back in the 1990s and kept growing and flourishing like Match did. Once again, this seems proof that of its stable leadership and wide moat.

While it seems clear to us that Match.com should enjoy similar valuations to other internet platform companies, it is by far, the cheapest of the group on any imaginable measure.

Company	EV /EBITDA (16E)	Price / Earnings (16E)
Match.com	11.16	17.64
Facebook	19.81	33.11
LinkedIn	16.12	39.52
Twitter	11.89	29.67
Average of Peers	15.94	34.10
Upside	42.83%	93.31%
Two Metric Averaged Upside: 68.07%		Target Share Price: \$23.52

Although at FCL we have some criticism towards the “target price” model, a simple average of the multiples of Facebook, Twitter and Linked in would result in a 42.83% upside in terms of EBITDA

multiples to its peers group, reflecting the difference in valuation to its peers. Even more importantly in this sector, a 93.31% upside in terms of expected net 12 months' earnings per share to its current share price, resulting in a 68.07% upside (from current share price levels) and a theoretical target price of \$23.52 per share for match.com when we average the two different multiples.

### **Money for nothing, Tinder for free.**

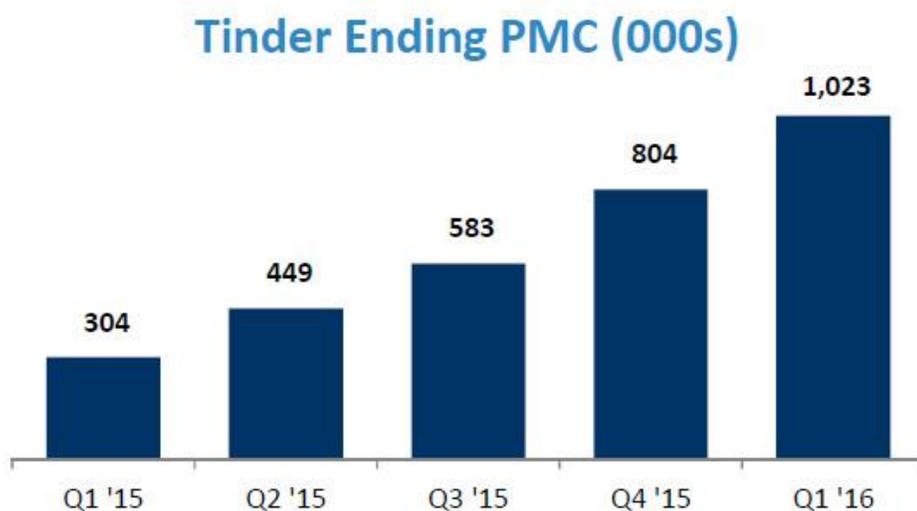
Obviously valuation multiples only go so far. They can be misleading and compare apples to oranges, and there is one very interesting fact about Match current multiples. They obviously reflect the past 12 months. As it happens, in this period Match was only beginning to implement Tinder's monetization program.

The company's strategy is usually as follows: first, they launch or purchase a new product, then after a few years they gradually start to experiment in terms of monetization and then this process starts its ramp up.

We will talk more about Tinder later in this report. As for now, we will only say that the company's star product has only had its

premium paid features, called "Tinder Plus" launched on the market a little over a year ago and the monetization process is a huge success so far.

While the graph below shows the success of the monetization program, it also shows that since Tinder is on a rump up process, its current revenues are very far away from where they will be. In other words, Match's current cheap multiples are actually a lot cheaper than they appear since they do not take into account Tinder's ramp up monetization process.



Even more interestingly, if Match.com was not the sole owner of Tinder, a platform that is on its way to becoming the world's first global dating platform, it would already be a very cheap company.

To see how cheap this company would be, you only have to see the company's current multiples, since they largely do not take into account Tinder's monetization. To see the future possibilities once you realize how far Tinder can go, some imagination is required.

## **Unicorns and private VS public companies valuation**

As our regular readers know, we have long argued that private tech companies were experiencing bubble level valuations. <sup>1</sup>

No profound exercise can come from comparing hugely different companies that operate in different sectors of the economy. Furthermore, private companies' numbers are almost by definition unreliable and uncertain. That being said, if we compare some basic Tinder metrics, like number of global users, estimated current revenue (an educated guess can be reached through Match's public reports), growth and monetization prospects, we are confident that Tinder could be in the headlines for attracting investing rounds from venture Investors at a valuation close to \$ 10 billion. Alone. Without considering any other part of Match Group.

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<sup>1</sup> [Link: Tech Crunch Unicorn Leaderboard](#)

Once again, we can never know for sure. Tinder was bought by Match group and is experiencing tremendous growth and probably better monetization prospects that it ever could without Match's know how and experience. At the same time, this certainly is a less disruptive and glamorous road.

*Our major point in this report: There are two major ways to look at match.com. If it weren't the sole owner of Tinder it would already be a very attractive and cheap platform company, with great legacy assets ( Match.com, Ok Cupid, Meetic, Plenty of Fish) and trading at a cheaper valuation than other other major internet platform company. On the other hand, if Tinder were a separate company, it alone would be trading possibly at twice the valuation the entire group currently sells for in the market. But since they are just one single company, at the current valuation we see a major buying opportunity.*

**Misconceptions about online dating. People are not angels and times are changing.**

As in many things that are new or misunderstood, there are quite a few misconceptions about the dating industry in general and Match.com in particular:

**Myth 1: Online dating is a niche, done by odd people.**

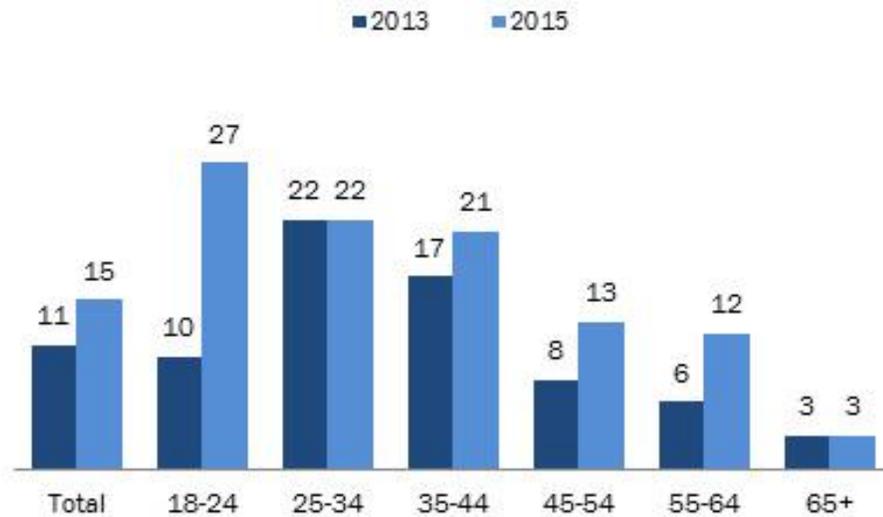
**Truth:** In fact, online dating is increasingly becoming the default way to meet new people. And the younger, wealthier you are the more likely you will meet your future significant other through online dating, especially if you live in a urban area. As millennials age and ever-younger generations grow older almost no one will go through their lives without using online dating to meet new people at some point in their lives.

**Myth 2: A problem with the online dating industry is that once the companies provide the service the customer is paying for and they find someone, their revenues are gone.**

**Truth:** This is possibly the deepest misconception about the online dating industry (and since Match.com is the undisputed leader in the industry, it is obviously also a misconception about the company itself.

## Use of online dating sites or mobile apps by young adults has nearly tripled since 2013

*% in each age group who have ever used an online dating site and/or mobile dating app*

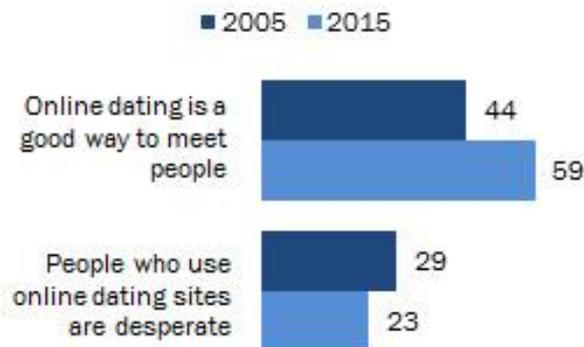


Source: Survey conducted June 10-July 12, 2015.

PEW RESEARCH CENTER

## Attitudes toward online dating grow more positive

*% of U.S. adults who agree with the following statements*



Source: Survey conducted June 10-July 12, 2015. Trend data from previous Pew Research Center survey.

PEW RESEARCH CENTER

First, it is a well-known fact that people are steadily marrying later everywhere in the world, a fact that by itself assures that Match will have a growing potential market for years to come even in countries with stagnant populations. Match.com does not need an increase in the number of singles (although this would surely help). It only needs that the same populations spend a greater part of their lives being single and paying for its services.

There is an even more important underappreciated aspect. One of the worst kept secrets of the industry since its foundation back in the 1990s is that a surprising percentage of users (possibly as high as 20%) is in fact, in a relationship, most of them married (reliable statistics are impossible to get for obvious reasons).

This shouldn't be as surprising as it seems. The same technology that allows people to more easily than ever before connect with new people, find new mates, obviously allows many people that may be unhappy in their relationships or simply wanting some adventure, to "shop around".

The success of the website Ashleymadison.com (until its hacking fiasco) is proof that there are millions of people using technology to cheat on their significant others. Match.com is a very ethical

company that provides users with a basic service: the possibility to find love or lust. The fact is that in a world where people increasingly marry late and a good part of the users “shop around” thanks to the possibilities of technology, is a future where the undisputed leader in the online dating industry will have an ever-wider moat and growing demand.

The revenue stream does not end once the company “provides” the service, even discounting Tinder and Ok Cupid, more focused on casual dating in the first place.

### **Myth 3: Online dating is a fragmented and local market.**

**Truth:** We live in an ever more connected world. An increasing proportion of workers are in the knowledge economy and do business travelling.

One of the reasons for the global rise of Facebook is that millennials are the more connected generation ever. They have friends from different parts of the world. They are curious about people everywhere. In Brazil for example, one of the reasons Orkut was supplanted by Facebook was this advantage as a global platform where all your friends, from everywhere, could be found.

Likewise, for the first time ever the world is starting to witness a global online dating platform. With the advent of Tinder Plus millions of people everywhere are swiping to find dates and start conversations. The service has been used in some ingenious ways, like:

- A preparation for upcoming trips where users would like to arrive with some pre-arranged dates and acquaintances .(say: an American student who is going to Paris and would like to get in touch with locals);
- Business travelers arranging dates for upcoming trips;
- Married people using the “passport” function to start conversations with people from nearby or different cities.

We are aware we should not push the Facebook analogy too far. Match is a global undisputed leader and a global platform. In our opinion, its valuation should recognize this.

#### **Myth 4: Tinder is cannibalizing the legacy Match brands.**

**Truth:** In fact, all of the company’s brands are still individually growing. They attend different needs and niches. The only reason the average ARRPU has fallen is that a growing proportion of the consolidated company’s users are in platforms, like Tinder and Ok

Cupid, where a lower average price per user is paid. This does not mean that the legacy brands, like Match.com are suffering any pressure on ARPPU, a fact overlooked by the market.

All of the company's websites have different purposes and serve different niches forming together a more powerful system than each ever could alone.

**Myth 5: Match faces significant new competition that could disrupt its model.**

Truth: Although no company can rest on past success, as we said before very few internet companies can claim 20 years of uninterrupted leadership.

Besides, we would argue that if anything the company's leadership has been widening. The industry is becoming more mature and this will naturally raise barriers to entry. It is not as easy as before to start a new service, burn cash and attract the necessary millions of users to compete with Match, OkCupid or Tinder. Even if someone could do that, it would face competition from a well-capitalized and experienced company. Never say never but we are not losing any sleep on this. Any way we see it, we think Match.com is, with the obvious pun, a perfect match for longer-term value investors.

## Sobre a FCL Capital

A FCL Capital é uma gestora de recursos sediada no Rio de Janeiro, cujo objetivo é maximizar o retorno de seus investidores. A FCL tem como nicho principal, mas não exclusivo, investimentos em empresas abertas, listadas em bolsa de valores (posições compradas e vendidas nos mercados acionários). Para saber mais sobre nosso trabalho, entre em contato conosco ou acesse nosso website: [www.fclcapital.com](http://www.fclcapital.com).

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