

Grubhub Inc. (GRUB)

Forecasting GFS slightly below consensus as deteriorating market share and customer engagement trends persist

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	M Science Estimate	Consensus	Delta to Consensus	Year Ago Reported	Y/Y Change
Gross Food Sales	\$1,375.0	\$1,386.5	-\$11.5	\$1,138.8	20.7%
Take Rate	21.1%	20.6%	50 bps	18.0%	17.1%
Revenue	\$290.00	\$290.1	-\$0.1	\$205.1	41.4%
Active Diners	17,900	17,384	0.516	14,462	23.8%
Daily Average Grubs ('000's)	470.0	481.2	-11.2	392.5	19.7%
Average Order Value	\$31.80	\$32.30	-\$0.50	\$31.54	0.8%

* amounts in millions, except take rate, daily average grubs, and average order value
* consensus values may not be consistent as not all firms display detailed estimates

Source: M Science, company data, FactSet

OVERVIEW

- **Despite establishing Q4 '18 GFS and revenue estimates roughly in line with consensus, we remain concerned about the business's 2019 outlook.** We expect material deceleration for Grubhub's top-line growth in 2019 and/or a significant increase in marketing to offset the pressures on growth. These factors include aggressive competitors, persistent market share losses, and expansion to less-productive markets.
- **We are fine-tuning our gross food sales (GFS) forecast to \$1,375 million, up from \$1,350 million and slightly below consensus of \$1,386.5 million. This represents Y/Y growth of 20.7%, down from Y/Y growth of 40.1% in Q3 '18.** Assuming a \$10 million contribution from recently acquired LevelUp, we forecast Q4 '18 revenue of \$290.0 million, in line with consensus of \$290.1million. This implies Y/Y growth of 41.4% (36.5% excluding LevelUp), down from 51.6% Y/Y growth in Q3 '18. Our estimate implies a take rate of 21.1% — or 20.4% when excluding LevelUp contributions — similar to the 20.4% take rate in Q3 '18.
- **In our market analysis, Grubhub's competition is growing the market and simultaneously capturing share from Grubhub.** The industry accelerated to growth in the low-to-mid-40% range within our consumer panel, an increase from the low-to-mid-30% range we saw in Q3 '18, whereas Grubhub registered 5.4% Y/Y spending growth in Q4 '18.
- **We believe that new markets are not scaling due to the lower productivity of customers acquired in these geographies. This is highlighted by weakness in spending growth during Q4 '18, characterized by decelerating customer growth and worsening customer engagement in our panel.** Decelerating customer growth was expected, given the overlap of the acquisition of Eat24, but declines in purchase frequency raise concerns over Grubhub's ability to improve productivity from acquired businesses.
- **In our data, a growing portion of Grubhub diners each quarter has also ordered a meal from another delivery platform.** During the quarter, 71% of customers used the Grubhub platform exclusively, down from 74% in Q3 '18, and 77% in Q2 '18. Moreover, as

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of December '18, new diners were placing their first food order via DoorDash (38%) more frequently than Grubhub (33%).

- **We believe that competitors have been able to better execute on national partnerships, while Grubhub is struggling to leverage its agreement with Yum! Brands.** In our data, 13% of DoorDash orders in December were from large restaurant chains with an exclusive agreement (Chipotle, Wendy's, and The Cheesecake Factory). Grubhub's partnership with Yum! Brands composed roughly 1% of all orders.
- **We believe that the operating environment in Tier 2 markets does not offer the same opportunity that Tier 1 cities possess given their higher population densities.** Inevitably, longer wait times and travel distances at a higher cost to diners are leading to declining purchase frequency as the platform expands to lower-tier markets.

DETAILS

Based on data through the end of Q4 '18, we are forecasting Grubhub gross food sales (GFS) of \$1,375 million, slightly below consensus of \$1,386.5 million. This represents Y/Y growth of 20.7%, down from Y/Y growth of 40.1% in Q3 '18. Some of the slowdown reflects overlapping the Eat24 acquisition in October 2017. Assuming a \$10 million contribution from the acquisition of LevelUp (which is based on management's guidance), we forecast Q4 '18 revenue of \$290 million, in line with consensus of \$290.1 million. This implies Y/Y growth of 41.4%, down from Y/Y growth of 51.6% in Q3 '18. When excluding LevelUp, Y/Y revenue growth is 36.5%. Our estimate implies a take rate of 21.1% — or 20.4% when excluding LevelUp contributions — in line with the 20.4% take rate in Q3 '18.

During the most recent quarter, Grubhub faced a significant deceleration in spending growth, as it overlapped the Q4 '17 acquisition of Eat24 (which closed Oct. 10, 2017). In our market analysis, the combination of low switching costs for customers and the presence of aggressive competitors poses a headwind to Grubhub's growth prospects in the intermediate and long run.

MARKET ANALYSIS

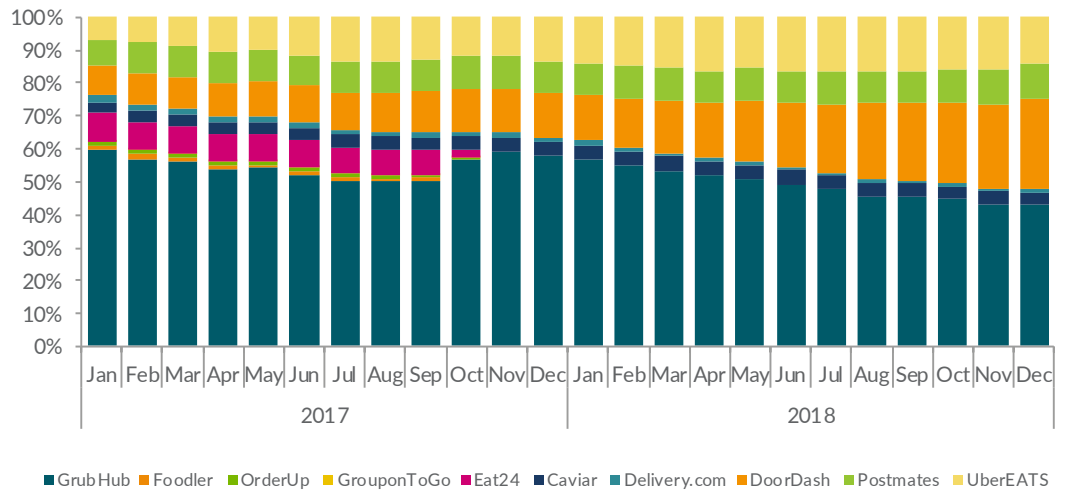
Based on our market analysis, we believe that the industry has been benefiting from a secular shift to delivery and grew in the low-to-mid-40% range Y/Y during Q4 '18. Outside secular tailwinds shaping customer behavior, growth was driven by DoorDash and, to a lesser extent, UberEATS, the fastest growers in the space. In 2018, Grubhub faced significant market share losses, claiming 43% of market share in both December and November, down from 45% in October, and 58% in December '17 (Figure 1). Based on our analysis, we believe that the growth of competitors expanded the overall industry and further diluted Grubhub's share of the market.





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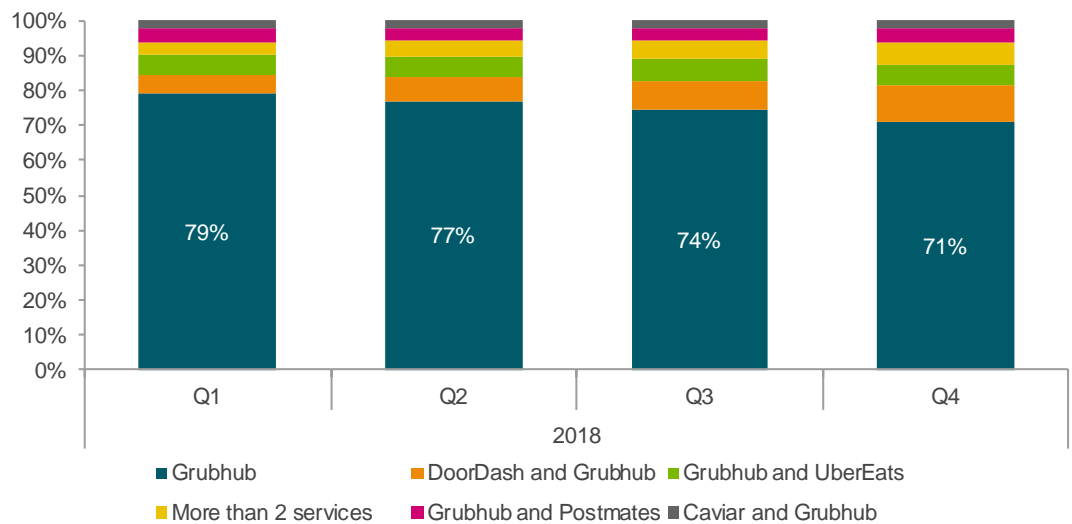
Figure 1: GRUB Market Share



Source: M Science

Our customer overlap analysis indicates that a growing portion of Grubhub diners is using other platforms (see Figure 2). This lack of exclusive diners presents an industry-wide challenge, which, in our view, stems from low switching costs for customers. While Grubhub may still possess the largest portion of exclusive diners compared to the competition, this is to be expected, as it is the largest platform in the space. Regardless, declines in customer loyalty are concerning, especially as peers like DoorDash introduce membership programs.

Figure 2: Quarterly Customer Overlap



Source: M Science

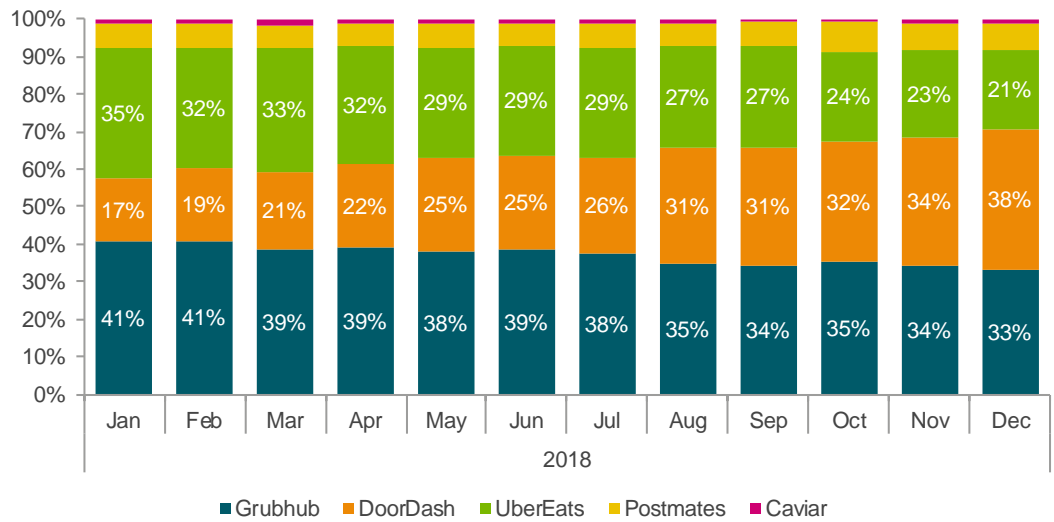
Our analysis of each brand's share of first-time industry diners shows a growing portion of customers make their first purchase via DoorDash (see Figure 3). December '18 marked the crossing of an important threshold: first-time users more frequently ordered via DoorDash than Grubhub — 38% of the time vs. 33%, respectively. This is a decline from November '18, when both platforms accounted for 34% of first-time industry customers, and from October '18, when Grubhub accounted for 35% of first-time users and DoorDash accounted for 32%.





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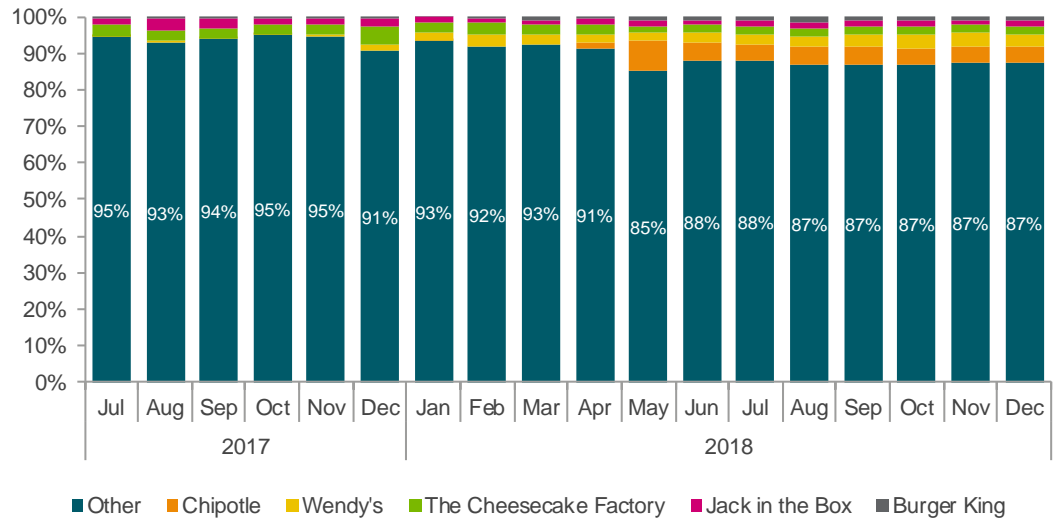
Figure 3: First-Time Industry Customers — Share



Source: M Science

We believe that growth experienced by competing delivery platforms has benefited from exclusive partnerships with large restaurant chains. Analysis of our receipt panel shows that 13% of all DoorDash orders in December were for restaurants with which DoorDash had exclusive agreements in place, in line with trends we've observed since June '18 (see Figure 4). In contrast, orders for Yum! Brands restaurants accounted for roughly 1% of all Grubhub orders in December '18.

Figure 4: DoorDash Share of Orders by Restaurant



Source: M Science

Our market share analysis on a city level highlights the fact that Grubhub has been steadily ceding market share to Postmates and DoorDash in markets outside of New York (Figure 5). We see these markets as generally less-productive per customer and as such a less-attractive value proposition. The lack of value derived from these markets compounded with poor market share trends since the Eat24 acquisition raise concerns around execution and the sustainability of growth.



Figure 5: GRUB Market Share by City for Q4 '18

	2015	2016	2017	2018
Dallas, TX				
GrubHub	34.2%	28.1%	25.8%	28.3%
Eat24	18.6%	15.0%	10.2%	1.4%
Foodler	0.4%	0.1%	0.0%	0.0%
OrderUp	0.9%	0.0%	0.0%	0.0%
Caviar	9.6%	8.6%	7.8%	11.5%
Delivery.com	1.6%	0.6%	0.2%	0.1%
DoorDash	27.9%	36.1%	44.7%	46.9%
Postmates	6.7%	11.4%	11.4%	11.7%
Houston, TX				
GrubHub	48.0%	30.8%	26.4%	22.5%
Eat24	21.2%	14.0%	9.8%	0.8%
Foodler	0.1%	0.6%	0.0%	0.0%
OrderUp	0.2%	0.1%	0.1%	0.0%
Caviar	0.0%	0.0%	1.5%	0.0%
Delivery.com	0.1%	0.0%	0.0%	0.1%
DoorDash	22.9%	44.3%	55.1%	69.2%
Postmates	7.5%	10.3%	7.1%	7.4%
Las Vegas, NV				
GrubHub	33.7%	43.5%	34.2%	37.1%
Eat24	47.0%	28.3%	14.9%	2.9%
OrderUp	0.6%	0.1%	0.0%	0.0%
Caviar	0.0%	0.5%	0.5%	0.3%
Delivery.com	0.1%	0.0%	0.1%	0.0%
DoorDash	0.8%	1.7%	15.9%	19.7%
Postmates	17.8%	25.9%	34.4%	39.9%
Miami, FL				
GrubHub	19.2%	26.0%	15.4%	21.5%
Eat24	60.1%	40.9%	26.9%	5.0%
Foodler	0.2%	0.3%	0.0%	0.0%
OrderUp	0.1%	0.1%	0.0%	0.0%
Caviar	2.7%	0.1%	0.1%	0.2%
Delivery.com	0.3%	0.6%	0.2%	0.3%
DoorDash	0.1%	0.4%	7.9%	14.6%
Postmates	17.3%	31.7%	49.5%	58.5%
San Diego, CA				
GrubHub	26.3%	26.5%	23.5%	30.2%
Eat24	36.1%	23.3%	14.6%	2.5%
Foodler	0.0%	0.2%	0.0%	0.0%
OrderUp	4.1%	3.8%	0.8%	0.0%
Caviar	0.1%	0.3%	0.4%	0.4%
Delivery.com	0.3%	0.3%	0.0%	0.0%
DoorDash	13.7%	24.0%	27.5%	33.9%
Postmates	19.4%	21.7%	33.1%	32.9%
Seattle, WA				
GrubHub	26.1%	22.6%	33.6%	28.9%
Eat24	41.9%	27.6%	16.2%	3.3%
Foodler	0.1%	0.3%	0.0%	0.0%
OrderUp	0.0%	0.0%	0.0%	0.0%
Caviar	11.5%	17.0%	14.7%	21.3%
Delivery.com	0.0%	0.2%	0.0%	0.1%
DoorDash	1.4%	9.6%	9.4%	18.8%
Postmates	19.0%	22.7%	26.1%	27.6%

*Market data includes the following companies: GRUB, Caviar, Delivery.com, DoorDash, Eat24, OrderUp/GrouponToGo, Postmates
Source: M Science

GROWTH METRICS

Grubhub spending growth decelerated to 5.4% Y/Y growth during Q4 '18, down from 20.6% Y/Y growth in Q3 '18. The deceleration in spending growth during Q4 '18 was driven by slower customer growth and further declines in customer engagement. Customer growth experienced a deceleration to 10.1% Y/Y growth from 34.0% Y/Y growth in Q3 '18 and transaction frequency declined 8.8% Y/Y, a mild improvement from the 15.6% Y/Y decline in Q3 '18.

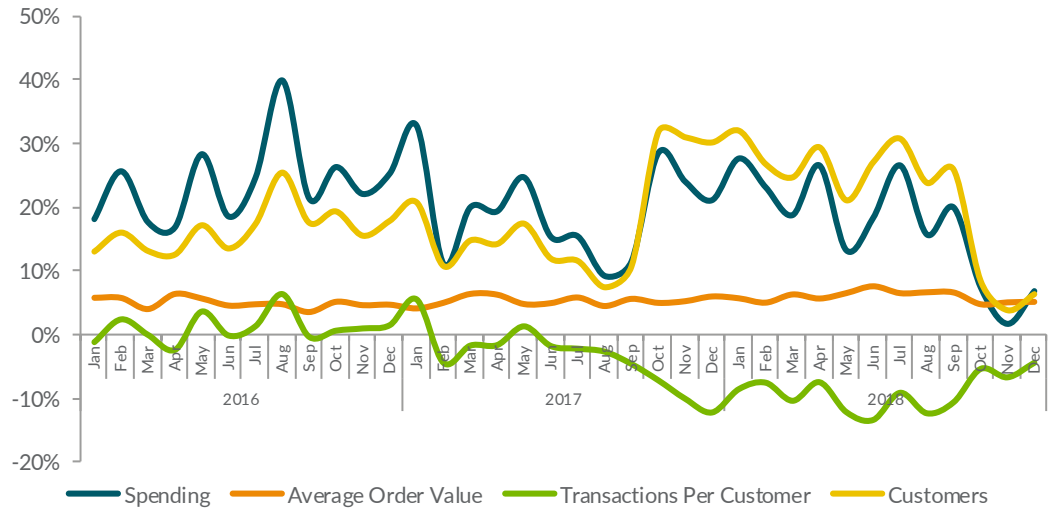




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Given the overlap of the acquisition of Eat24 during the quarter, we expected to see a slowdown in customer growth. However, persisting declines in purchase frequency at this stage raise concerns around Grubhub's execution in markets acquired during Q4 '17. Trends in customer engagement have been in decline since then. Grubhub's low spending growth during Q4 '18 is worrisome given that spending growth across the industry accelerated into the low-to-mid-40% range from the low-to-mid-30% range in Q3 '18.

Figure 6: Monthly Y/Y Growth in Our GRUB Consumer Panel



Source: M Science

CUSTOMER ENGAGEMENT

Transactions per customer kept declining, even as Grubhub overlapped the acquisition of less-productive users in Q4 '18. Transactions per customer declined 8.8% Y/Y, mildly improving from a 15.6% Y/Y decline in Q3 '18. We believe persistent declines at this stage are concerning as they highlight Grubhub's struggle to shape customer behavior and close the gap in engagement trends between New York and most other markets. At a city level, we saw no indication of this trend reversing, with our frequency buckets remaining flat Y/Y in most markets.

We believe these trends are a result of the operating environment presented by Tier 2 markets. Outside of New York, customer engagement trends are tempered despite aggressive competition and growth in restaurants on the platform. We believe Tier 2 cities struggle to gain traction due to structural factors, including longer wait times and travel distances, resulting in a diminished value proposition for diners in these markets.





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Figure 7: GRUB Transaction Frequency Buckets for Q4 '18

	1x	2x	3x	4x	5x	>5x
New York, NY						
2016	18%	10%	8%	6%	5%	53%
2017	18%	10%	8%	6%	5%	53%
2018	18%	11%	8%	6%	5%	52%
Boston, MA						
2016	34%	17%	10%	9%	5%	25%
2017	33%	14%	10%	10%	6%	28%
2018	33%	18%	8%	10%	5%	26%
Dallas, TX						
2016	49%	18%	9%	6%	5%	14%
2017	52%	15%	9%	6%	4%	14%
2018	48%	18%	7%	8%	5%	14%
Houston, TX						
2016	50%	15%	10%	5%	4%	16%
2017	56%	20%	7%	5%	2%	10%
2018	58%	17%	7%	4%	4%	9%
Las Vegas, NV						
2016	45%	15%	9%	6%	5%	19%
2017	44%	19%	9%	7%	4%	17%
2018	45%	16%	10%	5%	4%	20%
Miami, FL						
2016	49%	14%	12%	4%	4%	17%
2017	48%	16%	8%	7%	3%	18%
2018	48%	18%	9%	6%	3%	16%
San Diego, CA						
2016	50%	18%	8%	7%	4%	14%
2017	51%	18%	11%	6%	3%	12%
2018	47%	19%	9%	6%	4%	14%
Seattle, WA						
2016	49%	21%	10%	5%	4%	11%
2017	51%	19%	8%	4%	3%	15%
2018	47%	18%	11%	7%	3%	15%

Source: M Science



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WEATHER TRENDS

We note a higher percentage of days with rainfall in Q4 '18 for all major markets except New York. This may have provided a mild tailwind to GFS in the quarter.

Figure 8: Percentage of Days with Rainfall

	Oct	Nov	Dec	Q4
Boston				
2016	29.0%	29.8%	38.7%	32.5%
2017	32.5%	30.2%	29.0%	30.6%
2018	51.6%	50.0%	32.2%	44.5%
Chicago				
2016	21.9%	20.3%	28.5%	23.6%
2017	37.9%	36.5%	32.5%	35.6%
2018	60.1%	56.0%	40.3%	52.1%
Los Angeles				
2016	10.4%	12.8%	28.5%	17.3%
2017	0.0%	12.3%	3.2%	5.1%
2018	7.0%	13.3%	6.5%	8.9%
New York				
2016	26.8%	22.3%	42.2%	30.5%
2017	59.0%	41.0%	36.5%	45.6%
2018	43.2%	50.0%	44.2%	45.7%
Philadelphia				
2016	19.4%	16.1%	35.7%	23.8%
2017	33.8%	33.3%	27.0%	31.3%
2018	37.0%	43.3%	37.3%	39.1%
San Francisco				
2016	25.7%	20.0%	24.1%	23.3%
2017	8.0%	31.7%	3.2%	14.1%
2018	10.5%	20.0%	22.3%	17.6%
Washington				
2016	19.4%	13.3%	28.5%	20.5%
2017	30.0%	33.8%	16.6%	26.8%
2018	29.5%	39.5%	35.5%	34.8%

Source: M Science



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Figure 9: Average Temperatures (°F)

	Oct	Nov	Dec	Q4
Boston				
2016	54.2	45.3	34.8	44.7
2017	60.1	43.8	30.5	44.8
2018	53.8	43.0	37.6	44.8
Chicago				
2016	58.0	47.6	26.0	43.8
2017	56.5	40.2	27.4	41.4
2018	52.4	35.1	33.6	40.4
Los Angeles				
2016	67.3	63.3	56.5	62.4
2017	70.3	63.8	59.4	64.5
2018	67.6	63.5	57.3	62.8
New York				
2016	58.1	49.3	37.9	48.4
2017	63.6	46.6	34.8	48.4
2018	57.9	44.7	39.7	47.5
Philadelphia				
2016	57.9	48.0	37.3	47.7
2017	61.5	45.8	34.3	47.2
2018	57.2	42.8	39.3	46.5
San Francisco				
2016	60.8	57.7	50.8	56.4
2017	61.0	57.2	53.5	57.3
2018	60.5	58.1	54.2	57.6
Washington				
2016	60.2	49.6	39.4	49.7
2017	62.0	47.9	38.0	49.3
2018	59.5	44.6	41.7	48.7

Source: M Science





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INDUSTRY COVERAGE		
Consumer – US, Europe		
Auto Retail	Hardline	Softline Retail
Casinos	Home Furnishings	Specialty Retail
Cruiselines	Lodging	Theme Parks & Ski Resorts
Department Stores	Motorsports	UK Food Delivery & Restaurants
Discounters/Off-Price	Rental Cars	UK Grocers
Grocers	Restaurants	UK Retail
		UK Real Estate
TMT – US, Asia		
Cable/Satellite	Digital Media Services	Semiconductors
China Internet	Domain Registration	Telecom
Cloud Infrastructure	Internet/E-Commerce	Video Games
Consumer Technology	Payments	
Industrials – US, Europe		
Airlines	Electric Vehicles	
DIFFERENTIATED DATA		
Proprietary Data	Cruiselines	Global Smartphone Activations
Purchase Data	Casinos	Mobile Transactions
Consumer Spending Panels (US, Europe)	Web Technology Usage	China Online Media & Entertainment
	Global Travel	
IP Survey	Inventory Management	Wireless Retailer Point-of-Sale
WHOIS	Real Estate	Number Portability
Vehicle Registrations	Weather	Semiconductor Equipment Sell-In
Airline Pricing	US & China Handsets	Global Video Games
	Conversational Data	
M SCIENCE SOLUTIONS		

