MARCH 2021

ADVFN International Financial Awards WINNER 2021 Best Advisory CFD Services

ATLANTIC CAPITAL MARKETS

DELIVEROO IPO

01872 229 000
www.atlanticmarkets.co.uk

Introduction

Deliveroo are looking to list in April 2021 and have now announced the price range which is 390-460p which gives the business a valuation somewhere between £7.6bn to £8.8bn While the IPO was initially though to target a valuation of around £5bn the confirmation of the price range puts a much higher level on this.

The food delivery sector has benefitted greatly during the Covid-19 pandemic, but can they really continue this trend as lockdowns ease, and is the valuation really justified?

The company's goal is not just to make restaurant quality food more easily accessible but to kill home cooking altogether. A bold and ambitious statement, whilst the first part may be achievable, I wouldn't hold your breathe on them converting the entire public to stop home cooking.

The Deliveroo app uses an algorithm (named Frank) to ensure the efficient delivery, this helps them try to maximise earnings for both restaurant and couriers, and minimise customer waiting time. Delivery radius is limited to maintain this level of efficiency, and to encourage people to order from restaurants that are local to them.

History

Based in London, Deliveroo was founded in 2013 by Will Shu and Greg Orlowski. The business model is one that has really taken off in recent years with several business' operating in the sector, the main competitors that Deliveroo are sizing up against are Just Eat, GrubHub and UberEATS.

The companies involved in this new wave tech sector make revenue(and sometimes profit) by charging restaurants a commission fee, as well as charging customers a per-order fee. Deliveroo currently operate in the UK, The Netherlands, Kuwait and Hong Kong ,France, Belgium, Ireland, Spain, Italy, Australia, Singapore, United Arab Emirates.

Deliveroo works with some of the biggest chain restaurants across the UK, with the majority currently available exclusively on the Deliveroo app along with thousands of independent restaurants. In November 2016 Heineken also teamed up with Deliveroo to deliver the beverages.

In April 2017, Deliveroo's Editions kitchens was also launched. These delivery-only kitchens, sometimes known as ghost restaurants, allow restaurants to access customers in locations without needing High Street premises, thereby reducing set-up costs compared to a full-service restaurant. Deliveroo uses its data to identify areas where customer demand for certain cuisines is high and predicts which restaurants are likely to succeed there.

The IPO

Deliveroo's IPO plans were revealed earlier this month however, it has only recently confirmed the price range for the shares. The announcements timing comes only days after the UK government committed to changing the rules on IPO's in favour of the founders. The new rules allow founders to keep control of their companies despite selling shares to investors on the stock market.

The new rules focus on a dual-class share structure, split into class A and class B shares. This structure will last for three years and temporarily strip investors of typical ownership rights. The firm have stated that its class B shares would be held solely by Shu, who also serves as the company's chief executive. It means that when shareholder votes are held, Shu will be granted 20 votes per share, versus one vote per share for regular investors.

Class A Deliveroo shares

The expectation is that we will see £50 million shares available to existing Deliveroo customers and on an invite-only basis. Anyone that isn't a Deliveroo customer can still register their interest but will take second place to those with active Deliveroo accounts. Deliveroo shares in this category will be sold during the IPO. They will be a mix of new and existing shares in the company and private investors will be able to purchase Class A shares in Deliveroo.

Class B Deliveroo shares

The B class will not be sold as part of the IPO but instead they will be held by founder and CEO Will Shu. The B class will also give Shu 20 votes for every one vote made by a Class A shareholder. These arrangements will give Shu more control over the company. The dual share structure is set to remain in place for three years then the Class B shares will convert to Class A shares and become eligible for sale to institutional and private investors.

Business Opportunity and Risk

Covid Troubles

By mid-2020, Deliveroo hadn't benefited from the COVID-19 pandemic as much as some of its peers, at a time when demand for food delivery from restaurants and takeaways surged. This was quite a surprise to commentators and certainly prompted the question that if you can't make a profit in these conditions then when you can! During the period Deliveroo reported that they were cutting 367 jobs and furloughing 50 more from its workforce of 2,500.

The company had 2500 employees, connections with over 115,000 restaurants in 12 countries. The delivery riders serve six million customers in these countries. Deliveroo also secured £132 million of private funding in January 2021, placing its projected value at more than £5 billion.

The coronavirus pandemic of 2020 did add a strain on the company. While we might have expected it to thrive in the circumstances, it seems a considerable proportion of Deliveroo revenue came from big chains. With these shutting their doors, Deliveroo revenue was consequently hit. This also undermines Deliveroo's claims that its model centres on independent, local businesses.

Loss making from day one

Deliveroo’s troubles, however started prior to the pandemic, it has made a loss on every delivery made since day one. While revenue continues to rise, losses continue to deepen calling the robustness of the business model into question. After ranking first and second in the Financial Times‘ list of Europe’s fastest growing companies in 2018 and 2019, it completely fell out of the ranking in 2020.

Amazon Investment

In 2019 an Investment from Amazon was intended to give Deliveroo a boost. The UK Competition and Markets Authority launched an investigation into the investment under anti-monopoly laws. Eventually, provisional approval was given in April 2020.
However, it has also recently been confirmed that Amazon could raise as much as £107mn by selling some of its stake in Deliveroo at the IPO, the numbers discussed would leave Amazon with 11.5% of Deliveroo following its listing, reduced from the 15.8% it currently holds - according to the prospectus for the sale. These numbers imply Amazon could sell as many as 23.3 million shares.

Regulatory Probes

The prospectus also highlights the potential regulatory probes in Britain, France, Spain, Italy and the Netherlands over how it employs its delivery couriers. Uber have recently lost a landmark case in the UK that has led to the firm having to re-classify 70,000 UK drivers as employees entitling them to legal rights such as a minimum wage, holiday pay and a pension. Clearly having to reclassify riders with holiday and sick pay, minimum wages and other benefits would mean significant changes to the way it operates as well as the costs to run.

“Riders partner with us for the freedom to work when, where and how frequently they want,” it said in the prospectus.

“Changes to laws governing the classification of independent contractors, or judicial or governmental decisions involving us or our competitors regarding independent contractor classification, could require us to consider classifying riders as employees.”

Italy recently ruled against the company and have requested they backdate benefits for riders from 2015 up until 2020. At this point Deliveroo are appealing this judgment.

GTV

“Deliveroo said the total value of transactions (GTV) were up 121% year on year in January and February.

“This marks a significant acceleration from the +64% growth run rate through 2020 and indicates that the £5bn estimated GTV in 2021 could be easily exceeded". GTV is defined as the total value paid by consumers, excluding any discretionary tips. In 2020, Deliveroo an underlying loss of £223.7mln which was down from a 317.3mln loss in the prior year. The total amount of transactions processed on its platform soared 64% to £4.1bn as takeaways became a popular buy during lockdowns.

Summary

With some of the details confirmed in the prospectus I can't help but feel a large side serving of caution needs to be applied to anyone looking at getting involved, Yes it's a hot stock and yes the sector is growing but fair warning, there are concerns to be aware of.

- The company is still loss making (Granted not so much of an issue with the unicorns these days but still sits uncomfortably with me) equally they have just gone through a period that has seen a boom in the online delivery sector and yet struggled to make the most of it.

- Amazon are looking to dump some of its stake at the opening bell, - not a particularly bullish signal.

- the probe into how staff are classified in several European countries, if this probe goes against them it could have a very material impact on the running of the business. A similar scenario has recently hit Uber.

- The share price range announced see's the firm valuing themselves way beyond the initial £5bn expected.

If they do pull it off the Deliveroo IPO will be the largest LSE IPO by market capitalisation since Royal Mail in 2013.

About Atlantic Capital Markets

We are a multi-Asset brokers offering clients the ability to buy the shares either in a traditional fashion with standard shares or taking advantage of leverage and purchase via a CFD.

Call us on 01872 229 000.