CFA Institute

CFA Institute Research Challenge

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CFA Society Argentina & Uruguay

Universidad del CEMA

MercadoLibre Inc. (MELI: NASDAQ)

CFA Research Challenge

Rating	Target Price	Ticker
OUTPERFORM	USD 93.85	MELI :NASDAQ

DATE
November 16th 2012

Investment Thesis Summary

- **MercadoLibre, Inc. (MELI) is a leading e-commerce player in Latin America with commanding 28% market share and a strong competitive platform of services, which drives innovation and e-commerce penetration in the region.**

- **MELI has succeeded in consolidating a value generating business model for high growth reflected in a low capital utilization, and a stabilized ROIC since 2007 averaging 30.3% approximately between 2007 and 2012E, well exceeding its cost of capital estimated to be around 11.3%.**

- **Further growth is expected to arise from regional macroeconomics and increasing internet and e-commerce penetration, and shall deliver between 2012 and 2017 a 20% CAGR for GMV, 27% CAGR for Revenues, 19% CAGR for NOPAT and 18% CAGR for Free Operating Cash Flow.**

- **A target USD 93.85 price was achieved through DCF methodology, discounting 2012-2017 FCF at 11.3% WACC, and capitalizing a declining growth rate towards a 3% perpetual growth by year 2034.**

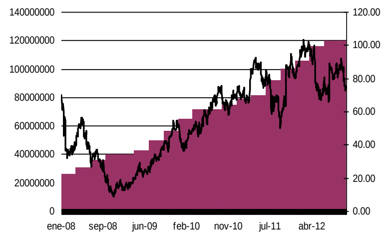
- **MELI currently trades at PE(13E) of 32.7x and EV/EBITDA (13E) of 19.8x. Our target price represents a 24% upside which translates into target trading multiples of 40.6x PE(13E) and 24.9x EV/EBITDA (13E).**

- **Comparison to Ebay and Amazon further highlights the opportunity considering MELI's stronger fundamentals such as average 3 years return on equity of 37% and EPS growth of 52%, compared to Amazon's (17% and 7% respectively) and Ebay's (17% and 4% respectively).**

Company Overview

Price Target	93.85 USD
Market price	75.43 USD
Market Cap (mm USD)	3,330.3
Enterprise Value (mm USD)	3,156.4
52-Week High/Low (USD)	104.5/64.18

Price relative to LTM Operating Income



Source: S&P Capital IQ

Business Overview

Mercadolibre Inc., headquartered in Buenos Aires and incorporated in Delaware, represents Latinamerica's leading e-commerce platform, **with a commanding market share of 28%.**

The company has developed an online community to which it provides web-based services and tools designed for buying, selling, paying, collecting and comparing transactions. Products offered include everything that can be legally traded, ranging from real state, motorized vehicles, home, sports apparel, collectibles and clothes.

MELI hold the largest customers base in the region with a total 77.2 mm registered users, which represents 13% of a 591 mm combined market population, and 29% of 266mm internet users' population, which shows a commanding presence with significant upside. Registered users have been growing more than 24% per annum for the last 5 years and is affecting directly the number of items successfully sold, growing more than 30% p.a. since 2008, showing that **users, on average are also more active in the site**. Furthermore, the company holds 33 mm unique visitors, being the **most visited e-commerce site in Latin America and ranks within the top ten visited internet sites in the region**.[1]

[1] According to alexa.com, MELI ranks Nº10 in Brazil and Mexico, and Nº 7 in Argentina and Venezuela as top visited sites per country.

Exhibit 1: MELI's users.

	Year Ended December 31,					Nine Months Ended
	2007	2008	2009	2010	2011	Sept 2012
Number of confirmed registered users at the end of period	24.9	33.7	42.6	52.9	65.8	77.2
Number of confirmed new registered users during period	6.7	8.8	8.9	10.3	12.9	11.3
Gross Merchandise Volume (GMV)	1511.5	2078.9	2750.7	3405.9	4820.1	4057.4
Number of Successful items sold	17.5	21.1	29.5	39.2	52.8	48.4
Total payment volume	158.0	255.9	382.5	697.5	1311.9	1261.8
Total payment transactions	1.3	1.9	3.1	6.7	14.3	16.8

Source: *Sept 2012's 10-Q and recompilation of earlier Filings*

The company has capitalized these growth opportunities arising from the increasing penetration of e-Commerce and macroeconomic growth in the region, achieving a **CAGR of 37% for Revenues between 2007 and 2011 (387% expected for 2011 - 2012E), with positive and stabilized Free Operating Cash Flow since 2008.**

MELI has succeeded in consolidating a value generating business model reflected in a low capital utilization, and a **stabilized ROIC since 2007 averaging 30.3% approximately between 2007 and 2012E,** well exceeding the opportunity costs of the capital of the firm, estimated around 11.3% at present.

We consider that from an operating and financial perspective MELI is well positioned to generate fundamental value and shareholders' return, by replicating and further enhancing its existing business in the years ahead.

MELI e-Commerce Ecosystem

Its services are organized under four business units:

- Mercadolibre: online marketplace where users can sell and buy products ;
- MercadoPago: a payment solution available both onsite as well as offsite;
- MercadoClics: an advertisement service that allows third parties to promote themselves onsite;
- MercadoStores: an online service to host offline stores on the web.

Marketplace, **representing 85% of consolidated revenues**, is a virtual place where users can sell and buy products on either a fixed-price or auction-based format. MELI neither provides any of the products offered nor arranges its deliveries.

Revenues come from fixed or percentage fees charged to the sellers, depending on the type of listing. Fixed charges are paid in advance whether or not the article is sold. Proportional charges are based on a rate applied on the transaction value and is only due if the article is effectively sold.

Growth in this unit is driven by internet and e-commerce penetration in LATAM, reflected in Gross Merchandise Volume (GMV), generational turnover, as purchase power reach more internet-users, general reputation of MELI and its services, Innovation and technology platform upgrade and growth in overall economy of the countries it serves

MercadoPago is a payments solution platform, available both onsite and offsite. This business **represents about 15% of consolidated revenues and delivers the highest growth within the company**, but at lower operating margins.

The **revenue** of this unit comes from direct processing charges to offline payments and interest rate spreads capitalized by discounting credit card receivables related to financings of customers' purchases. Almost 50% of all purchases trough MercadoPago are paid through monthly installments. When a transaction is completed, buyers deposit cash in MercadoPago, which holds the payment to the seller until the buyer receives and accepts the product and also benefits financially by holding such cash position.

Growth in this unit has been driven by MELI's efforts to include MercadoPago as a payment method, even making it mandatory for some users and products, the increasing reputation of MELI as a valid intermediary of the transaction and general increase of the e-payment utilization for a wide range of customers.

MercadoClics is an advertisements service that allows third parties to promote themselves onsite. Growth in this unit has been driven mainly by the traffic on MELI's marketplace.

MercadoStores is an online service to host offline stores on the web.

These two units represent the **smallest portion of consolidated revenues, and are accounted for under Market Place's revenues**.

Brief Industry Overview

The key industry driver is GMV driven by the number of registered users. This target audience is a narrowed percentage of the population that has access to internet, engage on online commerce and belong to the Mercadolibre community[2] with a yearly budget restriction.

Internet penetration is the amount of the population with internet access - increasing from 24% on 2007 to 45% on 2011 - with a 17% per annum increase.

Exhibit 2: 2007-2011 Internet penetratrion.

	Year Ended December 31,				
	2007	2008	2009	2010	2011
Country:					
Argentina	41%	50%	57%	66%	75%
Brazil	24%	29%	35%	37%	39%
Venezuela	21%	26%	33%	38%	40%
Mexico	21%	22%	26%	31%	36%
LATAM	**24%**	**29%**	**35%**	**38%**	**45%**

Source: *Internet World Stats, eBit, conScore.com, Cámara Argentina de Comercio Electrónico and AMPICI. Own making*

Whether internet user may or may not engage on online e-commerce, e-commerce penetration reflects the amount of internet users that sell or purchase online. This driver is related to e-commerce infrastructure, such as online banking penetration, mobile and high speed internet availability as well as market willingness to move from traditional to online channels. LATAM has the fastest growing e-commerce drivers in the world. With improving infrastructure, e-commerce penetration has increased its share on internet users from 16% to 31% from 2007 to 2011 at a 18% yearly growth.

Exhibit 3: 2007-2011 e-commerce penetratrion.

	Year Ended December 31,				
	2007	2008	2009	2010	2011
Country:					
Argentina	17%	20%	22%	26%	30%
Brazil	21%	24%	26%	32%	41%
Venezuela	16%	25%	28%	31%	35%
Mexico	9%	11%	13%	14%	15%
LATAM	**16%**	**20%**	**22%**	**26%**	**31%**

Source: *Internet World Stats, eBit, conScore.com, Cámara Argentina de Comercio Electrónico and AMPICI. Own making*

These booming industry drivers flow through to registered site users: from 12.2 mm users on 2005 to 65.8 mm on 2011, or a 32% CAGR. Registered users sell or buy merchandise with an unwavering frequency of around 0.7 transactions per user. Therefore, increasing transactions have improved MELI's GMV from USD 1,511.5 mm to USD 4,820.4 mm for the period 2007 to 2011.Moreover - and as a result of management's interest to develop the business – total payments volume has increased its participation from USD 158 mm (10% penetration on GMV) to USD 1,311.9 mm (27% penetration on GMV) from 2007 to 2011.

Competitive Strategy

Competition in LATAM e-commerce is intensifying due to increasing internet and e-commerce penetration in the countries, and it includes not only C to C sites such as MELI, but also pure internet retailers, standard retailers extending into e-commerce and online auction sites, just to mention some categories. **However MELI continues to hold a commanding market share of 28%**, well ahead of its closest competitor who holds 8% share. On a by country basis, market share is either stable or growing, except for Mexico which nonetheless shows revenue growth.

To strengthen further its competitive position, special attention is gathered by management on innovation. Investments aim to leverage revenues by keeping a competitive user interface through R&D and the technology roll-out recently implemented. Vertical integration is also a key. Hence, investments were allocated on new features, such as the payment solution, and on R&D to create added value for paying customers, marketable onsite and offsite.

To raise this entry barrier, MELI has acquired few players such as **former Ebay's subsidiary iBazar.com in 2001, DeRemate.com in 2005, 2006 and completing it in 2008 or AutoPlaza in 2011.**

[2] $\text{Users} = \sum_{\text{LATAM}} \text{Population} \times \text{Internet Penetration} \times \text{E-commerce Penetration} \times \text{MELI Marketshare}$

Potential strong competition from Amazon is certainly a threat, given its existing customer network in LATAM countries, its wide experience in e-commerce and its big pockets to make investments. Though Amazon's business structure is similar to MELI's, it seems to be rather custom-made for the US market, as they participate more actively in fabrication and distribution of products. Their entry would probably deteriorate their financials in the short and medium term as they get the marginal know-how necessary to operate in this market and adapt their business model. Amazon is offering nowadays cloud computing services in Brazil, but hasn't expressed official guidance related to entering the e-commerce business directly. Public rumors may be quite revealing of its entry activities, which may even include acquisitions.

As for Ebay, it has owned 18.4% of MELI's shares since 2001, and it also had a non-competition agreement since that time which has expired in 2006. Ebay have shown only small efforts to enter the region since then, and in case it would seriously consider an entry, we rather believe that it would attempt to either acquire or work together with MELI to capitalize its knowhow and profitable business model.

Given that profitable growth business models for the industry have truly been proven, particularly by MELI's operations, we do expect competition to intensify around MELI's environments. However, we believe that the company will maintain is commanding position with a profitable business model which will generate value.

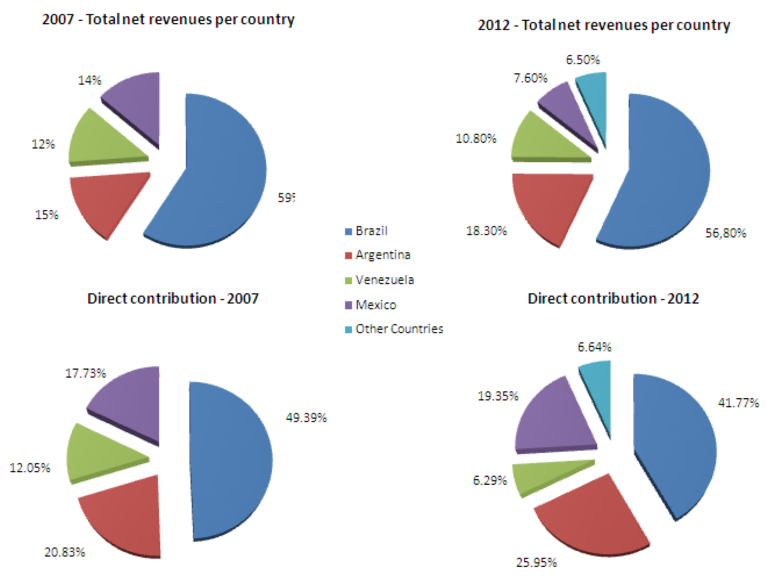
Regional Growth

The company has operations in Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, Mexico, Peru, Uruguay, Venezuela, Dominican Republic, Panama and Portugal. The combined markets served have total population of 591 mm approximately, significantly larger than the 314 mm of the USA.

LATAM e-commerce market is still developing, with an internet penetration of just 45% (YE 2011) for the entire region, but evolving faster than any other region in the world.

Furthermore, other big populated countries have MercadoLibre as one of the main pages visited, even as they are not generating much revenue to the company nowadays. In the general ranking of top visited internet sites by country, MELI occupies Nº6 in Uruguay, Nº12 in Colombia, Nº13 in Chile, Nº15 in Peru and Nº15 in Ecuador[3], being the main e-commerce site visited in all these countries except for Ecuador, where is the second after Amazon.

Graph 1: Revenues and contribution by Country.



Source: *Sept 2012's 10-Q and recompilation of earlier Filings*

[3] According to alexa.com

Financial Overview

Revenues and Operating Cash Flow

As seen above, the company's consolidated revenues have grown at a CAGR of 37% between 2007 and 2011, mainly driven by GMV growth at a 33% CAGR.

Exhibit 4: Operating Margin and NOPAT.

	Year Ended December 31,					LTM Ended	Estimated
	2007	2008	2009	2010	2011	sep-2012	Full 2012
Gross Merchandise Volume	1511.5	2078.9	2750.7	3405.9	4820.4	5579.1	5857.7
Growth Over Prior Year (in %)	*40.59%*	*37.54%*	*32.32%*	*23.82%*	*41.53%*	*15.74%*	*21.52%*
Net Revenues	85.1	137.0	172.8	216.7	298.9	356.3	411.7
Growth Over Prior Year (in %)	*63.34%*	*60.99%*	*26.13%*	*25.41%*	*37.93%*	*19.20%*	*37.74%*
Cost of Net Revenue	(18.3)	(27.5)	(36.0)	(46.5)	(72.1)	(91.4)	(107.2)
Gross Profit	**66.8**	**109.5**	**136.8**	**170.2**	**226.8**	**264.9**	**304.5**
Gross Margin	**78.50%**	**79.93%**	**79.17%**	**78.54%**	**75.88%**	**74.35%**	**73.96%**
Operating Expenses:							
Product and Technology Development	(4.4)	(7.3)	(12.1)	(15.9)	(23.3)	(28.5)	(33.0)
Sales and Marketing	(27.6)	(40.0)	(42.9)	(48.9)	(65.0)	(70.3)	(85.5)
General and administrative	(13.2)	(22.8)	(25.8)	(30.8)	(38.8)	(46.8)	(51.1)
Total Operating Expenses	**(45.2)**	**(70.1)**	**(80.8)**	**(95.6)**	**(127.1)**	**(145.4)**	**(169.6)**
Income From Operations	**21.6**	**39.4**	**56.0**	**74.6**	**99.7**	**119.5**	**134.9**
Growth Over Prior Year (in %)	*401.30%*	*82.41%*	*42.13%*	*33.21%*	*33.65%*	*19.86%*	*35.31%*
Operating Margin	**25.38%**	**28.76%**	**32.41%**	**34.43%**	**33.36%**	**33.54%**	**32.77%**
Hipotetic Tax (33%)	(7.1)	(13.0)	(18.5)	(24.6)	(32.9)	(39.4)	(44.5)
Hipotetic NOPAT	**14.5**	**26.4**	**37.5**	**50.0**	**66.8**	**80.1**	**90.3**

Source: *Income Statement data and self data processing*

Gross Profit margins have slightly declined since 2008, from 80% in 2008 to 76% in 2011 and is expected to further decline towards 74% in 2012E. This trend highlights the increasing participation of MercadoPago (27% at 2011 in lieu of 10% at 2007 over GMV) in consolidated revenues, which has a lower gross profit margin than Marketplace.

Cost of Net Revenue is related to transaction expenses, mainly driven by financing cost related to MercadoPago's processing fees charged by credit card issuers, IT related such as ISP suppliers, service fees, taxes and customer service.

From 2009 financing costs have increased at a 50% growth rate. Additionally, payroll on customer service has also increased at a faster rate than revenues at a 49% y-o-y from 2010 to 2011. Both grow faster than revenues and therefore deteriorate gross profit's growth rate. See Exhibit 1 in the appendix.

Operating expenses have increased at a lower rate than revenues, all which has resulted in an attractive level growth and a substantial improvement in Operating Profit margins from 25% in 2007 to an estimated level of 33% in 2012E.

Operating expenses are gathered under 1) Product and Technology Development (R&D), 2) Sales & Marketing and 3) General & Administrative. Across these centers, costs are related expenses such as compensation costs driven by employee headcount on all three centers, departmental budget expenses such as depreciation & amortization on R&D, online and offline advertisement in S&M, outsourced services in G&A and other expenses across all departments. See Exhibit 2 in the Appendix.

NOPAT has improved from 14.5 mm in 2007 to 66.8 mill in 2011 (46% CAGR). It is calculated by applying the weighted average tax rate (33%) of the company in each fiscal year to its effective operating profit.

Investments and Operating Free Cash Flow

Net Operating Investments, driven primarily by Capital Expenditure and changes in Net Working Capital, has shown a moderate expansion between 2007 and 2012E, reflecting a low capital intensity of the business which immobilizes relatively low amounts of Capital Employed.

Total Operating Assets (Net), which represent the operating platform that generates NOPAT through the normal course of business, has shown only modest expansion, which is consistent with the Operating Investment strategy just described.

The company also holds a relatively large position of financial investments on its balance sheet, through the accumulation its free operating cash flow in recent periods. Although such financial assets do immobilize a relatively large portion of its capital employed, we trust that management's good judgment will bring such resources to good use through acquisitions of further investment expansion that generate fundamental value, or otherwise it will simply be returned to shareholders at some point if.

Operating Free Cash Flow has stabilized to positive grounds since 2008, after several years of positive and negative numbers. This is a clear reflection of NOPAT's continuous improvement in the last 6 years on a business model, which is achieving a solid return on capital performance.

Exhibit 5: Operating Cash Flow .

	Year Ended December 31,					LTM Ended	Estimated
	2007	2008	2009	2010	2011	sep-2012	Full 2012
NOPAT	14.5	25.1	37.5	50.0	66.8	80.1	90.4
Depreciation & Amortization	2.3	3.3	3.9	4.9	7.3	8.4	8.8
Gross operating investment	(19.8)	(13.4)	(25.3)	(4.8)	(31.3)	(39.3)	(18.8)
OPERATING FREE CASH FLOW	-3.0	16.4	16.1	50.1	42.8	49.2	80.4

Source: *Cash flow data and self data processing*

Financial investments have grown 21% CAGR in the 2007-2012E period. Positive Operating Free Cash Flow has been partially used for the payment of dividends since 2011, but on a larger scale, it has been retained in the balance sheet as financial investments, which immobilize a large portion of Capital Employed. We certainly hope that such cash shall be returned to shareholders unless invested for profitable growth or utilize for acquisition that create synergies. This shall be considered as an opportunity for which the timeline is rather uncertain.

Capital Employed

Total Capital Employed is mostly composed by Total Shareholders' Equity, since the company has reduced Interest Bearing Debt to a negligible number, while minority interest is well bellow 2% of total Capital Employed. Since the company's IPO in 2007, internally generated resources capitalized as Retained Earnings have been the primary source of Capital Employed expansion and it is likely to remain this way.

Exhibit 6: ROIC & ROE.

	2007	2008	2009	2010	2011	sep-2012	Full 2012
Capital Employed:							
Total Gross Debt	9.7	17.8	3.2	0.3	0.3	0.2	0.2
Total Equity (book Value)	91.7	93.4	114.2	171.7	219.2	268.1	298.3
Minority Interest	0.0	-	0.0	-	4.0	4.0	4.5
Total Capital Employed	**101.4**	**111.3**	**117.4**	**172.0**	**223.5**	**272.3**	**302.9**
ROIC	21.7%	24.9%	32.8%	34.5%	33.8%	32.3%	34.3%
ROE	16.9%	20.3%	32.0%	39.2%	38.9%	38.6%	38.7%

Source: *Balance Sheet data and self data processing*

Return on Invested Capital & Equity

Return on Invested Capital has shown a clear improvement since commencement of business, and seems to have overcome its opportunity cost of capital already since 2007, stabilizing above a 32% since 2009 and an average of 30.3% between 2007 and 2012E. This is a clear indication that the business model of the company and the performance of the operating units have stabilized, representing declining operating risk. And most important, the company generates returns well in excess of its cost of capital of 11.3%, which is a key to secure that future growth will be a source of value generation and not a cause for value destruction.

Business Outlook

MELI's prospects for profitable growth are encouraging. High revenue growth will be primarily driven by increasing LATAM e-commerce penetration and further enhanced by general macroeconomic. New players are expected to enter the e-commerce space and become an additional driver to support industry growth. MELI's outstanding innovation skills and commanding market position, combined with management's proven capabilities for value generation are expected to capitalize upcoming growth opportunities successfully.

Macroeconomic Assumptions

LATAM is among the fastest growing economies in the world, and a high growth is expected to continue in coming years. IMF is estimating a 3.6% real GDP growth for LATAM in 2012, and despite potential down side economic and political volatility in certain countries, our GDP estimates for the next 5 years is 6.5% per annum, bellow IMF estimations. Expected growth on a by-country basis is presented bellow. See exhibit 4 in the Appendix.

Foreing exchange rates are reflecting a slight nominal decline for the local currencies, reflecting lower expected inflation and lower real interest rates for the US dollar currency as compared to the local currencies in major LATAM countries. The potential scenario for strengthening of real exchange rate of local currencies against the US dollar – reflecting higher economic growth and increases of general price level of non-tradable goods - has not been incorporated in our model into our base assumptions and is embedded in our valuation only as an opportunity factor. See exhibit 5 in the Appendix.

Industry operations assumptions

In terms of industry operating assumptions, which are the key drivers for top line growth, our expectations are in line with a vibrant market environment, eager to trade in a growing on-line community. Internet penetration is expected to grow by an additional 12 percentage points to reach 60% of the population by 2017 from a 48% at present day. E-commerce will also increase by an additional 12 percentage points to 47% of Internet share by 2017 from 35% at present day. Estimations on a by country basis are presented in tables bellow.

Exhibit 7: E-commerce penetratrion assumptions.

	Year Ended December 31,					
	2012E	2013E	2014E	2015E	2016E	2017E
Country:						
Argentina	33%	36%	40%	43%	47%	50%
Brazil	52%	62%	68%	74%	78%	82%
Mexico	15%	15%	15%	15%	15%	15%
Venezuela	35%	35%	35%	35%	35%	35%
LATAM	**35%**	**39%**	**42%**	**44%**	**46%**	**47%**

Source: *Forrester estimates, Alexa.com and Internet World Stats. Own making*

Competitive Overview

New players are expected to enter the e-commerce space but such entry is expected to become an additional driver to support industry growth. MELI's outstanding innovation skills and extensive market presence are key advantages which will consolidate its market presence and allow the company to sustain its market share.

Gross Merchandise Volume

These assumptions will result on a 20% CAGR GMV expansion from USD 4,820.4 mm at 2011 YE to USD 14,477.8 mm by 2017. A 33.5% of total variance is due to LATAM's internet penetration increase, 55.5% is due to higher e-commerce penetration and the remaining 11% due to economic expansion net of exchange exposure. MercadoPago's GMV will expand from USD 1,311.9 mm on 2011 to USD 11,582.2 mm on 2017 at a 44% CAGR.

Brazil GMV reaches USD 8 Bb by 2017 from USD 3.3 Bb estimated in 2012, growing at 28% in 2012, slowing to 25% in 2013 and further towards 16% on year 2017, primarily driven by softlanding of e-commerce penetration. See Exhibit 7 in the Appendix.

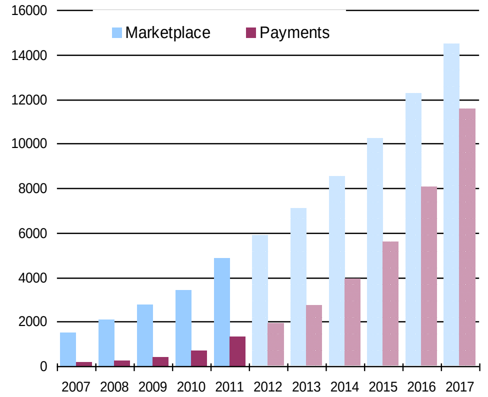
Argentina's GMV is expected to grow at a declining annual rate from a USD 0.6 Bb and 13% p.a. in 2012, to USD 0.88 bn and 2% p.a. by 2017. This slowdown is due to internet users' saturation and devaluation of the Peso from 4.6 to 8.4 Pesos/USD. See exhibit 8 in the Appendix.

Mexico's GMV is improving from and estimate of USD 1.3 Bb in 2012 to USD 5.4 Bb in 2017 at a 32% CAGR, primarily driven by GDP expansion and an increasing internet penetration. See exhibit 9 in the Appendix.

Venezuela GMV will deteriorate from USD 0.3 Bb to USD 0.2 Bb, primarily due to devaluation from 5.2 to 16.3 Bolivares/USD. See exhibit 10 in the Appendix.

GMV growth for other reporting countries - mostly Caribbean - are considered flat since 2011 (0% CAGR)

Graph 2: MELI GMV forecast.



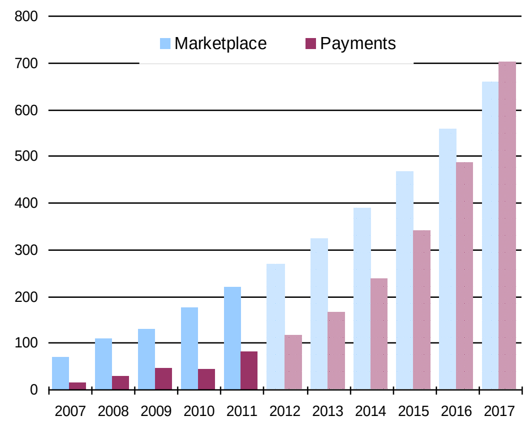
Source: *2011, 2010 & 2009 MELI 10K SEC filings. Own making.*

Revenues

The estimated take rate for revenues from 2013 to 2017 as percentage of marketplace GMV is considered constant at 4.55% following 2011 rate. The take rate for MercadoPago is expected to remain flat at 6.05% (5.6% of financial charges reported in 2009YE 10K, plus a 450 bps spread due to Argentina's transactions recorded as MercadoPago's revenue). See exhibit 11 in Appendix.

Consequently, **revenues will expand at 29%** CAGR, which is higher than GMV's growth rate due to MercadoPago's higher impact on consolidated revenues. Marketplace revenues is estimated to increase from USD 219.5 Mm on 2011 to USD 659.2 Mm on 2017 (20% CAGR), while MercadoPago's revenues is expected to increase from USD 79.4 mm in 2011 to USD 700.7 mm in 2017 (44% CAGR).

Graph 3: MELI Revenue forecast.



Source: *2011, 2010 & 2009 MELI 10K SEC filings. Own making.*

Operative Margins & Profits

Gross margin was estimated from financial statements. The last two reporting years, since the business has consolidated and economics of scale opportunities seem exhausted.

The cost of net revenues for Market place is expected constant at around 14% from 2011 onwards. Cost of net revenues for MercadoPago -mostly related to financial charges- is considered to be constant at 51% from 2011 onward too.

Consequently, a 29% CAGR in consolidated revenues by 2017 will bear the impact of higher weight by MercadoPago, resulting in consolidated gross margin deterioration from 74% in 2012 down to 67% by 2017.

Other centrally held operating costs shall have a 43% impact on margins. Therefore, due to the increase of MercadoPago impact on revenues, operating margin is expected to drop from 31% in 2012 to 24% in 2017, representing an increase of Operating profit from USD 134.8 mm in 2012 to USD 321.6 mm in 2017, reflecting mostly the effect of volume improvement.

Exhibit 8: 2007 – 2017 Operating margin evolution.

	Year Ended December 31,										
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Gross Margins	25%	29%	32%	34%	33%	31%	30%	29%	27%	25%	24%

Source: *2011, 2010 & 2009 MELI 10K SEC filings. Own making*

NOPAT

The tax rate applied to profits is a flat weighted average rate of 33%. NOPAT improves at a 19% CAGR from USD 90.3 mm in 2012 to USD 215.5 mm in 2017, consistent with revenues' improvement.

Operating Investments and Free Operating Cash Flow

Operating investments are expected to be modest. Capex is estimated to remain constant at 5% of revenues, and growing at its same rate. Working capital assumptions are based on historical turnover ratios with an improvement in collection terms due to MercadoPago's penetration. Overall, Total Operating investments will remain slightly above D&A, resulting on Net Operating Investments expected to grow at 23% CAGR for the next 5 years, which addresses the advantages of MELI's business model.

Operating Free Cash Flow

NOPAT will remain well above Net Operating Investments resulting on a scaling Free Operating Cash Flow, which will grow from USD 80.4 mm in 2012 to USD 187.6 in 2017 at 18% CAGR.

Valuation

The target USD 93.85 price was achieved through DCF methodology, complemented by trading multiples comparison against competitors and other companies in the internet space. The key assumptions to build the target price are grounded on our business and financial analysis of performance and the business outlook presented above.

Considering that MELI's business model requires a relatively low level of Net Operating Investments, the most representative driver in the DCF methodology is NOPAT and its growth. Cash flows for two separate business units were projected: Marketplace and MercadoPago. Free Cash Flow has been forecasted through years 2012 to 2017 as a positive value in all these years. Terminal value represents a large portion of Net Enterprise Value reflecting the value of future growth.

The company's terminal value is calculated at year five, capitalizing a progressive slowdown in growth in the subsequent years as the industry approaches a steady growth stage at some future. Marketplace revenues were projected with a 20% CAGR, while MercadoPago is expected to surpass marketplace increase due to its accelerated penetration to reach 80% target over GMV, resulting in a 40% CAGR (compared to 66% CARG during previous seven years).

Future cash flows and terminal value were discounted at an 11.3% WACC (See exhibit 14 in the Appendix). Capital structure is taken as full equity capital, thus WACC is equal with the shareholder's expected return. WACC is calculated on a 6.5% market risk premium and a risk factor for MELI of 1.5, which is consistent with a declining operating risk reflected on a stabilized Free Cash Flow and a stable and high ROIC, and manifested on its market price behavior. In addition, cash and equivalents were considered as part of net operating working capital, with the purpose of providing liquidity to "funds payables to customers".

Exhibit 9: Value Calculation (USD mm).

Net Enterprise Value	3961
(+) Cash and equivalents	98
(+) Short Term Investements	**79**
(-) Total Debt	**0,2**
(=) Total Equity Value	**4139**
(/) #Shares	**44,1**
(=) Target Price per share (USD)	**93,85**

Exhibit 10: WACC.

WACC	11,30%
R Free	**1,50%**
Market Risk Premium	6,50%
MELI's Risk Factor	**1,5**

Source: *Own estimate based on company data*

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Comparable Multiples

Valuation achieved through DCF methodology was compared to value obtained through comparable multiples valuation, to obtain a reference for relative market pricing within related industries. Comparable firms were selected considering competencies, average return on capital, growth of operating income and EPS growth.

MELI currently trades against 2013 estimates at PE(13E) of 32.7x and EV/EBITDA (13E) of 19.8x. Our target price of USD 93.85 represents a 24% upside which translates into target trading multiples of 40.6x PE(13E) and 24.9x EV/EBITDA (13E). We see that our target multiples represent a reasonable upside for MELI as compared to top tier e-commerce operators such as Ebay and Amazon. In particular, when considering MELI's stronger fundamentals such as average 3 years return on equity of 37% and EPS growth of 52% - both expected to remain in high levels for the coming years - we observe that such fundamentals are significantly stronger than those of Amazon (17% and 7% respectively) and Ebay (17% and 4% respectively).

In comparison to the rest of peers in the table, MELI's multiples are comparatively higher. However our target price multiples are justified once again by the stronger fundamentals of MELI. Even companies such as Navtec, which trades at 45.1x 2013 earnings on a high 3yrs average ROE of 33%, has a lower 3yrs EPS growth of only 19%. Also Shunwang, which trades at 25.2x 2013 earnings on an 3yrs average ROE of 32% has a low averaged 3yrs EPS growth of only 1%. Fundamentals for the rest of the table are even weaker.

We also need **to keep in mind that current trading multiples of comparable companies are being affected by unstable market conditions in global markets**, which is less the case for LATAM markets and for MELI consequently. Additionally, MELI's terminal value on DCF calculation represents a multiple to 2017 cash flows of 9.6x EV/EBITDA, which under current market condition seems highly reasonable for a market which is just 5 years forward.

In our view, the relative value analysis supports our USD 93.85 price target recommendation, showing an attractive value opportunity in relation to the top tier e-commerce players and other players in the industry.

Exhibit 11: Relative valuation.

	Estimate Year Ended December 31,						Business Desctiption
	EV/EBITDA			P/EPS			
	2012	2013	2014	2012	2013	2014	
Priceline	14,1	11,5	9,6	19,9	16,3	13,9	Online travel company
Ebay	12,1	10,4	9,1	20,1	17,1	14,8	Online and mobile commerce and payments
Amazon	29,8	21,7	15,9	-	114,9	58,5	Online retailer
Baidu	14,6	11,1	8,7	19,4	15,3	12,1	Internet services and e-commerce
Tencent	19,3	15,1	12,1	27,7	21,6	16,9	Internet service primarily in China
NIC	18,6	15,2	12,6	39,9	32,7	26,6	eGovernment services in USA
Yandex	15,9	11,7	9,4	26,3	19,4	15,4	Specialized search, news, information, price comparisson, consumer reviews
Netflix	29,2	21,5	13,9	-	268,0	67,1	Internet TV sunscription service for shows and movies
SHUNWANG	23,5	16,6	11,4	36,7	25,2	17,1	Internet entertainment platform in China
NAVTEQ	NA	NA	NA	68,4	45,1	45,0	Digital map information and other location-based content
Expedia	8,8	7,6	6,8	18,7	16,1	13,7	Online travel company
Rakuten	5,0	4,2	3,6	18,4	15,3	12,9	e-commerce and payment
Mail.ru	16,1	13,1	10,6	27,1	21,5	17,3	Online communications, entertainment and also e-commerce.
GTECH	NA	NA	NA	23,3	21,5	22,5	Game content, financial transaction processing
Average	**17,3**	**13,3**	**10,3**	**28,8**	**46,4**	**25,2**	
MercadoLibre - Trading Multiple	**21,9**	**19,8**	**16,1**	**32,7**	**32,7**	**26,7**	

Source: *Own Estimate, Company and Market data*

Risks and Opportunities

Our USD 93.85 target represents a fair balance of the various risks and opportunities embedded on its business. Exhibit 18 in the Appendix summarize our view on the various risks and opportunities and a brief description addresses the more relevant factors.

Opportunities are related to real foreign exchange potential appreciation, macroeconomic acceleration, acceleration of penetration rates for internet, general e-commerce and mobile e-commerce, M&A activity, declining operating risk factors, potential for incorporation of debt to capitalize tax shield benefits, and general price increases for overall services.

- **Currencies revaluation:** Higher economic growth expected by LATAM economies against the US economy usually carries an impact of relative price increase for non-tradable good in those higher growth economies. The expected consequence would be for a strengthening of real exchange rate of local currencies against the US dollar. Such effect has not been incorporated into our base assumptions for our valuation model and remains as an opportunity factor in our valuation.
- **Mobile Commerce Development:** The rapid adoption of smartphones and mobile Internet usage is changing the way consumers shop. Regarding Forrester information, although still nascent, mobile commerce is poised for exponential growth. Mobile retail and travel spending grew by 80% in 2011 and is expected to more than double by the end of this year. This situation could directly impact over MELI, generating an upside in E-commerce Industry. By 2017, mobile commerce is expected to quadruple. Retail will be the fastest-growing category, reaping approximately $25 billion in 2017. Consumers will spend about half of this on media products, which currently dominate the retail landscape.

- **Acquisitions within the internet space that deliver synergies for growth:** MELI announced its intentions to continue to acquire businesses, technologies, services or products for the creation of synergies, as previously done with the acquisitions of iBazar, Lokau, DeRemate, CMG and Autoplaza, among others.

Risks are related to potential currencies devaluation in Venezuela and Argentina in the medium term, macroeconomic slowdown, entry by social media players into e-commerce, higher competition and slower growth for Mercadopagos.

- **Currency devaluation in the medium term:** Strong devaluations, particularly in Argentina and Venezuela could materially affect the company's results, negatively affecting nominal US dollar income. Timing remains an open issue, and is a function of monetary expansion financing budget deficits.
- **Social Media engagement on e-commerce:** Several factors may not realize the expected increase in e-commerce in LATAM. The expansion of the phenomenon is associated mostly to consumer perception as to the feasibility of on-line shopping successfully.
- **Higher Competition:** Barriers-to-entry to be relatively low for existing as well as and new competitors, and the launch of new or better sites at relatively low cost using commercially available software can be easily organized. As more shoppers migrate online, more players are tempted to move online, taking market share from existing players.

Glossary

E-COMMERCE: or electronic commerce, a subset of e-business, is the purchasing, selling, and exchanging of goods and services over computer networks (such as the Internet) through which transactions or terms of sale are performed electronically. Ecommerce can be broken into four main categories: B2B, B2C, C2B, and C2C.

- B2B (Business-to-Business)
- B2C (Business-to-Consumer)
- C2B (Consumer-to-Business)
- C2C (Consumer-to-Consumer)
-

E-COMMERCE PENETRATION RATE: is a term used to describe the number of active e-commerce users within a internet users population

GMV: is the onsite volume of successful transactions, on which the company charges a take rate for both commission on down payments and financial charges for payments made in installments. GMV is explained by volume of goods sold and their list prices.

IMF: International Monetary Fund

INTERNET PENETRATION: is the percentage of a population using the internet

MELI: It is the ticker symbol for Mercadolibre Inc in Nasdaq

MOBILE COMMERCE: is any transaction, involving the transfer of ownership or rights to use goods and services, which is initiated and/or completed by using mobile access to computer-mediated networks with the help of an electronic device.

NOPAT: Net operating profit after tax or NOPAT is the after-tax operating cash generated by the business, excluding unusual losses and gains, and financing costs.

NOPAT = Operating Profit x (1 - Tax Rate)

ROIC: Return on capital employed is an accounting ratio used in finance, valuation, and accounting. More specifically the return on investment capital is the percentage return that a company makes over its invested capital.

ROIC = NOPAT / Capital Employed (average)

TAKE RATE : Marketplace revenues as a percentage of gross merchandise volume

Appendix

Exhibit 1: Cost of net revenues breakdown.

	Year Ended December 31,					LTM Ended	Estimated
	2007	2008	2009	2010	2011	sep-2012	Full 2012
Cost Of Net Revenues:							
Financing	(6.9)	(10.9)	(13.9)	(19.4)	(30.6)	N/A	(45.5)
Taxes	(5.0)	(8.1)	(10.7)	(15.0)	(21.3)	N/A	(31.7)
Payroll	(4.6)	(6.2)	(7.8)	(11.1)	(16.6)	N/A	(24.7)
Others	(1.7)	(2.3)	(3.5)	(1.1)	(3.6)	N/A	(5.4)
Total Cost of Net Revenue	**(18.3)**	**(27.5)**	**(36.0)**	**(46.5)**	**(72.1)**	**(91.4)**	**(107.2)**

Source: *2009, 2010 & 2011 MELI 10K SEC filings and self estimation*

Exhibit 2: Operating expenses breakdown.

	Year Ended December 31,					LTM Ended	Estimated
	2007	2008	2009	2010	2011	sep-2012	Full 2012
Operating Expenses:							
Product and technology development:							
Payroll	(1,9)	(3,9)	(5,7)	(8,0)	(10,7)	N/A	(15,2)
Maintainance	(0,5)	(0,9)	(0,9)	(1,4)	(3,3)	N/A	(4,7)
Depreciation & Amortization	(2,1)	(2,5)	(2,5)	(3,2)	(4,9)	N/A	(6,9)
Others	-	(0,1)	(3,0)	(3,3)	(4,4)	N/A	(6,2)
Sales and Marketing:							
Advertisements	(16,9)	(22,1)	(21,6)	(21,4)	(30,0)	N/A	(39,5)
Bad Debt Charges	(6,2)	(8,6)	(10,0)	(14,9)	(19,0)	N/A	(25,0)
Payroll	(3,2)	(6,4)	(8,4)	(9,3)	(11,0)	N/A	(14,5)
Others	(1,2)	(2,8)	(2,8)	(3,3)	(4,9)	N/A	(6,4)
General and administrative:							
Payroll	(6,1)	(10,6)	(12,4)	(16,6)	(21,3)	N/A	(28,0)
Others	(7,2)	(12,2)	(13,4)	(14,2)	(17,6)	N/A	(23,2)
Compensation costs related to acq.	-	(1,9)	-	-	-	-	-
Total Operating Expenses	**(45,2)**	**(72,0)**	**(80,8)**	**(95,6)**	**(127,1)**	**(145,4)**	**(169,6)**

Source: *2009, 2010 & 2011 MELI 10K SEC filings and self estimation*

Exhibit 3: Operating Assets.

	Year Ended December 31,					LTM Ended	Estimated
	2007	2008	2009	2010	2011	sep-2012	Full 2012
Operating Assets:							
Net Property, Plant & Equipment	4.1	5.9	5.9	20.8	30.9	35.2	42.7
Goodwill	23.0	65.7	59.8	60.5	62.1	61.4	61.4
Other intangible assets	0.4	7.3	4.5	4.1	6.5	7.5	7.5
Net Working Capital	18.9	(12.0)	8.5	(0.3)	6.3	30.8	0.5
Operating Assets	**46.4**	**66.9**	**78.8**	**85.1**	**105.8**	**134.9**	**112.1**
Short Term Investments	52.3	31.6	14.6	5.3	74.9	79.4	80.8
Long Term Investments	1.3	9.2	26.6	64.5	25.6	59.4	59.4
Operating Assets + Financial Investments	**100.0**	**107.7**	**120.0**	**155.0**	**206.4**	**273.7**	**252.3**

Source: *Balance Sheet data.*

Exhibit 4: GDP CAGR (Source currency).

	Avg CAGR
	2012-2017
Country:	
Argentina	6.5%
Brazil	4.5%
Venezuela	8.0%
Mexico	3.0%
LATAM	**6.5%**

Source: *International Monetary Fund World Economic Outlook Oct 2012. Own making.*

Exhibit 5: 2012 to 2017 Exchange Rate assumptions.

	Year Ended December 31,					
	2012	2013	2014	2015	2016	2017
Country:						
Argentina	4.62	5.21	5.88	6.65	7.46	8.35
Brazil	1.83	1.95	2.00	2.05	2.10	2.15
Venezuela	5.21	6.55	8.28	10.41	13.03	16.25
Mexico	13.47	13.81	13.98	14.15	14.30	14.43

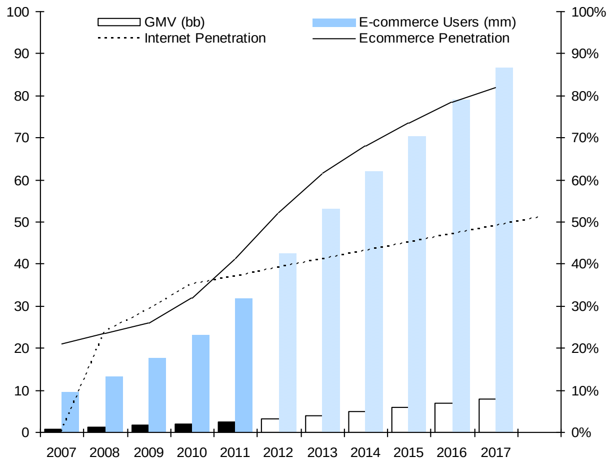
Source: *International Monetary Fund World Economic Outlook Oct 2012. Own making.*

Exhibit 6: Internet penetration assumptions.

	Year Ended December 31,					
	2012E	2013E	2014E	2015E	2016E	2017E
Country:						
Argentina	82%	87%	92%	92%	92%	92%
Brazil	41%	43%	45%	47%	49%	51%
Mexico	41%	46%	52%	57%	62%	67%
Venezuela	43%	46%	49%	52%	54%	57%
LATAM	**48%**	**50%**	**53%**	**55%**	**58%**	**60%**

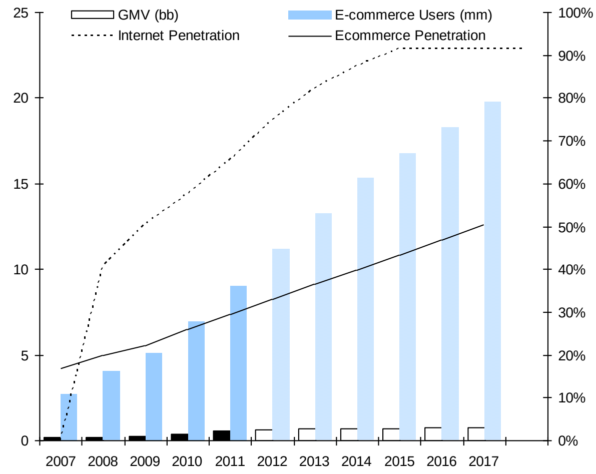
Sources: *Forrester estimates, Alexa.com and Internet World Stats. Own making*

Exhibit 7: Brazil e-commerce trends and forecasts.



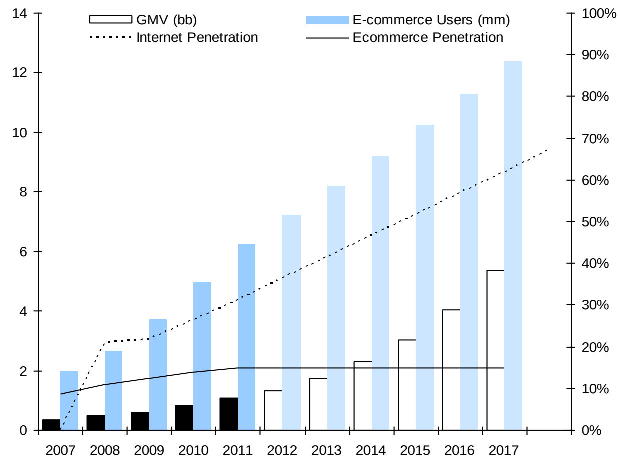
Source: *Forrester estimates, IMF, World Internet Stats and eBit. Own making*

Exhibit 8: Argentina e-commerce trends and forecasts.



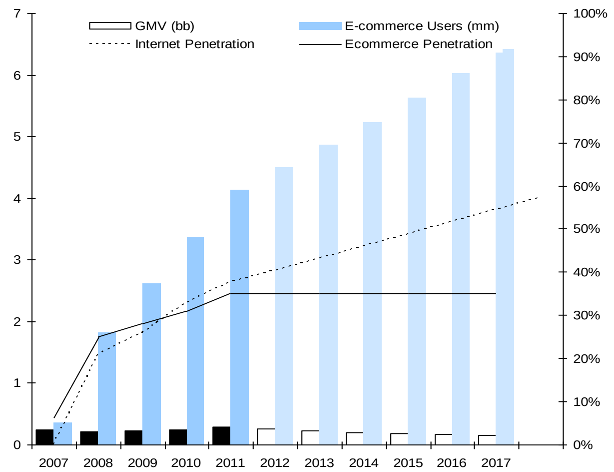
Source: *Forrester estimates, IMF, WIS and Cámara Argentina de Comercio Electrónico. Own Making.*

Exhibit 9: Mexico e-commerce trends and forecasts.



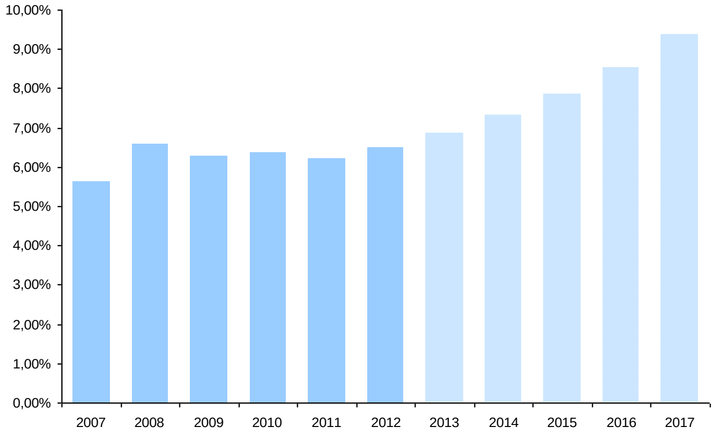
Source: *Forrester estimates, IMF, World Internet Stats and AMIPCI. Own making*

Exhibit 10: Venezuela e-commerce trends and forecasts.



Source: *Forrester estimates, IMF, World Internet Stats. Own making.*

Exhibit 11: 2007-2017 Weighted average take rate evolution.



Source: *2011, 2010 & 2009 MELI 10K SEC filings and GMV estimates. Own making.*

Exhibit 12: 2007-2017 Gross margin evolution.

	Year Ended December 31,								
	2007	2008	2009	2010	2011	2012	2013	2014	2015
Gross Margins	79%	80%	79%	79%	76%	74%	73%	72%	7(

Source: *2011, 2010 & 2009 MELI 10K SEC filings. Own making*

Exhibit 13: Projected Balance Sheet.

	Year Ended December 31,						
	2011	IVQ 2012	E 2013	E 2014	E 2015	E 2016	E 2017
ASSETS	0	0	0	0	0	0	0
Cash And Equivalents	67.4	130.0	254.9	410.3	614.3	877.2	1,213.6
Short Term Investments	74.9	79.4	79.4	79.4	79.4	79.4	79.4
Accounts Receivable	16.8	31.9	26.0	32.5	40.8	51.5	65.2
Credits card receivable	23.9	23.2	33.4	47.9	68.9	99.1	142.5
Prepaid Exp.	1.3	2.2	1.9	2.4	3.1	4.0	5.3
Deferred Tax Assets, Curr.	9.1	10.7	10.7	10.7	10.7	10.7	10.7
Other Current Assets	6.9	8.2	8.2	8.2	8.2	8.2	8.2
Total Current Assets	200.2	285.6	414.4	591.4	825.4	1,130.1	1,524.8
Net Property, Plant & Equipment	30.9	42.7	55.1	70.4	89.6	114.0	145.5
Long-term Investments	25.6	59.4	59.4	59.4	59.4	59.4	59.4
Goodwill	62.1	61.4	61.4	61.4	61.4	61.4	61.4
Other Intangibles	6.5	7.5	8.1	8.6	9.2	9.9	10.6
Deferred Tax Assets, LT	6.5	6.1	6.1	6.1	6.1	6.1	6.1
Other Long-Term Assets	24.1	6.0	6.0	6.0	6.0	6.0	6.0
Total Assets	**355.9**	**468.8**	**610.6**	**803.4**	**1,057.2**	**1,387.0**	**1,813.8**
LIABILITIES	0	0	0	0	0	0	0
Accounts Payable	20.3	32.5	25.3	29.4	40.1	54.9	75.6
Funds payable to customers	69.2	83.6	120.1	172.7	248.3	356.9	513.1
Accrued Exp.	13.5	24.4	21.7	29.4	40.1	54.9	73.1
Curr. Port. of Cap. Leases	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Curr. Income Taxes Payable	11.6	5.7	18.8	23.0	28.0	34.2	41.5
Other Current Liabilities	3.5	4.8	4.8	4.8	4.8	4.8	4.8
Total Current Liabilities	118.3	151.0	190.9	259.4	361.4	506.0	708.2
Capital Leases	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Def. Tax Liability, Non-Curr.	8.7	8.4	8.4	8.4	8.4	8.4	8.4
Other Non-Current Liabilities	5.6	6.7	6.7	6.7	6.7	6.7	6.7
Total Liabilities	132.8	166.1	206.0	274.5	376.5	521.1	723.3
Total Common Equity	219.2	298.2	398.6	521.2	670.7	853.2	1,074.4
Minority Interest	4.0	4.5	5.9	7.8	10.0	12.7	16.0
Total Equity	223.2	302.7	404.6	528.9	680.7	865.9	1,090.5
Total Liabilities And Equity	**355.9**	**468.8**	**610.6**	**803.4**	**1,057.2**	**1,387.0**	**1,813.8**

Source: *2009, 2010 & 2011 MELI 10K SEC filings and self estimation*

Exhibit 14: Projected Valuation.

	Year Ended December 31,						
	2011	IVQ 2012	E 2013	E 2014	E 2015	E 2016	E 2017
	0	0	0	0	0	0	0
Revenue	269.8	141.8	486.6	624.3	805.3	1,045.0	1,360.0
Operating Profit	90.5	44.3	147.2	179.4	218.5	266.0	321.6
Taxes	26.9	15.1	50.2	61.3	74.8	91.2	110.6
NOPAT	60.7	29.7	98.6	120.2	146.4	178.2	215.4
Net Capex	11.7	11.7	24.3	31.2	40.3	52.2	68.0
Change Intangible Assets	1.3	0	0.5	0.6	0.6	0.6	0.7
Change Working Capital (en Sentido Estricto)	24.4	(30.3)	10.0	2.8	(3.9)	(3.7)	(4.1)
Total depreciations & amort.	6.4	2.4	12.0	16.0	21.2	27.9	36.7
OPERATING FREE CASH FLOW	**29.6**	**50.7**	**75.7**	**101.6**	**130.6**	**156.9**	**187.6**
Terminal Value	1,240.6						
Cash And Equivalents	98.2						
Short Term Investments	79.4						
Gross debt	0.2						

Source: *2009, 2010 & 2011 MELI 10K SEC filings and self estimation*

Exhibit 15: Potential impacts associated with risks and opportunities.

	Geographic	Industry	Operating and General
Upside	• Currencies revaluation • Economic acceleration	• Mobile e-commerce development • Internet penetration acceleration • E-commerce penetration acceleration	• Declining risk factor • Potential for Tax shield capitalization due to positive FCF • Acquisitions for growth synergies within internet space • Price movements
Downside	• Currencies devaluation in medium term • Economic slowdown	• Social Media engagement on e-commerce • Higher Competition	• Slower growth for MercadoPago Business

Source: *Own Estimate*

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CFA Institute

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Misprint corrections.

Exhibit 16: Projected Income Statement.

	9 Months Ended		Year Ended December 31,				
	sep-2012	4° Q 2012	E 2013	E 2014	E 2015	E 2016	E 2017
Total Revenue	269,80	141,80	486,60	624,30	805,30	1045,00	1360,00
Cost Of Goods Sold	-70,70	-36,50	-130,20	-176,40	-240,50	-329,70	-453,60
Gross Profit	**199,20**	**105,30**	**356,40**	**447,90**	**564,80**	**715,30**	**906,40**
Selling General & Admin Exp.	-86,90	-49,60	-170,30	-218,50	-281,80	-365,70	-476,00
R & D Exp.	-21,70	-11,30	-38,90	-49,90	-64,40	-83,60	-108,80
Operating Income	**90,50**	**44,40**	**147,20**	**179,50**	**218,60**	**266,00**	**321,60**
Interest Expense	-	-	-	-	-	-	-
Interest and Invest. Income	9,00	1,40	4,90	6,20	8,10	10,40	13,60
Income Tax Expense	-26,90	-15,10	-50,20	-61,30	-74,80	-91,20	-110,60
Net Income	**72,60**	**30,60**	**101,90**	**124,30**	**151,80**	**185,20**	**224,60**
EPS	**1,64**	**0,69**	**2,31**	**2,82**	**3,44**	**4,19**	**5,09**

Source: Sept 2012 10-Q SEC Filling and self estimation.