Investment Research

Angie's List (ANGI)

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The Business Model

From membership, ANGI has to elicit consumer reviews with common gift certificates! Or it has to offer ANGI CASH for membership referrals! Why? According to its 5 year average, ANGI recognizes 92% of its revenue as a sales and marketing expense! Wow!

If ANGI positions correctly in the market, the consumer naturally provides the review. And if the service provided by ANGI actually creates value in the market, then the consumer naturally joins the membership and uses the service.

Since the most recent upgrade by Bank of America Merrill Lynch on 6/6/14, ANGI has generated an ROI of approximately 25%. Bank of America Merrill Lynch cited an increased confidence in the ANGI business model, but this is the weakest link in ANGI. How can it be a strength if ANGI has to spend 92% of its revenue on sales and marketing? It's an unsustainable business model!

At the Bank of America, Merrill Lynch Global Technology Conference, Bill Oesterle (ANGI CEO), described ANGI as a consumer paid service selling higher quality data to a target market of approximately 31 million U.S. households.

In the ANGI health care segment, both the data gathering and the data quality is ***very*** weak! Frequently, the SAME healthcare provider (doctor, dentist) has been entered into the ANGI system using different naming conventions. This produces no accountability within the ANGI system and – more importantly – no accountability within the market. To create real satisfaction in the market, there has to be accountability within the market. The consumer review has to be associated with a specific healthcare provider in order to create the satisfaction in the market. Unfortunately, the current ANGI system doesn't ***efficiently*** provide this level of specificity.

ANGI could develop this specificity internally. Every healthcare provider has to be licensed. ANGI could secure the licensing data from the relevant agency and build a database of healthcare providers for its membership. And through regulatory licensing requirements, ANGI could maintain the accuracy of the healthcare provider's information. This would allow the consumer review to be associated with a specific healthcare provider (doctor, dentist), strengthening a significant weakness within ANGI.

In order to create real satisfaction in the market, the consumer review has to be associated with a specific healthcare provider (e.g.; doctor, dentist). Does ANGI build this, or does ANGI acquire this?

With its publicly-traded equity, ANGI has the currency to acquire "healthgrades" – an organization owned by Vestar Capital Partners. "healthgrades" has developed a comprehensive database of healthcare providers driven from relevant licensing data. As a result, the consumer review can be associated with a specific healthcare provider (e.g.; doctor, dentist).

The process of gathering a consumer review within ANGI is way too cumbersome! To create a consumer review, ANGI requires the consumer to rate nine categories using five or six degrees of satisfaction. Furthermore, the consumer has to address at least six additional categories or questions to finish the review.

If the consumer review creates the value, why make the process of gathering it so tedious? The process of gathering the review should be short and efficient:

- Simplify the process – measure one variable to statistically rate the experience.
  - Rate the degree of satisfaction from the experience using a scale A – F
- Simplify the process – provide only one variable to describe the experience. What happened?
- Simplify the process – use one variable (automatically entered) to measure a point in time.

Simplifying the process encourages the consumer review, tightens the measurement parameters and improves the ability to statistically segment the data and stratify the market. This creates significant value for the service provider. It's a direct connection to the consumer. It's the most efficient form of marketing, making it very valuable to the service provider, which makes it easier to sell ANGI in the market.

Capital Executive LLC recognizes the incredible value within ANGI. But something is wrong given the relative performance of ANGI in the market! ANGI has generated a ***negative*** return for its shareholders since its IPO on 11/15/11, whereas YELP has generated a ***positive*** return for its shareholders of more than 400% since its IPO on 3/1/12. Why is there such a significant difference?

At the end of the day, both ANGI and YELP should basically operate from the same business model. Essentially, both provide consumption advice through the consumer review. The only difference is the target market. YELP targets restaurants, bars and coffee establishments, whereas ANGI targets the home repair, yard maintenance, automobile restoration and health care segments of the market.

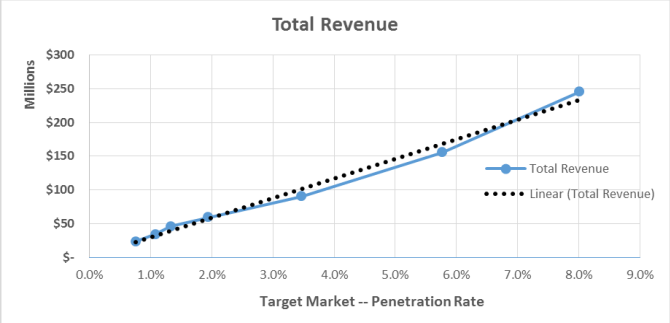
Given the similarities, why has ANGI so dramatically underperformed in the equity market? Several reasons: a) consumer pricing; b) data gathering; c) and data quality. However, the consumer pricing strategy has driven the significant underperformance. The real-value isn't the paid subscription; it's the membership!

Using the annual operating data of ANGI from 2007 through 2013, with the penetration rate as the independent variable (x) and total revenue as the dependent variable (y), the regression analysis produced the following table.

Regression Statistics	
Multiple R	0.993866214
R Square	0.987770051
Adjusted R Square	0.985324061
Standard Error	9771314.41
Observations	7

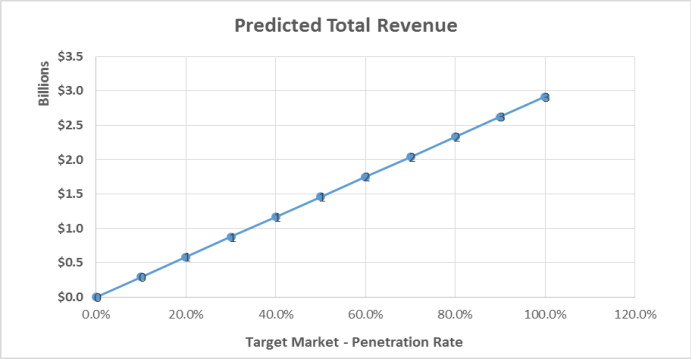
These statistics suggest a very strong relationship between the variables. But where is the real-value for ANGI? Is it the penetration rate (membership) or is it the paid subscription? In this analysis, these variables have to be contrasted because one variable (price) undermines the other variable (quantity) – or in this case: the target market penetration.

The following graph illustrates the statistical relationship between the penetration rate into the target market and the total revenue generated by ANGI from 2007 through 2013.



The statistical relationship between the variables is so strong, the predicted line (black dots) is right on top of the actual line. This creates a reasonable argument for extrapolating the strong, operating relationship between the penetration rate and total revenue!

To help illustrate the real-value of membership for ANGI, the following graph extrapolates the strong, established, operating relationship between the penetration rate and total revenue. The extrapolation indicates total revenue of approximately $500M – if ANGI achieved a penetration rate of 20% across the board into the target market. It also indicates total revenue of approximately $1.2B – if ANGI achieved a penetration rate of 40%. And if ANGI achieved a penetration rate of 100%, the extrapolation indicates total revenue of approximately $2.9B.



Granted, the preceding graph is theoretical, but it is based on the established relationships created by the operations of ANGI. It's a reasonable argument, and it's clearly impressive in terms of potential. In addition, the established relationships don't even consider ecommerce. And by considering ecommerce potential, the demand line (total revenue) shifts up – perhaps significantly. Maybe the potential is $5B, or $10B, or $25B. The degree of the demand shift will be determined by the penetration into ecommerce. And the potential of ecommerce is absolutely staggering!

Unfortunately, ANGI will never realize anything close to this potential under the current, consumer pricing strategy. Price (by definition) creates an impediment to consumption. And ANGI complicates this impediment with a tiered consumer pricing strategy. Each pricing tier not only impedes penetration but also multiplies the impediments to consumption when factored together. It's a misguided strategy given the current environment!

Please change the consumer pricing strategy. The value is in the membership – not the membership fee! Please require membership registration, including credit information. But give away the consumer membership! Take a leap of faith and provide an altruistic service to the consumer!

If the service really creates value in the market, the consumer will naturally gravitate to the service. This will create a bigger a market for the service provider, which creates significant value for the service provider, making it extremely efficient to sell the value of ANGI in the market. And thereby, create significant value for the ANGI shareholder.

But why has ANGI so dramatically underperformed in the equity market? ***The main reason:*** the consumer pricing strategy! This strategy has actually created significant impediments to the consumption of the ANGI service. Price (by definition) creates an impediment to consumption.

In the beginning, ANGI had to sell a consumer paid membership because the service provider had greater control in the market. But the market has changed! Decision making information has become ubiquitous within the United States. Therefore, the value is in the membership (because it creates a market for the service provider) – not the membership fee!

Maximize the penetration into the target market by giving away the consumer membership! Replace the membership fee with an ecommerce transaction fee and a business development fee to the service provider. This pricing strategy reinforces itself in the market. By increasing the size of the market (memberships), ANGI creates more value for the business development fee, which reinforces the potential of an ecommerce fee. The goal is 100% penetration into the target market!

The current consumer pricing strategy of ANGI has destroyed significant shareholder value, because it has failed to recognize the real-value of membership! The membership creates the market, and the market creates the value for the service provider! But a consumer membership fee actually creates significant impediments to the consumption of ANGI! The real-value is in the membership – not the membership fee!

The membership creates the market, and the market creates the value for the service provider! ANGI sells the value of the market to the service provider! And ANGI creates significant value for the shareholder!

Why is Facebook (FB) so valuable in the market? A market cap of ~$165B. Because Facebook (FB) has recognized the real-value of membership! The goal is to achieve 100% penetration into the target market.

Think about it! How many members would Facebook (FB) have today using the consumer pricing strategy of ANGI? Clearly, not ~1.2B! The real-value is the consumer membership – not the membership fee!

The Consumer Pricing Strategy of ANGI fails to recognize the real-value of membership! And if the real-value is the membership, then maximize the membership by giving it away to the consumer!

Guaranteed! The revenue lost from the consumer membership fee represents only a fraction of the value created for the service provider! Maximize the membership, increase the market and replace the membership fee with an ecommerce transaction fee and a business development fee to the service provider!

For more information about Capital Executive LLC, please visit the website listed below.
Sincerely,
Ken Copley
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