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Temple and Webster

Internet

18 November 2018

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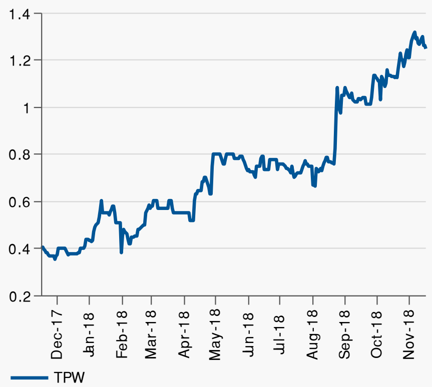
BUY

PRICE TARGET	A$1.55
Price (16-Nov)	A$1.25
Ticker	TPW-ASX

52-Week Range (A$):	0.33 - 1.35
Market Cap (A$M):	141
Dividend /Shr (A$):	0.00
Enterprise Value (A$M):	130
Cash (A$M):	10.5
Long-Term Debt (A$M):	0.0

FYE Jun	2017A	2018A	2019E	2020E
Sales (A$M)	64.5	72.6	96.1	118.6
Gross Profit (A$M)	17.8	22.5	29.8	35.6
EBITDA (A$M)	(6.8)	(0.6)	1.1	2.7
EBIT (A$M)	(7.4)	(0.8)	0.9	2.5
Net Income Adj (A$M)	(3.4)	(0.1)	0.9	2.5
EPS Adj&Dil (A$)	(0.07)	(0.00)	0.01	0.02
Equity FCF (A$)	(7.7)	1.2	1.1	2.8
EV/Sales (x)	2.0	1.8	1.3	1.1



Source: FactSet

Priced as of close of business 16 November 2018

Initiation of Coverage

A small fish in a big TAM

Temple & Webster (TPW) is Australia's largest online furniture and homewares retailer with an estimated **online category market share of ~14% (total category share 0.6%).** TPW operates via 'templeandwebster.com.au' and aims to create a premium shopping experience for customers by having a large and continually refreshed catalogue of products, superior delivery and customer service.

- The company generates the majority of its revenue through the sale of third-party produced furniture and homewares (>80% revenue) with its private label products (i.e. Milan Direct and Temple & Webster brands, ~1k SKUs) a smaller contributor to revenue (<20%). TPW reports >125k product SKUs across 185 sub-categories, sourced from >700 brand owners and distributors in Australia. Key categories include dining, décor, lighting, outdoor, flooring, soft furnishings, consumables, tabletops, bath and wall art with revenue broadly skewed 50%/50% Furniture/ Homewares. During FY18 TPW reported a +26% increase in unique customers to ~198k (purchase item within the prev. 12 months) with 1.1m unique customers visiting its website each month.
- TPW operates within the domestic A$13.6b furniture and homewares industry where online penetration remains low at just ~4% (UK/US 14%). TPW should benefit from the structural shift to online (3-year CAGR +14%) coupled with millennials entering the category who are more accustomed to purchasing goods online (online spend growth for <30yo +21% vs. >40yo +10% growth).
- Following a large restructuring in FY17, TPW has been managing the business to break even. However, the business is at a pivotal crossroads as it can now reinvest incremental gross profit (FY19e Δ gross profit ↑ $7m pa) in various growth initiatives. This includes 1) increasing new product categories (home improvements/DIY, flooring, window coverings, sinks, taps and baths); 2) expanding into new geographies (New Zealand FY19); 3) technology investment (mobile apps, VR) to improve consumer experience and conversion rates; 4) expanding B2B (commercial/trade) product offering (>10k trade accounts); 5) increasing S&M spend to drive brand awareness across diverse channels (immediate 2.1x GP/CAC, TPW ~25% Aust. brand awareness); and 6) enhancing in-house logistics for large/bulky items (>50% volume).
- **TPW has exhibited an accelerating revenue growth profile (1H18a +1%, 3Q18a +22%, 4Q18a +28%, Jul-18 +34%, 1Q19a +39%) as it passes through FCF breakeven.** This revenue acceleration and gross profit margin expansion (↑ 4ppts to 31%) has been achieved with prudent cost control (FY18 CODB growth -6%). Given TPW's category position and long-tailed growth opportunities, we believe management is likely maintain a breakeven mantra and reinvest to capture the long-term opportunity (0.6% market share).

TPW's financial profile is comparable to other high growth online retailers targeting a large and structurally under-penetrated TAM (A$13.6b, ~4% online) with limited earnings. As TPW generates elevated gross profit margins, we believe it can produce long-term adj. EBITDA margin of ~10% (CGau FY22), implying the marginal investor is paying for forward revenues of $130m. We initiate coverage of TPW with a BUY recommendation and price target of A$1.55ps premised on a DCF methodology.

For important information, please see the Important Disclosures beginning on page 25 of this document.

Figure 1: Financial summary and forecasts for TPW

Temple & Webster (TPW)

Profit & Loss ($m) - Jun YE	2017A	2018A	2019F	2020F	2021F
Sales Revenue	**64.5**	**72.6**	**96.1**	**118.6**	**142.4**
COGS/Fullfillment	-46.7	-50.0	-66.3	-83.0	-102.5
Gross Profit	**17.8**	**22.5**	**29.8**	**35.6**	**39.9**
Marketing	-8.2	-8.1	-11.5	-14.2	-17.1
Opex	-16.4	-15.0	-17.2	-18.6	-19.7
EBITDA	**-6.8**	**-0.6**	**1.1**	**2.7**	**3.0**
D & A	-0.6	-0.2	-0.2	-0.2	-0.2
EBIT	**-7.4**	**-0.8**	**0.9**	**2.5**	**2.8**
Net Interest Expense	0.3	0.1	0.0	0.0	0.0
NPBT	**-7.2**	**-0.7**	**0.9**	**2.5**	**2.8**
Tax expense	2.1	0.7	0.0	0.0	0.0
NPAT (Normalised)	**-3.4**	**-0.1**	**0.9**	**2.5**	**2.8**
Non-recurring	-2.7	0.0	0.0	0.0	0.0
NPAT (Reported)	**-7.8**	**0.0**	**0.9**	**2.5**	**2.8**
Gross Profit Margin (%)	*27.6%*	*31.1%*	*31.0%*	*30.0%*	*28.0%*
CODB margin (%)	*38.1%*	*31.9%*	*29.9%*	*27.7%*	*25.9%*
EBITDA Margin (%)	*-10.5%*	*-0.8%*	*1.1%*	*2.3%*	*2.1%*
EBIT Margin (%)	*-11.5%*	*-1.1%*	*0.9%*	*2.1%*	*2.0%*
NPAT Margin (%)	*-5.3%*	*-0.1%*	*0.9%*	*2.1%*	*2.0%*

Cash Flow ($m) - Jun YE	2017A	2018A	2019F	2020F	2021F
Operating EBITDA	**-6.8**	**-0.6**	**1.1**	**2.7**	**3.0**
- Interest & Tax Paid	0.3	0.1	0.0	0.0	0.0
+/- change in Work. Cap.	-1.1	1.8	0.5	0.6	0.5
- other	0.0	0.0	0.0	0.0	0.0
Operating Cashflow	**-7.6**	**1.3**	**1.6**	**3.3**	**3.5**
- Capex	-0.1	-0.1	-0.5	-0.5	-0.5
- Aquisitions/divestments	-2.0	0.0	0.0	0.0	0.0
Free Cashflow	**-9.7**	**1.2**	**1.1**	**2.8**	**3.0**
- Ord Dividends	0.0	0.0	0.0	0.0	0.0
- Equity /other	0.0	0.0	0.0	0.0	0.0
Net Cashflow	**-9.7**	**1.2**	**1.1**	**2.8**	**3.0**
Cash at beginning of period	18.4	8.7	9.9	11.0	13.8
+/- borrowings / other	0.0	0.0	0.0	0.0	0.0
Cash at end of period	**8.7**	**9.9**	**11.0**	**13.8**	**16.9**

Balance Sheet - Jun YE	2017A	2018A	2019F	2020F	2021F
Cash	8.7	9.9	11.0	13.8	16.9
Debtors	0.0	0.0	0.0	0.0	0.0
Inventory	1.4	2.2	3.1	3.8	4.8
PPE	0.2	0.2	0.5	0.8	1.1
Intangibles	7.7	7.5	7.5	7.5	7.5
Other assets	0.9	1.8	1.8	1.8	1.8
Total Assets	**18.9**	**21.7**	**24.0**	**27.8**	**32.1**
Borrowings	0.0	0.0	0.0	0.0	0.0
Trade Creditors	7.3	9.4	10.8	12.1	13.5
Other Liabilities	1.5	1.5	1.0	1.0	1.0
Total Liabilities	**8.8**	**10.9**	**11.8**	**13.1**	**14.6**
NET ASSETS	**10.0**	**10.8**	**12.1**	**14.7**	**17.5**

Target Price $ 1.55
Share Price $ 1.25

Valuation ratios	2017A	2018A	2019F	2020F	2021F
EPS (cps)	-0.07	0.00	0.01	0.02	0.03
Enterprise Value ($m) - pro-for	131.9	130.7	129.6	126.8	123.7
EV/Revenue	2.0	1.8	1.3	1.1	0.9
EV/Gross Profit	**7.4**	**5.8**	**4.4**	**3.6**	**3.1**
EV / EBITDA (x)	-19.5	-223.0	119.7	46.1	40.7
EV / EBIT (x)	-17.8	-157.8	146.9	49.8	43.6
P/E (x)	**nmf**	**nmf**	**nmf**	**nmf**	**nmf**
DPS (cps)	0.0	0.0	0.0	0.0	0.0
Div yield (%) - 100% franked	0%	0%	0%	0%	0%
Payout ratio (%)	0%	0%	0%	0%	0%

Dupont Analysis	2017A	2018A	2019F	2020F	2021F
Net Profit Margin	-5.3%	-0.1%	0.9%	2.1%	2.0%
Asset Turnover	3.4	3.3	4.0	4.3	4.4
ROA (%)	-18.1%	-0.2%	3.7%	9.2%	8.8%
Financial Leverage	1.9	2.0	2.0	1.9	1.8
ROE (%)	-34.0%	-0.5%	7.3%	17.4%	16.2%
ROIC (%)	-398.6%	-16.4%	80.3%	300.7%	439.6%

Balance Sheet ratios	2017A	2018A	2019F	2020F	2021F
Net Debt (cash)	-8.7	-9.9	-11.0	-13.8	-16.9
NTA per share ($)	0.02	0.03	0.04	0.06	0.09
Price / NTA (x)	55.3	40.7	30.4	19.6	14.1
Shares on issue	105.7	107.6	112.5	112.5	112.5
EFPOWA (m)	105.7	107.6	112.5	112.5	112.5

Assumptions	2016A	2018A	2019F	2020F	2021F
Revenue Growth	5%	13%	32%	23%	20%
Gross Profit Margin	28%	31%	31%	30%	28%
Contribution Margin	15%	20%	19%	18%	16%
Opex Growth	1%	-9%	15%	8%	6%

Interim Analysis	2H17A	1H18A	2H18A	1H19E	2H19E
Revenues	30.4	34.4	38.2	46.5	49.6
Gross Profit	8.9	10.6	12.0	14.4	15.4
EBIT	-2.3	-0.9	0.1	0.5	0.4
EBIT margin (%)	-7.7%	-2.7%	0.2%	1.0%	0.9%
DPS	0.0	0.0	0.0	0.0	0.0

Valuation			
Discounted Cash flow			
Beta	1.4	WACC	10.1%
Cost of equity	10.1%	Discount period	6 years
EFPOWA*	112.5	**DCF**	**1.55**

Board of Directors / Substantial Shareholders		
Board of Directors	**Shareholding**	**%**
Susan Thomas	0.0	0.0%
Conrad Yiu	3.2	2.9%
Stephen Heath	0.2	0.2%

Source: Company reports, Canaccord Genuity estimates

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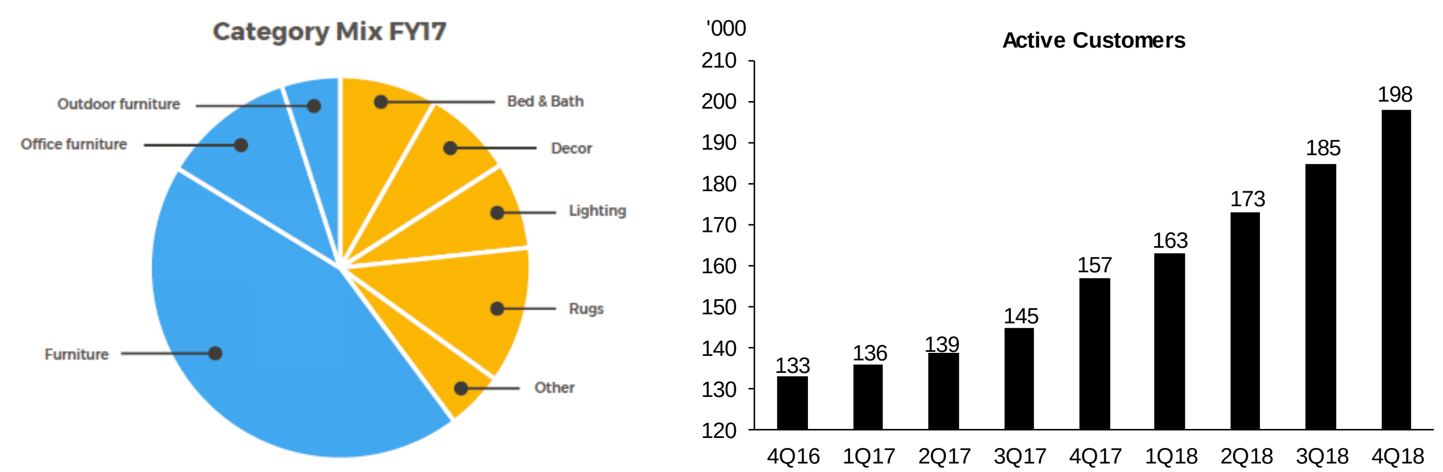
Company profile

- Temple & Webster (TPW) is the largest online-only furniture and homewares retailer in Australia with an estimated category market share of ~14% (FY18a rev. $72.6m, vs. online category size >$500m [Euromonitor]).
- TPW operates via “templeandwebster.com.au” and aims to create a premium shopping experience for customers by having a large and continually refreshed catalogue of products (125k), superior delivery (avg. dispatch time ~2 days) and customer service.
- The website is overlayed with limited-time promotions and curated content capturing different trends and styles at different points in the season. At the end of FY18, TPW reported it has ~198k active customers (customers who have made a purchase from its website within the last 12 months) with ~1.1m unique customers visiting the site each month. Given the low marketing spend relative to revenue, the majority of TPW’s traffic is sourced from free/unpaid sources with >50% sourced through a mobile device.
- TPW was founded in 2011 and scaled its operations with the acquisitions of ZIZO (formerly Australian subsidiary of Wayfair, ~$6m) and Milan Direct (~$20m) in Oct-15, before listing on the ASX in Dec-15 with a valuation of $123m (EV/gross profit 9.1x). In CY16, the ZIZO and Milan Direct brands were consolidated into the Temple & Webster platform, with Milan Direct closing its e-commerce website and serving as TPW’s private label furniture brand.
- The Temple & Webster platform has >125k product SKUs available, sourced from >700 brand owners and distributors. TPW currently divides its product SKUs into 185 sub-categories within home furnishings and home improvement including dining, décor, lighting, outdoor, flooring, soft furnishings, consumables, tabletops, bath and wall art.

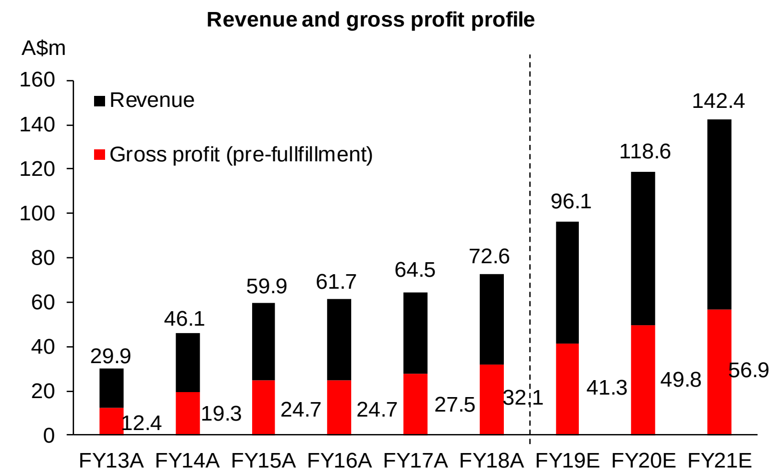
Figure 2: Revenue profile and revenue split by product category

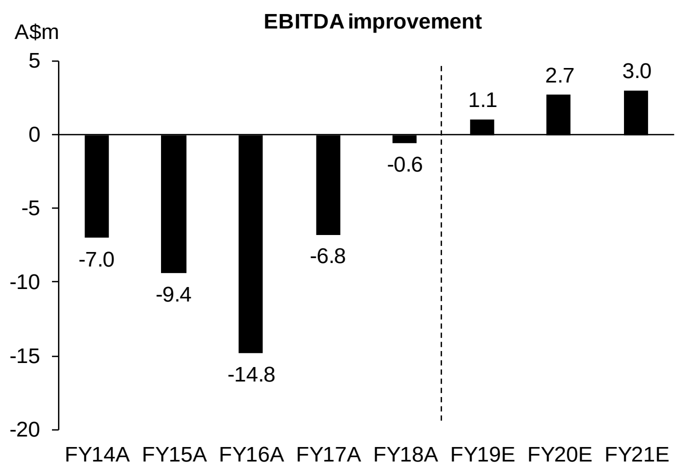


Source: Company reports, Canaccord Genuity estimates

- The company generates the majority of its revenue (>80%) through the sale of third party-produced furniture and homewares to consumers, with private label (through Temple & Webster and Milan Direct brands) being a smaller contributor to revenue (<20%). We expect direct sourcing from Asia and warehousing products on behalf of brand owners to be a source of growth for TPW.
- TPW primarily uses a drop-ship model where goods are sent directly from a supplier to a consumer, resulting in faster shipping times and lower operating costs. While currently utilising an outsourced logistics function, the company is investing in its own in-house delivery vans to further reduce the cost of delivering bulky items and increase service to consumers.
- TPW is based in Sydney and, following restructuring efforts made during FY17 (change in board of directors, new CEO/CFO/CMO), the group reports ~130 full-time employees (Aust. ~90, Manilla ~40) across sales, marketing and operations.

Figure 3: Revenue and gross profit growth and EBITDA improvements (passing breakeven)





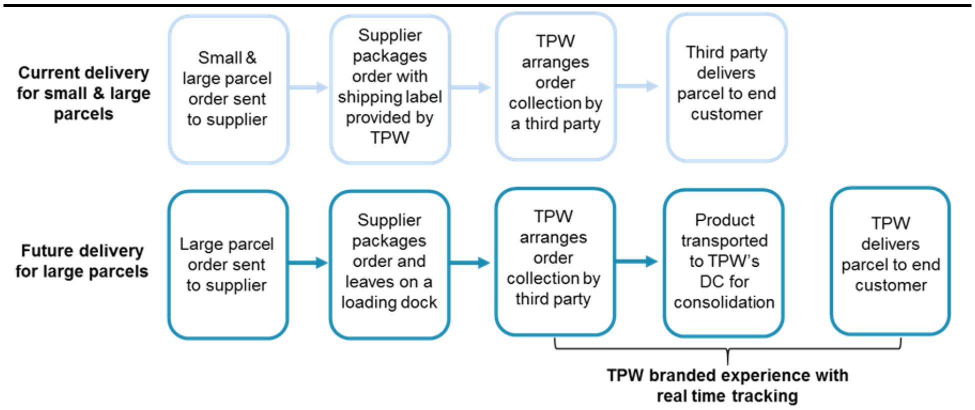
Source: Company reports, Canaccord Genuity estimates

- During 2H18, TPW became FCF breakeven and is expected to be profitable in future periods; however, we expect incremental gross profit is likely to be reinvested for long-term growth (logistics, marketing, private label/direct sourcing).

Supply chain overview

- TPW currently outsources almost all of its small parcel delivery to Australia Post and maintains a largely drop-ship model from suppliers to consumers.
- Following a customer's order on the Temple & Webster website, TPW purchases items from its suppliers (>700) which is typically held in the supplier's own warehouse. As such, the business operates a capital light/negative working capital business model as customers are charged upfront with TPW paying suppliers ~30days later.
- From suppliers' perspective, TPW:
  - Provides exposure to the rapidly growing e-commerce market without the large upfront cost to build an online presence;
  - Can take more of their products than traditional retailers, typically with improved payment terms;
  - Provides a real-time view of demand, enabling suppliers to improve inventory and cash flow management; and
  - Arranges logistics with third-party carrier (small items: Australia Post) to get the product delivered to the consumer.
- Currently TPW outsources its small parcel deliveries to logistics providers (primarily Australia Post). CGAu and TPW classify small parcels as items <22kg (which could be as big as a chair or coffee table). Currently when a small or large parcel is purchased, the supplier packages the item and places it on a loading dock where TPW provides the third-party shipping sticker. TPW then organises for Australia Post (or large-item third-party carrier) to collect the parcel from the supplier's warehouse and deliver to the customer, with dispatch typically done within two days.
- An illustrative example of TPW's current and future logistics process:

Figure 4: Current supply chain. Investment in large parcel logistics underway



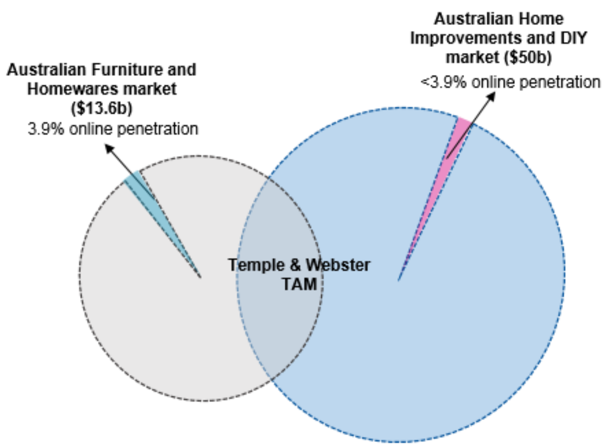
Source: Canaccord Genuity

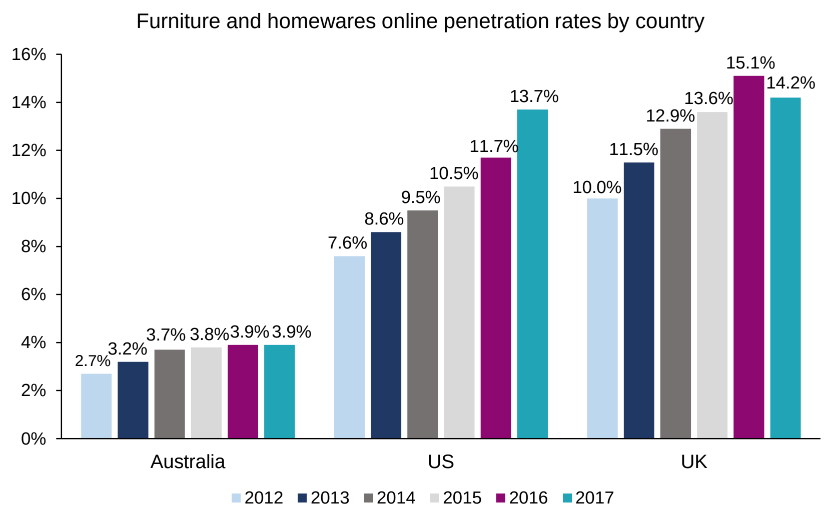
- TPW's logistics function is the only part of the business model that is outsourced and arguably the most important. A key initiative for TPW is expanding its own delivery function for large parcels to metro areas. TPW has begun launching its own fleet of Temple & Webster branded delivery vans to fulfil bulky items and improve customer service. This is currently in trial. We expect the group to mimic the logistics process of established peers, where small parcels are drop-shipped from suppliers, while large parcels are consolidated at a centralized TPW distribution centre in Sydney/Melbourne/Brisbane and then delivered to the customer via the TPW's own branded delivery vans. We expect this strategy to be executed over the coming 3-5 years.

Total addressable market ($13.6b, 3.9% online)

- TPW's revenue profile is derived primarily in the B2C furniture and homewares e-commerce market with a smaller contribution from B2B customers (<10%). The overall online retail market is large and rapidly evolving, driven by increasing consumer acceptance to purchase goods through the internet.
- According to Euromonitor data, the Australian furniture and homewares (offline and online) market is estimated at A$13.6b and includes indoor furniture, home textiles, outdoor living and homewares. Online penetration remains low at just 3.9% (A$530m, TPW ~14% category share); however, it is expected to grow at a three-year CAGR of +14%. In our view, the Australian market is likely to follow the increased online penetration in the developed markets such as the US and the UK, where category online sales penetration in 2017 was 13.7% and 14.2%, respectively.

Figure 5: TPW Total addressable market (>$13.6b) with an implied category share (online) of 14%. Australia's online penetration of furniture and homewares lagging established markets such as US/UK



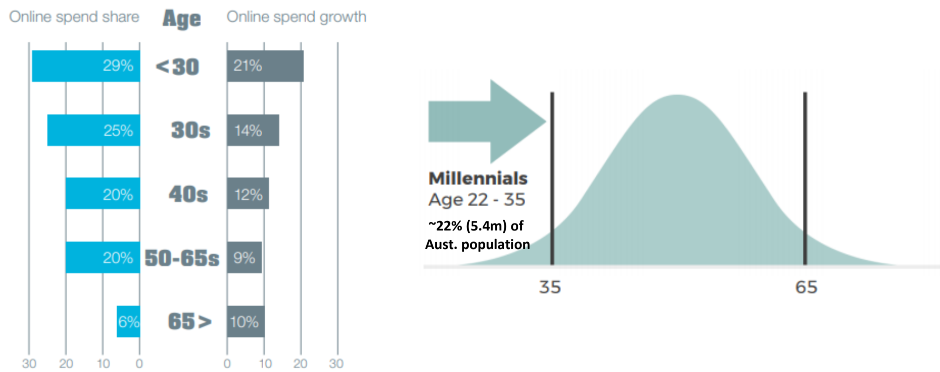


Source: Euromonitor, IBIS World, Canaccord Genuity estimates

- TPW is also expanding its TAM by entering new categories. For example, in May-17, TPW introduced a paint range as its first step in entering the Australian home improvements/DIY market, sized at A$50b (IBISWorld). The company has future plans to add flooring, window coverings, sinks, taps and baths to complement its existing range.
- We believe growth in online home furnishings to be driven by the following major global trends:
  - **Favourable demographic shifts and technological advances:** The transformation in shopping habits is driving an online shift in this category as consumers are now less reluctant to buy furniture and homewares online. Within the $13.6b Australian furniture and homewares TAM, online sales represent <3.9% (~$530m) of total sales at present compared to ~8% for the broader Australian retail sales on average ($21.3b).
  - **Millennials aging into TPW's target demographic:** TPW's typical customer is between the ages of 35-55; however, individuals fitting this demographic are less likely to shop online than millennials (now aged 22-35, representing ~22% of the Australian population) who are accustomed to purchasing goods

such as fashion and electronics online. We expect TPW's target market to grow as millennials start to enter the 35-55 age group. A potential tailwind is from an increasing prevalence of Australians under 55 renting rather than owning, which may see them changing furniture and homewares more often than if they owned a property for an extended period of time.

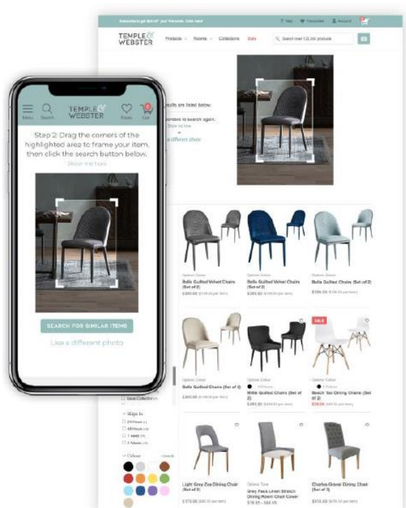
Figure 6: Large demographic shift who have a higher propensity to shop online



Source: CBA, Company Reports, Canaccord Genuity estimates

- **Virtual reality (VR) and artificial intelligence (AI) improving experience and conversion:** In our view, VR and AI could accelerate the category's e-commerce shift. VR allows customers to virtually see how items would look in their homes, reducing the need to visit stores physically. And through AI, customers can search for products by uploading a photo from either their phone or computer. Ikea, the largest furniture retailer globally and Wayfair, the largest online retailer of furniture and homewares in the US, launched this technology during FY18 and we expect others to follow. The need for visualisation has been a key criticism for the category and likely the reason for the sub-optimal penetration. TPW launched its own Visual Search technology in CY18.

Figure 7: VR/AI enables customers to shop for similar products by using their camera



Source: Company reports, Canaccord Genuity estimates

- **Improvements in logistics:** The rise in e-commerce should continue to increase scale for logistics and freight operators, lowering delivery costs for users of these services including TPW. We expect development of logistics networks with fast, reliable and easy delivery for bulky items to support further growth in the online market for furniture and homewares which has historically been expensive and slow with poor service.

Figure 8: Launching branded delivery vans (currently Melbourne only)

Source: Company reports, Canaccord Genuity estimates

- To illustrate the scale of the opportunity, below we show the sensitivity of online penetration in the Australian furniture and homewares market relative to TPW's market share. Assuming the total furniture and homewares market reaches an equivalent 14% online penetration rate ($1.9b) with TPW achieving a 25% market share, we derive a $476m revenue opportunity and A$4.45ps valuation (10x implied EBIT multiple on 10% scaled EBIT margins).

Figure 9: 14% online penetration, 25% market share deriving $476m in revenue

		Online Penetration					
Aus Market	%	3.8%	6%	8%	10%	12%	14%
	A$m	517	816	1,088	1,360	1,632	1,904
Aus Market Share of Online Furniture	14%	72	114	152	190	228	267
	20%	103	163	218	272	326	381
	25%	129	204	272	340	408	476
	30%	155	245	326	408	490	571
	35%	181	286	381	476	571	666
							US/UK Current

Valuation $ps (10x EBIT multiple at 10% margins)		Online Penetration					
		3.8%	6%	8%	10%	12%	14%
Aus Market Share of Online Furniture	14%	0.68	1.07	1.42	1.78	2.14	2.49
	20%	0.97	1.53	2.03	2.54	3.05	3.56
	25%	1.21	1.91	2.54	3.18	3.81	4.45
	30%	1.45	2.29	3.05	3.81	4.58	5.34
	35%	1.69	2.67	3.56	4.45	5.34	6.23

Source: Company reports, Canaccord Genuity estimates

- In our view, demographic trends and technological advances in Australia should enable the market to reach online penetration in this category similar to the US (13.7%) and the UK (14.2%).

Competitive landscape and positioning

- The Australian furniture and homewares industry is going through a period of rapid e-commerce adoption; however, it remains in its infancy relative to more established retail categories.
- TPW considers its competitors to be other online-only retailers, multi-channel retailers and horizontal retailers as illustrated below:
  - **Online-only:** Retailers such as Zanui, Brosa, Amazon, eBay.
  - **Furniture stores (including multi-channel):** These companies operate established offline stores that also have an online presence, including IKEA, Nick Scali, Freedom, Adairs, Fantastic Furniture, Domayne, Matt Blatt, Bed Bath 'N' Table, Coco Republic and Pottery Barn, Harvey Norman.
  - **Horizontal retailers** including department stores and hardware stores such as David Jones, Myer and Bunnings.

Figure 10: Highly fragmented industry with no clear leader in online (TPW largest online)

Furniture Stores (online/offline)	Big Box Retailers	Department Stores	Online Marketplaces
Fantastic Furniture	IKEA	Myer	Amazon
Domayn	Target	David Jones	eBay
Freedom	Bunnings	Harvey Norman	Catch
Amart	Big W		
Adairs	Kmart		
Bed Bath 'N' Table			
Coco Republic			
Zanui			
Brosa			
Koala			
Pottery Barn			

Source: Canaccord Genuity estimates

- In our view, the biggest threat to an online-only retailer such as TPW is a large multi-channel retailer with a strong brand presence becoming more aggressive in e-commerce (IKEA, Adairs). However, TPW's business model is highly complex, with the sourcing of quality suppliers and execution of technology and logistics critical to gaining meaningful market share. Offline retailers typically cannot be price competitive versus pure online players given the large fixed-cost component (lease expenses, employees etc) that require elevated gross profit margins (online ~40%, offline ~60%). Competing in online by discounting instore products online would cannibalise a retailer's core brick-and-mortar offering.
- Observing the US experience, price is generally not one of the key competitive differentiators versus a brand's emphasis of assortment and experience. In our view, key competitive advantages of TPW in the online furniture and homewares market are:
  - **Broadest (and growing) range in Australia:** TPW takes a marketplace approach with its large catalogue of >125k product SKUs, sourced from >700 suppliers, making it Australia's largest online player in this vertical. The company sells products catering to various income levels, demographics and styles; by having something suitable for the mass consumer, TPW is often able to reach a larger target market than direct competitors.
  - **Innovative search tools and functionalities:** TPW launched its Visual Search tool using artificial intelligence during FY18, enabling customers to quickly and easily find what they are looking for by uploading a picture. This feature is currently unique to TPW and we believe it is a key competitive advantage,

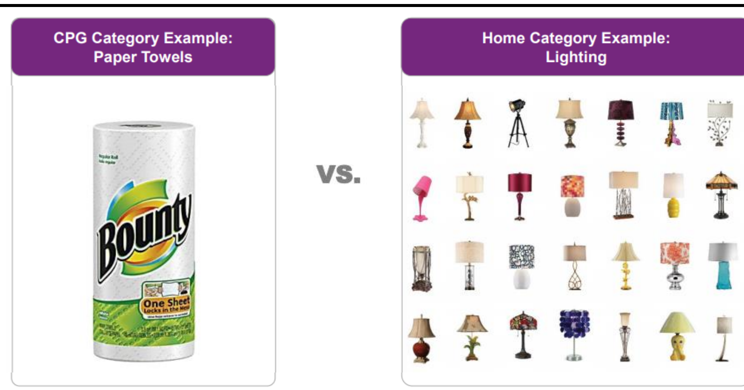
simplifying the online shopping process and therefore increasing the probability visitors will transact.

- **Superior delivery vs. competitors:** TPW operates a drop-ship model where orders usually arrive within in a matter of days (1-3 in many cases) once an order is placed as suppliers ship directly to a customer. This is extremely quick compared to many of TPW's competitors, with their delivers often taking weeks or sometimes months. TPW is making ongoing investments to in-source its delivery and freight operations and we expect this to be highly additive to the company's value proposition.
- **Capital efficient and inventory-light:** TPW purchases its goods from suppliers based on orders received from customers, meaning it doesn't need to forecast design trends and order quantities, promote heavily to sell excess stock or hold outdated inventory in its warehouses. In addition, cash collection from customers is up front at order while TPW has longer payment terms with its suppliers, resulting in reduced working capital requirements. A challenge many retailers face is the difficulty in scaling their business given the large working capital required to hold their inventory. As TPW benefits from a negative working capital balance, management can reinvest its "float" to accelerate its growth profile.

- In the furniture and homewares category, we believe the retailer's brand is often more important than the product's brand. For example, a typical customer doesn't set out to buy a certain brand of sofa, as they would in the case of an iPhone or Sony TV.
- **A common question for emerging online players is what about the impact of Amazon?** We believe foreign markets provides a proxy for success in the home goods market. TPW's website focuses exclusively on the home category and emphasizes a browse-and-discover strategy. Home and furniture consumers seek unique products and rarely have a specific product in mind for their search.

  Consumers are encouraged to locate a product by sifting and sorting through TPW's visually inspiring platform and imagery. This differs from Amazon, whose platform is built around key word searches, bestselling items and branded full-price merchandise such as consumer electronics, TVs and computers.

Figure 11: Amazon targets highly commoditised items with targeted search. This compares to the browse-and-discover strategy of TPW



Source: Wayfair, Canaccord Genuity estimates

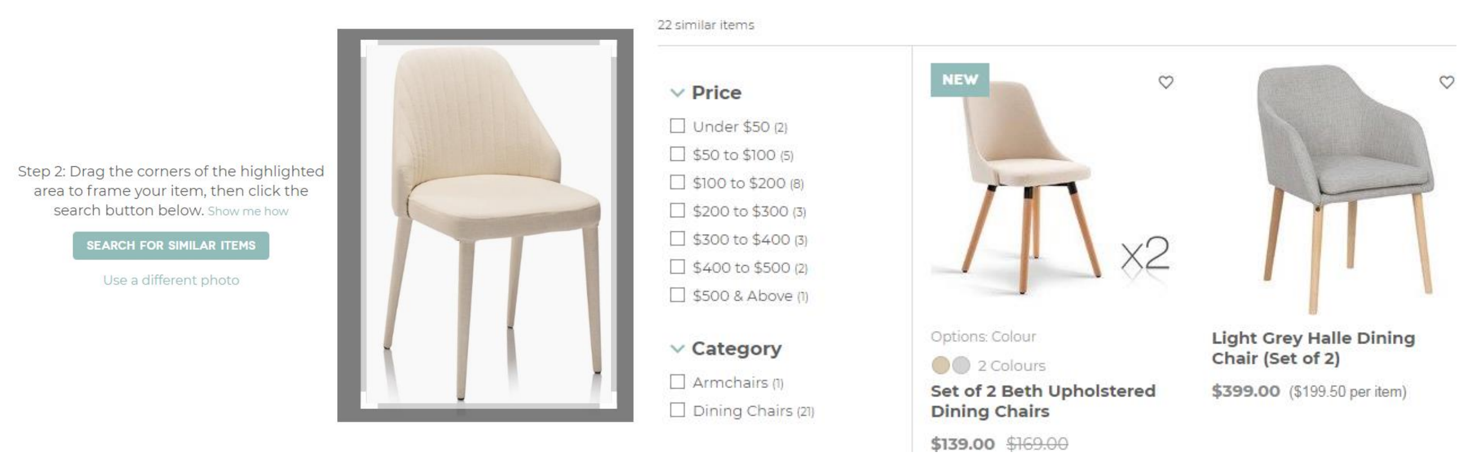
- Ultimately, we believe consumers prefer to shop for furniture and homewares from a specialist retailer as opposed to a website that sells toothpaste and sunglasses. TPW is also currently investing in its logistics and distribution network that will be optimized for large/bulky items, whereas Amazon's distribution network (in the US) is optimised for smaller packages.

Growth drivers

- **Industry tailwinds:** TPW's growth is influenced by the growth in overall e-commerce, as customers increase their propensity to transact over the internet, and the continued shift in offline to online spending habits within the home furnishings and home improvement category. The Australian e-commerce landscape grew 18.7% to $21.3b in 2017 and Australia Post expects this trend to hold with 1 in 10 items being bought online by 2020. Within the combined $63.6b Australian furniture and homewares ($13.6b) and home improvement ($50b) TAM, online is highly under-penetrated (3.9% vs. UK at 13.7%, US at 14.2%) growing rapidly at a five-year CAGR of 13.8%. For context, 26.5% of fashion and apparel and 25.6% of consumer electronics are sold online today in Australia.

- **Visual Search:** TPW is the first Australian furniture and homewares retailer to launch Visual Search. This innovative tool helps customers to search through TPW's >125k product SKUs and identify items based on pictures they upload from their mobile or computer. With this technology, individuals are able to do a direct product and price comparison when they are browsing other stores. The company has partnered with GrokStyle using artificial intelligence to determine which products are being clicked on the most, to refine how this matches TPW's products, and to sort by relevance for customers (i.e.: items are displayed from lowest price first). This type of technology encourages the industry's e-commerce shift and, with valuable first-mover advantage, TPW has the best chance of capturing new online customers, underpinning sales growth, in our view.

Figure 12: Visual Search - we searched for this chair (RRP $425) and the first two results includes these similar matches (at lower prices)

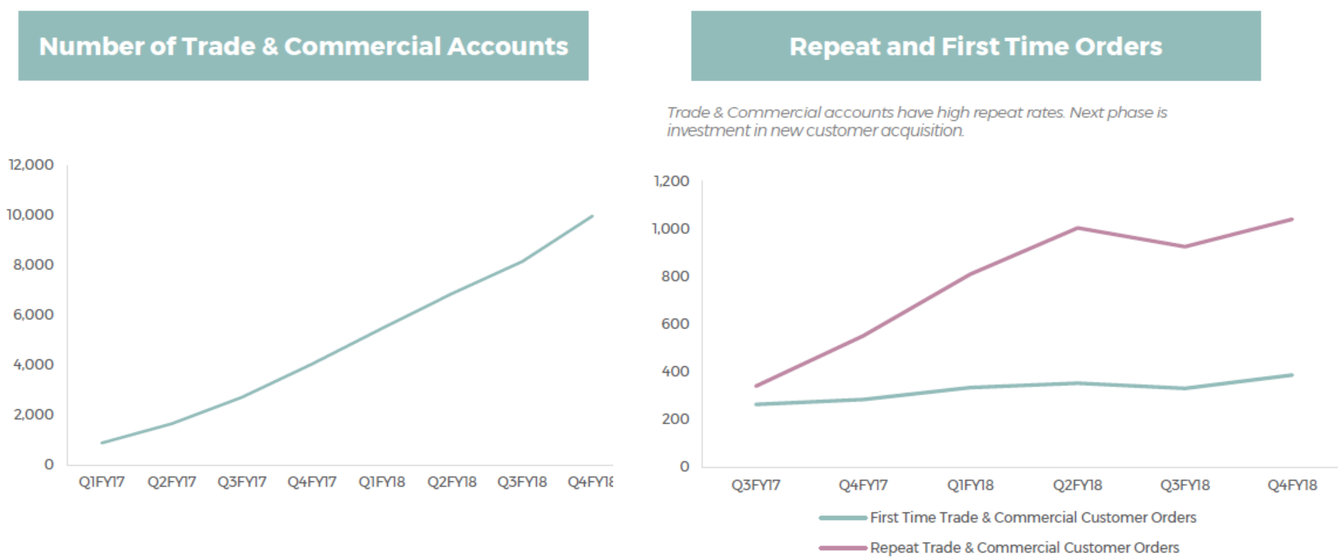


Source: Company reports, Canaccord Genuity estimates

- **Mobile app:** TPW is launching its mobile app in FY19 with the aim of improving conversion and taking advantage of the increasing shift of consumers shopping via a mobile device. According to Australia Post data, purchases made from mobile devices increased +58% in 2017 with 1 in 5 online purchases being made from a mobile device today. Mobile currently accounts for the vast majority of traffic and TPW's app should also enhance the customer's shopping experience and brand recognition, while lowering the group's marketing spend to acquire new customers (push notifications). While TPW has a mobile-enabled website, we believe it is rare for a large online-only retailer to operate without an interactive mobile app; we believe this presents an opportunity to the group. We expect the app to have an enhanced delivery functionality and transparency with delivery tracking.

- **Expansion of B2B (trade & commercial) business and opening design studio:** TPW expects to open its first design studio for its B2B and large B2C customers, providing in-person styling services to customers at its Sydney head office. TPW reports >10k commercial trade accounts (interior designers, developers etc) and B2B is increasingly becoming a material contributor to revenue (CGAu est. <10%). We expect the studio will be aimed at enhancing the customer's shopping experience where traders and commercial partners will be able to see samples of products and speak to account managers and sales representatives. TPW believes this is also an opportunity to trial a new brick-and-mortar format; however, the company has stated its core business will remain online.

Figure 13: B2B becoming an increasingly material contributor to revenue



Source: Company reports, Canaccord Genuity estimates

- **Category expansion:** The group is entering new categories, especially in the home improvements/DIY market. In May-17, TPW began selling a paint range as its first step in this category and plans for the future include adding flooring, window coverings, sinks, taps and baths to its selection. We exclude these products from our estimates, assuming TPW still has a minor presence in this segment, but including them would increase its TAM by $50b (to $63.7b). Overall, TPW appears to be well positioned to grow organically within furniture and homewares as well as benefit from growth in adjacent business lines.

- **Geographic expansion:** TPW is exploring the option to expand into New Zealand through an online pilot during FY19. Although the overall e-commerce market is relatively small, at ~$3.5b (Australia Post), NZ is the top e-commerce destination for Australian goods and could be a meaningful contributor to the group's revenue in future periods if the trial is successful.

- **Temple & Webster private-label brands:** TPW has a number of Temple & Webster private-label brands and Milan Direct products (~1k SKUs) that typically sell at higher margins than its traditional drop-shipped products. Expansion of this product range should aid the broader growth of gross profits in future periods.

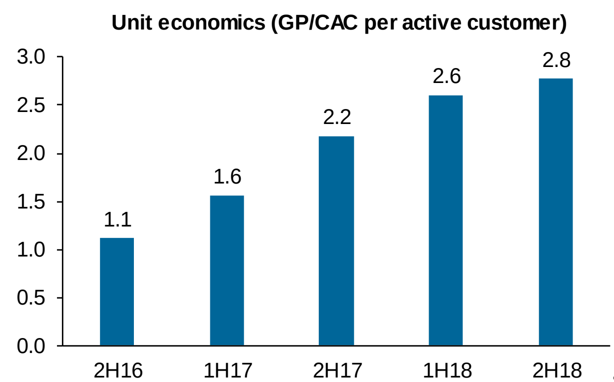
- **In-house delivery:** TPW is making investments to in-source its freight operations by operating its own fleet of delivery vans, which should further reduce the cost and time needed to ship bulky items. Superior delivery is a key component of TPW's value proposition as orders are usually shipped within two days vs. peers often taking weeks or months, and we believe this growth initiative will only enhance the customer experience.

Other key points to note

- **Favourable unit economics:** As of Aug-18, TPW's cost of acquisition for a new customer, defined as total marketing spend divided by gross new active customers, was ~$55 and compares favourably to an indicative gross profit per active customer of $114. This equates to an immediate >100% return on investment capital and illustrates the prudent marketing methods, which remain relatively low to date (11% of revenue/36% of gross profit). However, the chart below illustrates the improving unit economics over the previous three years, with the gross profit per active relative to marketing currently standing at 5.9x. We believe this is derived from improving customer retention/repeat order rate.

Figure 14: Efficient marketing return with improving group unit economics (gross profit/marketing per active customer)

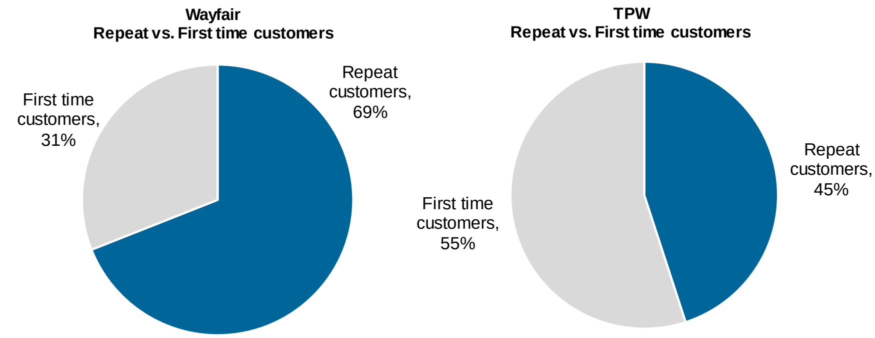
		2H16	1H17	2H17	1H18	2H18
Revenue (trailing)	A$m	62	64	64	65	73
Gross Profit (trailing)	A$m	13	16	18	19	23
Active Customers (000s)	#	133	139	157	173	198
Net additions (000s)	#		6	18	16	25
Marketing (trailing)	A$m	12	10.1	8.2	7.5	8.1
CAC (new active)	A$		1691	453	468	325
CAC (all users)	A$	90.2	73.0	52.0	43.3	41.1
ARPU	A$m	463	457	411	375	367
Avg. Gross Profit PU	A$m	101	114	113	113	114
Unit economics	x	1.1	1.6	2.2	2.6	2.8



Source: Company reports, Canaccord Genuity estimates

- **Majority of traffic to Templeandwebster.com sourced from free sources:** The strength of the Temple & Webster brand is the company's best asset with the vast majority of traffic generated through free sources. TPW reports 1.1m unique monthly website visits (50k/pa) with the majority of traffic (and likely revenue) being derived through unpaid sources. This includes email direct marketing, organic search and referrals. The company expects this to be a sustainable source of traffic and a key competitive advantage over new entrants with little brand association who will need to pay via marketing expenditure to generate traffic and revenue to their website. We note repeat customers represent 45% of total orders, however in 1Q19 orders from repeat customers increased >50% relative to group revenue growth of +39%. We note TPW's repeat rate of ~45% compares to Wayfair at 69%, providing upside to revenue and GPAPA margins.

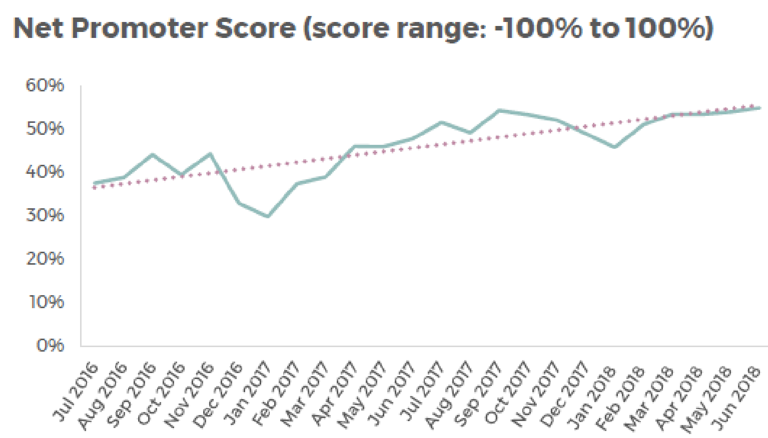
Figure 15: TPW vs. Wayfair repeat customer presents an opportunity



Source: Wayfair, Canaccord Genuity estimates

- **Net Promotor Score (NPS):** NPS is a customer loyalty metric used by leading corporations globally. The NPS is calculated by asking every new TPW customer "How likely are you to recommend Temple & Webster to a friend?" thirty days after their purchase on a scale of 1 to 10. In Jun-18, TPW reported a NPS score of 55 which has been incrementally increasing since listing on the ASX (Jun-16: 37). A strongly positive Net Promotor Score acts as a leading indicator of growth and the likelihood of a repeat purchase. If a company's NPS is higher than its competitors, it is likely the business will outperform its peer group over the medium term.

Figure 16: Continually improving NPS score



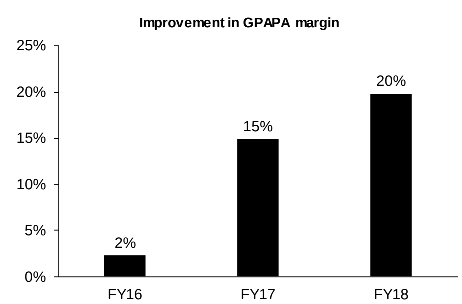
Source: Company reports, Canaccord Genuity estimates

- **Inventory-light business model reducing working capital requirements:** TPW operates a drop-ship business model by purchasing items from suppliers only after customer orders are transacted through the Temple & Webster website. The items are then shipped directly from the supplier to the end customer which means TPW does not carry the inventory. Key advantages of this inventory-light model is the lack of capital being tied up. Cash collection from customers is up front at the time of purchase while TPW has longer payment terms with suppliers (typically within ~30-45 days). This creates a virtuous cash flow cycle for TPW and we expect working capital to become a greater source of cash as revenue increases. This benefit should enable TPW to accelerate its growth profile vs. peers as a challenge other retailers may face is the difficulty in scaling their business given the large working capital requirements to hold inventory.

Financial and earnings growth forecasts

- TPW's financial profile is comparable to other high growth online retailers targeting a large and underpenetrated TAM with elevated revenue growth and negligible EBITDA.
- TPW's business model enables it to benefit from reduced working capital requirements, providing it with a favourable cash flow cycle as it grows. This cash flow model is different from traditional internet retailers that require sizeable outlays in working capital for inventory and warehousing, which can result in a trade-off between growth and capital.
- Our revenue and earnings growth forecasts are derived using the following assumptions:
    - We expect **strong revenue growth** to continue for the foreseeable future (projected FY19-FY22 revenue CAGR +18%) given TPW's market-leading position in the online furniture and homewares sector (online growth +14%, market share gains +4%). The main factors underpinning growth are an increase in Active Customers correlating to an increase in marketing spend and a higher conversion due to enhanced customer experiences on the Temple & Webster platform (i.e.: Visual Search and category browsing).
    - TPW should see its **fulfilment costs** as a percentage of revenue decline to ~10-11% of revenue in the long term (FY17: 15%, FY18: 13%). We expect this to be driven by the company benefitting from economies of scale as well as expanding its in-house delivery function.
    - As TPW continues to scale, the company should be able to expand its **gross profit margin** via transportation efficiencies, slightly favourable supplier terms and higher private label penetration through both Milan Direct and Temple & Webster brands.
    - A key determinant of our model and valuation is the effectiveness of TPW's **marketing and advertising spend.** The former management team invested heavily in brand marketing (billboards, TV, airport advertising etc), but the revised management team has a more targeted digital marketing approach. As the company passes through breakeven we expect the group to increase marketing at a similar pace to revenue growth.
    - Given its capital light business model, we estimate **capex** at ~1-3% of revenue per annum over the medium term.

Figure 17: High degree of operating leverage as TPW passes breakeven



	FY16	FY17	FY18
Revenue	100%	100%	100%
COGS	60%	57%	56%
Gross margin	**40%**	**43%**	**44%**
Fullfillment costs	18%	15%	13%
Delivered margin	22%	28%	31%
Marketing	19%	13%	11%
GPAPA	**2%**	**15%**	**20%**

		FY18	Earnings leverage to revenue			
Revenue	**A$m**	**72.6**	**100.0**	**125.0**	**150.0**	**200.0**
GPAPA margin	%	20%	20%	20%	20%	20%
GPAPA	A$m	14.4	19.8	24.8	29.7	39.6
Opex	A$m	-15.0	-15.0	-15.0	-15.0	-15.0
EBITDA	**A$m**	**-0.6**	**4.8**	**9.8**	**14.7**	**24.6**
EV/EBITDA	**x**		**27.2**	**13.4**	**8.9**	**5.3**

Source: Company Reports, Canaccord Genuity estimates

Figure 18: TPW P&L, balance sheet and cash flow statement

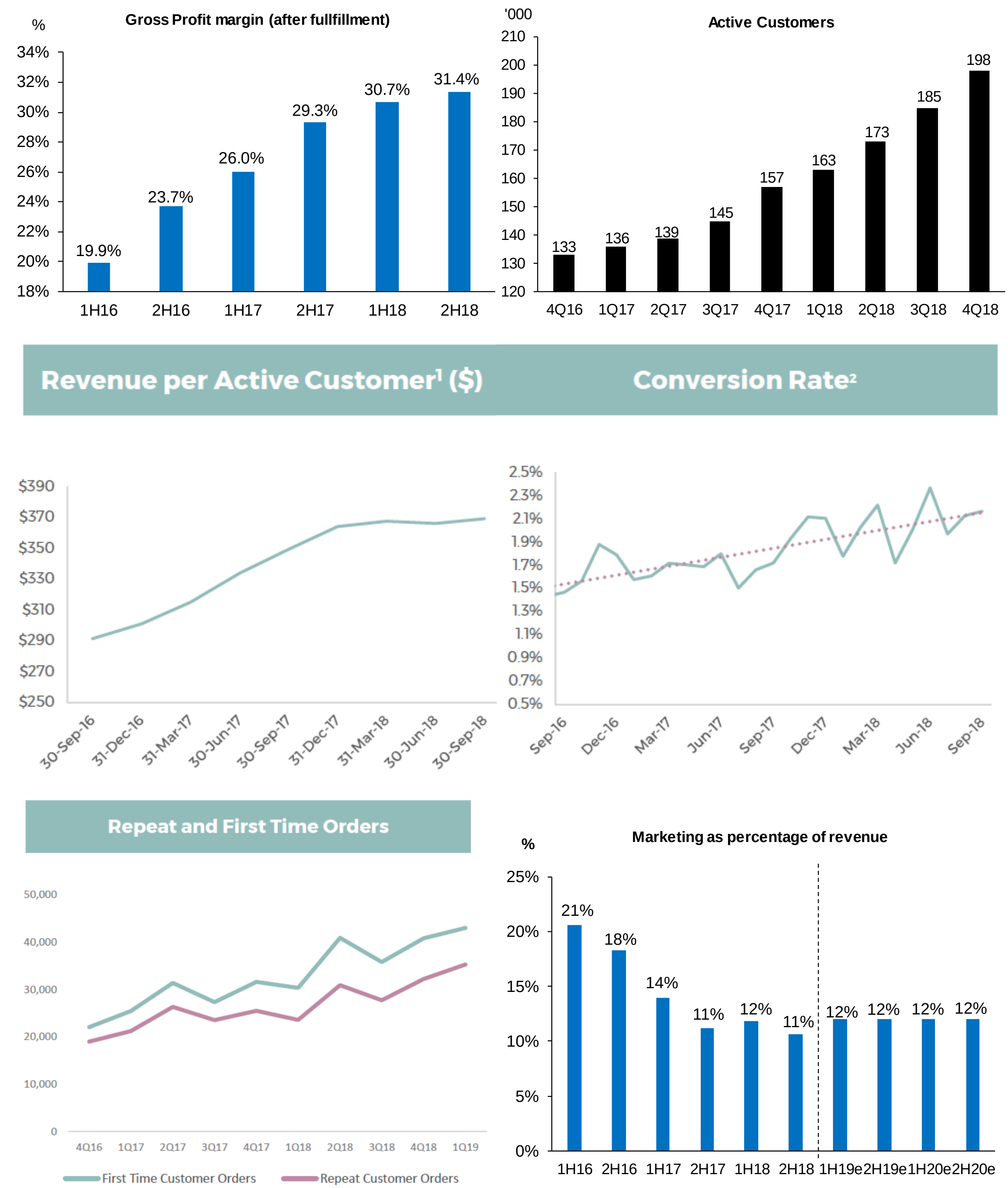
Profit & Loss		FY16A	1H17A	2H17A	FY17A	1H18A	2H18A	FY18A	1H19E	2H19E	FY19E	FY20E	FY21E	FY22E
Revenue	**A$m**	**61.7**	**34.0**	**30.4**	**64.5**	**34.4**	**38.2**	**72.6**	**46.5**	**49.6**	**96.1**	**118.6**	**142.4**	**167.3**
Growth			6%	3%	5%	1%	25%	13%	35%	30%	32%	23%	20%	18%
COGS	A$m	-37.0	-19.8	-17.2	-37.0	-19.2	-21.2	-40.5	-26.5	-28.3	-54.8	-68.8	-85.4	-100.4
COGS Margin	%	*60%*	*58%*	*57%*	*57%*	*56%*	*56%*	*56%*	*57%*	*57%*	*57%*	*58%*	*60%*	*60%*
Fulfilment expenses	A$m	-11.2	-5.4	-4.3	-9.7	-4.6	-4.9	-9.6	-5.6	-6.0	-11.5	-14.2	-17.1	-18.4
Fulfilment Margin	%	*18%*	*16%*	*14%*	*15%*	*13%*	*13%*	*13%*	*12%*	*12%*	*12%*	*12%*	*12%*	*11%*
Gross Profit	**A$m**	**13.5**	**8.9**	**8.9**	**17.8**	**10.6**	**12.0**	**22.5**	**14.4**	**15.4**	**29.8**	**35.6**	**39.9**	**48.5**
Gross Profit Margin	%	*22%*	*26%*	*29%*	*28%*	*31%*	*31%*	*31%*	*31%*	*31%*	*31%*	*30%*	*28%*	*29%*
Marketing	A$m	-12.0	-4.7	-3.4	-8.2	-4.1	-4.1	-8.1	-5.6	-6.0	-11.5	-14.2	-17.1	-20.1
Opex	A$m	-16.3	-9.0	-7.4	-16.4	-7.3	-7.7	-15.0	-8.3	-8.9	-17.2	-18.6	-19.7	-20.9
Total Opex	**A$m**	**-28.3**	**-13.7**	**-10.8**	**-24.6**	**-11.4**	**-11.8**	**-23.1**	**-13.9**	**-14.9**	**-28.7**	**-32.8**	**-36.8**	**-41.0**
EBITDA	**A$m**	**-14.8**	**-4.9**	**-1.9**	**-6.8**	**-0.8**	**0.2**	**-0.6**	**0.6**	**0.5**	**1.1**	**2.7**	**3.0**	**7.5**
Depreciation and Amortisation	A$m	-0.5	-0.2	-0.4	-0.6	-0.1	-0.1	-0.2	-0.1	-0.1	-0.2	-0.2	-0.2	-0.2
EBIT	**A$m**	**-15.3**	**-5.1**	**-2.3**	**-7.4**	**-0.9**	**0.1**	**-0.8**	**0.5**	**0.4**	**0.9**	**2.5**	**2.8**	**7.3**
Net Interest	A$m	-4.4	0.2	0.1	0.3	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
NPBT	**A$m**	**-19.6**	**-4.9**	**-2.3**	**-7.2**	**-0.9**	**0.1**	**-0.7**	**0.5**	**0.4**	**0.9**	**2.5**	**2.8**	**7.3**
Tax Expense	A$m	5.9	1.5	0.7	2.1	0.3	0.4	0.7	0.0	0.0	0.0	0.0	0.0	0.0
NPAT (Normalised)	**A$m**	**-13.8**	**-3.4**	**-1.6**	**-5.0**	**-0.6**	**0.6**	**-0.1**	**0.5**	**0.4**	**0.9**	**2.5**	**2.8**	**7.3**
Non-recurring	A$m	-30.7	-2.0	-0.8	-2.7	-0.3	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
NPAT (Reported)	**A$m**	**-44.4**	**-5.4**	**-2.4**	**-7.8**	**-0.9**	**0.9**	**0.0**	**0.5**	**0.4**	**0.9**	**2.5**	**2.8**	**7.3**
EFPOWA	#	105.8	105.7	105.7	105.7	107.6	107.6	107.6	112.5	112.5	112.5	112.5	112.5	112.5
EPS	cps	-0.42	-0.05	-0.02	-0.07	-0.01	0.01	0.00	0.00	0.00	0.01	0.02	0.03	0.06

Balance Sheet		FY16A	1H17A	2H17A	FY17A	1H18A	2H18A	FY18A	1H19E	2H19E	FY19E	FY20E	FY21E	FY22E
Cash	A$m	18.4	12.3	8.7	8.7	8.8	9.9	9.9	10.4	11.0	11.0	13.8	16.9	24.2
Receivables	A$m	0.1	0.1	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Inventory	A$m	3.5	3.2	1.4	1.4	2.0	2.2	2.2	2.9	3.1	3.1	3.8	4.8	5.6
PPE	A$m	0.2	0.3	0.2	0.2	0.2	0.2	0.2	0.3	0.5	0.5	0.8	1.1	1.4
Intangibles	A$m	7.3	7.2	7.7	7.7	7.6	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5
Other	A$m	1.0	0.4	0.9	0.9	1.0	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Assets	**A$m**	**30.6**	**23.4**	**18.9**	**18.9**	**19.8**	**21.7**	**21.7**	**23.0**	**24.0**	**24.0**	**27.8**	**32.1**	**40.5**
Payables	A$m	9.1	8.5	5.5	5.5	6.7	7.2	7.2	8.0	8.5	8.5	9.8	11.3	12.4
Deferred Revenue	A$m	3.9	1.9	1.6	1.6	2.0	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Provisions	A$m	0.7	1.3	1.2	1.2	1.0	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Interest bearing liabilities	A$m	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	A$m	0.6	0.6	0.6	0.6	0.6	0.7	0.7	0.3	0.3	0.3	0.3	0.3	0.3
Liabilities	**A$m**	**14.3**	**12.2**	**8.8**	**8.8**	**10.3**	**10.9**	**10.9**	**11.3**	**11.8**	**11.8**	**13.1**	**14.6**	**15.7**
Equity	**A$m**	**16.4**	**11.2**	**10.0**	**10.0**	**9.6**	**10.8**	**10.8**	**11.7**	**12.1**	**12.1**	**14.7**	**17.5**	**24.8**
ROE	*%*	*-84.0%*	*-49.6%*	*-30.0%*	*-42.1%*	*-12.4%*	*11.0%*	*11.0%*	*8.1%*	*7.1%*	*7.1%*	*19.0%*	*17.6%*	*34.5%*
Working Capital	*A$m*	*-5.5*	*-5.2*	*-4.1*	*-4.1*	*-4.5*	*-4.9*	*-4.9*	*-5.1*	*-5.5*	*-5.5*	*-6.0*	*-6.5*	*-6.8*

Cash Flow Statement		FY16A	1H17A	2H17A	FY17A	1H18A	2H18A	FY18A	1H19E	2H19E	FY19E	FY20E	FY21E	FY22E
EBITDA	A$m	-14.8	-4.9	-1.9	-6.8	-0.8	0.2	-0.6	0.6	0.5	1.1	2.7	3.0	7.5
Change in working capital	A$m	-1.1	0.9	-1.9	-1.1	0.9	0.9	1.8	0.2	0.4	0.5	0.6	0.5	0.3
Net interest paid	A$m	0.2	0.0	0.3	0.3	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Income taxes paid	A$m	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net operating cash flows	**A$m**	**-15.7**	**-4.1**	**-3.5**	**-7.6**	**0.1**	**1.1**	**1.3**	**0.7**	**0.9**	**1.6**	**3.3**	**3.5**	**7.8**
Payments for PPE/Intangibles	A$m	-0.4	-0.1	-0.1	-0.1	0.0	0.0	-0.1	-0.3	-0.3	-0.5	-0.5	-0.5	-0.5
Other/Acquisitions	A$m	-13.7	-2.0	0.0	-2.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net investing cash flows	**A$m**	**-14.1**	**-2.0**	**-0.1**	**-2.1**	**0.0**	**0.0**	**-0.1**	**-0.3**	**-0.3**	**-0.5**	**-0.5**	**-0.5**	**-0.5**
Proceeds from issue of securiti	A$m	61.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net borrowings	A$m	12.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other/Dividends	A$m	-27.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net financing cash flows	**A$m**	**46.4**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Net change in cash held	**A$m**	**16.5**	**-6.1**	**-3.6**	**-9.7**	**0.1**	**1.1**	**1.2**	**0.5**	**0.6**	**1.1**	**2.8**	**3.0**	**7.3**
Cash at beginning of period	A$m	1.9	18.4	18.4	18.4	8.7	8.8	8.7	9.9	10.4	9.9	11.0	13.8	16.9
Cash at end of period	**A$m**	**18.4**	**12.3**	**14.9**	**8.7**	**8.8**	**9.9**	**9.9**	**10.4**	**11.0**	**11.0**	**13.8**	**16.9**	**24.2**

Source: Company reports, Canaccord Genuity estimates

Figure 19: Key metrics improving



Source: Company reports, Canaccord Genuity estimates

Valuation

- TPW is in the early stages of becoming a significant player in the fast-growing Australia online furniture and homewares market (4% online penetrated). The company's financial profile appears robust with increasing Active Customers (FY18 +26%), improving ARPU (FY18 >+10%), rising gross profit margins (FY18 ↑ 350bps cont. to 31.1%) whilst maintaining a stable CAC ($55/new active).
- In assessing a fair value for TPW, we apply a DCF valuation methodology to arrive at a $1.55ps target price (12 month forward). We do not view a multiple analysis as a relevant metric to value the company given dissimilar revenue models between its peer groups. In addition, market valuations always reflect investor expectations for future cash flows and, as such, we believe this methodology better represents the long-term value of TPW.
- TPW has high visibility to gross margin and operating expense leverage; however, customer acquisition and retention are critical factors to growth and earnings given TPW has a high variable cost model.
- **DCF methodology ($1.55ps, K_e 9.3%, β 1.2x, ERP 5.5%)**:
    - Our terminal value incorporates a long-term cash EBIT margin of 10% (gross profit margin 30%, steady state S&M expense 10%, capex/G&A 10%) on our FY24e revenue expectations of $215m (6-year revenue CAGR +18%). Our revenue CAGR is derived from category growth (+14%) and slight share gain (+4%).
    - We assume a terminal EBIT multiple of 10x which is broadly in line with its ASX industrial peers.

Figure 20: DCF valuation

DCF Analysis - Firm Value	FY19	FY20	FY21	FY22	FY23	FY24
1. Explicit cash flow						
EBITDA	1.1	2.7	3.0	7.5	11.2	14.9
Less cash tax	0.0	0.0	0.0	0.0	-3.3	-4.4
Less Increase in Working Capital	0.5	0.6	0.5	0.3	0.7	0.7
Less Capex	-0.5	-0.5	-0.5	-0.5	-0.5	-0.5
Free Cashflow to Firm	**1.1**	**2.8**	**3.0**	**7.3**	**8.1**	**10.7**
Discount factor	*0.91*	*0.82*	*0.75*	*0.68*	*0.62*	*0.56*
PV of Free Cashflow	1.0	2.3	2.3	5.0	5.0	6.0
Total PV of Explicit Free Cashflow						21.5
2. Terminal value						
Terminal revenue (FY24)						226.0
LT Sustainable EBIT margins						10.0%
Cash EBIT						22.6
Long Term Multiple						10.0
Terminal value						226.0
Discount factor						0.56
PV of Terminal Value						126.7
Firm Valuation						**148.3**
Net Debt						-10.5
Equity Valuation						**158.8**
EFPOWA						112.5
Value per share						**1.41**
Target price (rolled forward by K_e)						**1.55**

Risk Free Rate	2.7%
Beta	1.4
Equity RP	5.5%
Cost of Equity	**10.1%**
Cost of Debt	**5%**
Gearing Ratio	0%
WACC	**10.1%**

LT sustainable cash EBIT margins	
Revenue	100%
Gross profit margins	**30%**
Marketing	10%
Opex	7%
Capex	3%
EBIT margin	**10%**
LT EBIT multiple	10.0

Source: Canaccord Genuity estimates

Peer analysis

- We also draw similarities to peers in the domestic ecommerce market (Redbubble, Kogan, Marley Spoon) as well as other more established businesses in the furniture and homewares segment (Harvey Norman, Nick Scali, Adairs).
- From an international perspective, we view Wayfair (NYSE: W) as the closest listed peer to TPW with a similar business model based in the US. W is the largest online furniture and homewares retailer in the US (and the world) with a selection of >10m product SKUs supported by insourced delivery and customer service. W's revenue has experienced a >20% CAGR each year since FY15, but the company is unprofitable.
- We believe TPW's premium rating relative to Wayfair and other ecommerce peers illustrates investors' expectations of above-peer revenue growth for the foreseeable future (Wayfair FY19e +31%, TPW 1Q19 +38%) coupled with the currently low market penetration of TPW (total category share ~0.6%, online share ~14%).

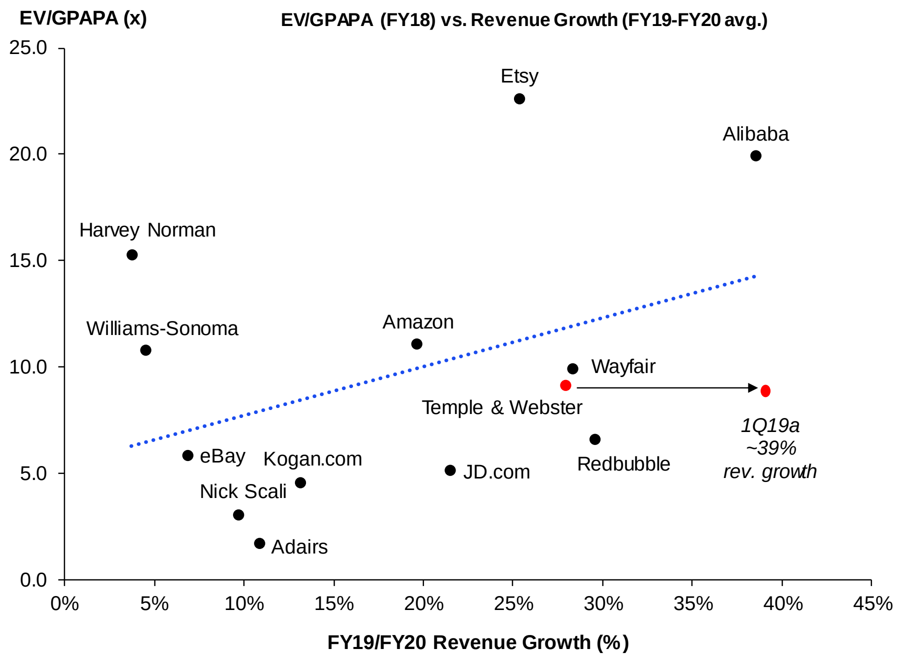
Figure 21: Peer analysis

Company	Price	Market Cap	Enterprise Value	Revenue			EV/Revenue			EV/Gross Profit			Revenue Growth		
				FY18	FY19	FY20	FY18	FY19	FY20	FY18	FY19	FY20	FY18	FY19	FY20
Domestic e-commerce players															
Temple & Webster	$1.25	$140	$130	73	96	119	1.8	1.4	1.1	5.8	4.4	3.7	13%	32%	23%
Redbubble	$1.43	$359	$331	231	359	451	1.4	0.9	0.7	5.2	3.2	2.6	30%	55%	26%
Kogan.com	$2.78	$261	$218	412	468	528	0.5	0.5	0.4	2.7	2.4	2.1	42%	13%	13%
Marley Spoon	$0.50	€ 43	€ 22	93	150	206	0.2	0.1	0.1	1.0	0.5	0.3	75%	61%	37%
Average							***1.0***	***0.7***	***0.6***	***3.7***	***2.6***	***2.2***			
Domestic furniture retailers															
Harvey Norman	$3.22	$3,799	$4,522	3,140	3,315	3,479	1.4	1.4	1.3	6.8	6.4	6.1	-3%	6%	5%
Nick Scali	$5.10	$413	$410	251	274	302	1.6	1.5	1.4	2.6	2.4	2.2	8%	9%	10%
Adairs	$1.69	$280	$293	315	352	387	0.9	0.8	0.8	1.5	1.4	1.3	19%	12%	10%
Average							***1.3***	***1.2***	***1.1***	***3.6***	***3.4***	***3.2***			
International e-commerce players															
Amazon	$1,599.01	$781,866	$799,320	232,461	281,019	332,777	3.4	2.8	2.4	9.3	7.7	6.5	31%	21%	18%
ETSY	$47.71	$5,747	$5,443	598	776	939	9.1	7.0	5.8	13.8	10.6	8.8	36%	30%	21%
eBay	$27.89	$26,853	$31,263	10,736	11,304	12,252	2.9	2.8	2.6	3.8	3.6	3.3	12%	5%	8%
Alibaba	$150.44	$386,921	$380,614	39,129	54,828	75,431	9.7	6.9	5.0	16.6	11.8	8.6	-75%	40%	38%
JD.com	$22.76	$32,917	$28,942	67,072	83,039	99,458	0.4	0.3	0.3	6.5	5.2	4.4	-81%	24%	20%
Average							***5.1***	***4.0***	***3.2***	***10.0***	***7.8***	***6.3***			
International furniture retailers															
Wayfair	$87.85	$7,937	$7,949	6,730	8,840	11,073	1.2	0.9	0.7	5.0	3.8	3.0	43%	31%	25%
Bed Bath & Beyond	$13.63	$1,882	$2,299	12,349	12,144	12,101	0.2	0.2	0.2	0.5	0.5	0.5	1%	-2%	0%
Williams-Sonoma	$61.78	$4,977	$5,102	5,292	5,646	5,737	1.0	0.9	0.9	2.6	2.5	2.4	4%	7%	2%
Average							***0.8***	***0.7***	***0.6***	***2.7***	***2.3***	***2.0***			
Peer set average								***1.6***	***1.4***		***4.0***	***3.4***			

Source: CapitalIQ, Canaccord Genuity estimates, *All earnings estimates are CapitalIQ except TPW which is CGAu est.

- Given the sensitivities to valuation multiples relative to revenue growth, we look at TPW's EV/GPAPA (gross profit after marketing spend) relative to its two year forward revenue growth. If TPW can maintain its above-average revenue growth, we would expect its multiple to expand.

Figure 22: EV/GPAPA [FY18] multiples relative to revenue growth expectations (FY19/FY20 average)



Source: CapitalIQ, Canaccord Genuity estimates, *All earnings estimates are CapitalIQ except TPW which is CGAu est,

Key management

- **Mark Coulter (CEO):** TPW is led by co-founder Mark Coulter. He is based in Sydney and has been involved as an advisor to the company since its inception in 2011. Prior to TPW, Mr. Coulter held senior roles at News Limited and was previously a solicitor at Gilbert & Tobin as well as a management consultant at McKinsey & Company.
- **Adam McWhinney (Group Customer Experience Officer/Executive GM Temple & Webster):** Mr. McWhinney is also a co-founder of TPW and has 15 years of experience in senior digital product development roles. He is responsible for leading the brand-driven customer experience across the group. Prior to TPW, Mr. McWhinney was a product director at News Limited and was the creator of Taste.com.au, one of Australia's most successful lifestyle websites.
- **Mark Tayler (CFO):** Mr. Tayler joined the company in 2016 and is an experienced CFO/COO of both public and private companies spanning e-commerce, retail, wholesale and IT services. Prior to TPW, he was the CFO of DealsDirect Group.
- **Michael Henriques (CIO):** Mr. Henriques joined TPW in 2015 holding previous experience in senior roles at Wayfair Australia and Wotif Group.
- **Peter Neal (Head of Operations):** Mr. Neal joined TPW in 2012 and has overseen all distribution during the company's growth and currently manages operational and technical changes. He is a logistics, operations and warehouse specialist with over 20 years of experience, of which 12 years have been within e-commerce including Grays Online.
- **Dean Ramler (Executive General Manager, Milan Direct):** Mr. Ramler is responsible for the day to day operations of the Milan Direct brand and its growth initiatives. He was a founder of Milan Direct in 2006 and joined the group at the time of acquisition, having deep experience in the Australian furniture and retail industries.
- **Susie Sugden (Chief Commercial Officer/Chief Marketing Officer):** Ms. Sugden joined the company in 2016 having experience in both offline and online retail across Australia and South East Asia as a specialist in digital marketing and merchandising. Prior to TPW, she led a number of businesses in Indonesia, including being a co-founder of Lazada, Indonesia's largest e-commerce website acquired by Alibaba in 2016.
- **Lucy Sutherland (Head of Trade & Commercial):** Ms. Sutherland joined TPW as head of trade & commercial in 2016. Prior to joining TPW, she was the general manager of ISCD (International School of Colour & Design) and also the managing consultant of Colourways.
- **Christie McGuiness (HR Director):** Ms. McGuiness joined TPW in October 2015 and has extensive experience in human resources from medium, large, private and public organisations across print media, digital media, ecommerce, finance and agriculture (i.e. GrainCorp, News Limited, equigroup).

Board of Directors

- **Stephen Heath (Chairman, Independent Non-Executive Director):** Mr. Heath is a specialist in consumer goods brand management and brings over 25 years of manufacturing, wholesale distribution and retail experience across Australia, New Zealand and Asia. He has led some of Australia's best-known consumer brands such as Rebel Sport, Godfrey's and Fantastic Holdings.
- **Susan Thomas (Independent Non-Executive Director):** Ms. Thomas joined the board in 2016 and is an experienced company director and audit and risk committee chair. She established FlexiPlan, a funds management business which was later sold to MLC. Ms. Thomas is currently a director of Grant Thornton Australia, Fitzroy River Holdings, PEXA, Advance Asset Management, Asgard Capital Management, BT Portfolio Services and Westpac Financial Services.
- **Conrad Yiu (Non-executive Director):** Mr. Yiu is a co-founder of TPW and was appointed to the board in 2011. Previously, he was a chairman of the company and holds over 20 years of commercial and advisory experience with a focus on investing in and building high growth businesses in the consumer and technology industry. He is currently also a principal of ArdenPoint, an investment firm which he co-founded alongside Mark Coulter in 2011.

Risks

- **Increased competition in a post Amazon world:** We expect increased competition given the size of the potential market, especially from brick-and-mortar stores expanding online and Amazon. In other retail categories, online players have proved to be more competitive than store-based operators as the cost to do business is significantly reduced. TPW's broad catalogue, supply chain, delivery and customer service are current competitive advantages; however, this can be copied and could be managed more effectively by other retailers with an established presence, operating history and a large customer base. A meaningful rise in competition may materially shift TPW's customer retention and acquisition costs which could ultimately compromise margins and top-line momentum. We note there is upside if competition is weaker than expected and downside if Amazon's offering in this category improves rapidly.
- **Housing market downturn impacting Australian retail environment:** Home furnishing retailers are historically correlated to housing trends and we believe the upturn in the Australian housing market over the last 2 years has aided TPW's growth. We believe an economic slowdown is a risk to TPW as consumers tend to limit spending on bigger-ticket, discretionary products. In addition, stocks in this industry are typically rate sensitive.
- **Key supplier and counterparty risk:** TPW largely acts as a bridge to suppliers and therefore carries minimal inventory and is self-funding. However, this makes TPW highly dependent on suppliers, and losing key vendors could result in reduced sales. We expect that finding new suppliers on favourable terms, in a timely manner or in sufficient volume, may be challenging for the group. In addition, there is reputation risk to the Temple & Webster brand if a vendor's products do not meet customer expectations.
- **Operational and technological failure:** TPW is reliant on its online platform and supply chain to deliver a premium shopping experience from initial browsing to having an order fulfilled. Operational disruption within the order process (i.e.: system failure to its websites or to third-party suppliers) could impact the group's ability to deliver the correct items on time to a customer, which may negatively affect the Temple & Webster brand and reputation.
- **Marketing strategy fatigue:** TPW may experience marketing strategy fatigue with a growing customer base. The frequency of TPW's marketing may be underestimated or overestimated and have the result of reducing sales conversion rates. If the group does not make efficient use of data analytics, update its segment listings and decide accurately when to deploy re-engagement campaigns to improve performance metrics, this could adversely affect financial and operational performance.

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Investment Recommendation

Date and time of first dissemination: November 18, 2018, 14:59 ET

Date and time of production: November 18, 2018, 14:47 ET

Target Price / Valuation Methodology:

Temple and Webster - TPW

We derive our target price based on a DCF methodology ($1.55ps, K_e 9.3%, β 1.2x, ERP 5.5%):

- Our terminal value incorporates a long-term cash EBIT margin of 10% (gross profit margin 30%, steady state S&M expense 10%, capex/G&A 10%) on our FY24e revenue expectations of $215m (6-year revenue CAGR +18%). Our revenue CAGR is derived from category growth (+14%) and slight share gain (+4%).
- We assume a terminal EBIT multiple of 10x which is broadly in line with its ASX industrial peers.

Risks to achieving Target Price / Valuation:

Temple and Webster - TPW

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Global Stock Ratings (as of 11/18/18)

Rating	Coverage Universe		IB Clients
	#	%	%
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Hold	203	23.02%	30.05%
Sell	9	1.02%	33.33%
Speculative Buy	109	12.36%	66.97%
	882*	100.0%	

*Total includes stocks that are Under Review

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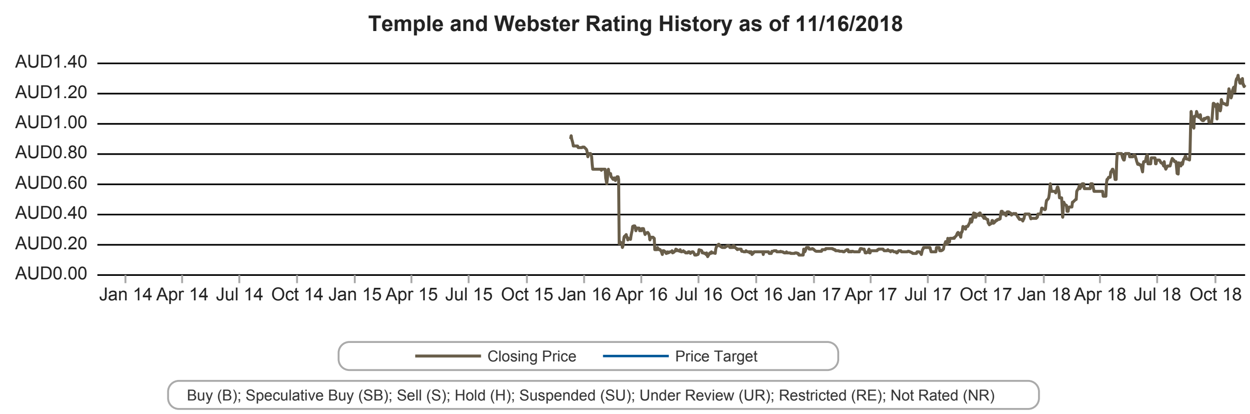

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