Falling Knife You Don't Want to Catch – Part 1

We counsel investors to take care not to be cut by falling knives – stocks that have seen steep declines but still have further to fall. As the market rotates away from high-flying growth names to more stable cash generators, investors need reliable fundamental research, more than ever, to protect their portfolios from falling knives.

We continue to post an exceptional hit rate on spotting overvalued stocks. Currently, 62 out of our 65 Danger Zone stock picks are down from their 52-week highs by more than the S&P 500. Figure 1 lists the open Danger Zone picks that are down at least 40% from their 52-week highs. Our Focus List Stocks: Short Model Portfolio, the best-of-the-best of our Danger Zone picks, outperformed the S&P 500 as a short portfolio by 36% in 2021 with 29 out of our 31 picks outperforming the index.

This report highlights one particularly dangerous falling knife: Uber (UBER: $35/share). We highlight four other falling knives in other reports published today: Affirm (AFRM: $60/share) here, Rivian (RIVN: $60/share) here, DoorDash (DASH: $104/share) here, and Warby Parker (WRBY: $35/share) here. Each of these stocks have dropped at least 40% from all-time highs, yet still carry at least 40% additional downside risk.

Figure 1: Danger Zone Picks Down >40% From 52-Week High – Performance through 1/28/22

Company	Ticker	Off 52-Week High
Koss Corp	KOSS	-94%
Robinhood Markets Inc.	HOOD	-85%
Peloton Interactive Inc.	PTON	-84%
GameStop Corporation	GME	-80%
AMC Entertainment Holdings, Inc.	AMC	-79%
Cronos Group Inc.	CRON	-78%
Beyond Meat Inc.	BYND	-71%
Pinterest Inc.	PINS	-70%
Rivian Automotive Inc	RIVN	-68%
Express Inc.	EXPR	-68%
Affirm Holdings Inc.	AFRM	-66%
Allbirds Inc	BIRD	-64%
Snap Inc.	SNAP	-63%
LivePerson Inc.	LPSN	-63%
Carvana Co.	CVNA	-61%
DoorDash, Inc.	DASH	-60%
Wayfair, Inc.	W	-59%
Coinbase Global Inc.	COIN	-59%
Spotify Technology S.A.	SPOT	-55%
Domo Inc.	DOMO	-55%
Squarespace Inc.	SQSP	-53%
Shake Shack, Inc.	SHAK	-53%
Eventbrite Inc.	EB	-51%
Shopify Inc	SHOP	-51%
Diebold Nixdorf, Inc.	DBD	-49%
Sweetgreen Inc	SG	-48%
LYFT Inc.	LYFT	-48%
PROS Holdings, Inc.	PRO	-46%
Netflix Inc.	NFLX	-45%
Uber Technologies Inc.	UBER	-45%
Zendesk, Inc.	ZEN	-43%
Warby Parker Inc.	WRBY	-42%
Nutanix Inc	NTNX	-41%

Sources: New Constructs, LLC

Falling Knife: Uber Technologies (UBER): Down 45% from 52-Wk High & 49%+ Downside Remaining

We named Uber (UBER) one of the most dangerous stocks for fiduciaries in August 2020 when we reiterated our original Danger Zone report from April 2019. Since our original report, Uber has outperformed the S&P 500 as a short by 69% and could fall another 49%. We detail Uber's broken business model, the commoditized nature of its industry, and more challenges facing the company in our most recent report here.

Current Price Is So Overvalued that it Implies Uber Owns 123% of 2030 TAM

Below, we use our reverse discounted cash flow (DCF) model to analyze the expectations for future growth in cash flows baked into Uber's current share price and show that it could fall 49%+ further.

To justify its current price of $35/share, Uber must immediately:

- Improve its pre-tax margin to 4% (compared to -34% TTM), which is similar to airlines prior to consolidation and
- grow revenue by 33% compounded annually for the next 10 years.

In this scenario, Uber would earn $189 billion in revenue in 2030. At its 3Q21 take rate of 21%, this scenario equates to over $901 billion in gross bookings in 2030.

In other words, to justify its current stock price, Uber must capture 123% of the combined projected TAM[1] for rideshare and food delivery in 2030. For reference, Second Measure estimates Uber's share of the U.S. rideshare TAM is 70% in December 2021 and its share of the U.S. food delivery TAM sits at 27% (including acquired Postmates) in December 2021.

Keep in mind, the number of companies that grow revenue by 20%+ compounded annually for such a long period are unbelievably rare, making the expectations in Uber's share price outright unrealistic.

49% Downside Even if Uber Meets Industry Growth

Uber's economic book value, or no growth value, is negative $40/share, which illustrates the overly optimistic expectations in its stock price.

Even if we assume Uber:

- improves its pre-tax margin to 6% (greater than pre-consolidation airlines) and
- grows revenue by 19% compounded annually (equal to projected rideshare market CAGR through 2026) through 2030, then

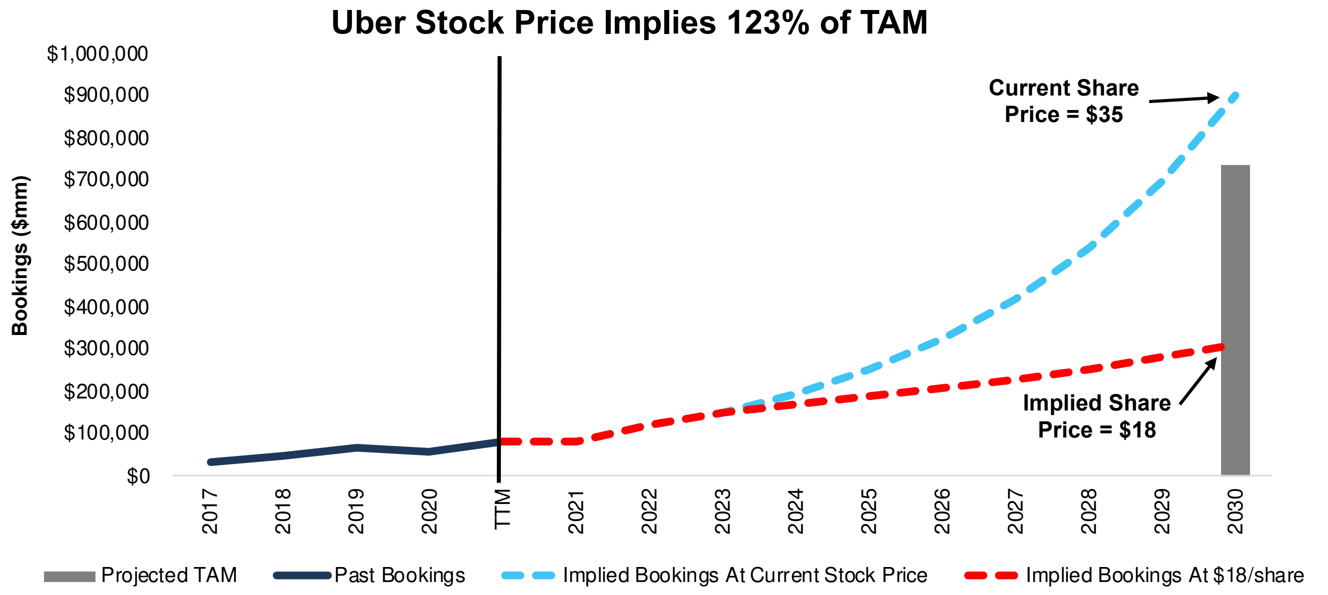
the stock is worth just $18/share today – a 49% downside. Even in this scenario, Uber would earn $65 billion in revenue in 2030. At its 3Q21 take rate, this scenario equates to over $310 billion in gross bookings in 2030.

This scenario may even prove too optimistic as it assumes a significant improvement in NOPAT margin in an industry with little pricing power due to the abundance of alternatives, in which case the downside to the stock would be even larger.

Figure 2 compares Uber's implied future gross bookings in these scenarios to its historical gross bookings, along with the expected TAM for rideshare and food delivery in 2030.

[1] 2030 TAM estimate equals a $423 billion global ridesharing market and $312 billion global food delivery market. Global ridesharing TAM assumes the global rideshare market continues growing at 19.2% annually from 2026-2030 (consistent with Mordor Intelligence's estimated CAGR through 2026). Global food delivery TAM assumes the global food delivery market continues growing at 10.9% annually from 2028-2030 (consistent with Research and Market's estimated CAGR through 2028).

Figure 2: Uber's Historical and Implied Bookings: DCF Valuation Scenarios



Sources: New Constructs, LLC and company filings.

Each of the above scenarios also assumes UBER is able to grow revenue, NOPAT, and FCF without increasing working capital or fixed assets. This assumption is highly unlikely but allows us to create best-case scenarios that demonstrate how high the expectations embedded in the current valuation are. For reference, UBER's invested capital has increased by $5.1 billion (36% of TTM revenue) over the trailing-twelve-months (TTM) and by an average of $5.8 billion (42% of TTM revenue) over the past three years.

Fundamental Research Provides Clarity in Frothy Markets

2022 has quickly shown investors that fundamentals matter and stocks don't only go up. With a better grasp on fundamentals, investors have a better sense of when to buy and sell – and – know how much risk they take when they own a stock at certain levels. Without reliable fundamental research, investors have no way of gauging whether a stock is expensive or cheap.

As shown above, disciplined, reliable fundamental research shows that even after plummeting, Uber, Affirm, Rivian, DoorDash, and Warby Parker still hold significant downside.

Check out this week's Danger Zone interview with Chuck Jaffe of Money Life.

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Disclosure: David Trainer, Kyle Guske II, and Matt Shuler receive no compensation to write about any specific stock, style, or theme.

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It's Official: We Offer the Best Fundamental Data in the World

Many firms claim their research is superior, but none of them can prove it with independent studies from highly-respected institutions as we can. Three different papers from both the public and private sectors show:

1. Legacy fundamental datasets suffer from significant inaccuracies, omissions and biases.
2. Only our "novel database" enables investors to overcome these flaws and apply reliable fundamental data in their research.
3. Our proprietary measures of Core Earnings and Earnings Distortion materially improve stock picking and forecasting of profits.

Best Fundamental Data in the World

Forthcoming in The Journal of Financial Economics, a top peer-reviewed journal, Core Earnings: New Data & Evidence proves our Robo-Analyst technology overcomes material shortcomings in legacy firms' data collection processes to provide superior fundamental data, earnings models, and research. More details.

Key quotes from the paper:

- "[New Constructs'] *Total Adjustments* differs significantly from the items identified and excluded from Compustat's adjusted earnings measures. For example… 50% to 70% of the variation in *Total Adjustments* is not explained by *S&P Global's (SPGI) Adjustments* individually." – pp. 14, 1st para.

- "A final source of differences [between New Constructs' and S&P Global's data] is due to data collection oversights…we identified cases where Compustat did not collect information relating to firms' income that is useful in assessing core earnings." – pp. 16, 2nd para.

Superior Models

A top accounting firm features the superiority of our ROIC, NOPAT and Invested Capital research to Capital IQ & Bloomberg's in Getting ROIC Right. See the Appendix for direct comparison details.

Key quotes from the paper:

- "…an accurate calculation of ROIC requires more diligence than often occurs in some of the common, off-the-shelf ROIC calculations. Only by scouring the footnotes and the MD&A [as New Constructs does] can investors get an accurate calculation of ROIC." – pp. 8, 5th para.

- "The majority of the difference…comes from New Constructs' machine learning approach, which leverages technology to calculate ROIC by applying accounting adjustments that may be buried deeply in the footnotes across thousands of companies." – pp. 4, 2nd para.

Superior Stock Ratings

Robo-Analysts' stock ratings outperform those from human analysts as shown in this paper from Indiana's Kelley School of Business. Bloomberg features the paper here.

Key quotes from the paper:

- "the portfolios formed following the buy recommendations of Robo-Analysts earn abnormal returns that are statistically and economically significant." – pp. 6, 3rd para.

- "Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts." – pp. 20, 3rd para.

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