genial Equity Research

MERCADO LIBRE

2Q23 Review: A gala ball

LatAmTech

Main takeaways for e-commerce:

(i) GMV growth above expectation; **(ii)** Brazil GMV driven by continued market-share gains; **(iii)** Mexico is continuously establishing itself as a headliner; **(iv)** Macro scenario still weighs in on Argentina; **(v)** +200bps y/y in E-commerce Take-rate; **(vi)** E-commerce revenue growth of 38% y/y.

Main takeaways for Fintech:

(i) Strong expansion of total TPV; **(ii)** Off-platform TPV remains the largest contributor; **(iii)** TPV digital account driven by Argentina and Mexico; **(iv)** TPV acquiring continues to sustain solid growth levels; **(v)** Loan portfolio evolution in line with our projections; **(vi)** Gradual acceleration of credit card operations; **(vii)** Alert on NPL < 90 days; **(viii)** On the other hand, NPL>90 is still on a good downward trend; **(ix)** Fintech Take-Rate down by -45bps y/y; **(x)** Fintech Revenue growth of 24% y/y.

Main takeaways for the Consolidated Result:

(i) Consolidated net revenue growth above expectations (+3.0% vs. Gen. Est.); **(ii)** COGS slightly above expectations (+2.5% vs. Genial Est.), driven by logistics costs; **(iii)** Gross margin expansion (+92bps y/y), due to cost dilution; **(iv)** SG&A better than expected, due to efficiency gains (-9.2% vs. Genial Est.); **(v)** PDA shows a slowdown above expectations; **(vi)** Dilution of expenses leads to strong +671bps a/a profitability gain; **(vii)** FX losses still impact the bottom line; **(viii)** Still, profit grows +113% y/y; **(ix)** With an **EV/EBIT** of **39.7x** for **23E** and **25.7x** in **24E**, we reiterate our **BUY rating**, with **12M Target Price at US$1,520**, representing an **upside** of **30.49%.**

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Company

MELI US Equity
Buy

Price: US$ 1.164 (2-Aug-2023)
Target Price 12M: US$ 1.520 (Nasdaq)

MELI34 BZ Equity
Target Price 12M: R$ 60 (B3)

Mercado Libre (MELI-Nasdaq) released its 2Q23 results on August 2nd, 2023, after market hours on the Nasdaq exchange. Overall, the result came in slightly above our expectations, which were already quite optimistic, demonstrating again the Company's great execution capacity, **posting an impressive operating profit**, exceeding our estimates and consensus. We detail our optimism in Mercado Libre and our recent revisions made in order to incorporate risks related to **(i)** cross-border threats and **(ii)** exposure to Argentina in our earnings preview, which is attached ([MELI: 2Q23 Previews]).

2Q23 Review

E-commerce

GMV growth above expectation. Mercado Libre reported a +22.9% y/y acceleration in total GMV, reported at US$10.5bn (+3.9% vs. Genial Est.), delivering another quarter of solid performance in the e-commerce vertical.

Brazil GMV driven by continued market-share gains. Mercado Libre is once again consolidating its position as the top player in Brazilian e-commerce, managing to continuously capitalize on the share opportunities generated by the Americanas event at the beginning of the year. We believe the new market circumstances allowed for the +59% y/y (FX-Neutral) expansion of 1P GMV, which further boosted the performance of the local operation. With a +20% y/y increase in items sold, the Company reported GMV growth of +24.0% y/y and +6.4% q/q, totaling US$4.6bn (+1.9% vs. Genial Est.).

Mexico is continuously establishing itself as a headliner. As Mercado Libre increases its presence in the country, the e-commerce operation in Mexico continues to deliver growth at exponential rates, becoming the Company's 2nd largest operation in terms of GMV, surpassing Argentina this quarter.

Featuring **(i)** the highest acceleration in terms of successfully sold Items among the three countries of operation (+34% y/y) and **(ii)** the highest level of new shopper growth in 2 years, the Mexican operation achieved a +52.0% y/y acceleration in local GMV, reaching US$2.5bn (+52.0% y/y; +18.4% q/q).

Macro scenario still weighs in on Argentina. Impacted by the country's macroeconomic environment, the Argentine operation once again posted the weakest performance among the countries where Mercado Libre operates. In line with our expectations, in local currency terms, the evolution of GMV was driven by the country's inflation, such that we did not see relevant growth in terms of sold items (+1% y/y), nor as any kind of growth in real values (excluding inflation).

Local GMV totaled US$2.5bn (+12.0% y/y; +14.8% q/q), (+9.8% vs. Genial Est.). In our view, the above-expected performance in the country demonstrates the contribution of Mercado Libre's microeconomic quality, overcoming the adversities of the macro scenario. Quarter after quarter the Company, continues to post dollarized growth even faced with a persistent inflationary crisis weakening local consumer demand, and with a rather unfavorable USD/AR$ exchange rate.

+200bps y/y in E-commerce Take-rate. E-commerce take-rate was 18.4% (+200bps y/y; +60bps q/q). In line with our expectations, the higher commissioning rate was driven by **(i)** a higher penetration of Ads revenue and **(ii)** marketplace fees revision. Additionally, **(iii)** higher 1P penetration over total GMV also had a positive impact on commissioning, so that the reported take-rate was +40bps above our estimates.

E-commerce revenue growth of 38% y/y. Once again, Mercado Libre demonstrated an operational capacity well above its peers, standing out in the e-commerce business amid a slowdown scenario in the industry. The +23% y/y growth in total GMV, coupled with the +200bps y/y increase in Take-rate, allowed the Company to post a +37.9% y/y acceleration in Consolidated E-commerce Revenue, reaching US$1.9b (+37.9% y/y; +15.5% q/q).

Table 1. E-commerce Operational Data (2Q23 vs. Genial Est.)

	2Q23A	2Q23E		2Q22A		1Q23A	
[USD m]	**Reportado**	**Genial Est.**	**% R/E | bps**	**Reported**	**% y/y | bps**	**Reported**	**% q/q | bps**
Total GMV	**10.506**	**10.112**	**3,9%**	**8.551**	**22,9%**	**9.434**	**11,4%**
GMV Argentina	2.514	2.289	9,8%	2.245	12,0%	2.190	14,8%
GMV Brasil	4.620	4.534	1,9%	3.726	24,0%	4.340	6,4%
GMV México	2.494	2.270	9,9%	1.641	52,0%	2.107	18,4%
% Commerce Take Rate	**18,4%**	**18,0%**	**+40bps**	**16,4%**	**+200bps**	**16,4%**	**2p.p**
Commerce Net Revenue	**1.936**	**1.820**	**6,4%**	**1.404**	**37,9%**	**1.404**	**37,9%**

Source: Genial Investimentos, Mercado Libre.

Mercado Pago

Strong expansion of total TPV. The volume transacted in the quarter was driven by the up-market movement that the Company has been making in the acquiring business towards SMB merchants, with slightly higher revenues than the micro-merchants that were the main focus previously. TPV amounted to US$42bn (+39.3% y/y; +13.7% q/q) vs. +0.96% vs. Genial Est., in line with our forecasts.

Off-platform TPV remains the largest contributor. The above dynamics mainly benefit off-platform volume, leading to a FX-neutral acceleration of +128.7% y/y of this type of TPV (+46.4% y/y in USD). Driven by the growth levels of the acquiring operation in Mexico, Off-platform TPV amounted to US$30.9b (+0.4% vs. Genial Est.), while on-platform TPV stood at US$11.0b (+3.2% vs. Genial Est.).

TPV digital account driven by Argentina and Mexico. Consolidating a +22% y/y increase in the number of wallet payers, Mercado Libre delivered a +58.2% y/y growth in digital account TPV, reaching a total of US$14.8bn (+58.2% y/y; +16.4% q/q), slightly above our estimates (+3.3% vs. Genial Est.). TPV generated by digital accounts had a strong contribution from Argentina and Mexico, which continue to deliver relevant growth across all wallet products.

TPV acquiring continues to sustain solid growth levels. TPV acquiring totaled US$27.2bn (+30.8% y/y; +12.3% q/q), fully in line with our estimates. The ramp-up of the acquiring operation in Mexico was the main driver for TPV acquiring growth, as the Company continues to make an up-market move towards merchants in the country.

As we have mentioned in previous reports, since the beginning of the year, Mercado Libre has been gradually shifting from a focus on micro-merchants (Long-tail), to small businesses (SMB -Small and Medium Business). To remain competitive, the company is likely to employ a strategy that utilizes lower MDRs due to the upward movement in merchant mix. This is particularly pertinent with the entry of companies in the SMB category that generate up to R$360k in net revenue per year. Mercado Pago will face increased competition from companies specialized in this niche, such as Stone and PagSeguro. Consequently, the Company could maintain lower take-rates in response to this competition, particularly in the Brazilian market, in order to expand its merchant base.

Thus, the Company gradually consolidates a new merchant mix with slightly higher revenues, benefiting transacted volume growth. In the Mexican vertical, this up-market movement contributed to triple-digit growth in TPV per point of sale in 2Q23, offsetting the slowdown in the growth pace of the acquiring operation in Brazil.

Table 2. TPV Data (2Q23 vs. Genial Est.)

	2Q23A	2Q23E		2Q22A		1Q23A	
[USD m]	**Reported**	**Genial Est.**	**% R/E | bps**	**Reported**	**% y/y | bps**	**Reported**	**% q/q | bps**
Total TPV	**42.064**	**41.595**	**1,1%**	**30.194**	**39,3%**	**36.986**	**13,7%**
TPV Acquiring	27.246	27.245	0,0%	20.830	30,8%	24.259	12,3%
TPV Digital Account	14.818	14.349	3,3%	9.364	58,2%	12.727	16,4%
TPV Off-Platform	30.990	30.864	0,4%	21.175	46,4%	27.037	14,6%
TPV On-Platform	11.074	10.731	3,2%	9.019	22,8%	9.949	11,3%
% Fintech Take Rate	**3,52%**	**3,64%**	**-12bps**	**3,97%**	**-45bps**	**3,73%**	**-21bps**

Source: Genial Investimentos, Mercado Libre.

Mercado Credito

Loan portfolio evolution in line with our projections. The consolidated loan portfolio came in line with our estimates, totaling US$3.2bn (+21.0% y/y; +6.6% q/q) vs. US$3.3bn Genial Est., mainly driven by the expansion of the Consumer book in Mexico and the resumption of the acceleration of credit card operations in Brazil, with a dynamic very similar to what we have commented in our previous earnings release.

As the efforts made in terms of credit scoring improvement and prioritization of less risky users start to materialize in a better performance of the new cohorts, we see a sequential growth rate of the portfolio slightly accelerating from the levels presented in 2H22 (+6.6% y/y vs. +3.2% y/y 3Q22 and +2.4% y/y 4Q22).

Gradual acceleration of credit card operations. Two main dynamics drove the evolution of the credit card portfolio this quarter: **(i)** the gradual resumption of credit card issuance in Brazil, which started at the end of 1Q23 and **(ii)** the expansion of the operation in Mexico. As a result, we again observed higher sequential growth of the Credit Card portfolio, at +12.8% q/q vs. 8.5% q/q in 1Q23.

Alert on NPL < 90 days. For the first time in 12M, Mercado Libre reported an acceleration in the percentage of the portfolio in default for less than 90 days, reaching 9.9% (vs. 9.5% in 1Q23 vs. 10.3% in 4Q22). We understand that this reversal was due to the pickup in the In-store Merchant portfolio, a segment considered riskier due to the low level of data available on the behavior of these users to make an appropriate scoring.

In our view, the reversal of the positive trajectory of this indicator is a warning. Normally, there is a transitory effect of default linked to the proceedings between the first half of the year and the last quarter of the previous year. This is due to festive dates, seasonally stronger for retail, being positioned at the end of the quarter, such as Christmas. Thus, part of the installments, diluted in the constitution of the portfolio with maturities in subsequent months, are sometimes more exposed to a greater propensity of default. The increase of +4bps t/t may have occurred in the face of this mismatch, however, we believe that the 1Qs of each year are usually the most affected, suggesting that the advance in 2Q23 may have occurred in the face of a slight worsening in new cohorts, especially for In-store Merchant.

To avoid pressures on the vertical's profitability and maintain a sustainable growth of credit operations, we believe that delinquency should remain a point of attention, especially at a time when the Company is starting to re-ramp its credit card operation. Since we started our coverage, this indicator is the one we have been watching most closely and we will remain vigilant about NPL progress.

On the other hand, NPL>90 is still on a good downward trend. The better performance of the new cohorts was able to reduce the negative effects of portfolio aging on NPL > 90. Thus, the indicator stood at 25.1% vs. 28.2% in 1Q23, continuing on a downward trajectory.

Even so, if delinquency < 90 days continues to deteriorate, we understand that we would naturally tend to see new pressures on the over-90 default due to the aging effect of the portfolio. Considering the new card operation in Mexico and the acceleration of card issuance in Brazil, we believe the Company should continue to maintain a cautious stance on originations to avoid reversing the positive trajectory of the indicator.

Table 3. Credit Portfolio (2Q23 vs. Genial Est.)

	2Q23A	2T23E		2Q22A		1Q23A	
[USD m]	Reported	Genial Est.	% R/E | bps	Reported	% y/y | bps	Reported	% q/q | bps
Total Credit Portfolio	**3.250**	**3.262**	**-0,4%**	**2.687**	**21,0%**	**3.049**	**6,6%**
On-line Merchant	429	432	-0,7%	414	3,6%	413	3,9%
In-store Merchant	278	257	8,2%	276	0,7%	260	6,9%
Consumer	1.795	1.858	-3,4%	1.472	21,9%	1.713	4,8%
Credit Cards	748	720	3,8%	525	42,5%	663	12,8%

Source: Genial Investimentos, Mercado Libre.

Fintech

Fintech Take-Rate down by -45bps y/y. The Fintech take-rate stood at 3.52% (-45bps y/y; -21bps q/q), pressured by **(i)** the slower pace of expansion of the credit business compared to last year and **(ii)** the slight retraction of the Fintech take-rate ex-credit, due to the adoption of more competitive MDR rates given the change in the Merchants mix, as we commented throughout this report as well as in the preview report.

We expect NPLs to continue to cool it off. In 1Q23, NPL > 90 days decelerated for the first time in four consecutive quarters. We assess that the more conservative positioning adopted over the last few quarters, which naturally lowered NPL < 90 through the increased focus on low-risk cohorts, also helped cushion the impacts on NPL > 90, from which we expect to see a further improvement in performance in 2Q23. Still, as we have mentioned throughout the report, this remains an indicator that we look with great attention upon release of the results.

Monthly FIDC monitoring data in Brazil point in the direction of our estimate, also showing improvements in the NPL < 90 performance trend. The percentage of representativeness under the portfolio has gradually settled down, adjusting to a reality of a more troubled scenario for the granting of credit vis-à-vis the client profile that the fintech niche attacks. We see NPL < 90 falling to 9.5% in 1Q23 vs. 10.3% in 4Q22 and 13.1% in 3Q22. We estimate an improvement in the total percentage of the portfolio bad debt, reaching 36.3% Genial Est. vs. 37.8% in 1Q23.

Table 3. Credit Portfolio (2Q23 vs. Genial Est.)

	2Q23E	2Q22A		1Q23A	
[USD m]	Genial Est.	Reported	% y/y | bps	Reported	% q/q | bps
Total Credit Portfolio	**3.262**	**2.687**	**21,4%**	**3.049**	**7,0%**
On-line Merchant	432	414	4,4%	413	4,7%
In-store Merchant	257	276	-6,9%	260	-1,2%
Consumer	1.858	1.472	26,2%	1.713	8,4%
Credit Cards	720	525	37,2%	663	8,7%

Source: Genial Investimentos, Mercado Libre.

Fintech Take-Rate (inc. Credit) to retract y/y. On a year-on-year basis, we believe the slower pace of expansion of the credit business compared to last year, coupled with the slight retraction of the Fintech Take-rate ex-credit, should generate a y/y pressure on the vertical's total Take-rate. We project a Fintech Take-Rate of 3.64% Est. Genial (-32bps y/y; -9bps q/q).

Revenue growth pace impacted by credit operation slowdown. Consolidating Mercado Pago + Mercado Credito operations, we project Fintech net revenue at US$1.5bn Genial Est. (+25.3% y/y; +9.9% q/q). Considering the lower expansion of credit operations in recent quarters, the pace of growth should continue on a decelerating path already observed in previous quarters (40% y/y 1Q23 vs. 75% y/y 4Q22).

Still, we do not see this deceleration as negative. We believe that, in order to maintain the growth rate previously reported, a more aggressive acceleration of the loan portfolio would be necessary, which we believe is unsustainable in terms of defaults rates, given the current macroeconomic scenario.

Fintech Revenue growth of 24% y/y. Consolidating Mercado Pago + Mercado Credito dynamics, Fintech net revenue was US$1.5bn (+24.0% y/y; +8.7% q/q), quite close to what we projected (-1.1% vs. Genial Est.). As expected, the growth pace continues to decelerate (24% y/y vs. 40% y/y in 1Q23 vs. 75% y/y vs. in 4Q22), due to lower expansions of the credit business compared to the expressive levels reported in 2022.

We do not see this slowdown as negative. In our view, to maintain the previously reported growth rate, a more aggressive expansion of the credit portfolio would be required, which we do not think is sustainable in terms of delinquency, given the current macroeconomic scenario.

Consolidated

Table 4. Key Operationals (2Q23E vs. Reported)

	2Q23A	2Q23E		2Q22A		1Q23A	
[USD m]	Reported	Genial Est.	% R/E | bps	Reported	% y/y | bps	Reported	% q/q | bps
Total GMV	**10.506**	**10.112**	**3,9%**	**8.551**	**22,9%**	**9.434**	**11,4%**
% Commerce Take Rate	18,4%	18,0%	+40bps	16,4%	+200bps	17,8%	+60bps
Commerce Net Revenue	**1.936**	**1.820**	**6,4%**	**1.404**	**37,9%**	**1.676**	**15,5%**
Total TPV	**42.064**	**41.595**	**1,1%**	**30.194**	**39,3%**	**36.986**	**13,7%**
% Fintech Take Rate	3,52%	3,64%	-12bps	3,97%	-45bps	3,73%	-21bps
Fintech Net Revenue	**1.479**	**1.495**	**-1,1%**	**1.193**	**24,0%**	**1.361**	**8,7%**
Total Net Revenue	**3.415**	**3.315**	**3,0%**	**2.597**	**31,5%**	**3.037**	**12,5%**

Source: Genial Investimentos, Mercado Libre.

Consolidated net revenue growth above expectations (+3.0% vs. Genial Est.). Mercado Libre posted another quarter of strong growth (31.5% y/y; 12.5% q/q), reaching a consolidated net revenue of US$3.4bn In the e-commerce vertical, the company posted 37.9% y/y growth, driven by the performance of Mexico and Brazil. In the Fintech vertical, we saw a 37.9% y/y increase in net revenue (+6.4% vs. Genial Est.).

COGS slightly above expectations (+2.5% vs. Genial Est.), driven by logistics costs. Mercado Libre reported a COGS of US$1.7bn (29.1% y/y; 12.9% q/q). As mentioned in the preview, we already expected an increase due to the impact of the new logistics investments aimed at increasing the fulfillment footprint, but the intensity was higher than our estimates. Another relevant point that negatively impacted the company's COGS was the increase in funding costs. Our projection indicated a q/q increase of +3.5% Genial Est., however, although the Company does not disclose this type of information, we believe that due to the dynamics of interest rates that act in the increase in the cost of funding, the rise in the FIDC & SPEs line within COGS was potentially higher than our estimates.

Gross margin expansion (+92bps y/y), due to cost dilution. Even with the increase in COGS, the company managed to present a revenue growth above the cost growth (Net revenue +31.5% y/y vs. COGS +29.1% y/y), reaching a gross margin of 50.4% (+26 bps vs. Genial Est.).

SG&A better than expected, due to efficiency gains (-9.2% vs. Genial Est.). Mercado Libre reported an SG&A of -US$1.2bn (+12.4% y/y; -2.8% q/q), -9.2% below our expectations. We already expected efficiency gains in SG&A lines, as mentioned in the preview, but we overestimated three expense categories: **(i)** R&D; **(ii**) Sales & Marketing; **(iii)** PDA.

R&D comes as a surprise, with lower-than-expected impact from investments and hiring. The company reported R&D of -US$368mn (+40.5% y/y; -3.4% q/q). We had expected that the company would continue at a high pace of hiring and investments in product development, as presented in the last quarters, so we estimated it at 10.8% above the reported figure. Still, we observed an increase of +69bps y/y in the representativeness of this line in relation to revenue.

Selling and marketing expenses remain constant in the sequential view. The Company reported a selling expense of -US$383mn (+29.4% y/y; +0.0% q/q), consolidating a y/y reduction in its representativeness in relation to revenue (-18bps y/y) and maintaining a flat level q/q. This expense line came in -7.9% vs. Genial Est.

PDA shows a slowdown above expectations. As mentioned in our preview, we already expected an improvement due to a higher quality of the new cohorts. However, our estimates pointed to a slightly slower deceleration of this line, given the gradual resumption of credit operations, which only started last quarter. Thus, provision expenses came in below our estimates, totaling 6.8% of the total portfolio (vs. 8.0% Genial Est.), reaching -US$222mn (-26.7% y/y; -11.9% q/q).

As the NPL <90 days came in higher than we expected, a PDA expense below estimates remains as a point of attention. We believe that the slowdown in this line has to occur in a very prudent manner, so that the Company is able to calibrate the aging effect of the overdue installments in the credit portfolio with the PDA. When there is a mismatch between the two, the cost ends up being higher ahead, as the evolution of overdue installments moves towards write-off, the probability that these installments will be paid off decreases considerably. The PDA serves as a cushion to dampen the mastering of these losses. This mismatch did not occur excessively in 2Q23, and as it was below 90 days, it is difficult to say whether the new cohorts will prove potentially damaging, so we still see the situation at levels that are still contained.

Dilution of expenses leads to strong profitability gain. With a higher-than-expected expense dilution, Mercado Libre delivered an operational performance beating both our expectations and the market. EBIT margin was at 16.3% (+671bps yoy) vs. 11.5% Genial Est. vs. 11.3% Consensus, also driven by the gross margin gain in the quarter.

FX losses still impact the bottom line. Even with a solid topline performance allowing strong operating profitability gains, we still see this positive effect being partially offset by the level of FX losses in the quarter.

Mainly impacted by the macroeconomic situation in Argentina, we see FX losses 2x higher year-on-year, so as not to translate the full effect of the operating margin gain on the Company's net margin.

Still, profit grows +113% y/y. Despite this effect, Mercado Libre posted a 113.0% y/y bottom line expansion, reported at US$262mn (+113.0% y/y; +30.6% q/q). The profitability increase came on both +12.2% y/y vs. Genial Est. on the nominal number, and +62bps of margin expansion above our estimates. Consolidating an excellent bottom line result.

Table 5. Income Statement (2Q23 vs. Genial Est.)

	2Q23A	2T23E		2Q22A		1Q23A	
[USD m]	Reported	Genial Est.	% R/E | bps	Reported	% y/y | bps	Reported	% q/q | bps
Total Net Revenue	**3.415**	**3.315**	**3,0%**	**2.597**	**31,5%**	**3.037**	**12,5%**
E-commerce	1.936	1.820	6,4%	1.404	37,9%	1.676	15,5%
Fintech	1.479	1.495	-1,1%	1.193	24,0%	1.361	8,7%
(-) COGS	(1.695)	(1.654)	2,5%	(1.313)	29,1%	(1.501)	12,9%
Gross Profit	1.720	1.661	3,6%	1.284	**34,0%**	1.536	**12,0%**
% Gross Margin	50,4%	50,1%	+26bps	49,4%	+92bps	50,6%	-20bps
(-) SG&A	(1.162)	(1.280)	-9,2%	(1.034)	12,4%	(1.196)	-2,8%
EBIT	**558**	**381**	**46,4%**	**250**	**123,2%**	**340**	**64,3%**
% EBIT Margin	16,3%	11,5%	+484bps	9,6%	+671bps	11,2%	+516bps
Net Profit	**262**	**234**	**12,2%**	**123**	**113,0%**	**201**	**30,6%**
% Net Margin	7,7%	7,0%	+62bps	4,7%	+294bps	6,6%	+107bps

Source: Genial Investimentos, Mercado Libre.

Our Take on Mercado Libre

Without any surprise, Mercado Libre presents yet another result above our high expectations. As we have emphasized since the beginning of our coverage, the resilience and robustness of the numbers presented repeatedly reinforce the excellence in the Company's delivery capacity. With another market share gain in the Brazil operation, Mercado Libre reiterates its solid position as the leader of Brazilian e-commerce ahead of local competitors. For us, Mexico was the country that was going to drive the most growth, and that is exactly how it is turning out to be. Operations in the country are expanding exponentially, posting strong numbers in 2Q23 across all verticals of operation. Then, for the first time, **we saw Mexico overtake Argentina to become the second most important region in terms of GMV** after marking a +52.0% y/y delivery, **being the highlight of the quarter**.

With a user-friendly e-commerce ecosystem, speed of delivery and great customer experience, we saw Mercado Libre grow its Unique MELI Active Users by 28.8% y/y - signaling that despite more challenging consumer trends in a still difficult macroeconomic environment, the Company performs well and grows its digital environment.

Within Fintech, we already expected a **contraction of the Fintech Take Rate**, as mentioned in our preview, due to (i) softer credit portfolio growth compared to the sequencing run between 1H21 and 1H22; and (ii) competitive strategy within the acquiring market given the up-market movement to SMB. However, we do not see such cooling as negative, given that it shows the Company's prudence in credit origination for the Mercado Crédito vertical and signals its competitive ambitions to take share from Mercado Pago, in a much more competitive category, with more experienced players.

In our last report, we mentioned our sense of caution on the Argentina operation, reducing our estimates due to the level of complexity and lack of visibility on the country's macroeconomic scenario. Nevertheless, we still stand by our view where the market has overestimated such impacts.

Default remains as the only mixed signal. However, the situation remains under control. In default, we have always been attentive to the NPL indicators in order to monitor the Company's provision conditions (PDA). As a result, we observed NPL > 90, following a healthy downward trajectory vs. past quarters, which is positive. However, NPL < 90 grew for the first time LTM to 9.9% vs. 9.5% in 1Q23, triggering our alert on aging up to 90 days and, with this, may bring an unfavorable carry for NPL > 90, reflecting negatively on the Company's provisions.

As NPL <90 days was higher than expected, therefore, the lower-than-estimated PDA level remains as an additional concern. We believe that a proper calibration is needed between past due tranches in the loan portfolio and PDA. Mismatches between these two factors could result in high costs in the future, especially when past due installments start moving downwards in the portfolio. While there was no major mismatch in 2Q23, it is challenging to predict the impact of new cohorts, precisely because the maturity of the portfolio is short, and they are still very young. Although the dynamics raise our concern, the situation is currently under control.

As in a gala ball, Mercado Livre in yet another prestigious demonstration showed its power to deliver above the market's high expectations. What surprised us most was the operational delivery at EBIT levels, with a figure 46.4% and 49.2% beyond us and consensus, respectively. With an **EV/EBIT multiple of 39.7x for 2023E** and **25.7x in 2024E**, in which we believe Mercado Libre's track record of excellence justifies the premium embedded on its shares, characterizing them as still relatively discounted in our view. That said, **we reiterate our BUY recommendation**, with **12M MELI (Nasdaq) Target Price at US$1,520** and **MELI34 (B3) BRDs at R$60.00**, representing an **upside of 30.49%.**

Appendix: Mercado Libre

Figure 1. Mercado Libre – Income Statement in US$ Millions (Genial Est. 2023-2028)

Preview [USD mn]	2023E	2024E	2025E	2026E	2027E	2028E
Income Statement						
Net Operating Revenue	**12.884**	**16.431**	**19.979**	**25.615**	**28.592**	**32.287**
(-) COGS	(5.947)	(7.386)	(8.732)	(10.945)	(12.375)	(14.045)
Gross Profit	**6.937**	**9.046**	**11.247**	**14.670**	**16.218**	**18.243**
(-) Expenditures	(4.971)	(6.122)	(6.865)	(8.412)	(9.429)	(10.669)
EBITDA	**1.966**	**2.924**	**4.382**	**6.258**	**6.789**	**7.574**
D&A	(493)	(648)	(837)	(964)	(968)	(1.141)
EBIT	**1.473**	**2.276**	**3.545**	**5.294**	**5.821**	**6.433**
Financial Results	234	481	644	626	480	809
EBT	**1.380**	**2.829**	**4.083**	**6.105**	**6.488**	**7.560**
(-) Taxes	(527)	(1.080)	(1.559)	(2.330)	(2.476)	(2.886)
Net Profit	**853**	**1.749**	**2.525**	**3.775**	**4.011**	**4.674**
Rate of Return						
Net Margin (%)	6,62%	10,64%	12,64%	14,74%	14,03%	14,48%

Figure 2. Mercado Libre – Cash Flow in US$ Million (Genial Est. 2023-2028)

Discounted Cash Flow (DCF)	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E
Net Revenue	**12.884**	**16.431**	**19.979**	**25.615**	**28.592**	**32.287**	**35.948**	**40.190**	**45.428**
COGS	(10.918)	(13.508)	(15.597)	(19.358)	(21.803)	(24.714)	(27.523)	(30.744)	(34.574)
EBITDA Adj.	**1.966**	**2.924**	**4.382**	**6.258**	**6.789**	**7.574**	**8.426**	**9.446**	**10.854**
(+) Provision Expenses	1.079	1.287	992	871	1.023	1.125	1.210	1.285	1.362
(-) Taxes	(527)	(1.080)	(1.559)	(2.330)	(2.476)	(2.886)	(3.155)	(3.782)	(4.426)
(+/-) Δ WK	170	598	501	1.092	298	467	303	364	513
(-) Capex	(679)	(1.182)	(1.237)	(1.313)	(1.465)	(1.654)	(1.842)	(2.059)	(2.328)
Unlevered FCFF	**2.010**	**2.546**	**3.079**	**4.578**	**4.169**	**4.626**	**4.941**	**5.253**	**5.976**

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	Definition	Coverage
Buy	Expected return above +10% in relation to the Company's sector average	**46%**
Neutral	Expected return between +10% and -10% relative to the Company's industry average	**44%**
Sell	Expected return below -10% in relation to the Company's sector average	**5%**
under Review	Under review	**5%**

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