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Coupang, Inc. (CPNG)

Q4 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Hello, everyone. My name is Krista and I will be your conference operator today. At this time, I would like to welcome everyone to the Coupang 2023 Fourth Quarter Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

Now, I'd like to turn the call over to Mike Parker, Vice President of Investor Relations. You may begin your conference.

Michael Parker

Vice President & Head-Investor Relations, Coupang, Inc.

Thanks, operator. Welcome, everyone, to Coupang's fourth quarter 2023 earnings conference call. I'm pleased to be joined on the call today by our Founder and CEO, Bom Kim; and our CFO, Gaurav Anand.

The following discussion, including responses to your questions, reflects management's views as of today's date only. We do not undertake any obligation to update or revise this information, except as required by law.

Certain statements made on today's call include forward-looking statements. Actual results may differ materially. Additional information about factors that could potentially impact our financial results is included in today's press release and in our filings with the SEC, including our most recent Annual Report on Form 10-K and subsequent filings.

During today's call, we may present both GAAP and non-GAAP financial measures. Additional disclosures regarding these non-GAAP measures, including reconciliations to these measures to the most comparable GAAP

measures, are included in our earnings release, our slides accompanying this webcast and our SEC filings, which are posted on the company's Investor Relations website.

And now, I'll turn the call over to Bom.

Bom Kim

Founder, Chairman & Chief Executive Officer, Coupang, Inc.

Thanks, everyone, for joining us today. The fourth quarter of 2023 capped a year of accelerating growth, record profits and expanding free cash flows for our business. We believe that creating moments of wow for customers across selection, price and service formed the foundation for long-term growth, profitability, and ultimately, free cash flow, which serves as the basis of long-term shareholder value.

In 2023, our growth in both active customers and revenues accelerated every quarter. In Q1, we began the year with 5% year-over-year growth in active customers. In Q4, our active customers grew 16% year-over-year, and the spend of every annual customer cohort is growing over 15%, even our oldest cohorts.

In Q1, our revenues grew at 20% year-over-year on a constant currency basis. Apples-to-apples, without the FLC accounting change we made in Q2, our Q4 revenue growth rate would have been over 900 basis points higher than our Q1 growth rate of 20%. We also generated record net income and free cash flow for the year, thanks to the expanding profitability of Product Commerce, our largest and most established offering, whose adjusted EBITDA now exceeds 7% in Q4. We did all of this while only growing our share count by 1.3%. Our share dilution has remained at around 1% in each of the three years since we became a public company, including the year of our IPO.

And our free cash flow generation for 2023 totaled \$1.8 billion, even after investment of over \$450 million in our Developing Offerings. Our cash balance today stands at over \$5.5 billion. Sizable and durable free cash flow streams are not created overnight or even in a few quarters. Since the beginning of this company, we have made foundational bets on new competency initiatives. These are bold bets that required years of investment, persistence and patience before they began producing meaningful free cash flows for our business. They were attractive to us because we saw opportunities to break tradeoffs and deliver a wow experience to customers.

For example, Rocket Delivery was an entirely new competency. We had never purchased and managed inventory, opened fulfillment centers, assembled a nationwide logistics fleet or built bespoke technology to orchestrate one day delivery on our unique integrated network.

With the success of this new competency, we were able to add incremental initiatives that have expanded our impact, like Dawn Delivery. Today, we benefit from the success of the new competency initiatives we've scaled, and we have the ability now to seed and scale incremental initiatives, leveraging our vast technology, processes, scale and knowledge.

Our bar for investments remains incredibly high. We only invest when we have convictions that our opportunities can reach meaningful scale and deliver high returns on capital. We look for confirming evidence at each stage of investment. If they don't meet our high thresholds, we reduce or exit investments. And when we see strong signals, we're not shy about investing more.

A number of our investments are already showing remarkable progress and promise. One such incremental initiative is Fulfillment & Logistics by Coupang or FLC, for which we continue to make significant investment in

infrastructure and technology. Customers responded enthusiastically to expanding selection on Rocket. In Q4, our FLC volumes doubled year-over-year and the number of participating merchants in FLC jumped 80%.

Small and medium enterprises or SMEs, who do not have access to physical shelves in traditional retail and lack the capital to build their own technology and infrastructure, account for over 80% of our merchant base in FLC today. We're delighted to share with these enterprising small businesses access to billions of dollars of historical investment we've made in our Rocket network to help them delight customers and grow their businesses.

Another incremental investment that is proving its potential on growth, scale and impact is Taiwan. We're excited about the opportunity to challenge tradeoffs and wow customers in a geography with an attractive retail market. Since launching Rocket in October of 2022, Taiwan's customers and revenues have continued to compound at an incredible rate, more than doubling over the last two quarters alone. It's a pace of adoption and growth that exceeds what we experienced in Korea over the same period of time after the launch of Rocket.

In Taiwan, we're able to leverage the advanced technology, learnings and processes among other assets that we've developed over many years. We expect that to enable us to reach profitability in Taiwan faster than we did in Korea.

Many of our incremental investments benefit from our already strong customer cohort behavior. Our cohorts continuously expand their levels of spend across Coupang. With our new categories and offerings, we have the ability to further expand the spending and engagement potential of all of our customers.

Eats is a great example. Since we launched the WOW membership savings program in early Q2, we've seen our order volumes double. Every month, we've seen new adoption and strong retention of those new customers. And as we see one-time investments such as new merchant acquisition promotions expire, we expect Eats' positive underlying unit economics, along with scale, to drive cash generation in the future.

What is equally exciting is the positive externalities we've seen in customer engagement across our products and offerings. Just as purchasing in one category helped spur engagement in other categories, we've seen higher engagement on Eats lead to higher engagement in Product Commerce.

We also see this engagement pattern with Play, our video streaming service. Play was the most downloaded app in Korea in all categories on both iOS and Android in 2022 and 2023. It's also delighted customers by not just broadcasting, but creating from scratch unprecedented live sporting events in Korea. Some of the most streamed live sporting events over the past two years in Korea have been unique sports matches created and exclusively streamed by Play.

For the first time ever, millions were able to see Neymar, Haaland and Son play in Korea with international franchises like Manchester City, PSG and Tottenham Spurs. This spring, the Dodgers and Padres will open the regular season with two games in Seoul, for which tickets and live broadcasts in Korea will be available exclusively to WOW members. This will mark the first time the regular season MLB games have ever been played in Korea.

And last, a note about Farfetch. While we weren't seeking an acquisition, we came across a rare opportunity to buy a sector leading service with \$4 billion in GMV for a \$500 million investment. We hope in a few years, we'll be having the conversation about how Coupang turned Farfetch into a business that transformed the customer experience around luxury fashion while also providing strategic value for Coupang. It's too early for that conversation today.

Even if that full potential is not fully realized, we're highly confident that this will prove to be a prudent financial decision. We're already executing on a plan to make Farfetch self-funding with no additional investment beyond the announced capital commitment, and we see many paths to making this a worthwhile investment for shareholders.

And while we're excited about the long-term potential of such investments, we remain focused on our biggest priority. We have a very small share of the retail markets in Korea and Taiwan. Each of those opportunities are massive, and capturing them remains by far our greatest prospect and priority. As always, we remain committed to the relentless focus on wowing our customers to create a world where they wonder, how did I ever live without Coupang.

Now, I'll turn the call over to Gaurav to review the financials in more detail.

Gaurav Anand

Chief Financial Officer, Coupang, Inc.

Thanks, Bom. This quarter, we saw an even greater acceleration in customer engagement with a record 21 million active customers. The rate of active customer growth accelerated every quarter in 2023, culminating with 16% year-over-year growth in Q4. That's the highest growth rate we have seen in the past four years. We also now have 40 million WOW members, up 27% since last year, reflecting the broadening recognition of the tremendous value that WOW membership provides for our members.

Our total net revenues of \$6.6 billion grew 23% year-over-year or 20% in constant currency. Adjusted for the FLC impact, our growth would have been 940 basis points higher than the 20% constant currency revenue growth rate reported. Adjusting for this accounting change, constant currency revenue grew at an increasingly faster rate each successive quarter of 2023. The accounting adjustment is from the change in FLC accounting that we have highlighted earlier. It will continue to adversely affect our reported revenue growth rate for the next couple of quarters as they will comp against quarters with the previous accounting treatment.

It is important to highlight that the spend of every annual cohort grew over 15% year-over-year. Even our oldest cohorts continue to grow above that rate, demonstrating that there is still massive opportunity for us to continue to wow even our oldest customers with new selection at the best prices and a best-in-class delivery experience.

In addition, each successive annual cohort is starting with higher levels of spend and growing even faster. We saw a 3% increase in constant currency net revenues per active customer. While all our annual cohorts are growing over 15% year-over-year, our new active customers are naturally at much lower levels of spend than the mature cohorts.

The large number of new active customers we have added over the last few quarters has a short-term dilutive impact on the average spend per active customer. We believe a large amount of growth will continue to come from the spend of newer cohorts converging to the much higher spends of the older cohorts, whose spend levels also continue to climb.

In our Product Commerce segment, revenues grew 21% on a reported basis and 18% in constant currency. This growth is being driven by deeper spend penetration across many categories and offerings, higher spend levels per customer, and increasing adoption of our newer products and offerings. Our Product Commerce growth rate continues to compound at high multiples of the growth rate of total retail spend in Korea, which grew at 2% this

quarter. We believe we are in the very early stages of our growth journey in Korea, as Coupang currently represents a very small fraction of the projected \$560 billion of total commerce spend in Korea by 2027.

As Bom noted, we are also excited about the increasing momentum we are generating in Developing Offerings. Its segment revenue grew 105% year-over-year on a reported basis and 102% in constant currency. Along with other signals, this growth demonstrates a vast potential we are seeing from this portfolio of nascent initiatives, especially in Eats and Taiwan.

We delivered a record \$1.7 billion in gross profit, an increase of 32% year-over-year. This represents a gross profit margin offering 25.6%, improving 160 basis points year-over-year and 30 basis points quarter-over-quarter. We are driving higher efficiencies across our operations through improvements in our logistics network and greater utilization of automation and technology, including AI. We also continue to benefit from further optimization in our supply chain and the scaling of margin accretive offerings, including ads.

While these tailwinds were partially offset by the continued investment in selection expansion and increased investment in Developing Offerings this quarter, we see significant runway ahead of us to continue delivering margin expansion through each of these initiatives.

OG&A expense as a percentage of revenue increased 120 basis points this quarter versus last year. This change was due to an estimated 170 basis points negative impact from the FLC accounting change. This quarter, we recorded a non-recurring adjustment of \$895 million from changes in tax-related reserves, including the release of valuation allowances related to certain deferred tax assets from historical net operating losses. This resulted in an income tax net benefit of \$861 million for the quarter.

We generated net income of \$1 billion and diluted earnings per share of \$0.57, largely impacted by the \$895 million in tax reserve adjustments. This adjustment had a \$0.49 impact on diluted EPS. Removing the impact of one-time tax reserve adjustment, our diluted EPS for the quarter would have been \$0.08.

For our consolidated operations, we reported \$294 million of adjusted EBITDA this quarter and \$1.1 billion for the full year. The Q4 adjusted EBITDA margin was 4.5%, representing a 50-basis point improvement year-over-year, which includes a 40-basis point benefit from the FLC accounting change.

Our Product Commerce segment delivered \$444 million of adjusted EBITDA, an improvement of nearly 70% over the previous year. This resulted in a 7.1% margin, which expanded 190 basis points over the last year and includes a 60-basis point benefit from the FLC accounting change. The growth in margin was also driven by the expansion in gross profit margin this quarter, as well as improvements in efficiencies across our operations that we are harvesting from our many years of investments in infrastructure, technology and operational excellence. And we believe we are still in the early stages of realizing the full margin potential of the business. In our Developing Offerings segment, the adjusted EBITDA loss was \$150 million, increasing \$95 million year-over-year but decreasing \$10 million quarter-over-quarter.

We ended the year with roughly \$5.6 billion in cash, an improvement of more than 50% over last year. This was a result of producing \$2.7 billion in operating cash flow and \$1.8 billion of free cash flow for the full year. This is significantly higher than the \$1.1 billion of adjusted EBITDA this year due to some one-time and seasonal working capital benefits, among other factors. As we have previously communicated, we expect that over time, free cash flow on a TTM basis will be closer to the levels of adjusted EBITDA generated.

Now, a few comments on our outlook for 2024. While we are exiting 2023 with strong growth, we expect our growth rate going forward to be more consistent with the average growth rate we have seen over the past year. We anticipate incurring adjusted EBITDA losses in Developing Offerings of approximately \$650 million in 2024, excluding losses related to Farfetch. And as Bom noted, we do not anticipate incremental investment in Farfetch beyond our already communicated investments to get it to profitability. We continue to expect growing adjusted EBITDA margins on an annual basis, excluding Farfetch.

Due to the \$895 million taxes of adjustment we recorded this quarter, we anticipate we will experience a temporarily high effective tax rate between 45% to 50% in 2024. This is just an accounting effective tax rate, as we expect our cash tax obligation to be closer to 20% to 25%. Over the mid to long-term, we expect to normalize to an effective tax rate closer to 25%.

Bom and I are extremely proud of our teams, whose work over many years is responsible for the results we have enjoyed this past year. We are confident our teams will remain committed to execute with a passion for customer experience and operational excellence to deliver on the vast potential ahead.

Operator, we are now ready to begin the Q&A.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Stanley Yang with JPMorgan. Your line is open.

Stanley Yang

Analyst, JPMorgan Securities Far East Ltd. (South Korea)

Q

Thank you for the opportunity to ask questions. Congratulations on good result for fourth quarter. I have two questions. It's in regard to 2024 guidance. First question is about your Product Commerce strategy and the margin outlook. You have focused on selection increase and new merchant onboarding in 2023, which I think paid off in light of strong user and top line and the market share gains, but at the expense of the margin to a degree. Moving on to 2024, do you plan to maintain such selection increasing strategy? If so, do you expect the Product Commerce margin growth to sequentially soften into 2024?

My second question is about your Developing Offerings loss guidance of \$650 million. Is this inclusive of Farfetch deal? And I would appreciate if you provide a bit more color of the breakdown of each segment in terms of the Taiwan Eats and video. And when do you expect this developing often loss to peak out and start stabilizing or declining?

Bom Kim

Founder, Chairman & Chief Executive Officer, Coupang, Inc.

A

Hi, Stanley. Thank you for your questions. On our strategy to increase selection and merchant acquisition, the levers that we've been focused on – focusing on for growth remain the same. We do see some impact from our selection expansion, but we are expanding margins through improvements in our logistics network and greater utilization of automation, technology, including AI.

During 2023, we generated \$1.1 billion in adjusted EBITDA while increasing margins by 250 bps. Product Commerce adjusted EBITDA margin improved nearly 200 bps to 7.1%. As we stated in the past, margins may be

uneven quarter-to-quarter, but you should see our profit margins continue its march upwards over time, expanding on an annual basis, excluding Farfetch. And the improvements that we're driving come from years and years of investment in infrastructure, technology and operational excellence. We're seeing these efficiency improvements across our operations. The underlying drivers of margin are strong and there's still a lot of room for expansion.

On Developing Offerings, the \$650 million does not include Farfetch. We anticipate that the majority of the increase in these investments will be in Taiwan. Even with these investments, we expect to continue expanding our EBITDA margin on a consolidated basis, excluding Farfetch in 2024.

We continue to operate in line with the tenets we've shared in the past. We'll focus on opportunities where we can break tradeoffs and provide the best customer experience at the lowest cost. At each stage, we're evaluating with rigor and deciding which efforts demonstrate potential to achieve both meaningfully differentiated customer experience and significant future cash flows, and only these initiatives are earning their way to more significant investments.

We have in the past and we'll continue to discontinue investments that don't – do not demonstrate that potential to achieve these objectives. We are seeing positive signs in Taiwan, and where we see positive signals, we also won't be shy about investing more. As always, we'll continue to be disciplined and opportunistic to maximize long-term shareholder value.

Operator: Our next question comes from the line of Eric Cha with Goldman Sachs. Your line is open. Please ask your question.

Eric Cha

Analyst, Goldman Sachs (Asia) LLC (South Korea)

Q

Thank you for the opportunity to ask questions. I have two. First is on Farfetch and capital allocation. I know you said it's a bit too early, but can you share what was the biggest factor that appeared attractive to you to acquire Farfetch? And also, what would be your general principle regarding capital allocation, including share buybacks?

Second is on competition. There's a heightened interest in competition in the market. It seems related to the rise in Chinese cross-border e-commerce platforms. And when you look at your cohort behavior, do you see any impact on user attrition? And also, more importantly, do you see any impact on basket size among your cohorts related to this competition? Thank you.

Bom Kim

Founder, Chairman & Chief Executive Officer, Coupang, Inc.

A

Hi, Eric. Thanks for the question. Luxury is a very large market segment and it's one that hasn't been captured in any meaningful way by e-commerce players yet. We know marketplace. We know operations. We know how to focus on and drive innovation around customer experience. And we saw a business that we thought if it were better at those things, could be much more valuable, and if run differently, could create possibly billions of dollars of equity value. We also saw potential for strategic value for our existing Coupang business, but it's just too early to have a more in-depth conversation beyond that today.

M&A is not our strategy. I remind you that we weren't looking – we were not looking to do a deal. This was a very opportunistic situation. We're moving quickly afforded us the opportunity to buy Farfetch at a very attractive price. Our strategy remains growing organically, our very small share in our existing markets into much larger share

over time. We have so much opportunity in our existing markets for Coupang that our core strategy remains organic growth.

On your second question around competition, we continue to believe our success is determined primarily by our execution on improving customer experience and operational excellence. It's important to point out that we still have just single-digit share of the over \$560 billion projected retail market, just a massive opportunity in front of us. And the market is large enough to support many winners. Retail has been and continues to be dynamic and highly competitive, with many players ranging from traditional offline retailers to large Chinese competitors and a constant stream of new entrants, both domestic and international. Customers are always going to seek the best selection, the best price and the best service. And they have a lot of alternatives, whether down the street or across the border from China, a five-minute walk or a finger swipe away. So, we have to constantly find new moments of wow for our customers to fight for and earn their loyalty every day. That's what we spend all of our energy obsessing about.

We see the result of our efforts in our cohort behavior, where, as I mentioned earlier, every one of our cohorts is growing over 15%, even our oldest cohorts. Again, we still have just single-digit share of a massive retail market opportunity and we'll remain laser focused on customer experience and operational excellence to capture our share of that opportunity.

I'll point out one more time as well that we have a large – our newer cohorts are also joining at higher levels of spend and increasing spend faster than new customers in the past. And we've added a large number of new active customers over the last few quarters. That large mix of new customers portends a large amount of future growth, as the spend of newer cohorts converge to much higher levels of spend and the spend levels of the older cohorts also continue to climb, but that will be, of course, over a longer timeframe.

Operator: Your next question comes from the line of Se-Yon Park with Morgan Stanley. Your line is open.

Se-Yon Park

Analyst, Morgan Stanley & Co. International Plc (South Korea)

Hi. Thank you for the opportunity. I kind of just wanted to maybe follow-up on, I think it was a question that kind of Eric hinted on. But I mean, as you look at each quarter, I don't think over, I guess, the last two years, I don't think there's much doubt about execution. I think Bom, yourself and the company had done a tremendous job in terms of executing. I guess from an equity perspective, obviously, we kind of have an overhang with some of the sell-down that's coming from SoftBank and the like. So now that the company is in a much more comfortable position with respect to free cash flow, can you maybe just share your thoughts on how you're thinking about some kind of a way to address some of the share supply that continues to come to the market? Maybe it's not immediate. Maybe over the longer term, maybe how you're thinking about a potential share buyback or a tender to kind of address the supply, I think, would be very much helpful in understanding the equities. Thank you.

Gaurav Anand

Chief Financial Officer, Coupang, Inc.

Yeah, Se-Yon, I'll take that. Over the last year then before we went IPO, we have been working with our investors closely to find the optimal solution for everyone, for all shareholders, and we'll continue to do so. I think at this point, I think that's all we have to say on this. But that said, with [ph] other like (32:04) looking good, our profitability improving. We're excited about all the investment opportunities, we believe that will take care of itself.

Operator: Our next question comes from the line of James Lee with Mizuho. Your line is now open.

James Lee

Analyst, Mizuho Securities USA LLC

Q

Great. Thanks for taking my questions. I have two on Taiwan here. I was wondering if you guys can give more color on signals you guys saw in that market that gave you confidence to continue to lean in. And just curious, any learnings here that can help you adjust your execution tactically.

And secondly, on your guidance on EBITDA losses of \$650 million relating to Taiwan investment, can give a sense maybe, at the end of this year, what kind of investments on the ground should we visualize, should we get a sense of, including like selections, fulfillment center or even when it comes to local delivery? Thanks.

Bom Kim

Founder, Chairman & Chief Executive Officer, Coupang, Inc.

A

Hi, James. Thanks for your question. It's still early in Taiwan. We are seeing strong momentum there. As I mentioned, we launched Rocket in October of 2022 and growth there has been faster so far than it was in Korea. And in just the last two quarters alone, we've seen active customers and revenues double.

It's also worth noting that we are learning with every iteration, but we're also leveraging so much from what we've built over many years in Korea. Everything from our selection, processes and learnings, knowledge from building and optimizing fulfillment, logistics, supply chain optimization. The technology that we built over a decade, that's all contributing to our scaling faster in Taiwan. And we also expect that they will help us reach profitability there faster. I think it's still too early to have a long conversation, but we're very excited by the progress we're making and the promise we're seeing on the ground there.

I think that's – yeah. I think at the right time, we'll have a deeper conversation, but we'll be rigorous in our analysis, continue to assess at every stage and invest only in the opportunities, and when we believe that our investments will generate a meaningful differentiation of customer experience and meaningful returns for our shareholders.

Operator: [Operator Instructions] We will now take our last question from the line of Jiong Shao with Barclays. Your line is now open.

Jiong Shao

Analyst, Barclays Capital, Inc.

Q

Thank you very much for taking my questions. Congrats on the very strong results. I have two questions as well. First, sorry, I have to ask about Farfetch again. I understand you said you guys are ready to tell us a lot about it, but I was just wondering, would you be able to talk about sort of later on, how would you, accounting-wise, where do you book the revenues and expenses from Farfetch? And how big is Korea in today's Farfetch business? And what about the other countries they're in? Because Coupang is clearly only in Korea and Taiwan, not in these other countries. What – I mean, just broadly speaking, what are you going to do over there? And then on Farfetch, I think you said in your prepared remarks, if I'm not mistaken, I think you might have mentioned that the goal is for it to be self-funded. You are now going to spend your capital to kind of save the business, per se.

My second question is about the FLC or the accelerating growth for FLC, like you said, in the last few quarters, the growth for your FLC business is the delta, right, has been accelerating for the last few quarters since you changed the accounting. When your contracts all got to revise to the newer version by end of Q2, but you still see the growth accelerating in Q3 and Q4, I was just wondering what are the drivers you see behind that acceleration.

And then, any kind of outlook for that acceleration for the next quarter or two would be very helpful. Thank you so much.

Bom Kim

Founder, Chairman & Chief Executive Officer, Coupang, Inc.

A

So, let me address the FLC question first. First, our growth this quarter wasn't a reflection of any levers we pulled in this past quarter or specifically this past quarter or even recent quarters. It is – it really represents customer adoption of our investment over many years into providing the best experience at the lowest price across the broadest assortment. We are investing in growing our selection. And one of our initiatives is Farfetch – excuse me, FLC. And we believe our growth is a reflection of that customer response. We think the growth is, broadly speaking, a reflection of not only the investments that we've made, but also the stage that we're at in the market. We're still in the single-digit share of a \$560 billion retail market. It's – we're still very early and it is a massive opportunity. And there are tens of millions of shoppers who have yet to join our WOW membership. We are just at an early stage in our development and excited about the potential that we see ahead.

Gaurav Anand

Chief Financial Officer, Coupang, Inc.

A

On Farfetch, let me take that one. So we just finalized the deal a few weeks ago, and we are getting into the details. But on broad strokes, we will be consolidating it into our financials for a couple of months. On segment classification, we'll come back. We probably will take a one-time restructuring charge in Q1 and we'll split it out. But more to come on that in the next call.

Operator: There are no further questions. This concludes today's conference call. Thank you and you may now disconnect.

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