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Can Uber Ever Deliver? Part Ten: The Uber Death Watch Begins

Posted on [June 15, 2017](#) by [Yves Smith](#)

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

On June 13th Uber announced that its Board had accepted all of the management process recommendations of a study led by Eric Holder of the law firm Covington & Burling.^[1] Uber also announced that CEO Travis Kalanick would take a temporary leave of absence and that SVP Emil Michael, Kalanick's closest confidante, had been dismissed. The intent had been to turn the tide of highly negative stories on Uber since the beginning of the year.

Earlier installments in this Naked Capitalism series refrained from predicting Uber's future. However, given a business strategy that depended on achieving global industry dominance, the critical question was always : could Uber achieve that dominance before it burned through its massive \$13 billion war chest? Until recently it seems likely that it might, but recent events now strongly suggest that the answer may be no.

While Uber's finances are currently secure (in April it was reported to have roughly \$7 billion in cash on hand out of the \$13 billion originally provided by investors), it is increasingly difficult to see how Uber can survive in the longer term. For any company to rebound from a major crisis, it must have correctly identified its major problems and workable solutions, and installed strong, positive leadership that staff and other stakeholders can trust to navigate near term turmoil successfully. Uber has done none of these things.

For an immature company like Uber that has always been highly unprofitable to survive a crisis, it must have a clear, widely understood plan that will rapidly reverse the multi-billion dollar losses of recent years, as well as maintain the goodwill of customers, suppliers and outside industry observers through the turnaround process. Recent events have badly undermined goodwill. There is no evidence that Uber has a credible profit turnaround plan. None of the alternative strategic paths that one can imagine appear to have much chance of success.

Mature companies facing crises of culture and executive leadership usually have the cash flow and management depth that will give them the time needed to make major personnel and strategic changes. Uber does not have that time, as it has been burning through its cash for seven years, and its executive ranks have been decimated.

Before laying out Uber's existential crisis, let's quickly summarize recent events.

Uber has endured six months of intensively negative publicity that goes well beyond the sexual harassment issues that the Holder study was intended to address

A February 19th blog post by former Uber engineer Susan Fowler triggered the Holder report.^[2] Fowler described her own sexual harassment by senior Uber executives and argued that the Uber's refusal to take any action reflected a systemic toleration of sexual harassment.

But Uber has faced a huge range of other bad publicity this year, including a major lawsuit from Alphabet (Google) alleging that Uber conspired with a former employee of its Waymo driverless car unit to steal critical intellectual property, news that Uber developed software (Greyball) that was used to obstruct law enforcement efforts in Philadelphia and Portland to determine whether Uber was violating local laws, 2016 financial results showing negative EBITDAR contribution of \$2.8 billion (suggesting actual losses of over \$3 billion), reports that Uber software changes led to passenger overcharges and driver underpayments, reports that SVP Emil Michael tried to silence a woman who filed an HR complaint after a management dinner in Seoul led by Kalanick where escorts were provided for the male Uber executives in attendance, and video showing Kalanick verbally abusing an Uber driver who complained how he had been hurt by recent unilateral Uber compensation changes.

After Fowler's blog post appeared, a spate of news stories described a senior management culture that was highly insular and slavishly loyal to Kalanick. The New York Times said that Kalanick's inner circle, known as the "A-Team" internally, had been expunged of people who had not demonstrated their complete commitment to Kalanick's approach to competition and growth, described senior management as "a Hobbesian environment". It confirmed Fowler's observation that the A-team was "immune to internal scrutiny."^[3] A Financial Times story depicted senior management as "the cult of Travis."^[4] Uber's board has never exercised any independent oversight over management because Kalanick and two close friends (co-founder Garrett Camp and Ryan Graves, Uber's first employee) control 9 of the 11 board seats.

A spate of executive departures that have left Uber's management in serious disarray generated more bad publicity. In addition to this week's Kalanick and Michael moves, Uber had recently lost its President of Ridesharing (the nominal number 2 position), the CFO, the President of its Asia-Pacific operations, the EVP Engineering, the VPs of Public Policy/Communications, Product Growth and Mapping development and the Head of Driverless Car Development. Some of these were the dismissals of individuals who were PR liabilities in a post-Fowler world; others might be best characterized as "rats fleeing a sinking ship." Uber has been unable to fill its Chief Operating Officer position, which has been open since March, perhaps because of the lack of people who would be attracted to "a Hobbesian environment" at a company losing billions of dollars.

Uber's original whitewash plan has gone badly wrong

Uber's commissioning of the Holder study followed the standard crisis management playbook. It allowed the company to claim the review would be rigorous and independent, but Holder (and Covington & Burling) had done considerable work for Kalanick and Uber prior to the Fowler blogpost, so it wasn't really independent. Predictably, it was not seriously threatening either.

The review was narrowly limited to the discrimination and harassment charges in Fowler's blog post since Uber wanted to focus public attention to diversity and inclusion issues, not core governance issues or the possible causes of intellectual property theft, obstruction of justice, or profitability problems. Board member Arianna Huffington, a strong Kalanick ally, led the review. She gave multiple press interviews claiming the sexual harassment problem was limited and would soon be under control. "Yes, there were some bad apples, unquestionably. But this is not a systemic problem."^[5] Immediately prior to the planned June 6th public release of Holder's findings, Uber announced that 20 staff had been fired (none members of Kalanick's A-Team), that two women had been hired into management positions, and that a female Nestle executive would become an independent Board member. The Holder management process recommendations were entirely generic steps such as rethinking Uber's value statement, enhanced Board oversight, increased leadership training, reducing alcohol use at company events, and implementing a more formally structured complaint system.

On June 7th, Kara Swisher of Recode published a story revealing that Eric Alexander (Uber's President for Asia-Pacific and an A-Team member) had somehow obtained the records of a police investigation of a 2014 rape of a Uber passenger by an Uber driver in India, and those records were shared among Alexander, Kalanick and Michael for over a year.^[6] Those executives debated whether the evidence could be used to undermine the victim's testimony, and whether the incident had been concocted by a competing taxi company, although Uber eventually settled with the victim and accepted a six month ban from operating in Delhi. This information was apparently leaked to Swisher by an Uber employee who realized that the outside lawyers had not been provided (or ignored) this information. When Swisher contacted Uber to confirm the account, the release of the Holder study was suddenly postponed, and Uber quickly announced Alexander's dismissal.

A new Uber Board meeting was held on Sunday the 11th and lasted all day. Board members had only five days to rethink their plan, but realized that punishment for the rape documents would have to reach the top of the company. When those managers resisted, the Board increased pressure by leaking their demands to the press. Emil Michael was Kalanick's closest confidante and was considered the most powerful member of the A-team. In addition to his involvement with the Seoul escort and Indian rape incidents, he had led efforts in 2014 to intimidate Uber's strongest media critic by threatening to releasing information about her personal life. He had been in charge of Uber's disastrously failed attempt to enter the China market, but there were never negative repercussions because all of this was at Kalanick's direction.

Uber announced Michael's departure on Monday, but Bloomberg reported that "Michael believes that a weak board of directors, a lax internal legal team, coupled with his tight friendship with co-founder Kalanick, ultimately led to his downfall—not the scandals."^[7] There were apparently major disagreements among board members about sanctions on Kalanick. Uber announced his leave of absence Tuesday morning without disclosing its expected duration. There was also no explanation of how his responsibilities might change after he returns.

Recent events have badly undermined public goodwill towards Uber and the "narrative" explaining Uber's path to profitability is no longer credible

As discussed in parts eight and nine of this series, Uber's public goodwill depended in large measure upon a carefully developed PR/propaganda campaign designed to explain its inevitable success, and divert attention from the lack of evidence of profitability or competitiveness. Among other things, that narrative claimed Uber's global dominance would be driven by cutting edge technological innovations that were so powerful they could overwhelm incumbent competitors anywhere in the world and could eventually displace car ownership, that startup losses would soon give way to robust profits just like other technologically driven startups, that its meteoric growth was the result of consumers choosing their vastly superior services in competitive markets, and resistance to Uber's growth was entirely due to people fighting to preserve a status quo dominated by an Evil Taxi Cartel and corrupt regulators.

Until the events of this year, no one in the mainstream media bothered to scrutinize, much less question Uber's story. But enough doubts has been raised in the last couple years as to whether Uber was really an avatar of economic progress so that Fowler's description of a deeply flawed company was immediately and universally accepted. Last week's Indian rape revelations effectively killed the effort to convince outsiders that the company's only problem was a few bad actors who liked to hit on female staff and should similarly destroy any remaining perception that Uber management can be assumed to be wise or trustworthy.

It is not clear whether Uber will enjoy even a brief respite from its tsunami of negative publicity, as there may be further leaks of past bad behavior. In addition, court findings that Kalanick or other A-

Team members had actively conspired in the Google IP theft would be far more damaging than any of Fowler's statements.

Uber has no ability to earn profits within a competitive taxi industry

Uber could restore its credibility by presenting a convincing strategy to reverse its enormous losses. But no one at Uber has a credible plan and none of this week's actions move Uber closer to developing one.

As previous installments of the Naked Capitalism Uber series have documented in detail, Uber's real problem is that it is a staggeringly unprofitable company with fundamentally uncompetitive economics. It lost \$2 billion in 2015, \$3 billion in 2016, and another billion in China. It is a higher cost, less efficient producer of taxi service than traditional operators; all of its growth is explained by these multi-billion dollar subsidies as it has flooded markets with additional capacity offering unprofitably low fares.

It has none of the scale or network economies that allowed other startups to quickly grow into profitability. In its fifth year of operation Facebook had achieved 25% profit margins; in Uber's fifth year its profit margins were negative 149%. Absolute Uber losses have continued to worsen with recent growth. Margins improved somewhat in 2016, but only because Uber unilaterally reduced driver compensation by \$1 billion, leading to news reports of drivers sleeping in the cars in order to make ends meet. Uber never had any hope of profitability in a competitive market, even at its present scale.

Uber's original strategy for investor returns required global industry dominance but this may no longer be achievable

Travis Kalanick's goal was to build Uber into a globally dominant urban transport company. Its \$68 billion valuation reflects the hope that—once dominant—the ubiquity of the Uber platform and market power over passengers and suppliers would give it the kind of power Facebook and Amazon now enjoy. But those companies achieved quasi-monopoly power by inventing entirely new products that people hugely valued or by figuring out how to provide services massively more efficiently than any existing competitor could.

Uber's strategy was always to skip the hard "create real economic value" parts of this process, and focus strictly on the pursuit of artificial market power that global dominance would provide. As noted, Uber's \$13 billion investment base was used to fund the predatory competition needed to drive more efficient competitors out of business. This was 1600 times the investment funding Amazon needed prior to its IPO because Amazon could fund its growth out of positive cash flow. By contrast, Uber's carefully crafted "narrative" allowed it to pursue predatory competition for seven years without serious scrutiny of its financial results or whether its anticipated dominance would improve industry efficiency or consumer welfare.

Uber was always an all-or-nothing bet on achieving global dominance. A year or two ago few doubted that Uber would eventually achieve it. But its failure in China and serious pushback in many other overseas markets have effectively killed the "global" part, and the growing losses combined with all the other recent negative events may have killed the perception of inevitable dominance at home.

The Board's attempt to "fix" management culture cannot possibly work but will succeed in killing the culture that drove the company's growth

Kalanick's critical contribution was the creation of this tightly controlled, monomaniacal management culture willing to destroy anyone and anything standing in its way. The bad behavior that has been widely reported in 2017, such as theft of intellectual property and obstruction of justice, has existed over Uber's entire history. Earlier examples include willful lawbreaking, competitor sabotage, journalist intimidation, and willful falsehoods, including ones designed to deceive drivers about their actual compensation.

Kalanick's management culture, while repulsive on many levels, was actually brilliantly aligned with its business strategy and its investors' objectives. Companies that can make money in competitive markets by creating real economic value do not have to create ruthless, hyper-competitive cultures where there are no constraints on management behavior as long as they are totally loyal to the CEO's vision and can rapidly capture share from more efficient competitors. None of Uber's bad behavior was aberrant—it was a completely integral part of its business strategy. Without this culture, Uber would have never grown as rapidly as it has, and would have never had any hope of industry dominance.

The actions announced this week to reform Uber's culture will inevitably fail. Major cultural change in large companies is extraordinarily hard in the best of cases, and this may be one of the worst places to attempt it. The announced changes are based on the false presumption that the cultural "problem" is due to a few bad apples and is limited to diversity and inclusion type issues. They are also based on the false assumption that the company has solid cash flow and management resources that can keep the business strong while the areas affected by the toxic managers undergo some turmoil.

However, a longstanding culture where nothing is valued except the company's growth and everyone in senior management believes that the rules and norms do not apply to them, cannot be suddenly modified to incorporate values such as empathy, inclusiveness and respect for others. Kalanick's tight control of the Board and management ensured absolute focus on his strategic goals and approaches. The Board has weakened that control but has failed to replace it with any other means of ensuring strategic focus.

If the board somehow fosters cultural changes, or more likely, expends considerable energy in trying to do so, the focus on industry dominance will be lost. If they don't take hold, the drumbeat of negative publicity will continue and Uber will lose even more of its public support.

No one at Uber can answer the question of how they can reverse multi-billion dollar losses and become profitable because there is no good answer and all of Uber's potential paths forward are likely to fail

Uber's narrative that its powerful business model will inevitably achieve global dominance is no longer credible and can no longer divert public attention from Uber's dismal economics. If journalists or Uber staff ask Board members or senior managers to lay out the company's strategy and the how it will reverse multi-billion dollar losses, no one has any plausible answers. There are several hypothetical paths. While Uber has enough cash to pursue any of them for a while, none have any serious chance of success.

Uber's could stick with its original plan based for achieving investor returns, which was always based on exploiting market power once dominance was achieved. But no one can say this out loud, so it can't be used to motivate staff, or convince journalists that Uber has emerged from recent crises with strong, positive management that has abandoned the bad behavior of the past. And without ruthless focus and leadership it has virtually no chance of succeeding this way.

A new strategy based on limiting growth to “big but not dominant” in combination with some variety of cost cuts and price increases cannot possibly work given actual Uber economics. It is “big but not dominant” in many markets now yet the company is massively unprofitable. Driver compensation has already been cut to the bone. Many of Uber’s drivers are locked into expensive vehicle financing commitments and cannot quit tomorrow but the number of people willing to work on Uber’s terms is rapidly shrinking. Major capacity cuts and price increases cannot lead to profits. This would quickly kill the brand loyalty low fares had built and would accelerate negative press and the overall downward spiral.

Uber’s massive \$68 billion valuation is also a major obstacle going forward. Uber could hypothetically undertake a major restructuring, refocusing on a smaller set of markets but this would require a radical downsizing of the valuation and investor expectations. Uber’s investors have told themselves (and the rest of the world) that their investment in the taxicab industry would produce fabulous wealth, but never clearly explained where these huge returns would come from, or why no one else in taxicab history had ever discovered them. It will be interesting to see how these investors react once people start to ask whether that \$68 billion could completely disappear.

[1] Covington & Burling’s 13 page summary of its recommendations to the Uber Board are available at <https://drive.google.com/file/d/0B1s08BdVqCgrUVM4UHBpTGROLXM/view>. The law firm of Perkins & Cole conducted a linked review of individual sexual harassment claims

[2] Fowler, Susan J., *Reflecting On One Very, Very Strange Year at Uber*, 19 Feb 2017.

[3] Issac, Mike, *Inside Uber’s Aggressive, Unrestrained Workplace Culture*, New York Times, 22 Feb 2017.

[4] Hook, Leslie, *Uber: the crisis inside the ‘cult of Travis’*, Financial Times, 9 Mar 2017.

[5] O’Brien, Sara, *Arianna Huffington: Sexual harassment isn’t a ‘systemic problem’ at Uber*, CNNMoney, 23 Mar 2017.

[6] Swisher, Kara, *A top Uber executive, who obtained the medical records of a customer who was a rape victim, has been fired*, Recode, 7 Jun 2017.

[7] Newcomer, Eric & Stone, Brad, *Uber’s Michael Is Said to Blame Board, Not Behavior, for Ouster*, Bloomberg, 12 Jun 2017

<https://www.nakedcapitalism.com/2017/12/can-uber-ever-deliver-part-eleven-annual-uber-losses-now-approaching-5-billion.html>

Can Uber Ever Deliver? Part Eleven: Annual Uber Losses Now Approaching \$5 Billion

Posted on [December 12, 2017](#) by [Yves Smith](#)

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Previous Naked Capitalism Uber analysis now published as a law journal article

My Naked Capitalism series is the only (to my knowledge) analysis of Uber that assembled a complete picture of Uber's profitability over time from the various fragmentary press reports about financial results. It argued that all the available factual evidence about Uber's actual financial performance and competitive economics indicated that Uber's business model could never produce sustainable profits unless it was able to exploit significant anti-competitive market power. None of the contrary claims made by Uber supporters have been backed by any objective economic data. Most media coverage totally ignores the abysmal economics and as a result can't provide coherent explanations of Uber's recent scandals and governance battles.

The material that had originally been presented across ten NC posts is now available in a single article^[1] published in the Transportation Law Journal and available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2933177. The journal format allows for much more exhaustive documentation of evidence than internet posts, and makes it easier to demonstrate linkages between different aspects of the Uber story.

Newly released data affirm and strengthen my previous finding that Uber is hopelessly unprofitable

Since it is impossible to understand Uber's behavior without first understanding its actual financial performance, I have updated the data that was presented in Section II-A of the TLJ article and in several parts of this NC series.^[2]

On December 1st, Eric Newcomer of Bloomberg published a new batch of Uber financial data that had been included in a prospectus related to SoftBank's potential acquisition of Uber shares.^[3] The Uber historical P&L table below combines all available data and shows Uber full year results from 2012 to 2016; the estimated 2017 results are the actual 2nd/3rd quarter results reported by Newcomer multiplied by two.^[4] Uber has never challenged the accuracy of any of the P&L data that has appeared in the press.

The updated data demonstrates that Uber, in its eighth year of operations, continues to experience P&L losses that are staggering and still steadily growing. The data affirms that since there is no evidence of strong, ongoing profit improvement due to increasing efficiency or powerful scale/network economies, there is no basis for claiming that Uber can rapidly grow into profitability.

The data shows that while margin improvement occurred in 2015/16, it can be entirely explained by cuts in driver compensation unilaterally imposed by Uber, not by improved efficiency. New 2017 data strengthens the finding that the overall Uber business model (the combination of Uber and its nominally independent drivers) is not viable, and that all of Uber's growth to date is due to billions in predatory subsidies. Those unilateral driver compensation cuts still left Uber billions short of breakeven but threatened the rapid growth its valuation was based on; reversing the cuts restored volume growth but pushed annual losses towards \$5 billion.

Uber lost \$2.5 billion in 2015, probably lost \$4 billion in 2016, and is on track to lose \$5 billion in 2017.

The top line on the table below shows is total passenger payments, which must be split between Uber corporate and its drivers. Driver gross earnings are substantially higher than actual take home pay, as gross earning must cover all the expenses drivers bear, including fuel, vehicle ownership, insurance and maintenance.

Most of the "profit" data released by Uber over time and discussed in the press is not true GAAP (generally accepted accounting principles) profit comparable to the net income numbers public

companies publish but is EBIDTAR contribution. Companies have significant leeway as to how they calculate EBIDTAR (although it would exclude interest, taxes, depreciation, amortization) and the percentage of total costs excluded from EBIDTAR can vary significantly from quarter to quarter, given the impact of one-time expenses such as legal settlements and stock compensation. We only have true GAAP net profit results for 2014, 2015 and the 2nd/3rd quarters of 2017, but have EBIDTAR contribution numbers for all other periods.[\[5\]](#)

| <US\$millions> | 2012 | 2013 | 2014 | 2015 | 2016 | est2017 |
|---------------------------------|--------|-------|--------|---------|---------|---------|
| Total passenger payments | | 685 | 2,957 | 8,900 | 20,000 | 36,900 |
| Driver gross revenue | | | 2,462 | 6,890 | 13,550 | 29,560 |
| % pax fares retained by drivers | | | 83% | 77% | 68% | 80% |
| Uber Revenue | 16 | 104 | 495 | 2,010 | 6,450 | 7,340 |
| Uber Expense | 35 | 161 | 1,060 | 3,330 | 9,650 | 11,428 |
| EBIDTAR contribution | (20) | (57) | (585) | (1,330) | (3,200) | (4,088) |
| EBIDTAR margin | (126%) | (54%) | (118%) | (66%) | (50%) | (56%) |
| GAAP net income | | | (671) | (2,660) | | (5,040) |
| GAAP margin | | | (136%) | (132%) | | (69%) |

Uber had GAAP net income of negative \$2.6 billion in 2015, and a negative profit margin of 132%. This is consistent with the negative \$2.0 billion loss and (143%) margin for the year ending September 2015 presented in part one of the NC Uber series over a year ago.

No GAAP profit results for 2016 have been disclosed, but actual losses likely exceed \$4 billion given the EBIDTAR contribution of negative \$3.2 billion. Uber's GAAP losses for the 2nd and 3rd quarters of 2017 were over \$2.5 billion, suggesting annual losses of roughly \$5 billion.

While many Silicon Valley funded startups suffered large initial losses, none of them lost anything remotely close to \$2.6 billion in their sixth year of operation and then doubled their losses to \$5 billion in year eight. Reversing losses of this magnitude would require the greatest corporate financial turnaround in history.

No evidence of significant efficiency/scale gains; 2015 and 2016 margin improvements entirely explained by unilateral cuts in driver compensation, but losses soared when Uber had to reverse these cuts in 2017.

Total 2015 gross passenger payments were 200% higher than 2014, but Uber corporate revenue improved 300% because Uber cut the driver share of passenger revenue from 83% to 77%. This was an effective \$500 million wealth transfer from drivers to Uber's investors. These driver compensation cuts improved Uber's EBIDTAR margin, but Uber's P&L gains were wiped out by higher non-EBIDTAR expense. Thus the 300% Uber revenue growth did not result in any improvement in Uber profit margins.

In 2016, Uber unilaterally imposed much larger cuts in driver compensation, costing drivers an additional \$3 billion.[\[6\]](#) Prior to Uber's market entry, the take home pay of big-city cab drivers in the US was in the \$12-17/hour range, and these earnings were possible only if drivers worked 65-75 hours a week.

An independent study of the net earnings of Uber drivers (after accounting for the costs of the vehicles they had to provide) in Denver, Houston and Detroit in late 2015 (prior to Uber's big 2016

cuts) found that driver earnings had fallen to the \$10-13/hour range.^[7] Multiple recent news reports have documented how Uber drivers are increasingly unable to support themselves from their reduced share of passenger payments.^[8]

A business model where profit improvement is hugely dependent on wage cuts is unsustainable, especially when take home wages fall to (or below) minimum wage levels. Uber's primary focus has always been the rate of growth in gross passenger revenue, as this has been a major justification for its \$68 billion valuation. This growth rate came under enormous pressure in 2017 given Uber efforts to raise fares, major increases in driver turnover as wages fell, ^[9] and the avalanche of adverse publicity it was facing.

Since mass driver defections would cause passenger volume growth to collapse completely, Uber was forced to reverse these cuts in 2017 and increased the driver share from 68% to 80%. This meant that Uber's corporate revenue, which had grown over 300% in 2015 and over 200% in 2016 will probably only grow by about 15% in 2017.

If Uber had any ability to exploit the type of powerful efficiency and scale driven improvements that rapidly drove other tech companies towards sustainable profitability, one would see clear-cut evidence in this P&L table. There are undoubtedly a number of things Uber could do to reduce losses at the margin, but it is difficult to imagine it could suddenly find the \$4-5 billion in profit improvement needed merely to reach breakeven.

The P&L data illustrates why Uber cannot go public

Under Travis Kalanick, Uber had no interest in an IPO because he fully understood that the full financial disclosures required—including historical cash flows, balance sheets and much greater operational P&L detail—would expose Uber's abysmal economics, and destroy its PR narrative where powerful efficiencies would inevitably lead to success. Dara Khosrowshahi, under pressure from certain Board factions when he was first hired to replace Kalanick, promised an IPO by the end of 2019. This could be a disaster unless Uber somehow finds convincing evidence of profitable economics that it can put in the prospectus.

If Uber had accounting data that could demonstrate billions in efficiencies and a clear path to profits, they have ample incentive to share that data with reporters. Since they have not done that, it is reasonable to assume that evidence does not exist, and the additional data that would emerge during an IPO would actually strengthen the case that (in the absence of significant anti-competitive market power) Uber's business model can never produce sustainable profits.

^[1] Horan, Hubert, *Will the Growth of Uber Increase Economic Welfare?* 44 *Transp. L.J.*, 33-105 (2017)

^[2] That data, which had been leaked in dribs and drabs between August 2015 and April 2017, included the full years 2012-14, but only selected quarters in 2015 and 2016.

^[3] Newcomer, Eric, *Will Uber Ever Stop The Bleeding?*, Bloomberg, 1 Dec 2017. Softbank's tender offer is conditional on acquire a minimum of 14 percent of Uber shares at a price that would reflect a roughly 30% discount from Uber's last valuation. All publically available data is strictly limited to high level corporate P&L numbers; no balance sheet, cash flow or regional/product level reports have been released.

^[4] Data from the Softbank prospectus fills in the missing 2015 and 2016 data, and also provided results for the second and third quarter of 2017. There are some minor discrepancies between data

released at different points in time; the P&L table uses the most recently released data. Limited first quarter of 2017 data had been released in May, but the Uber revenue number was wildly higher than previous or subsequent quarters. Bensinger, Greg, *Uber Posts \$708 Million Loss as Finance Head Leaves*, Wall Street Journal, 1 Jun 2017

[5] Neither GAAP profit or EBIDTAR contribution includes expenses not directly related to current operations, such as long-term IT/market development costs, or expenses related to autonomous cars

[6] Given gross passenger payments of \$20.0 billion in 2016, driver compensation was reduced by \$3 billion due to Uber's unilateral decision to cut the driver's share from 83% (2014) to 68%

[7] See the TLJ article pp.46-49; the Denver/Detroit/Houston study is cited at note 37.

[8] One report cited the need for drivers to work marathon shifts focused on surge pricing periods. Masha Goncharova, *Ride-Hailing Drivers are Slaves to the Surge*, N.Y. Times (Jan. 12, 2017). Another report noted the increasing need for Uber drivers to actually sleep in their cars. Eric Newcomer & Olivia Zaleski, *When Their Shifts End, Uber Drivers Set up Camp in Parking Lots across the U.S.*, Bloomberg News (Jan. 23, 2017). A third report confirmed the marathon shifts and sleeping in cars, and compared Uber drivers to "migrant workers." See Carolyn Said, *Long-Distance Uber, Lyft Drivers' Crazy Commutes, Marathon Days, Big Paychecks*, S.F. Chronicle (Feb. 18, 2017).

[9] Observed driver turnover would have been even higher, but most Uber drivers are locked into vehicle financing arrangements, and thus have no short-term ability to move to other jobs.

<https://www.nakedcapitalism.com/2018/01/can-uber-ever-deliver-part-twelve-brad-stone-bloomberg-continue-get-uber-story-badly-wrong.html>

Can Uber Ever Deliver? Part Twelve: Brad Stone and Bloomberg Continue To Get the Uber Story Badly Wrong

Posted on [January 23, 2018](#) by [Yves Smith](#)

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Part Eight of this series^[1] documented the dreadful flaws in Brad Stone's major 2017 book on Uber, "The Upstarts."^[2] "The Upstarts" was not independent journalism. Stone acknowledged it was an explicit attempt to tell the story Uber wanted told, and described his efforts to convince Travis Kalanick that the book would help Uber tell its story. The central questions in the "The Upstarts" were "Did the benefits of their [Uber and Airbnb's] dominance outweigh the well-publicized drawbacks? What was their true impact on cities? Were they good for society or bad?" (p.243)

But few business books have ever gotten their story more completely wrong. "The Upstarts" valorized Travis Kalanick as the leader of a heroically innovative company that was "changing the world" just as an avalanche of stories about Uber's massive losses, dysfunctional management and corporate culture, systemic sexual harassment, intellectual property theft, obstruction of law enforcement and other endemic problems destroyed the credibility of Stone's narrative.

Stone, the senior executive editor for technology at Bloomberg News, has just published a Bloomberg BusinessWeek story entitled “The Fall of Travis Kalanick Was a Lot Weirder and Darker Than You Thought.”^[3] The central questions in “Weirder and Darker” were how did Uber suddenly change “from world’s most valuable startup to world’s most dysfunctional” and whether replacing Kalanick with Dara Khosrowshahi successfully solved Uber’s problems.

“Weirder and Darker” follows the exact same structure as “The Upstarts” and is equally flawed. Stone focused narrowly on the personalities of select insiders while ignoring all evidence about Uber’s economic and financial performance and the views of anyone outside Uber’s inner circle. He force fit his evidence into a pre-determined narrative designed to create a favorable emotional impression but never actually answered the questions he posed and gets important parts of the Uber story entirely wrong. And Stone never mentioned that “Weirder and Darker’s” portrayal of Kalanick and Uber is the polar opposite of what he’d published in “The Upstarts” last year.

Stone’s new Uber narrative is wildly inconsistent with the story he told last year

The narrative in “Weirder and Darker” is easy to summarize. Uber’s “melodrama began [o]n Jan. 27 [2017]” and grew from that point as a stream of negative publicity emerged^[4]. The underlying problems were Kalanick’s insistence “that the company had a public-relations problem, not a cultural one” and aspects of Kalanick’s personality (especially his “unrelenting combativeness”) that fueled Uber’s “absurdly bro-ish cultural values“, and alienated critical supporters such as Uber President Jeff Jones and Google Ventures (a major shareholder). Kalanick “embarked on a yearlong starring role as the villain who gets his comeuppance.”

Since “Kalanick was unable or unwilling to right himself” that comeuppance would be delivered by the Board, who hired former Attorney General Eric Holder to do an exhaustive review of Uber’s cultural problems (“We will leave no stones unturned. This company has one opportunity to get this right.”) and fired Kalanick after Holder delivered his report. New CEO Khosrowshahi’s personality makes him ideal to lead Uber into the future because he “was all that Kalanick wasn’t or couldn’t be: humble, a good listener, and a diplomat.” Khosrowshahi has already found a major capital infusion (from SoftBank) and is committed to taking the company public by October 2019.

Almost every element of Stone’s 2018 “Weirder and Darker” narrative contradicts his 2017 “Upstarts” narrative, yet Stone never acknowledges that his previous story is no longer operative. Kalanick’s “unrelenting combativeness” is now the root cause of Uber’s crises, but in “Upstarts” it was the driver of Uber’s great success and was perfectly suited to the marketplace challenges it faced (“The meeting thrust Kalanick into the thick of the familiar battle between new technology and the old, outdated ways of doing things” and the “powerful taxi interests” (p.122)). Kalanick’s hyper-aggressive, anti-diplomatic style was highly admirable (“Facts and intellectual arguments, not charm were his weapons, and he wasn’t about to kiss any political rings.” (p.191)). Kalanick’s willful refusal to obey existing laws is honorable because those obstacles would prevent Uber from “unlock[ing] the true potential of an on-demand transportation service.” (p.299).

The “absurdly bro-ish cultural values“ that Stone attacked in “Weirder and Darker” (and were formally opposed by the Board after its post-Fowler investigation), were glowingly described in “Upstarts” (pp.315-317). Stone pointed out the huge effort Kalanick had put in to articulating these values, noted how they culturally unified a rapidly growing company, emphasized that “many of Uber’s principles were comparable” to Amazon’s, and quoted senior staff saying that the rollout of the corporate values “was one of the most moving moments I had at Uber.”

“Upstarts” refutes the idea that Kalanick’s monomaniacal culture suddenly emerged as an issue on January 27, 2017; it had been clear to the Board from the earliest days of its operation. In 2010,

Kalanick said “I’ll stop at nothing to see Uber go to every major city in the US and the world” (p.123). By early 2011 he had “expelled from his inner circle anyone he thought might stand in the way of Uber’s manifest destiny to conquer the world.”(p.153).

In “Weirder and Darker,” Stone claims that Kalanick’s post January 27th 2017 missteps were horribly damaging and justified his dismissal, but when he documented the same type of missteps in “Upstarts” he insisted they were all minor issues that could be easily excused. In “Weirder and Darker,” Emil Michaels’ (Kalanick’s most important lieutenant) is emblematic of Uber’s cultural rot and senior staff are petitioning for his dismissal.

But in “Upstarts,” issues with Michaels are easily brushed aside. Stone briefly notes multiple public reports that Michaels led efforts to harass journalists skeptical of Uber, but then uncritically repeats Michaels’ false claim that all of these reports were fabrications. Stone expects readers to swallow the idea that Michaels had only wanted to “create a coalition for responsible journalism.” (p.262). After all, he had “a reputation of being effective, loyal and upbeat” (p.247). Stone glossed over false Uber claims that its drivers made over \$90,000 a year by suddenly focusing on how a Uber recruiter on Chicago’s South Side was creating wonderful opportunities for people short on cash.(p319-21). Uber burned over \$1 billion of its investors’ cash on its failed China venture, but Stone approvingly quotes Kalanick’s view that this effort was worthwhile because it was “romantic” and a chance to “do something interesting and beautiful” (p.329) and gives no indication that the China venture led to serious internal conflict.

Because Stone is trying to force-fit events into a simplistic narrative, he gets important parts of the Uber story badly wrong

Stone claim in “Weirder and Darker” that the shift “from “world’s most valuable startup” to “world’s most dysfunctional” is explained by major changes in Kalanick/Uber behavior first observed in early 2017 simply doesn’t hold water. The pre-2017 problems mentioned in “Upstarts” (journalist harassment, competitor sabotage, fabricated claims about driver pay, huge international losses) are every bit as problematic as profane tirades against drivers or mishandling the JFK taxi strike or the Trump business council. Much of the bad 2017 publicity (Greyball, tolerance of systemic sexual harassment) concerned longstanding patterns of bad behavior. Stone wants his readers to think major new problems had suddenly arisen since he wrote “Upstarts”, but neither Kalanick’s personality, nor Uber’s culture had actually changed.

Stone’s simplistic good guys/bad guys narrative falsely portrays the Board as responsible adults who suddenly discover major problems they’d never noticed before and then take the radical action needed to tackle these issues and put Uber back on a path to glory.

But Uber’s board had always been fully aware of these longstanding behavioral issues. Kalanick’s management style had been generating negative publicity since 2010 but it had also been generating staggering rates of growth and an unprecedented \$68 billion valuation, which they saw as an entirely satisfactory tradeoff. Thus the Board was always 100% complicit with the bad behavior that Uber’s culture produced, and (as Stone demonstrated in “Upstarts”) could always accept management’s claims that the bad publicity had been contrived by Uber’s enemies, or find other excuses for brushing it under the rug. The Board never uttered a single word critical of any management action in public until the post-Fowler public outrage could no longer be contained.

As noted, very little of the bad publicity Uber faced in early 2017 had any material impact on Uber’s financial performance, and none of it raised issues that were new or had dramatically worsened. But Stone’s narrative required major, new problems that would force the responsible adults on the Board to take radical action. But the triggering events in Stone’s story – things like the discovery that

subprime loan losses were worse than expected, and Kalanick's demand that Uber security search staff emails to identify the source of leaks — were also financially trivial and obviously do not answer Stone's question as to why the Board was suddenly motivated to violate the longstanding expectation that "Silicon Valley CEOs are supposed to be sacrosanct."

Stone's contrived narrative also means that he gets much of the story of Kalanick's actual dismissal wrong. Stone violates the chronology of his story and describes the release of the Eric Holder report, which occurred in mid-June, coincident with Kalanick's dismissal, in conjunction with events from March and April.

Stone's "no stone unturned" quotes deliberately misrepresents how Holder's investigation was actually conducted. The Board had narrowly limited the Holder investigation to the charges in Fowler's blogpost; other "cultural" and behavioral issues were out of scope. The original recommendations were limited to things like increased sensitivity training with no actions taken against Kalanick, Michaels or other senior executives close to Kalanick. The Holder review had been overseen by Board member Arianna Huffington, a strong Kalanick ally, who gave multiple press interviews claiming the sexual harassment problem was limited and would soon be under control. "Yes, there were some bad apples, unquestionably. But this is not [as Fowler had charged] a systemic problem."

The whitewash collapsed with the news that Kalanick and Michaels had obtained the confidential police records of the rape of a Uber passenger in New Delhi (also noted by Stone out of sequence). In the following seven days, the Holder report was hurriedly rewritten, and the Board had no alternative to firing Kalanick and Michaels.[\[5\]](#)

Stone's narrative misleads readers about the Board, which had been just as dysfunctional as senior management and heavily complicit in Uber's behavioral/cultural problems long before 2017. Huffington and Holder were trying to cover up serious problems instead of fixing them. They might have gotten away with it if the story of the rape victim's police file hadn't emerged. Arianna Huffington was resented not because she was trying to get Uber to hire her wellness company, as Stone claims, but because she had made herself into a central character in the Board's "Game of Thrones" dynamic, despite not being an actual investor and not having any actual expertise about Uber's business.

But just as the Board weren't really the responsible adult good guys in this story, Kalanick doesn't actually fit the simplistic, suddenly out-of-control bad guy role (the "villain who gets his comeuppance") Stone has assigned him.

Stone inaccurately describes Google Ventures as a close ally alienated by Kalanick's impulsive, hyper-aggressive 2017 push into driverless cars. As Stone himself described ("Upstarts" p.244-7), Google had decided to pursue driverless cars independent of Uber in 2013, and Kalanick (quite rationally) realized that future Google domination of robocars could eventually pose an existential threat to Uber. Kalanick did not remain closely in touch with Uber staff while on temporary leave as CEO because he "was unable or unwilling to right himself" as Stone insists, but because he was only on temporary leave at that point, he knew that no one else was actually in charge and because he was still a critically important Board member.

Benchmark did not suddenly decide to fight Kalanick because of subprime loan losses discovered in 2017. Benchmark's fight with Kalanick began much earlier over Uber's massive losses in China and Kalanick's ongoing refusal to consider the IPO Benchmark needed to realize actual returns. This was not a battle between good and evil; these were complex strategic issues where both sides had legitimate (but conflicting) concerns, but dysfunctional governance processes (that both sides had

contributed to) made compromise and resolution impossible. Khosrowshahi was not responsible for Softbank's recent stock purchases or the commitment to a 2019 IPO. Both had been engineered by Benchmark prior to Khosrowshahi's hiring as part of their campaign to limit Kalanick's control of the Board.

Stone wants his readers to believe that Uber's turmoil can be understood entirely on the basis of personalities, and that financial results had nothing to do with it

Although Stone totally changed the components of his account, the underlying narrative structure of "Upstarts" and "Weirder and Darker" are virtually identical. In both cases Stone's narrative is based exclusively on the words and actions of a handful of company insiders. In both cases Stone makes no attempt to provide input or perspective from drivers, local officials industry experts, or any other independent sources, or to put Uber's issues in the context of the experiences of any other comparable Silicon Valley funded startups.

Thus Stone's readers have no ability to evaluate whether Uber's problems are systemic or aberrant, deep-rooted or easily fixed, unique to Uber or common among startups. His readers have nothing to go on except for the sense they get of these personalities based on these limited quotes and descriptions. They can't tell whether insiders who seem likeable have covered up bad management decisions with self-serving assertions, or whether less likeable insiders have made good decisions that happen to have been difficult and unpopular.

In both cases Stone completely ignores profitability, cash flow, competitiveness or any other objective financial or economic evidence. In both cases Stone completely fails to answer the central questions he has posed because it is impossible to answer these questions without substantial economic evidence. Stone deliberately concealed information about Uber's massive losses from readers of "Upstarts" because a company that had failed to produce any economically sustainable efficiency or service advantages could not have possibly offset their drawbacks and problems and produced net benefits for society.

Similarly, by excluding financial/economic evidence, "Weirder and Darker" cannot elucidate how Uber suddenly changed "from "world's most valuable startup" to "world's most dysfunctional." Stone's efforts to account for this dramatic shift on the basis of the sudden deterioration of Kalanick's personality and the Board's sudden realization that they no longer liked the management practices that had driven Uber's huge growth and valuation cannot be taken seriously.

Stone underplays or ignores the many financial issues that Board members were actually concerned with, including the billions in ongoing losses (over \$10 billion in the last three years alone)[\[6\]](#), the Uber China debacle, the dubious investments in other businesses such as logistics and driverless cars, the threat of an extremely costly resolution to the Google lawsuit and Kalanick's refusal to focus on the IPO needed to provide its investors with actual returns.

The personalities and biases of key insiders can obviously influence major business decisions and competitive battles and news reports can usefully consider how those personalities can influence complex business issues at the margin. But Stone's approach absurdly assumes that the investors that put \$13 billion into Uber are totally driven by personality issues and pay little attention to things like profitability, cash flow or return on investment.

Stone's pieces are PR/propaganda, not journalism

Both "Upstarts" and "Weirder and Darker" follow the structural conventions of PR/propaganda, not journalism. Both assemble a set of events (and, I presume, quotes) that are factually accurate and

opinions that seem reasonable, that have been cherry-picked to fit a pre-determined narrative. All evidence inconsistent with that narrative has been excluded; including evidence published by Stone's colleagues at Bloomberg. That narrative presents a simple good guys versus bad guys type fight (heroic innovators fighting corrupt defenders of the taxi industry status quo, responsible Board members saving their company from a CEO who "was unable or unwilling to right himself") that misrepresents the actual complexity of events and conflicting interests.

These narratives are designed to force readers to respond on a purely emotional level and to see the triumph of the good guys as the only legitimate outcome. These narratives are constructed so that the narrator and his attempts to emotionally manipulate readers towards specific conclusions remain largely invisible. Absolutely no independently verifiable data relative to the battle is presented (e.g. Stone's complete refusal to present any Uber financial/economic data) that readers might use to pose questions that could undermine the story lines. They are structured as a complete package that will eliminate the need for further investigation, not the starting point for further discussion.

While the two pieces seem quite different on the surface — the story of the world's most valuable startup versus the story of the world's most dysfunctional startup — in both cases, Stone's objective was to construct the most positive pro-Uber narrative possible at that point in time. Stone was not working on behalf of his readers but on behalf of Uber's shareholders. Stone constructed "Upstarts" as a heroic innovation story, but constructed "Weirder and Darker" as a redemption story since Uber's bad behavior had become more widely known. Since propaganda pieces are self-contained, and not part of an ongoing public discussion, the fact that the evidence, logic and conclusions of the two pieces are wildly inconsistent can easily be overlooked.

In both cases, Stone's desire to write the most positive pro-Uber story possible meant preventing readers from understanding or thinking about Uber's actual business model, their actual competitive efficiencies and their actual financial performance.

If "Upstarts" had been grounded in economic evidence about the business model, readers would have quickly recognized that Uber's growth had been driven by massive subsidies not cutting-edge innovations, that Uber's investors had always been pursuing industry dominance and market power, and that a company unable to achieve sustainable profits in competitive markets could not possibly be seen as beneficial for society.

If "Weirder and Darker" had been grounded in economic evidence, readers would have quickly recognized that things like lawbreaking and toleration for systemic sexual harassment were inevitable byproducts of a business model that depended on Kalanick's monomaniacal, hyper-aggressive focus on growth at all costs, and that replacing Kalanick with someone who is "humble, a good listener, and a diplomat" will not reverse \$4-5 billion in annual losses within the next 18 months.^[7]

Any honest journalist who had attempted to tell these stories would have included outside voices and perspectives, and provided greater financial and industry context. There would be no pretense that definitive truth had been discovered, and the existence of conflicting evidence, complexities and viewpoints would not be deliberately withheld. An honest journalist might believe the available evidence supported a strongly pro-Uber conclusion but would clearly and openly state why they believed it was warranted and welcome outside scrutiny of that conclusion. Stone's reporting on Uber has consistently failed to meet these standards.

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Eric Newcomer, the Bloomberg reporter on the day-to-day Uber beat is listed as a co-author of “Weirder and Darker.” I have deliberately focused my criticisms on Stone (Newcomer’s boss) because what I see as the major flaws in the piece are completely consistent with “Upstarts” and other past pieces by Stone and are completely inconsistent with all of Newcomer’s Uber reporting. Like the other Uber beat reporters in the mainstream business press, Newcomer’s stories have never directly addressed the central economic questions (e.g. why is Uber still massively unprofitable, is Uber actually more efficient than traditional taxis, will cities be better off if Uber achieves the industry dominance it has been pursuing), but Newcomer’s reports have always been fundamentally fair and accurate. Newcomer broke a number of the stories about Uber’s actual losses, broke the story of Kalanick’s profane tirade against the Uber driver frustrated with its pricing policies, and (unlike his boss) has never presented Uber’s preferred framing of a story as “the story”. None of the information about Uber’s huge losses that Newcomer had published is mentioned anywhere in “Weirder and Darker” or anywhere in the 335 pages of “Upstarts.” Thus I have assumed that Newcomer shared the byline because he was the original source of some of the factual events included and I have assumed Stone is primarily (if not solely) responsible for how the story was actually written.

[1] <http://www.nakedcapitalism.com/2017/02/can-uber-ever-deliver-part-eight-brad-stones-uber-book-upstarts-prpropaganda-masquerading-journalism.html>

[2] Stone, Brad, *The Upstarts: How Uber, Airbnb, and the Killer Companies of the New Silicon Valley Are Changing the World*, Little, Brown 2017

[3] Stone, Brad & Newcomer, Eric, “The Fall of Travis Kalanick Was a Lot Weirder and Darker Than You Thought” *Bloomberg Business Week* 22 Jan 2018 (published online 18 Jan 2018)

[4] In the two months after January 27th this included Kalanick’s inept handling of his decision to join Donald Trump’s business advisory council Uber’s response to a taxi strike at Kennedy Airport, Susan Fowler’s blogpost documenting Uber’s tolerance of systemic sexual harassment, a video showing Kalanick’s profane response to a driver unhappy with changes to Uber’s pricing policies, the disclosure that Uber had used a system called Greyball to obstruct local law enforcement and Google’s lawsuit alleging Uber’s theft of its driverless car intellectual property.

[5] These events are described in greater detail in part ten of this series. <https://www.nakedcapitalism.com/2017/06/can-uber-ever-deliver-part-ten-uber-death-watch-begins.html>

[6] Part eleven of this series summarizes all of the currently available public data on Uber’s staggering losses through the 3rd quarter of 2017. <https://www.nakedcapitalism.com/2017/12/can-uber-ever-deliver-part-eleven-annual-uber-losses-now-approaching-5-billion.html>

[7] Uber’s economic problems are documented in detail in my journal article based on earlier parts of this Naked Capitalism series, *Will the Growth of Uber Increase Economic Welfare?* 44 *Transp. L.J.*, 33-105 (2017) Available for download at SSRN: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2933177

<https://www.nakedcapitalism.com/2018/02/can-uber-ever-deliver-part-thirteen-even-4q-cost-cuts-uber-lost-4-5-billion-2017.html>

Can Uber Ever Deliver? Part Thirteen: Even After 4Q Cost Cuts, Uber Lost \$4.5 Billion in 2017

Posted on [February 16, 2018](#) by [Yves Smith](#)

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Uber released new financial data this week, showing full year 2017 GAAP operating losses of \$4.5 billion, and an operating margin of negative 61%.

Uber's challenge is to get the business press to downplay or ignore its dismal financial results, and to present a narrative where these results demonstrate that Uber is making major progress. Although Uber has complete financial information, it only released detailed data for three quarters in 2017 and two quarters in 2016. Although much of the missing data can be filled in from earlier releases, Uber knew that reporters on deadline would not do that, and thus key changes over time would not be examined.

Uber's financial releases have never used consistent definitions of "losses," often using EBIDTAR or EBIT contributions instead of true GAAP Operating or Net Income. Stories about 2017 results would normally highlight comparisons with 2016, but because Uber has never supplied reporters with 2016 GAAP profit numbers, their stories did not mention that aggregate losses had continued to increase.

Every news report focused on the continued growth in top-line revenue. Most emphasized the major progress new Uber CEO Dara Khosrowshahi had made towards his goal of a 2019 IPO.

Only one news report, by Eric Newcomer of Bloomberg, highlighted the magnitude of total GAAP losses. Newcomer noted that "[t]here are few historical precedents for the scale of its loss" and explained "Uber prefers to use a different number to refer to its loss: \$2.2 billion." Newcomer recognizes that \$4.5 billion GAAP loss was the better indicator of Uber's current economic performance, but couldn't explain its superiority to his readers because Uber refused to identify the costs excluded from its preferred number.^[1]

The stories that highlighted Uber's preferred narrative had difficulty linking those claims to the financial numbers that had been released. Emir Efrati led off his story in The Information by saying "Uber is moving toward profitability" even though losses were actually increasing and then emphasized that "[t]he results suggest Uber is getting more efficient as it scales up, allowing it to improve profit margins"^[2] without any attempt to document evidence of meaningful scale economies.

The New York Times emphasized that the new numbers "reflect a steady improvement in the company's financial position, with revenues growing and losses narrowing" but never mentioned the \$4.5 billion annual loss (except to say that losses were "big").^[3] The Financial Times highlighted that "Improvements boost new chief Dara Khosrowshahi as he prepares to take company public" Its lead paragraph reported the smaller EBIDTAR contribution numbers as "losses;" did not mention actual GAAP losses until the end of the story, and made no attempt to explain why it had emphasized the smaller contribution numbers, or why Uber was emphasizing a "profit" measure that excluded \$2.3 billion in costs.^[4] None of the stories identified the actual magnitude of recent cost savings, or explained them in terms of the overall achievements that would be needed to reach breakeven.

Did Uber's 4th Quarter cost cuts reflect improved efficiency, or major progress towards profitability?

Uber did cut its costs in the 4th quarter, but a quick review of the reported data raises serious questions about the “Khosrowshahi making major progress towards profitability” narrative. As discussed at length previously, the issue is not whether a startup company might initially incur big losses, but whether its business model demonstrates the powerful scale or network economies that would steadily improve operating margins.^[5] The issue is not whether Uber has, and will continue to be able to show in its IPO documents how it can not only reverse \$4.5 billion in losses and achieve breakeven, but steadily grow profits for many years to come.

The table below shows quarter-to-quarter changes in revenues and operating expenses, based on the detailed data in Efrati's article.

| Quarterly % Increases | 3Q2016 vs 2Q | 3Q2017 vs 2Q | 4Q2017 vs 3Q |
|--------------------------|-----------------|-----------------|-----------------|
| Total Passenger Payments | 26% | 11% | 14% |
| Uber Revenue | 12% | 14% | 12% |
| Operating Insurance | 50% | 16% | 14% |
| Other Operating Expenses | 41% | 13% | (2%) |

Between the 2nd and 3rd quarter of 2016, Uber operating expenses rose 3-4 times faster than Uber's revenue (the portion of passenger payments that Uber retained). That is the polar opposite of what one would see if Uber had the kind of scale economies needed to “grow into profitability”. Between the 2nd and 3rd quarter of 2017, revenue growth rates had slowed but operating expenses were still growing just as fast. This represents an improvement over 2016, but unit costs were still not declining.

In the 4th quarter of 2017, Uber suddenly improved unit operating costs, but there is no reason to believe that Uber's underlying operating efficiency actually improved. In part eleven of this series,^[6] based on financial results through the 3rd quarter, I estimated a full year GAAP loss of roughly \$5 billion. After years of steady cost increases, Uber froze spending on Operations, Sales and Marketing, Research and Development, and General and Administration. Insurance, an entirely variable cost, continued to increase in line with revenue. 4th quarter costs would have been \$210-220 million higher (\$800-900 million annualized) if they had continued to grow in line with revenue. These are the kind of across-the-board budget cuts big companies frequently make to stem growing losses.

Perhaps this is an initial step in the right direction, but the budget freeze cannot be said to have seriously improved efficiency unless Uber can demonstrate that it can continue to produce 10-15% quarterly revenue growth on the frozen 3rd quarter 2017 cost base. And then Uber needs to find another \$4 billion in cuts..

Twitter just announced profit gains from similar (although larger scale) cost-cutting efforts, but press coverage was largely negative, noting that the cuts threatened the product and market development efforts critical to the long term survival of any rapidly growing technology-oriented company.^[7] But unlike Twitter, Uber is a younger, less-mature business that has not yet demonstrated the sustainability of its business model. Twitter's cost cuts actually produced GAAP profits. By contrast,

Uber needs to make another \$4 billion in cuts to reach breakeven. Twitter went public in 2013. If Uber wants to go public in 2019, it needs to be able to show that it is continuing to invest in future growth, and that rapid growth will continue to drive margin improvements for many years. Uber's attempt to cut costs in order to marginally reduce short-term losses directly undermines that narrative.

Is Uber artificially inflating its top-line revenue growth claims?

All previous releases of Uber revenue data were limited to the top-line "Gross passenger payments" (the total money paid by passengers) and "Uber revenue", the 20-30% of that total retained by Uber. In past analysis, I had assumed that the difference went almost entirely to drivers, but the newly released data shows this assumption is not true, and that Uber may be inflating the top-line revenue number.

In 2017, roughly \$3 billion^[8] of this revenue was "Refunds, Taxes and Fees" or "Rider Promotions." Government charges and fares that are refunded should not have been included in the original gross revenue number. The "Rider Promotions" item is more problematic.

If Uber offered discounts, the higher fare (that the passenger did not pay) appears to be included in gross revenue, while the promotional discount is a separate offset.^[9] These numbers do not affect bottom line P&L calculations, but inflating the top-line gross revenue number directly supports Uber's desire to show the strongest possible passenger demand numbers. Uber has steadfastly refused to release any numbers (such as market-specific fare and yield trends) that would meaningfully document whether (or where) its revenue performance might actually be improving.

Uber cut driver compensation by \$2.2 billion in 2017

The new data allows one to more precisely calculate recent Uber cuts in driver compensation. In the 2nd and 3rd quarter of 2016, 78% of gross passenger revenue went to "Driver earnings and bonuses." By the 3rd and 4th quarters of 2017, Uber had unilaterally imposed driver compensation cuts that reduced this to 72%. If the higher 2016 rates had remained in force, drivers would have gotten \$2.2 billion more in 2017, Uber's revenue would have been \$2.2 billion lower, and Uber's GAAP losses would have been much higher than \$4.5 billion.

It is perfectly reasonable for reporters to consider year-end financial results in the context of Uber's drive towards profitability and an IPO, but reporting on Uber has steadfastly ignored drivers (and the vehicles they provide) even though they are far and away the biggest component (85%) of what passengers are paying for.^[10] Uber still needs \$4.5 billion in profit improvement, but it is unclear that it has much scope to reduce driver compensation much further. Driver turnover has soared. There are growing anecdotal reports of drivers forced to sleep in their vehicles. Khosrowshahi has aggressively publicized efforts to repair relationships with its drivers. Unless Uber achieves quasi-monopoly control of taxi driver jobs, it is difficult to see how Uber can continue to take larger and larger shares of passenger fares.

Uber's narrative in 2018

Uber has always been a narrative-driven enterprise. Uber hopes that people overlook the fact that its previous narratives about Uber's powerful, cutting-edge technological innovations, and its unstoppable march to global industry domination have been exposed as nonsense.

Its current narrative seems to focus on three points; (1) everything bad you might have ever heard about Uber was entirely the fault of Travis Kalanick, and now that he's gone all those problems have

been completely solved; (2) Dara Khosrowshahi is already doing great things to restore the financial promise Uber always had; (3) the core business is still growing strongly and we are marching steadily towards profitability and a 2019 IPO.

As discussed at length in this series, Kalanick personally drove every aspect—good and bad—of Uber’s business model for eight years. Uber could not achieved its meteoric growth without the monomaniacal, hyper-aggressive culture Kalanick created. No one can explain how the bad behavior that culture spawned can be surgically removed from the rest of the business model, or how a less monomaniacal culture can rapidly fuel both strong growth and billions in profit improvement.

While it is too soon to judge his performance, Khosrowshahi has yet to say or do anything to suggest he actually has a plan that will successfully fuel many years of continued growth and the billions in needed profit improvement. Nonetheless, Uber continues to make major efforts to portray him as someone who has already driven major financial gains.

In reality, Khosrowshahi had little to do with the SoftBank investment or Google’s failure to achieve a major victory in its IP theft lawsuit. The SoftBank plan was established by Benchmark. Google simply didn’t have clear-cut evidence that Uber had incorporated stolen IP into its driverless car designs. The Google lawsuit settlement probably could have been achieved months ago, but Uber orchestrated a process that maximized Kalanick’s public embarrassment, and allowed Khosrowshahi to play the role of the “responsible adult” that made all the problems go away. Next year’s P&L will benefit from not having to spend any more money to defend the Google lawsuit, but these gains should not be attributed to Khosrowshahi’s management skills, or improvements in Uber operational efficiency.

Most importantly, the P&L data simply doesn’t support the “major progress towards profitability and IPO” that most press reports highlight. Yes, improvements have certainly been made and will continue to be made at the margin, but sustainable profits will require a combination of much bigger cuts to driver compensation, much bigger cuts to Uber’s own costs, and getting passengers to pay much higher fares. Since no one can define a path to true profitability, Uber continues to emphasize profit targets that exclude several billion of actual costs. Given Uber’s long success in managing its public narrative, the possibility that they somehow muddle through cannot be ruled out, but the available data strongly suggests that profitability mountain is too big, and many of the actions that could help reduce costs would also choke off future growth.

[1] Newcomer, Eric, *Uber Quarterly Sales Rose 61% to \$2 Billion Amid Heavy Loss*, Bloomberg, 13 February 2018

[2] Efrati, Emir, *Uber Narrowed Loss in Q4: Full Financial Breakdown*, The Information, 13 February 2018 (subscription required). Efrati appeared to be the only reporter that Uber provided with detailed P&L data.

[3] Wakabayashi, Daisuke, *As Uber Eyes I.P.O., Its Losses are Slowing. But They’re Still Big*. The New York Times, 13 February 2018

[4] Hook, Leslie, *Uber pares quarterly losses and lifts revenues*, Financial Times, 13 February 2018. There may be legitimate reasons that some of the costs included in Uber’s \$4.5 billion GAAP losses do not reflect its ongoing financial situation, but no one has documented the evidence here, and it seems inconceivable that the \$2.2 billion negative contribution is the best measure of its situation.

[5] The economic and competitive problems with Uber's business model are laid out in detail at Horan, Hubert, *Will the Growth of Uber Increase Economic Welfare?* 44 *Transp. L.J.*, 33-105 (2017)

[6] <https://www.nakedcapitalism.com/2017/12/can-uber-ever-deliver-part-eleven-annual-uber-losses-now-approaching-5-billion.html>

[7] For example see Wagner, Kurt, *Twitter made a profit by cutting costs, not by growing its business*, *Recode*, 8 February 2018

[8] \$3 billion is an estimated full year total based on the nine months of actual data released.

[9] Airlines could inflate total revenue by calculating it as "Full Fare" times the number of passengers, and then deducting the discount to the actual fare paid. This is not done because "Full Fares" have nothing to do with actual marketplace prices, and any gross revenue numbers based on them can be easily manipulated.

[10] Taxi service cost structures are documented in section II-B of my *Transportation Law Journal* article.

Hubert Horan: Can Uber Ever Deliver? Part Fourteen: The New Yorker Lays Out the Template for Pro-Uber Propaganda

Posted on [April 3, 2018](#) by [Yves Smith](#)

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

One of the themes of this "Can Uber Ever Deliver" series over the last eighteen months is how many mainstream business/technology publications have proactively worked to legitimize and amplify Uber's preferred PR/propaganda narrative.[1] Uber has always understood that the most effective way to instill belief in its public relations campaign is to have it presented by seemingly independent, objective outsiders.

The latest addition to the pro-Uber PR/propaganda genre is Sheelah Kolhatkar's [At Uber, a New C.E.O. Shifts Gears](#), the main feature in the 9 April edition of the *New Yorker* magazine.[2]The article fails to answer the central question it poses about Uber's future coherently, but provides a textbook illustration of how to write corporate PR/propaganda that naïve readers could easily mistake for honest journalism.

The problem is not that some stories have a pro-Uber slant or might reach pro-Uber conclusions. The problems are that the conclusions aren't backed by objective evidence, and the slants are created by artificially constructed story lines that prevent readers from evaluating available evidence and competing perspectives. These narratives use classic propaganda techniques to create favorable feelings about Uber, while distracting attention from Uber's uncompetitive economics and awful financial results, and from viewpoints inconsistent with the idea that Uber has an enormously powerful business model producing ongoing growth that will continue to be a wonderful thing for society.

A legitimate pro-Uber piece using traditional approaches would clearly state its pro-Uber conclusions, the evidence and assumptions supporting those conclusions, and would allow readers

to understand key contrary evidence and counter-arguments. PR/propaganda pieces are structured to look like objective reporting, but cherry pick available data while deliberately ignoring counter-arguments, present undocumented assertions as key findings, fail to clearly state or document major conclusions (so they cannot be readily challenged) and depend heavily on emotive language designed to manipulate readers. All of these approaches are used in Kohlatkar's article.

Totally Ignore Economic/Financial Evidence. In the case of Uber, the easiest way to distinguish pieces honestly trying to inform readers from pieces designed to mislead them is that the former will prominently feature hard data about Uber's competitive and financial performance and the latter will go to great lengths to ignore objective economic data. In an 8400 word article, only 11 words mention any of Uber's financial results. Kolhatkar briefly notes Uber's \$4.5 billion 2017 P&L loss at the end of the 32nd paragraph, and then quickly shifts to discuss the Eric Holder report about sexual harassment issues. In an 8400 word article, Kolhatkar chose not to mention that Uber's losses had been steadily increasing (up from \$2.6 billion in 2015)[3], or that Uber's losses have burned through \$10.7 billion of the investors' cash to date.[4]The author wanted to leave readers with a favorable impression of Uber but was not interested in helping readers understand why Uber has incurred such staggering large losses, or what it would take to achieve sustainable profitability, or how investors might actually earn returns on their investments.

Tell Only One Side of the Story. The second unmistakable giveaway that this is PR/propaganda, not honest journalism is that Kolhatkar and her editors only present one side of the Uber story. Everyone quoted is an Uber stakeholder, invested in Uber's eventual success. Nowhere in 8400 words is there any mention of anyone who might have a different perspective or hold different views—competitors, government officials, drivers, local transport experts or any of the many journalists who have been following Uber over the years.

The article relies heavily on lengthy interviews with new CEO Dara Khosrowshahi Uber investor Bill Gurley, and various other executives and Board members. As discussed in Part Eight of this series in the context of Brad Stone's January 2017 book *The Upstarts*, Uber has never provided this kind of inside access to journalists without assurances (implicit or explicit) that the resulting story would present Uber's spin and would exclude contradictory arguments and evidence. Kolhatkar doesn't disclose how she got detailed access to Khosrowshahi, Gurley and other insiders, or why she didn't interview anyone who wasn't an Uber insider.

Make False Central Claim: That Uber is “Financially Successful” . Financial data is ignored because the objective of Kolhatkar and her editors is to sell New Yorker readers on Uber's current narrative—it is a fundamentally successful company whose recent travails were anomalous and were fixed when Uber fired CEO Travis Kalanick and hired Khosrowshahi, and is now back on the path to further success. Those objectives are summarized nicely in the article's subtitle: “Dara Khosrowshahi is charged with turning the scandal-plagued startup into a traditional company—without sacrificing what made it successful.”

The word “success” is applied to Uber five times in the article's first 1000 words. But Kolhatkar's emphasis on “Uber's continued financial success” and her claim that Uber is “one of the most successful...companies in Silicon Valley” is fundamentally dishonest and easily refuted. This willful attempt to mislead readers depends on ignoring the financial data showing that Uber's growing multi-billion dollar losses in its eighth year of operations are unprecedented in Silicon Valley history[5], and that Uber's peer companies, who (unlike Uber) have fully exposed themselves to the scrutiny of capital markets and have actually produced strong positive cash flows, profits and shareholder returns. Kolhatkar's does not try to substantiate her central “success” claim save for vague references to rapid growth and strong brand awareness.

There may be a general perception that Uber is “successful” among readers of mainstream media, but this was manufactured by Uber’s communications programs, and reinforced by reporters like Kohlatkar who have no interest in seriously investigating the question.

Emphasize Emotive, Personality Issues to Distract Readers from Looming Business

Challenges. Kohlatkar’s story mentions the bad publicity Uber received in 2017,[6] and would have no credibility if she had ignored these widely known issues. This was also true of Brad Stone’s January 2018 article on the fall of Travis Kalanick;[7] Both show how the scandals and crises of 2017 forced Uber to shift its narrative from one depicting an unstoppable march to global industry dominance[8]to one emphasizing its redemption and recovery from an inexplicable run of ill fortune. In both cases, the stories present Uber’s currently preferred presentation in the guise of a story by an independent, objective journalist.

Kohlatkar glosses over the causes of recent crises, and falsely claims that Uber could not have foreseen that harassment issues raised by Susan Fowler but moved forcefully to solve those problems once they became aware of them. In order to make Uber seem more like a victim than a perpetrator, Kohlatkar absurdly asserts that “[p]roblems of gender discrimination weren’t as immediately obvious” ignoring a huge body of reporting where Uber was the poster boy for Silicon Valley misogyny, and the near-universal belief that Fowler’s claims of systemic harassment were entirely accurate. Kohlatkar willfully misrepresents the Eric Holder study, which was actually designed to whitewash the harassment issue. Its original version did not sanction anyone in Uber’s senior management, but was hurriedly rewritten after news of Uber’s misuse of police files on a Delhi rape victim emerged made the whitewash untenable.[9]

Kohlatkar dedicates almost a third of her entire story to creating a warm and fuzzy impression of Khosrowshahi. She is not writing a traditional “CEO profile” which would emphasize things like his specific actions and accomplishments at Expedia, his contract terms at Uber, and his proposed solutions for its various challenges. Those topics are ignored because Kohlatkar’s objective is to sell Uber’s “redemption/recover” story and to give readers the impression that, regardless of whatever happened before, the change of CEOs solved those problems. Thus she highlights the Kalanick—nasty guy/ Khosrowshahi—nice guy dichotomy. Since Khosrowshahi is a nice guy, readers should root for his (and Uber’s) future success.

Khosrowshahi is described as a “flatterer, diplomat, negotiator, and salesman” who was selected by Uber’s board “because of his personality: agreeable, unthreatening, comfortable with the kind of corporate talk that investors find reassuring.” He displayed cultural sensitivity while visiting Uber’s India operations. He supports the immigrant “dreamers” affected by the Trump Administration’s attempt to end the DACA program. He grew up in what colleagues described as “the most family-oriented family I ever met” and his parents valued education highly. He drove a rented Volvo on his first date with his current wife. Their current house (on 23 acres in the San Juan Islands) has been decorated in “eighty-year-old grandma rock star” style, and Khosrowshahi helped with the dishes after Kohlatkar ate dinner there.

But Kohlatkar provides absolutely no evidence explaining how Khosrowshahi’s positive traits could solve the business challenges he faces or how they could rapidly transform a company with a deeply entrenched personality that embodies its “nasty guy” former CEO. Nothing in the story explains why issues of personal style might have any bearing on whether Khosrowshahi can achieve his commitment to Uber’s board to a 2019 IPO at a \$120 billion public valuation, 75% richer than Uber’s inflated \$70 billion private valuation.[10] Or on his promise to eventually grow Uber to 20-30 times its current size (\$146-220 billion in annual revenue).

Depict 2017 Crises Falsely as Mere “Cultural” Issues Unrelated to the Underlying Business.

Kohlatkar’s narrative insists that the 2017 crises were purely “cultural.” “Uber’s board hopes that Khosrowshahi will be able to repair the company’s image.” That suggests that the board believes the crises wouldn’t have happened if Kalanick managed PR better and had hired someone to play the role Sheryl Sandberg has played at Facebook.[11] Kohlatkar quotes a Uber investor framing the challenge as “[h]ow does Dara preserve the positive aspects of the culture and change the aspects that are in desperate need of changing while still competing fiercely?” This reinforces the redemption/recovery narrative where the underlying business model was always sound, and the appointment of someone with Khosrowshahi’s personality will fix supposedly non-core problems that arose in 2017 and put Uber back on the path to success. There’s no need for readers to know more about problems with the underlying business.

But unfortunately for Kohlatkar, even if you withhold the overwhelming awful financial data from readers, the internal contradictions come through. The “nice guy cleaning up the nasty guy’s mess” meme fails because she admits that “Uber’s previous C.E.O., Travis Kalanick, had built the company into an extraordinary success.”

More importantly, her description of Kalanick’s culture shows that it was directly drove that “extraordinary success;” it wasn’t peripheral bad stuff can be readily excised from the good stuff. That culture included Kalanick’s monomaniacal focus on results, active support for “breaking rules” and taking a combative stance towards any competitor, regulator or journalist that might stand in the way of growth. The idea that high performers should operate totally free of any constraints was an explicit “corporate value”. Kohlatkar admits that “Uber’s continued financial success has reinforced the idea that ruthlessness will be rewarded.”

Uber’s “unexpected 2017 cultural problems that the Board fixed by hiring Khosrowshahi” meme requires ignoring (as Kohlatkar does) Uber’s long pre-2017 history of willfully disobeying local laws, competitor sabotage and journalist harassment.[12] A corporate culture that long celebrated ruthlessness and rule breaking will inevitably lead to the theft of intellectual property, the development of software designed to obstruct law enforcement, and attempts to use stolen police reports to attack rape victims and competitors. “High performers” free of any constraints will inevitably lead to the systematic harassment of their female staff.

As has been discussed at length in earlier parts of this series, the “culture” Kalanick established was an integral part of Uber’s business strategy. If Uber had not openly celebrated law breaking and a monomaniacal focus on bulldozing anything standing in its way, it would have collapsed long ago. Until mid-2017, Uber’s investors uttered nary a critical word about any of these issues, because they knew that Kalanick’s ruthless culture was directly responsible for the results (rapid growth, large valuation) they wanted.

Uber was not a “financially successful” company that happened to be run by a bunch of guys with unfortunate views about women. Uber’s had a ruthless culture because it has always had uncompetitive economics. Companies that can generate sustainable profits because they are significantly more efficient than competitors do not need to celebrate rule breaking, steal intellectual property, harass journalists or tolerate systemic sexual harassment. Uber will not resume its “financial success” with a more enlightened CEO and increased sensitivity training.

Alert readers will also note multiple cases where Kohlatkar presents comments from Uber insiders that contradict the “Uber now back on the path to success” part of the narrative.

If Uber’s past “success” was a function of rapid growth, and Khosrowshahi wants people to believe that Uber has the potential to grow by 20-30 times, doesn’t Uber’s steady recent abandonment of

overseas operations (China, Russia, Southeast Asia, and potentially India) contradict that strategy? If growth and dominating markets (the way other “tech” companies have done) is critical but was fueled by subsidies, won’t efforts to improve profits by eliminating subsidies reduce demand and increase competition?[13]

Uber may have realized that alienating drivers was a “strategic mistake” but wouldn’t higher commissions make losses even worse, and won’t Uber’s efforts to eliminate drivers make this alienation much worse? If long-term success in the driverless car industry is a strategic imperative, as Kalanick and now Khosrowshahi believe, doesn’t that suggest that they believe that they could never earn returns for investors by operating traditional taxis? Kohlatkar makes no effort to help her readers understand these questions, or anything that doesn’t directly support Uber’s preferred narrative.

Fail to Answer the Article’s Central Question. At the outset of the article, Kohlatkar tells her readers that she will address the question of whether Dara Khosrowshahi can turn Uber from a “scandal-plagued startup into a traditional company—without sacrificing what made it successful.” Despite 8400 words, the article totally fails to either answer that question, or to lay out for her readers the key issues that will determine whether Khosrowshahi can meet that challenge. While I had not known that Khosrowshahi’s home has a “eighty-year-old grandma rock star” style, I did not notice any substantive points in these 8400 words that had not been previously reported.

Kohlatkar’s actual objective is to get her readers to buy into the spin that Uber has always been a fundamentally successful company, and the recent crises her readers have heard about are utterly unrelated to problems with the company’s business model. Readers should root for Khosrowshahi because he’s such a nice guy, and should have some sympathy for Uber’s effort to redeem itself from an *annus horribilus* that no company deserved.

To sell this fable, Kohlatkar almost completely eliminates any mention of actual Uber financial results, makes no attempt to explain what she think caused Uber’s many 2017 issues and crises, spends much of the article on touchy-feely aspects of personality and style, presents the change of management as a victory for the good guy over a bad guy, and makes no attempt to help her readers understand what Khosrowshahi would actually have to do to reverse billions in losses and meet his ambitious IPO and growth objectives.

This narrative was not based on independent, objective reporting. It is central to the article because Kohlatkar and the editors of the New Yorker deliberately chose to support the PR/propaganda objectives of Uber’s investors.

[1]Part IV of my Transportation Law Journal article, *Will the Growth of Uber Increase Economic Welfare?*44 Transp. L.J., 33 (2017) Available for download at SSRN: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2933177 and Part Nine of this series (15 Mar 17) document how Uber’s narratives have always been directly based on propaganda techniques, the strategic importance of Uber’s PR/propaganda programs, and Uber’s success in getting its narratives uncritically endorsed in the mainstream media. Parts Six (2 Jan 2017) Seven (31 Jan 2017) Eight (16 Feb 2017) and Twelve (23 Jan 2018) of this NC series provide further examples of pro-Uber pieces presented in mainstream outlets as if they were independent, objective analysis but which follow the precise structure of propaganda.

[2]Kohlatkar, Sheelah, “At Uber, a New C.E.O. Shifts Gears”, New Yorker, 9 April 2018.

[3]Part 13 of this series (16 Feb 2018) summarizes Uber's P&L history through the end of 2017. Parts I and II of the Transportation law Journal document the reasons for these huge, ongoing losses—why Uber's is a structurally less efficient producer of taxi service than the incumbents it has been driving out of business, that it lacks the strong scale/network economies digitally based companies have used to “grow into profitability” and that its growth has depended on massive predatory subsidies funded by Uber's unusually large investment base.

[4]King, Ian & Newcomer, Eric, “Uber Spent \$10.7 Billion in Nine Years. Does It Have Enough to Show for It?” Bloomberg, 6 March 2018

[5]To cite one of many possible sources, King & Newcomer document that Uber's revenue and profit performance are dramatically inferior to other public companies with similar valuations, that no Silicon Valley funded startup lost anywhere near as much as Uber over its first eight years, that only one public “technology” related company experienced an annual loss larger than Uber's 2017 loss, and ratios of sales to market value show Uber offers much less potential to investors than comparable companies.

[6]Early 2017 crises included Kalanick's inept handling of his decision to join Donald Trump's business advisory council Uber's response to a taxi strike at Kennedy Airport, Susan Fowler's blogpost documenting Uber's tolerance of systemic sexual harassment, a video showing Kalanick's profane response to a driver unhappy with changes to Uber's pricing policies, the disclosure that Uber had used a system called Greyball to obstruct local law enforcement and Google's lawsuit alleging Uber's theft of its driverless car intellectual property. Later crises included lawsuits between Board members following the breakdown of company governance processes, the disclosure that senior managers had illegally obtained confidential police files on the rape of an Uber passenger in Delhi (and sought to blame the accusations on competitors), and the failure to disclose of major breach of confidential customer data. Kolhatkar failed to mention the shutdown of Uber China, which had lost over \$1 billion.

[7]The January 2018 Stone article on Kalanick, (“The Fall of Travis Kalanick Was a Lot Weirder and Darker Than You Thought” Bloomberg Business Week 22 Jan 2018) is discussed in Part Twelve of this series.

[8]Prior to 2017, Uber's narrative emphasized that its powerful business model was based on major technological innovations; that resistance to Uber was driven by regulators and “The Big Taxi Cartel” who wanted to corruptly deny consumers the benefits of Uber's substantially superior service; that strong profits would quickly emerge as they had for all other “tech” startups, and that since Uber's business model could overwhelm competitors anywhere, it would inevitably dominate the global taxi industry, and make major inroads on private car ownership and public transit. See the TLJ article pp.85-86, and Part Eight of this series, which documents how Stone's *The Upstarts* faithfully replicates that Uber narrative. Part Twelve notes that Stone's 2018 article is totally inconsistent with his 2017 book because he has shifted from amplifying (no longer credible) Uber's “global domination” narrative to its more realistic “redemption/recovery” narrative

[9]Events related to the Holder report are described in detail in Part Ten of this series (15 June 2017)

[10]Since it would undermine her attempt to generate reader sympathy, Kohlatkar also fails to mention that Khosrowshahi was one of the highest paid CEOs in America while at Expedia, and does not disclose his salary at Uber. Presumably, those terms are far more generous than his Expedia terms, even before the \$120 million bonus he could get following a successful IPO.

[11]The growing awareness of Facebook’s highly problematic business model illustrates a similar contrast between media coverage focused on emotive/personality based narratives (do Sandberg and Zuckerberg seem trustworthy?) and coverage focused on the underlying business issues (how can Facebook be trusted if its profits and growth totally depend on unlimited access to private user data?)

[12]Uber’s ruthless pre-2017 behavior is documented in detail in part IV-D of the TLJ article and Part Four of this series (5 Dec 2016)

[13]While Kohlatkar’s (very brief) mention of operating subsidies and Uber’s failure to eliminate competitive threats suggest she has not been as egregious as some other pro-Uber authors in eliminating anything that might raise doubts the business model, she doesn’t acknowledge (much less address) those doubts. And those mentions need to be considered in the context of the much broader range of readily available evidence she has omitted, and her extensive effort in articulating Uber’s preferred narrative.

This entry was posted in [Auto industry](#), [Free markets and their discontents](#), [Guest Post](#), [Legal](#), [Regulations and regulators](#), [Ridiculously obvious scams](#), [Technology and innovation](#), [Uber](#) on [April 3, 2018](#) by [Yves Smith](#).

Hubert Horan: Uber’s Q1 Results – Reporters Show They Aren’t Up to Reading Financials

Posted on [May 24, 2018](#) by [Yves Smith](#)

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Here are some of the stories about Uber’s 1Q published results.

<https://www.wsj.com/articles/ubers-first-quarter-sales-rise-70-as-it-preps-for-ipo-1527107700>

<https://www.nytimes.com/2018/05/23/technology/uber-finds-profits-in-leaving-tough-overseas-markets.html>

<https://www.bloomberg.com/news/articles/2018-05-23/uber-shows-a-quarterly-profit-sort-of-thanks-to-grab-deal>

<https://www.recode.net/2018/5/23/17380952/uber-2018-financials-yandex-grab-softbank>

<https://www.ft.com/content/d7ab2be4-5e1a-11e8-ad91-e01af256df68>

The (paywalled) WSJ article provided links to actual P&L and cash flow tables.

As usual, it's a mixed bag of reporting. The Recode, New York Times and Financial Times articles were especially weak, suggested the reporters hadn't really been following the Uber story and weren't good at reading financial reports. All stories mentioned that Uber's reported "profit" was entirely due to the one-time, \$2.94 B gain on the Grab sale. But most stories highlighted "Uber profit" in their headlines and ledes, and only Newcomer (Bloomberg) and Griswold (Quartz) made a serious attempt to explain to readers that this gain was a one-time accounting entry. Even with their attempts to clarify, the overall takeaway most people will get from these reports is "Uber is now profitable"

In contrast to these stories, the Financial Time's Lex column (behind a premium paywall) explicitly emphasized that [the results didn't mean that Uber was anything close to a profitable business](#). "Uber is solidly lossmaking with slowing growth...and has some way to travel to convince markets its numbers add up before going public" But people who read the FT's "news" story (or the NYT, or WSJ) would have no idea that the numbers told this kind of story.

None of the stories made any attempt to explain how the sale of a hopelessly unprofitable operation could generate a \$2.94B accounting "profit", or made any attempt to explain that it was entirely based on Uber's opinion about how much Grab (currently money-losing) might be worth some day. None of this "profit" had nothing to do with the exchange of assets where the underlying value had ever been audited or based on exchanges in public markets.

None of the reporters seemed to grasp that making a (roughly) half-billion P&L improvement (aside from the Grab accounting benefit) in a single quarter, if true, would be a major story in itself, and didn't explain how this was achieved. It appears to have come from a \$280m cut in driver compensation vs the 4th Q (drivers getting less and less of what passengers actually pay—a piece of the Uber story that every major outlet ignores) and a \$277m cut in G&A and Depreciation expense.

Most stories mentioned Uber's hoped-for 2019 IPO, but none attempted to explain whether the 1Q data points toward the narrative Uber will need to gain a strong public valuation. "We are no longer losing a billion dollars a quarter" may be better news than the alternative, but neither Uber nor these reporters can explain how or when Uber might achieve breakeven, much less the sustainable profits investors will need to see. Dara Khosrowshahi has publicly stated that he expects Uber to grow to 20-30 times its current size, and that Uber's driverless car "flying car" programs are critical to achieving those growth targets. But all of the things that drove the Quarter-over-Quarter P&L improvement directly undermine that "growth narrative."

Much of the huge G&A/Depreciation cuts were related to reduced spending on future growth. Any company can goose current earnings if they stop spending for the future, but this is not what potential investors in Silicon Valley "growth companies" want to see. Most stories quoted Khosrowshahi's comments about growth exceeding expectations, but none noted that the quarter-over-quarter growth in gross passenger payments was only 4%. Some of the stories mentioned the termination of driverless car testing in Arizona, and the recent departure of the head of Uber's flying car project, but no one attempted to explain how any of these facts could be consistent with the company's aggressive growth objectives. Obviously, the idea is that "growth companies" can use the strong profits and cash flow from their core business to fund a variety of longer-term growth opportunities. The reporting on Uber still ignores its awful year eight economics in its core businesses, and that its hope of eventually earning money in driverless and flying cars is even more inexplicable.

<https://www.nakedcapitalism.com/2018/08/hubert-horan-can-uber-ever-deliver-part-sixteen-morningstars-horrendously-bad-uber-analysis-preview-ubers-ipo-propsectus.html>

Hubert Horan: Can Uber Ever Deliver? Part Sixteen: Is Morningstar's Horrendously Bad Uber Analysis a Preview of Uber's IPO Propsectus?

Posted on [August 13, 2018](#) by [Yves Smith](#)

By Hubert Horan, who has 40 years of experience in the management and regulation of transportation companies (primarily airlines). Horan has no financial links with any urban car service industry competitors, investors or regulators, or any firms that work on behalf of industry participants

Overview

- Morningstar released a research report three weeks ago predicting that Uber would become profitable in 2020 and could achieve an IPO value of \$110 billion. Understanding the problems with Morningstar's report is important because it illustrates the exact process and challenges Uber will face when it tries to sell its shares to investors next year
- Morningstar's analysis is horrendously bad. Its profit forecast depends on plugging \$4.5 billion in arbitrary and indefensible P&L gains into its forecast spreadsheet. Its valuation estimate depends on the equally indefensible claim that 39% five-year CAGR demand growth will occur independently of pricing, industry profitability or economic conditions. It provides absolutely no evidence substantiating its various claims about Uber efficiency improvements, fails to explain the source of these efficiencies, let alone demonstrate how they could drive powerful P&L gains, or explain why they didn't generate profits until Uber's 11th year of operations. They omit major factors relevant to a legitimate valuation analysis, such as pre-2017 P&L results, cash flows, and the costs and returns from current investments in future businesses such as driverless cars.
- Uber's IPO will be the biggest challenge in its history. Uber's Board believes it needs to achieve an IPO valuation north of \$100 billion to ensure all existing investors achieve the profits they are expecting. The IPO process will inevitably result in Uber losing control of their heretofore tightly and effectively controlled media spin. The SEC requires that Uber release detailed, audited historical financial data, and independent financial analysts will be able to scrutinize their IPO forecasts and valuation claims
- As Morningstar's atrocious analysis demonstrates, there is no legitimate way to reconcile a valuation estimate anywhere near \$100 billion with objective data about Uber's abysmal economics and financial results.
- For its entire history, Uber has gone to considerable length to evade public scrutiny of its black hole of losses and the dependence of its business on massive, and ultimately unsustainable investor subsidies, most importantly by presenting only fragmentary financial data that is largely non-comparable over time. Uber has succeeded nevertheless in using talking points that plays heavily on Silicon Valley mythology and libertarian gospel to create the impression that it is a highly successful venture. Uber is

likely to rely heavily on PR and propaganda to convince investors it is worth over \$100 billion.

- Morningstar's report illustrates how difficult it will be next year for Uber to maintain its sales pitch in the face of hard financial data. A legitimate valuation would consider a wide range of objective evidence and critically scrutinize key company claims. Instead Morningstar's report uncritically repeats longstanding elements of Uber's sales talk. The report is not designed to help potential investors, but to serve as advocacy on behalf of Uber's current shareholders.
- Morningstar's report is potentially valuable to Uber because it allows them to claim that "independent" analysis by an "objective" financial firm endorsed the idea that Uber's is worth more than \$100 billion, and that claims Uber is likely to make during the IPO process have been independently verified. Given all of the problems and deficiencies documented here, it is important that no one ever grant any credibility to the profitability, valuation and long-term growth arguments Uber or others might make because Morningstar reached similar conclusions.

Uber's 2019 IPO will be the biggest challenge in its history

Uber plans to go public a year from now. Committing to a 2019 IPO was an essential element of the pact that resolved protracted board-level battles and allowed Dara Khosrowshahi to replace founder Travis Kalanick as CEO. Kalanick believed that Uber was not ready to face full capital market scrutiny, but faced open rebellion from Board members who wanted to convert their paper profits into real money.

Uber's IPO valuation needs to meet two objectives. It must be high enough that all of Uber's current investors can cash out with big profits on the funding (roughly \$18 billion) they have provided. However, the share price must also provide IPO investors with the opportunity for additional equity appreciation.

Uber's Board seems to believe an IPO valuation of \$100 billion would meet these objectives, and has agreed to pay Khosrowshahi a \$100 million bonus if the Uber goes public at that valuation in 2019.[1]

The Uber IPO process would start with the publication of a prospectus that would include much more detailed audited historical financial data than Uber has released to date. It would present a narrative explanation of why investors (despite dismal historical results) should expect the many years of robust, highly profitable growth needed to justify a \$100+ billion valuation. It would also need to include pro-forma forecasts of profits and cash flows consistent with the claims in the narrative.

The central question here is how Uber will be able to reconcile these aggressively optimistic pro-formas, narratives and valuation justifications with the documented, audited record of the first nine years of Uber's actual economics and financial results.

Over its nine-year history, Uber has largely succeeded in controlling how the public sees the company. While the press gave extensive and highly critical coverage of sexual harassment and other "cultural" issues at Uber, reporting about the business was almost completely consistent with Uber's positioning. Perversely, the press failed to connect the "cultural" issues with the fundamental businesses strategies that created them.

As Kalanick feared, Uber will no longer enjoy this freedom from scrutiny and level of control over public discussion once the IPO process begins. For the first time, independent outsiders will be able to use objective financial data to scrutinize its historical performance and business model economics, and anyone considering an actual investment will have ample incentive to do so.

If financial analysts and business reporters were to scrutinize the data in Uber's IPO prospectus seriously, it is difficult to see how they could ever reconcile that information with a \$100+ billion valuation.

Uber's losses have grown steadily. No previous venture-capital funded company lost over \$2 billion in its sixth year of operation and then doubled those losses to \$4.5 billion in year eight. It would take one of the biggest corporate turnarounds in world history to rapidly replace those growing losses with growing profits.

In addition, despite numerous attempts over nine years, Uber has never successfully leveraged its car service position into any other businesses. Many of its attempts to expand ridesharing overseas have been spectacular failures.[2]

If investors realize that Uber's economics are far worse than what past press coverage led them to believe and its current performance is totally inconsistent with claims that its equity will appreciate beyond its target \$100 billion value, Uber will face an enormous crisis. If IPO investors would accept only a substantially lower valuation, many current investors would lose money. Perhaps even more important, the bubble of favorable Uber publicity would burst, as Uber's claims could no longer be taken at face value.

On the other hand, Uber has survived and grown for nine years despite these abysmal economics and episodes of highly negative media stories. As this series has separately documented, one of Uber's greatest strengths is its ability to construct and promulgate a very positive public image. This image is divorced completely from Uber's performance because the company has successfully gotten the press and public to accept the sort of narratives commonly used in political campaigns. They rely heavily on emotive language to obscure agendas, distract attention from contrary arguments, and conceal the lack of factual support.[3]

Despite ample evidence to the contrary, Uber's executives have convinced the vast majority of interested observers that Uber is an extraordinarily successful company, that its rapid growth was driven by innovative, cutting-edge technology, and that it has transformed urban transport and created massive public benefits. It has even succeeded in portraying the rare voices criticizing Uber as either beholden to corrupt, entrenched interests or ignorant of what it takes to build economic value.

With \$100 billion on the line, can Uber develop an IPO narrative that will once again triumph over pesky facts like audited financials?

The Morningstar/Pitchbook Uber Report illustrates the structural approach Uber's IPO prospectus will likely take, and the problems it will likely face

While this series has described why Uber is structurally unprofitable, until now, no one had ever attempted to lay out a detailed quantitative counter-argument claiming that Uber could rapidly become profitable and justify the huge valuation its investors hope to achieve.

On July 19th, Morningstar (and its subsidiary firm Pitchbook) issued the report “Uber may Pick Up Investors, Along With Riders, in its IPO” and subtitled “The ride sharing pioneer is likely to maintain its competitive advantage via its network effect.”[4]

Morningstar did not include detailed historical Uber financial data. But its report covered everything else that a future Uber IPO prospectus would. It included pro-forma Uber financial projections through 2022 that showed Uber producing profits in 2020. The text described how Uber will gain share as it expands globally and thus grow much faster than competitors. The document asserted that there are “narrow moat” protections in the ridesharing market and forecasts profitable growth in food delivery, freight services, bikesharing, other public transit services. It also foresaw huge long term potential for autonomous and flying cars. And most importantly (certainly from Dara Khosrowshahi’s point of view) is the central finding that Uber’s greatly-improved economics justify an IPO valuation of \$110 billion.

A review of the Morningstar paper quickly answers the central question. ***There is no way that an honest, rigorous financial analysis could reconcile actual Uber economics with the need to justify the \$100+ billion valuation that Uber’s current owners need.***

The challenge here isn’t finding factual or logical flaws with Morningstar’s attempt to do this, but how to sort through and prioritize which of the many egregious analytical errors to document.

The Morningstar report is an embarrassingly shoddy piece of work, and its major conclusions don’t hold water. But it is important to understand why the Morningstar report is so bad: it shows the remarkable number of distortions and omissions that it takes to try to reconcile Uber’s story of an inevitable march to profits to at least some financial analysis.

We contacted the authors of the report, sent a detailed list of questions, and considered their responses. In most cases, the replies appeared to reflect a lack of comprehension of the issues we were raising.

The next two sections look at the problems with Morningstar’s forecast spreadsheet while the subsequent sections will discuss how Morningstar then refocused its efforts on building a propaganda-style narratives tightly aligned with existing Uber PR narratives.

Morningstar’s profit projection depends on \$4.5 billion in gains from two huge but totally unjustified spikes in profitability.

To claim that Uber will become a profitable soon enough to justify a high 2019 share price, Morningstar needs to quickly reverse Uber’s \$4.5 billion 2017 loss. It did this by making arbitrary, unexplained (and inexplicable) plugs in in 2018 (\$1.5 billion) and 2020 (\$2.5 billion) forecast numbers.

The table below combines historical data with Morningstar’s forecast, and shows year-over year changes in Uber Revenue and Uber EBIDTAR expenses and the calculated EBIDTAR contribution margin of the each year’s incremental growth.[5]

| year-over year change (\$m) in | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|--|-------|---------|-------|---------|-------|---------|-------|-------|
| Uber Revenue | 1,515 | 4,440 | 1,327 | 4,643 | 5,381 | 6,149 | 7,253 | 9,044 |
| Uber EBIDTAR Expense | 2,270 | 6,320 | 1,918 | 4,654 | 6,299 | 4,739 | 5,681 | 6,616 |
| EBIDTAR contribution | (755) | (1,880) | (591) | (11) | (918) | 1,410 | 1,572 | 2,428 |
| EBIDTAR margin of year-over-year growth | (50%) | (42%) | (45%) | (0%) | (17%) | 23% | 22% | 27% |
| Contrib @ previous year's margin | | (2,212) | (562) | (2,068) | (13) | (1,049) | 1,663 | 1,960 |
| Gain from improved EDIDTAR margin | | 332 | (29) | 2,057 | (905) | 2,459 | (91) | 468 |

The contribution margin of actual Uber growth 2014-17 improved very gradually, and Morningstar's post-2020 forecast shows similarly gradual EBIDTAR margin gains. But there is a 45 point margin improvement in 2018 growth versus 2017 growth and a 40 point margin improvement in 2020 growth versus 2019 growth, which drive P&L gains of \$2.0 billion and \$2.5 billion respectively. ***The text fails to mention these huge 2018 and 2020 profit spikes, much the less give any justification for them.***[6]

Morningstar's forecast is based on indefensible claims about exogenous market growth, and Morningstar assumes Uber can grow rapidly regardless of pricing or profitability

Morningstar must show extremely high rates of revenue growth to justify Uber's valuation target. Instead of basing its revenue forecast on Uber's actual past results and analysis of what prices Uber would need to charge to operate profitably in the future, ***Morningstar's forecasts assume demand will grow completely independently of the ability of operators or drivers to make money or the prices customers pay.***

The double-digit demand growth forecasts that drive Morningstar's valuation are based entirely on crude calculations that claim to measure the size of Uber's "addressable markets" (i.e. aggregate market demand for ridesharing, food delivery and other products). Morningstar claims that the overall rideshare market will grow at a 29% five year CAGR (compound annual growth rate) and that Uber will grow at a faster 39% rate. If Uber only grows at a 25% five-year CAGR (Morningstar's "bear-case"), its valuation estimate gets cut in half, to only \$49 billion.

Seasoned investors know that trees do not grow to the sky. 39% growth for years for an already large company entering its second decade in a well-established industry is in the category of trees growing to Mars.

For these growth forecasts to be remotely plausible, one would need to provide indisputable evidence of both overwhelming new efficiency advantages (e.g. ecommerce versus brick and mortar) and the huge cash flow/profit generation that would warrant ongoing investment in capacity growth. Morningstar gets the economics entirely backwards. Instead of growth occurring when companies figure out how to exploit major new efficiencies profitably, companies suddenly become efficient and profitable because market demand magically falls from the heavens into their shareholders' laps.

Data on the total market demand for urban car services is extremely limited and unreliable, and revenue data is largely nonexistent. Morningstar extrapolates a single revenue datapoint (New York City taxi revenue in 2014) to a global scale to come up with its ginormous growth forecast.

This is ironic in that New York City, having recognized the destructive impacts of a massive oversupply of unprofitable capacity, is considering limiting the number of Uber drivers.

Using ginned-up global numbers allows Morningstar to grossly inflate its growth multipliers, by combining demand for transport in hundreds of huge, rapidly growing non-US cities with the much more mature transport markets in the US.

This distortion also allows Morningstar to ignore the fact that with a handful of possible exceptions (e.g. London) the available evidence suggests that Uber's efforts to penetrate these faster growing markets have been financially disastrous.[7]

Finally, this approach also ignores evidence that (like many other startups) Uber's rate of revenue growth has slowed over its nine years of operation and was only 20% in 2017, in part due to efforts to reduce its financial losses. Nothing in Morningstar's report explains why, despite large continuing losses, Uber will suddenly increase revenue growth to 60% in 2018.

Morningstar's car service revenue analysis never mentions the word "price" and its report completely ignores the fact that its historical revenue growth was largely driven by multi-billion dollar subsidies. Readers have no way of knowing whether Morningstar's forecast of five year 39% revenue CAGR is due to market stimulation from increasingly lower prices, from Uber's ability to charge increasingly higher prices than customers they pay today, or whether Morningstar ever even considered these issues.

Morningstar's forecast of aggressive Uber growth in non-car service markets also depends on totally ignoring the economics of those industries. Its optimistic view of food delivery demand growth is based on a single article noting that Uber has rapidly captured share from a financially struggling (but still much larger) competitor. Morningstar has no evidence that Uber Eats generates positive cash flow or actual GAAP profits, or that the business is rapidly moving toward GAAP breakeven.

Morningstar's paper best seen as as PR and propaganda, not financial analysis

Morningstar's effort confirms that there is no legitimate way to reconcile financial forecasts that would justify a \$100+ billion IPO valuation with Uber's economics. As discussed earlier, if honest financial analysis cannot justify a \$100+ billion IPO valuation, the alternate path is to focus exclusively on boosterism.

The vast majority of Morningstar's report is pure narrative that is almost entirely disconnected from any specific spreadsheet numbers, and many of the critical numbers the spreadsheets are not explained in the text. In fact, the the apparent purpose of the spreadsheets is to create the appearance that the report's conclusions were based on legitimate financial analysis.

The next three sections will discuss specific components of Morningstar's narrative in greater detail—the emphasis on "network effects" in lieu of actual evidence of operational efficiency, the misrepresentation of the driver's role in Uber's business model, and how discussions of autonomous and flying cars are intended to create the vague impression of long-term growth potential but misrepresent their impact on Uber's actual value.

Morningstar's narrative depends on totally unsubstantiated claims about Uber efficiencies driven by "network effects"

Morningstar's central claim that Uber efficiencies are driven by "network effects" is false. Worse, Morningstar's attempt to imply that "network effects" could explain either a rapid \$4.5 billion profit improvement or profitable growth at 39% CAGR over five years is complete nonsense.

Morningstar's paper mentions "network effects" over 40 times. Evidently they believe the use of Silicon Valley buzzwords has a talismanic effect and eliminates the need for economic evidence.

The authors fail to explain where these alleged network benefits come from, how they actually drive cost efficiencies or increased revenue, or whether they create any material, sustainable advantages over competitors. Morningstar presents absolutely no evidence linking any operating efficiencies to the dramatic revenue growth and profit improvement they are claiming. In keeping, they cannot explain why these effects have failed to produce profits over the past nine years, let alone why they will suddenly gain immense power. Nor do they provide any other examples where a new entrant with "network effects" was able to drive incumbent operators out of business and create \$100 billion in corporate value.

They claim that "Uber's network effects benefit drivers and riders; the benefits for each create a continuous virtuous cycle" and cite Facebook's network effects as a comparable example of network benefits for consumers.

But Uber has *none* of Facebook's network economies, where (following what is known as "Metcalfe's Law"), each additional user makes the company and its platform more valuable to all other (existing and potential) users.[8]

Uber users may like its prices and service, but they do not care how many other people download the app. Aside from purely digital companies like Facebook and Ebay, no consumer companies with app-based platforms have created the tens of billions in corporate value that Uber falsely attributes to "network effects."

Similarly, if Uber "network effects" created meaningful (and steadily increasing) benefits for drivers, there would be corresponding evidence of better (and rapidly improving) driver economics and work satisfaction.

In fact reports of drivers having to sleep in their cars are becoming more common. Driver take-home pay has fallen below minimum wage in most large cities,[9]and as Morningstar acknowledges, 96% of drivers quit Uber within the first year.[10]

"Network effects" supposedly explain Uber's capacity utilization advantage, as they eliminate the "need for bright yellow cars to roam about, waiting for a hand in the air to match with it." In fact Morningstar has no evidence that Uber has a capacity utilization advantage over traditional taxis that could have any material bearing on its growth and profitability forecasts. The only relevant data Morningstar actually provides shows Uber utilization falling 7% in 2017.[11]

Morningstar badly misrepresents the economics of Uber's drivers

As readers of this series, know, the Uber/driver split of gross passenger fare revenue is critical to any discussion of Uber's economics and profitability. To stem losses, Uber had been unilaterally increasing its "commission" from 20% to 30% while also eliminating many driver incentives. These changes resulted in the driver share falling from 83% in 2014 to 68% in 2016.

That increased Uber's EBIDTAR contribution by over \$2.6 billion, and improved EBIDTAR margins from (118%) to (50%). But Uber would have still had triple digit negative margins if the driver share had remained above 80%. The only major progress Uber has made towards a breakeven P&L required pushing driver compensation to (or below) minimum wage levels.

Morningstar's forecast ignored the importance of the Uber/driver revenue split to Uber's bottom line, and asserted that 21-22% Uber shares (similar to 2017 actuals) will remain stable for the next ten years.

Even though it would be arithmetically impossible for both Uber and drivers to increase their share at the same time, Morningstar set that forth as a scenario. The report made the absurd claim that as pressure to increase driver pay increased (as seems likely given tightening labor markets, regulatory pressures and widespread driver recognition of the raw deal they've gotten), Uber would respond by simply increasing its share of passenger fares from 20% back towards 30%.

More fundamentally, this intelligence-insulting narrative illustrates either Morningstar's ignorance of Uber's business model or its willingness to flagrantly misrepresent it.

Morningstar insists Uber is not a transportation company but a software company, and its software serves as a passive intermediary between passengers and wholly independent drivers. Aside from eliding questions about depriving drivers of basic labor law protection, Uber drivers are not economically independent; Uber's business model ties them into vehicle financing obligations. Uber could not have imposed \$2.6 billion in unilateral compensation cuts on truly independent drivers.

The fiction that the drivers are "independent" conceals the fact that Uber's drivers contribute 83% of what passengers are paying for, and that the overall Uber-driver business model cannot survive unless both parties can earn satisfactory returns on what they contribute to the business.

Morningstar's narrative badly misrepresents the impact of Uber's autonomous car and flying car programs on its corporate value

Morningstar provides detailed arguments about Uber's long term potential to exploit businesses such as autonomous vehicles (AVs) and flying cars (Uber Elevate) but then totally excludes the cost of developing them from their valuation estimates. One might argue that these investments will increase the value that IPO investors will get (long-term potential greatly exceeding near-term costs) or that they will actually decrease Uber's value (the low probability of far-off returns doesn't justify the costs and risks), But it is unacceptable for Morningstar to claim a specific (\$110 billion) Uber value while pretending none of these issues exist.

Morningstar defense of Uber's AV program rests on Dara Khosrowshahi's false claim that autonomous vehicles would allow Uber to reduce the price of rides by 60%.^[12] Drivers do account for roughly 60% of the costs of a traditional taxi operation, but the introduction of autonomous vehicles would significantly increase other costs (vehicles, databases, communication links, machine learning systems, vehicle planning and control systems, new safety/insurance models, etc).

More important, a shift to autonomous vehicles would also require Uber to become a highly-capital intensive business, since it could no longer push all the costs and risks of AVs onto its drivers. It is not clear whether Uber has the management skills or strengths appropriate to the challenges AV or flying car businesses would pose. Since Morningstar ignores the questions of what would be required to succeed in those businesses or how long it would take to determine who the competitive winners would be, it is impossible for a reader of this report to have any idea whether Uber's current investments make any sense.

Uber has openly acknowledged that Khosrowshahi's narrative is the primary driver of its AV and flying car investments. As one interview reported, "... working on flying cars is important to the Uber narrative, according to Uber COO Barney Harford.. 'I think being able to demonstrate [to investors] that we are a company that is able to deliver multiple growth engines and is able to incubate and execute upon a few different opportunities, I think that's a really important story.'"[13] IPO narrative imperatives have led Uber to claim it can have flying cars in full revenue service within five years, a ludicrous claim given the immaturity of the technology, the huge public safety and infrastructure implications, and the well-established rigor of aviation regulatory requirements.[14]

Khosrowshahi has acknowledged that his original plan after joining the company was to cancel both programs given their huge cash drain and uncertain returns, but changed his mind once he recognized that the IPO pitch required giving investors the prospect of growth beyond ridesharing.[15] That narrative transforms Uber's rideshare ordering app into the gateway to all forms of urban transport, and transforms Uber into "...the Amazon for transportation." [16]

Lots of investors might be interested in investing in the "Amazon of transportation". But a good-faith valuation analysis of this opportunity would examine whether Uber's economics gave it the same potential to profitably expand across new transport modes that Amazon demonstrated when it expanded from bookselling into other ecommerce fields. Morningstar fails to provide that legitimate valuation analysis.

Morningstar's evasiveness here is designed to prevent its readers from understanding a fundamental contradiction in Uber's pursuit of a \$100+ billion valuation. There are many things Uber could do to improve short term profitability, such as abandoning unprofitable overseas markets, eliminate spending on AVs and flying cars, but all of them would directly undermine their long-term growth narrative. Hypothetically, one could show strong 2018-19 P&L improvements, or one could show the investments Uber thinks will be required to become the "Amazon of transportation" but under no circumstances could one show both.

The report shifts Morningstar from independent analysis of Uber to proactive advocacy on behalf of Uber's shareholders

Regardless of the size of the final estimate, even if it were supporting a strong, positive valuation, the text explaining a bona fide valuation analysis would show how it had considered a wide range of objective evidence (historical financial trends, sensitivities to external factors, comparisons showing how claimed strengths/risks affected similar companies) supporting it and that it had critically scrutinized key company claims.

Morningstar's narrative did not do any of these things. Reading it one gets the impression that it started with its bottom-line conclusion (a \$110 billion valuation), worked backwards and plugged

numbers into a spreadsheet that would produce that bottom-line, and then filled its paper with unsubstantiated but pro-Uber opinions roughly in line with its positive valuation.

Much of Morningstar's story line repeats longstanding elements of Uber's talking points uncritically, without any attempt to provide objective supporting evidence. Thus Morningstar's report should not be seen as independent analysis designed to help investors but as proactive Uber advocacy, in support of the number 1 priority of current Uber shareholders, an IPO valuation north of \$100 billion.

Uber wants people to believe that its growth was driven by powerful operational efficiencies derived from things like "network effects" "capacity utilization" and "synergies between ridesharing and food deliveries." Morningstar simply repeats Uber's preferred messaging, without providing any evidence that things are real or economically important, or explaining why they won't produce profits until Uber's 11th year of operations.

Uber wants people to believe it is a technology company, and not a company that provides rides in automobiles. Morningstar simply repeats the claim that Uber is a software company, and that independent drivers freely chose its software because of the huge benefits it provides them, without showing any tangible evidence of these benefits, or explaining why their well-documented experience blatantly contradicts the idea of driver benefits.

Morningstar emphasizes that "ridesharing" is significantly different economics than "taxis" even though it has not done any analysis of the competitive economics of the two approaches.

Morningstar then claims that the companies with the most comparable economics are Facebook, Microsoft and Google. This serves Uber's theme that its IPO value should not be based on comparisons with any other transportation companies but only with reference to the most elite companies in the Silicon Valley.

Morningstar does not explain why Uber is many years behind these "most comparable" companies in terms of the scale economies needed to convert growth into profitability, in terms of generating enough positive cash flow its core business to fund all its future growth, in terms of achieving dominant market positions or being able to go public.

As with any propaganda-based approach, distracting attention from the issues Morningstar (and Uber) don't want investors to think about is just as important as the positive impressions that one is trying to create.

Morningstar presents no pre-2017 Uber financial results, and heavily emphasizes size metrics, in order to distract attention from the nine years of huge, steadily increasing losses in pursuit of growth-at-all-costs. This also allows Morningstar to conceal the huge discrepancy between recent P&L trends and the sudden \$4.5 billion profit spikes it has forecast for 2018 and 2020. Morningstar asserts that "network effects" fully explain Uber's ability to capture share from yellow taxis in Manhattan, in order to distract attention from the huge subsidies that actually created Uber's price and service advantage.

Although Morningstar's methodology statement opens with "At the heart of our valuation system is a detailed projection of a company's future cash flows" its report does not actually include projections of Uber cash flows. These would seem to be critical to any investors trying to evaluate Uber's future value, but Morningstar wants to distract attention from the nearly \$11

billion in cash[17]Uber has already burned through so far, the continuing operating losses Uber needs to fund, and the huge cash requirements of its longer-term growth opportunities that Morningstar failed to analyze.

The Morningstar does mention a variety of widely-known negative Uber issues (low entry barriers in ridesharing, the failure of Uber China, the pedestrian killed by an Uber AV, growing legal/regulatory threats, etc.) But it ignores other important issues such as Uber's open pursuit of quasi-monopoly industry dominance and artificial market power, the huge sensitivity of the P&L to driver compensation changes, and Uber's inability to produce urban car services as efficiently as the traditional taxi operators it has been driving out of business, and makes only passing reference to its largely dysfunctional management and corporate culture.

Morningstar's worst case scenario does not consider the possibility that it may take years longer to reach breakeven, or that full-time Uber drivers win the labor law protections of other full-time employees, or that its autonomous and flying car programs fail to ever generate positive cash flow. The only downside Morningstar quantifies is that 2018-22 Uber revenue grows at a 25% CAGR, instead of 39%.

It is not obvious as to why Morningstar chose to publish an Uber IPO valuation estimate a full year before they go to market, although the report would seem to be highly useful for Uber as it builds its own valuation PR/propaganda narrative. The Morningstar report will allow Uber to claim that "independent" analysis by an "objective" financial firm has directly endorsed the idea that Uber's 2019 IPO might yield a valuation north of \$100 billion and that many of the justifications Uber is likely to use have been independently vetted. One can expect that as the actual IPO approaches, more seemingly "independent" voices will endorse the idea that Uber has a value north of \$100 billion, with many years of robust, highly profitable growth ahead of it.[18]Given all of the problems and deficiencies documented here, it is important that no one ever grant any credibility to the profitability, valuation and long-term growth arguments Uber or others might make because Morningstar reached similar conclusions.

[1]Kolhatkar, Sheelah, "At Uber, a New C.E.O. Shifts Gears", New Yorker, 9 April 2018.
<https://www.newyorker.com/magazine/2018/04/09/at-uber-a-new-ceo-shifts-gears?currentPage=all>

[2]Source references for evidence and arguments presented in prior parts of this series will not be repeated here. All of the central arguments about Uber's economics, and Uber financial results through mid-2017 are documented in my Transportation Law Journal article *Will the Growth of Uber Increase Economic Welfare?* 44 *Transp. L.J.*, 33-105 (2017) which is available for download at SSRN: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2933177 Uber financial results for full year 2017 and the first quarter of 2018 were presented in this series in Part 13: Even After 4Q Cost Cuts, Uber Lost \$4.5 Billion in 2017 (16 Feb 2018) and Part 15: Uber's Q1 Results – Reporters Show They Aren't Up to Reading Financials (24 May 2018)

[3]The evidence showing that Uber's communication efforts fit academic definitions of propaganda, and the actual development of Uber's PR/propaganda narrative over time is laid out in part IV of the Transportation Law Journal article.

[4]The 48 page report can be downloaded at <https://pitchbook.com/news/reports/3q-2018-morningstar-pitchbook-uber-may-pick-up-investors-along-with-riders-in-its-ipo>. The authors are listed as Ali Mogharabi, Julie Bhusal Sharma, Asad Hussain and Brian Colello. Three of the four work for Morningstar; for the sake of brevity I will refer to this as the Morningstar report instead of the Morningstar/Pitchbook report.

[5]It is not possible to prepare a similar table showing year-over-year changes in total revenue versus total expenses because Uber has never disclosed total expense or net income data for 2016.

[6]I sent Morningstar's authors (via email) the table shown here and asked them to explain how their of 2018 and 2020 forecasts could diverge by \$2+ billion from the P&L trends in every other year between 2015 and 2022. Their answer completely ignored the question I had posed and simply repeated the following text from their report: "Besides the driver take rate, which is netted out of Uber's net revenue, we believe a portion of Uber's cost of goods sold is fixed and revenue will grow at a faster pace than these costs, leading to gross margin expansion. We also project that Uber will benefit from operating leverage in the years ahead. The firm might be able to increase revenue at a faster pace than selling, general, and administrative costs, especially in the sales and marketing lines, while also having to spend relatively less on operations and support costs. However, we anticipate that R&D will remain elevated as Uber invests in new ventures, resulting in only slight declines in R&D as a percentage of net revenue."

[7]Given the failure of Uber China Morningstar does exclude China ridesharing demand from its claimed "total addressable market" but it did not exclude other markets Uber has already abandoned (Russia, Southeast Asia) or is rumored to be failing badly (India) markets where it has been totally blocked (e.g Japan), or where it is facing much better financed competitors such as Didi Chuxing. Morningstar fails to disclose what portion of its future Uber revenue estimates are domestic and foreign.

[8]Andreessen Horowitz, *All about Network Effects*, 7 March 2016; <http://a16z.com/2016/03/07/all-about-network-effects/> Noah Smith, Uber Still Doesn't Look Like the Next Facebook—it lacks the powerful network effects that compel customers to stick with it, Bloomberg 6 June 2017; <https://www.bloomberg.com/view/articles/2017-06-06/uber-still-doesn-t-look-like-the-next-facebook> Many companies have app-based platforms that generate no network economies. For example no airline passenger or pizza consumer cares how many other people use the American Airlines or Domino's Pizza app. Consumers may derive benefits from the size of these companies (enabling them to offer more flights or take-out locations) but those are scale economies, not network economies.

[9]Mishel, Lawrence, Uber and the labor market: Uber drivers' compensation, wages, and the scale of Uber and the gig economy, Economic Policy Institute, 15 May 2018; <https://www.epi.org/publication/uber-and-the-labor-market-uber-drivers-compensation-wages-and-the-scale-of-uber-and-the-gig-economy/>

[10]Amir Efrati, How Uber Will Combat Rising Driver Churn, *The Information*, 20 Apr 2017; <https://www.theinformation.com/articles/how-uber-will-combat-rising-driver-churn> Chantel McGee, Only 4% of Uber drivers remain on the platform a year later, CNBC, 22 Apr 2017 <https://www.cnbc.com/2017/04/20/only-4-percent-of-uber-drivers-remain-after-a-year-says-report.html>

[11]This is shown in Morningstar’s Exhibit 11. The issue isn’t that Uber might not have some utilization advantages in some situations, but that there is no public evidence supporting the broader claim, and no evidence that it has a powerful impact on overall cost competitiveness.

[12]Amir Efrati, Uber Seeks Deal for Waymo Cars, *The Information* 5 Mar 2018
<https://www.theinformation.com/articles/uber-seeks-deal-for-waymo-cars>

[13]Johana Bhuiyan, Uber wants to sell a flying car service in five years — but we don’t know if the tech (or the law) will happen by then, *Recode* 11 May 2018
<https://www.recode.net/2018/5/11/17332646/uber-flying-car-vtol-barney-harford>

[14]Bhuiyan 11 May, also Sean Captain, How Uber Plans To Get Flying Taxis Off The Ground, *Fast Company*, 2 May 2018. <https://www.fastcompany.com/40522758/how-uber-plans-to-get-flying-taxis-off-the-ground>

[15]“To Kalanick, the autonomous-driving unit was the jewel of the company. When Khosrowshahi took over, he considered closing the program, since it could potentially cost billions of dollars.” Kolhatkar, Sheelah, “At Uber, a New C.E.O. Shifts Gears”, *New Yorker*, 9 April 2018. “Khosrowshahi now believes Elevate fits into Uber’s mission to be a platform for all types of transportation. “What you’re trying to do as a company is take growth that is coming in today and stage them and invest them in forward opportunities down the road ... opportunities four years and six years and eight years from now,” he said.” Johana Bhuiyan, Uber’s CEO says he’s willing to lose money on flying cars — at first, *Recode* 9 May 2018.
<https://www.recode.net/2018/5/9/17337764/uber-ceo-dara-khosrowshahi-flying-cars-elevate-vtol> “

[16]“Khosrowshahi says he wants to transform Uber into a multi-modal company that connects people to bikes, buses, car rentals, and maybe even flying taxis” Andrew Hawkins, Uber CEO: Our Future Won’t Just Be Cars, *The Verge*, 15 May 2018.
<https://www.theverge.com/2018/5/15/17340064/uber-ceo-dara-khosrowshahi-interview-elevate-flying-cars> “..we wanna kinda be the Amazon for transportation.” Swisher, Kara, Uber CEO Dara Khosrowshahi at Code 2018, *Recode*, 31 May 2018
<https://www.recode.net/2018/5/31/17397186/full-transcript-uber-dara-khosrowshahi-code-2018>

[17]King, Ian & Newcomer, Eric, “Uber Spent \$10.7 Billion in Nine Years. Does It Have Enough to Show for It?” *Bloomberg*, 6 March 2018 <https://www.bloomberg.com/news/articles/2018-03-06/uber-spent-10-7-billion-in-nine-years-does-it-have-enough-to-show-for-it>

[18]This is consistent with Uber PR/propaganda techniques previously documented in this series. Part Eight of this series (Brad Stone’s Uber Book “The Upstarts”— PR/Propaganda Masquerading as Journalism, 16 Feb 2017) describes how Uber got a seemingly independent journalist to write an entire book promulgating Uber’s main PR/propaganda narratives while ignoring all contrary financial and economic evidence. Part Six (Latest Data Confirms Bleak P&L Performance While Stephen Levitt Makes Indefensible Consumer Welfare Claims, 12 Jan 2017) illustrates how Uber paid a seemingly objective outsider to make (largely specious) claims about how Uber created huge consumer welfare benefits, and then how press reports and articles by Uber supporters amplified the findings and created the appearance that it was a widely-held consensus view.

<https://www.nakedcapitalism.com/2018/08/hubert-horans-quick-take-ubers-second-quarter-results.html>

Hubert Horan's Quick Take on Uber's Second Quarter Results

Posted on [August 16, 2018](#) by [Yves Smith](#)

From Hubert via e-mail:

Uber released 2Q P&L results Wednesday.

1. GAAP Net Loss for the quarter was \$891 million. This was significantly worse than its 1Q \$551 million loss.

The (paywalled) WSJ story, [Uber's Revenue Growth Keeps Up Fast Pace](#) includes a link [to the detailed P&L data](#).

Bloomberg's press report, [Uber CEO Embraces Losing Money With Revenue Growth Slowing](#), had a bit better balance.

2. Unlike 1Q, reported 2Q results did not appear distorted by any major accounting games. In 1Q Uber sold failing Asian operations to Grab, and asserted the Grab shares it obtained in the transaction were worth \$3.0 billion, producing a 1Q accounting profit of \$2.5 billion. Many (but not all) of the media reports of Uber's 1Q results fell for the "Uber is now profitable" gambit. Press coverage generally emphasized the "2Q losses increasing" point, reversing whatever short-term PR benefits Uber might have gotten from its claims of 1Q "profit".

3. Uber's GAAP net loss for the year ending June 2018 was \$4.00 billion. Its net loss for the year ending December 2017 was \$4.46 billion. So losses are shrinking very slowly; at this rate they might achieve breakeven in their 15th year of operations. This dramatically contradicts the Morningstar claims (discussed [in Part 16 of our series last Monday](#)) that Uber would achieve a 45 point margin improvement in 2018 versus 2017, and achieve breakeven in 2020.

4. Uber supporters tend to emphasize revenue growth, while ignoring the profit problems. But Uber Net Revenue for the year ending June 2018 had increased 28% over Net revenue for the year ending December 2017. But Morningstar had predicted 2018 net revenue would be 60% higher than 2017. Without this type of rapid revenue growth, their entire case for a \$100+ billion IPO valuation totally collapses. Other recent pro-Uber press reports have claimed extremely strong growth for Uber's food delivery service. None of these claims have been substantiated, but they raise concerns that growth in Uber's core car service business may be even less than 28%

5. A (paywalled) Tuesday piece in the tech site The Information — usually a reliable source of pro-Uber spin — [reported that Uber was losing \\$125-200 million a quarter \(\\$500-800 million annualized\) on its driverless car efforts](#).

This would confirm the argument laid out in [Monday's Part 16 of our series on Uber's economics](#) that there is a fundamental contradiction between actions Uber might take to stem short term losses, and Uber's need to promulgate an IPO narrative highlighting years of robust, profitable growth. Morningstar's \$100+ billion valuation estimate was based on ignoring the huge costs of developing these highly speculative future businesses. Even normally pro-Uber media outlets are beginning to recognize that they can't continue to ignore \$500-800 in annualized expense.