

February 2019

To our shareholders:

Thank you for caring about Wayfair. We can honestly say that 16 years ago, when we were starting out, we did not fully understand the incredible journey which we were embarking on. Now, today, I think we do, and it is clear to us that Wayfair is just getting started.

2018 was another great year for Wayfair and we are delighted with what our team of over 12,000 people has enabled us to achieve. It really is quite amazing. We have created a platform that is changing how people shop for their homes.

As we look back on how the business has developed in recent years, it is clear that our value to customers and suppliers is resonating more strongly than ever. Despite already having millions of loyal customers we are still in the very early days of penetrating the market. As we enter 2019, we want to share with you our view of what we are building as a business; where we are on our journey; and why we are incredibly excited about how we are positioned for the future.

### **Founder's Perspective**

Every quarterly earnings call, we speak about how the business has developed over the prior three months, which is a very short period of time for any business, particularly one growing at our pace. In fact, talking in terms of quarterly trends lends itself to false precision because actual wins are achieved over six and 18 and 36 months. This false precision can lead folks outside the business to have less clarity as to what we are building and how it is progressing. To us, it is very clear what we are building: the market-leading platform in the home category; a platform that is coveted by our supplier partners, and is loved by our mutual customers.

We operate in a category with a very attractive total addressable market (TAM) worth an estimated \$300 billion in North America and \$300 billion in Europe. Online is a small portion of the market but it is growing very quickly, with increasingly favorable customer demographics as millennials age into the category. Home is a category that is like no other, it has unique complexities that make it ripe for innovation. Critical to our success has been our focus on innovating to solve the specific challenges that customers face when shopping for the home. These challenges include the importance of browsing rather than searching; the need for inspirational and descriptive imagery; servicing a desire for uniqueness without seeming overwhelming; shipping big, bulky, damage-prone items with a low ratio of monetary value to physical size; overcoming a desire to touch and feel through speedy delivery, rich content, and great customer service with deep knowledge; and delivering a highly consistent experience across a broad set of categories.

By focusing solely on the home category, and taking a long-term view, we have been able to invest in building a platform that is quickly becoming the big winner with customers and suppliers. We have done this across five brands that serve distinct tastes yet benefit from the complex and focused infrastructure we have been building: Perigold focused on the luxury segment while Wayfair serves the mass market, and our three specialty lifestyle brands – Joss

& Main, AllModern and Birch Lane. Despite the success of our first 16 years, we are still quite small with a market share of ~1% and we really believe our most exciting days are still ahead of us.

## **A Platform for Home**

Given the size of the TAM, the unique challenges of our category and the distance-less nature of the internet we believe there will be an online destination that is the best place for customers, and therefore, the most obvious choice for the 11,000+ entrepreneurial suppliers who service it to market their products. We are building Wayfair, with all of our brands and resources, to be this place.

A key question is therefore “What would a market-leading platform do to capture this opportunity better than anyone else?” We think the answer is simple – give customers and suppliers what they want by optimizing all aspects for this unique category.

Customers want the experience of shopping for the home to be easy and fun, avoiding the anxiety that is often associated with the process. This includes:

- A huge selection.
- A consistent experience.
- Rich product information.
- Frictionless tools that make it easy to navigate a huge selection (AI-driven search, house brands, visual navigation, search by photo, Idea Boards, etc.).
- Rich content (beautiful imagery, customer reviews, 3D view in room, etc.).
- Clear and consistent shipping and delivery.
- Great service and support throughout the shopping and delivery experience.

Supplier partners want:

- The ability to tell their product story to customers in the best possible way.
- To be able to get products to market faster than they have historically.
- Tools that complement their skills and resources (e.g., logistics, delivery).
- Access to a large and growing customer base.
- To be able to trust that the complexities of the category are addressed.
- Support in solving issues they face as a small and medium-size business.
- Ultimately, to be in control of their own success.

## **Wayfair Today**

While we are proud and excited by what we have accomplished, we are even more excited that there are still rich opportunities for innovation. We are currently investing in initiatives across our business that will make the platform stronger and continue to differentiate us as the best platform for home.

We operate our platform on extensive software that we have largely purpose-built ourselves (this includes the site and app technology, the ad tech stack, the software behind customer service and logistics etc.) with millions of hours of product and engineering team time invested,

focused on building an e-commerce technology-based business solely for our home customers and home suppliers. Today there are over 2,300 people in the company working to build the unique custom technology on which we operate 24/7.

Where we have not built in-house solutions, we have instead created deep, innovative, relationships with key partners, such as media partners (including Google, Facebook, Pinterest, and others); key transportation and logistics partners; and our suppliers.

We provide both pre-sales and post-sales service with an in-house team of over 2,800 amazing people, organized in a very specific way to serve the customer best. We believe that our customer service team plays a key role in bringing customers the end-to-end support that differentiates us in the market. The ability to speak with a member of our team is often a key part of the customer's experience with us. Our team treats every interaction with our customers as an opportunity to cement our relationship with them for life.

The consistency of the experience we provide would not be possible without the warehouse and logistics footprint we have put in place and the dedicated teams of people we have built to better serve our customers and reduce the anxiety associated with this historically stressful part of shopping for the home.

We have a truly extensive product offering, with over 14 million products from over 11,000 suppliers. We pride ourselves on having great images, descriptions, and most importantly consistently high fulfillment metrics, across this vast product selection.

## **Our Supplier Partners**

Our suppliers are our partners and are paramount to our mission. We couldn't have built the best destination for customers without the time and effort we have invested over these 16 years in our partnerships with suppliers.

They are often small and medium-size businesses with a strong entrepreneurial spirit, trying to grow their business online and offline. For some of them we can be more than 25% of their business and for others we are still less than 1%. Our suppliers are highly skilled in designing, sourcing, manufacturing, and ensuring the quality of home items that they believe will resonate with the changing tastes of consumers, while also meeting functional needs that can often be complex.

For suppliers, our platform is much more than an exchange – it reduces friction between them and our customers, making it easier for both to get what they want. We do not sell branded commodity goods like paper towels or dish soap that are easy to search and describe. We sell complex, emotive, highly considered items. We have built logistics and customer service offerings that suppliers simply do not have the scale or expertise to create – this is a key enabler of their success with us.

We give suppliers tools to access the end customer in a way that is more straightforward and efficient than selling to traditional retailers who are often guessing what customers want and

who seek to serve as an intermediary rather than as a partner. The internet enables openness, and a consistent theme over the last 25 years has been that transparency wins. This does not favor those who try to restrict selection or otherwise impede access.

We develop “self-service” tools for suppliers like data and analytics, merchandising, 3D image creation, and sponsored SKUs. We equip suppliers to easily expose their known best sellers or new product launches to customers quickly and grow their business.

Overall, we aim to help our suppliers win. We do that by investing in capabilities that complement them, rather than compete with them.

## **Brand**

We have always believed superior customer experience drives superior growth, and that belief remains central to how we invest across the business and how our teams prioritize their time. Our brand promise and our ability to deliver on that promise consistently over time has been central to our success.

Since founding the business, the only major pivot we have made in our business was the launch of the Wayfair brand in 2011. At the time Steve remarked, “Imagine if every 10th can of soda that you drank made you ill, it would be impossible to build a brand with that level of inconsistency”. We were thoughtful about not building a brand until we had achieved a consistent customer experience that we felt good about. And every day we aim to root out customer issues in a permanent way so that our level of quality and consistency is continuously on the rise.

We have seen our brand awareness grow considerably as customers learn that they can rely on us. In the U.S. we have close to 90% aided awareness, Canada is at 80%, the UK has quickly grown to over 60%, and in Germany we are seeing promising results from our recently started brand building. Last year, notably, we launched Way Day, which performed extremely well for us, and underlined the power of the brand we have built with customers.

While helping a customer find the perfect item is very hard, the reality is that it is even harder to consistently deliver the implicit “back-end” promise that a brand makes on the front-end of the business to consumers – this is particularly true in our category where the back-end is complex. We could not have reached the scale we have today in the home category without relentlessly focusing on innovating in these areas. To a high degree, our success is also due to the fact that there is no challenge that we have been unwilling to take on. Others view outsourcing as an easy solution to solve their most difficult challenges but we view it as an insufficient way to deliver a winning proposition for our customers over the long-term. You either need to build the world-class solution, or deeply partner to get there.

## **Unit Economics**

We run the business in a practical, quantitative way that delivers economic returns. We bootstrapped the business at the start in 2002, and we did not utilize outside capital for growth

until we were 10 years in and at a scale of ~\$500 million in annual revenue. Until 2011 we only grew the business utilizing free cash flow. This discipline of making sure that we have an economic return on every dollar we invest exists today in everything we do.

The key place where you see this consistency is in the way we protect our unit economics. We have done that from day one, and this discipline is embedded in our culture today.

The core driver of the improving economics in our business is the growth in our repeat customer base, with approximately two-thirds of our orders coming from customers that have shopped with us before.

Future gains in profitability are fundamentally the result of customers repeating with us – by doing all we can to ensure shoppers have a great first experience, we give them reason to come back to us again. As their experience with us builds, it takes less and less advertising spend to remind them that they love us. This growing base of repeat customers drives leverage in both advertising spend and operating expenses, as well as driving gains in gross margin resulting from the associated growth in scale of our business (yielding lower product cost and lower logistics cost).

### **The Future Is Exciting**

Platforms are harder to create than marketplaces. We have had to invest deeply and with a long-term orientation to build the business we have today. We have proven the initial success of the key parts of our platform, many of which we have discussed in this letter. We are being rewarded for these efforts by our growing base of repeat customers, and our resulting scale enables us to keep investing in these initiatives, and to generate very attractive and growing financial returns over time.

The home category has historically been very fragmented, and largely occupied by small and medium-size retailers, often with limited technology capabilities. As a result, we are able to invest in initiatives that others simply have not been able to. Modern technologies (the internet, smartphones, high-speed data, 3D imagery, etc.) have changed the home market in a way that allows a platform like ours to exist and flourish.

We are convinced that someone will be the platform winner in home, and we believe it will be Wayfair. We have invested to be that winner, and it is working. The related unit economics we are seeing have enabled us to be profitable, on an Adjusted EBITDA\* basis, in the majority of quarters over the last two years in the U.S. business, despite very heavy long-term investments. The U.S. business is now of such a scale that its profit potential is clearer to folks externally – and was clearer to us even earlier given the data that we see and use every day.

We are thrilled with the prospects for our business and the team that we have in place to achieve our ambitions. We hope this letter gives you a further sense of the opportunity we see ahead of us and the steps we are taking with customers and suppliers to continue to capture it at a fast pace. With just 1% of the market today, we think that the platform we are building is just getting started.

Thank you for taking the time to read this letter, and thanks for your interest in Wayfair.



Niraj Shah  
Co-founder, Co-chairman & CEO



Steven Conine  
Co-founder & Co-chairman

*\*Non-GAAP financial measure; non-GAAP financial measures should not be considered replacements for, and should be read together with, the most comparable GAAP financial measures. For full financial data and non-GAAP reconciliations, please refer to Wayfair's earnings release issued on February 22, 2019, available at <https://investor.wayfair.com/investor-relations/events-and-presentations/default.aspx>*

*Caution Concerning Forward-Looking Statements: This letter contains forward-looking statements within the meaning of federal and state securities laws. All statements other than statements of historical fact contained in this letter, including statements regarding the strength of our customer offering and delivery experience, the progress of our business in Canada, the United Kingdom and Germany and the parallels to our growth in the U.S., the expansion of our logistics network, our future results of operations and financial position, our business strategy and our plans and objectives of management for future operations, are forward-looking statements. You are cautioned not to rely on these forward-looking statements, which are based on current expectations of future events. For important information about the risks and uncertainties that could cause actual results to vary materially from the assumptions, expectations, and projections expressed in any forward-looking statements, please review the "Forward-Looking Statements" section of the Wayfair earnings release issued on February 22, 2019 as well as the most recently filed Wayfair Reports on Forms 10-K and 10-Q. Wayfair does not undertake to update any forward-looking statement as a result of new information or future events or developments.*