3 Reasons Wall Street Shouldn't Hit the Brakes on Uber and Lyft

Description

Investors are cooling on **Lyft** (NASDAQ: LYFT) and **Uber** (NYSE: UBER), with shares of the two ridesharing leaders hitting new lows this month. Analysts are also cooling on the stock, with at least three Wall Street pros checking in on Thursday with less flattering takes on the two transportation industry disruptors.

Both stocks are now broken IPOs, trading below their debutante prices earlier this year. Let's dive into each of the fresh Wall Street views, countering those analyst notes with a more optimistic perspective on the road ahead.

1. California regulation isn't the end of the industry

Jeffrey Kauffman at Loop Capital is lowering his price targets on the two titans of ridesharing, concerned about the long-term earnings power for the industry given AB5 legislation in California, which will make it more expensive to do business in the country's most populous state. Forcing Uber and Lyft to turn their drivers into employees with guaranteed wages and benefits — and not independent contractors — is going to force the ride-hailing companies into a lose-lose situation. They can't really absorb too much of the incremental costs, as the two companies are already losing billions a year between them. The logical conclusion is that passengers will be the ones bearing the higher costs, as Kauffman believes, and that could price Uber and Lyft out of consumer consideration.

With the cloud of negative demand elasticity looming, Kauffman is lowering his price target on Uber from $54 to $48. His price goal for Lyft is getting a haircut from $60 to $52. He's sticking to his bullish rating on the two stocks, and those revised price targets still offer some upside from the current level. However, let's go down the independent contractor rabbit hole since it's what the gig economy is hinging its existence on these days.

Having to pay out wages and benefits in California and any other states that follow suit would make it more expensive for Uber and Lyft to grant rides, but this is a two-way street. As W-2 employees, Uber and Lyft could exert a bit more control over their reclassified hires in terms of noncompetes, hours worked, and heightened expectations — things that I imagine most drivers would prefer to avoid. We'll see how this plays out, but for now Uber's global diversity makes it less dependent on its home turf than Lyft.

2. Starting lines matter in sizing up lower price targets

Brian Nowak is lowering his price target on Uber from $57 to $53, but that's actually a bullish development. With Uber stock closing at $34 on Wednesday, we're looking at a hearty 56% of upside even at the new lower price goal.

Nowak is naturally sticking to his earlier bullish overweight rating on the stock, and his update is loaded with positives. He is optimistic about the operating details that Uber is providing now that it's breaking down the contributions between ride-hailing and Uber Eats, giving investors more clarity on the business. He's lifting his adjusted EBITDA projections for this year and 2020, despite lowering his bookings estimates. Yes, starting lines matter.

3. Uber and Lyft aren't going away

The third analyst wasn't as upbeat as the other two, who adjusted their price targets to levels well above where the stocks are now. Jim Kelleher at Argus initiated coverage of Uber with a hold rating, arguing that the stock is fairly valued at current levels.

The argument that Uber is worth so much less than its $45 IPO — with Lyft also trading well below its springtime launchpad at $72 — doesn't make a lot of sense. Both companies continue to grow their businesses faster than the transportation industry, so they continue to gobble up market share. Lyft revenue soared 72% in itsÂ latest quarter. Uber is growing much slower, but it's hard to call a company growing its gross bookings at a 31% clip a failure.

We live in a mobile world, and ridesharing has carved out a market of convenience that isn't possible with cheaper mass transit options and a market of value for others relative to the high costs of car ownership for what is a dormant asset most of the day. The trend is there, and it's not going to shift into reverse anytime soon.

Investing in IPOs is risky, but the sell-offs for Uber and Lyft appear overdone. The companies aren't going anywhere, especially given the massive losses they've incurred just to win gold or silver in this race. There's no point in hitting the brakes when the accelerator pedal is just a few inches away.

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