

Snapchat (SNAP)

Attractive

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SNAP 4Q First Look; Clear Positives with App Redesign Front and Center for 2018-Major Prove Me Year Ahead

After the bell SNAP reported much stronger than expected total revenues and pro forma EPS of \$285.7 million and (\$0.13) vs. the Street's estimates of \$253 million and (\$0.16). This eye popping top-line beat was a "shocker" and was a stark contrast to the overwhelming bear sentiment heading into the 4Q print and speaks to a company with strong growth prospects, albeit clear business challenges ahead to iron out in 2018. After much pain that investors have endured since SNAP went public, this quarter was finally a breath of fresh air that gives new life to the SNAP turnaround story in 2018. That said, SNAP added roughly 9 million users this quarter vs. our expectations for 6 million users bringing the company to 187 million DAUs, which represents roughly 20% year over year growth with a trajectory to exceed 200 million users during the course of 2018. Better than expected ARPU of \$1.53 (vs. the Street at \$1.36) will be a major focus of 4Q which we believe will grow 30%-35% YoY in 2018, although still a major Achilles heel which is well below industry norms and a front and center strategic focus going forward for Spiegel & Co as part of the app redesign. Overall, this quarter was a major step in the right direction for the company and will be a tough pill to swallow for all the naysayers that threw in the white towel over the last few months.

While we believe there is modest near-term risk to SNAP's numbers in 2018, our checks with advertisers show that anecdotally speaking trends are slowly moving in the right direction as engagement, pricing, and ad load/inventory should improve during the course of 2018 as the "long overdue" app redesign helps put the SNAP train (hopefully) back on the tracks in our opinion. We note that SNAP's major overhaul of its app design and a key focus of tonight's conference call will make it easier and more intuitive for new users to be attracted to the platform, as the complexity has been a clear inhibitor especially for older demographics (key advertising target market) vs. the likes of Twitter, Instagram, and Facebook. While

DAU and growth remain an uphill battle, we believe heading into 2018 SNAP's multitude of newer organic initiatives (e.g. self service platform, programmatic ad model, app redesign) will start to pay dividends and stabilize growth and start to turn this story around over the coming year with this quarter a great start. That said, SNAP clearly has challenges ahead and a lot of wood to chop on its platform as well as with investors to make sure this transition period and app overhaul leads to brighter days ahead in 2018. It all comes down to monetization in our opinion, and SNAP is going through a painful maturation phase to turn this one trick pony platform into a broader, ad centric consumer app that will enable SNAP to increase ARPU and DAU growth over the next 12 to 18 months. While Facebook remains our clear favorite social media name, we are positive on SNAP as the risk/reward and engagement potential still exists, although now its about the company executing and better monetizing its 187+ million DAUs (trending to be roughly 205-210 by the end of 2018) and growing over the coming year. **We maintain our Attractive rating and \$17 price target on shares of SNAP.**