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Technology Research

Industry Update

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Initial Thoughts on the Tech Earnings "Superbowl" Results; Amazon and Alphabet Bright Stars

Daniel Ives, Head of Technology Research | 917.210.3220 | daniel.ives@gbhinsights.com

Alphabet (GOOG, Highly Attractive, $1,280 Price Target)

- **Rock solid 4Q growth and underlying metrics**. Alphabet reported rock solid 4Q results with total revenues of $25.87 billion beating the Street's $25.6 billion, while EPS of $9.70 came in below the Street's $10.02 on higher expenses and will be a focus of the bears. The star of the show for Alphabet was yet again ad growth (which remains our core focus) as accelerating ad momentum from search and YouTube was a major growth catalyst and enabled the company to handily beat expectations. Importantly paid clicks was up 43% year over year vs. the Street at 42%, which is an eye popping number in our opinion. TAC trends will be a focus this quarter as TAC of $6.45 billion vs. the Street at $6.28 billion, although we expect this to moderate during 2018. This does speak to the company's mobile advertising impression success as this is a key going forward for Google in this very competitive land grab market opportunity. The main growth drivers and key monetization engine for Google/Alphabet into 2018 remain mobile search, YouTube, and overall advertising strength which have clear tailwinds heading into 2018 as evidenced this quarter. We continue to believe YouTube is the major growth driver on the ad front, as this dominant platform now has north of 1.5 billion users watching on average 60 minutes per day. As Google further monetizes this "golden advertising gem" over the coming 12 to 18 months we believe this will be a major growth catalyst that is under appreciated by investors in our opinion and a key driver of ad growth for 2018 and beyond. Overall, we believe solid 4Q earnings (despite higher expenses and TAC costs) and strong enough 2018 guidance could be a positive catalyst for shares despite the knee jerk negative reaction after hours with much fuel left in the growth tank in our opinion. **We maintain our Highly Attractive rating and $1,280 price target.**

- **The advertising kingdom continues to expand.** We continue to believe that improving TAC trends for 2018 are a major part of the Google narrative going forward (will be a focus on the call), as mobile advertising impression success like we saw this quarter holds the key to the advertising kingdom in our opinion. Overall while initiatives around Google Home and the fertile smart speaker market, hardware (Pixel), cloud (recent partnership with Cisco), AI, and Other Bets (Nest, Fiber) are all important growth initiatives to expand the company's growth tentacles on both the consumer and enterprise front for 2018/2019, it all comes down to stellar mobile search and advertising growth with YouTube remaining a key under penetrated asset in the Google product portfolio in our opinion. With the competition for mobile ad dollars becoming fiercer it is becoming incrementally important for Google to successfully monetize its search kingdom, YouTube asset, and mobile impression success in 2018 as the coming year could be a huge leap forward for the company around monetization of its platform. However, this will not be an easy task as we believe Google has some more wood to chop ahead on its "bread and butter" advertising platform/AI capabilities as mobile remains the gateway to its next phase of growth with an increasingly more crowded and price competitive landscape abound which represents an ongoing lingering risk around the name.

Amazon (AMZN, Highly Attractive, $1,500 Price Target)

- **Bezos & Co. deliver another gem.** After the bell Amazon delivered another blow out quarter with total revenues and pro forma EPS of $60.45 billion and $3.75 (not apples to apples with tax and other one time benefits) handily beating the Street's $59.75 billion and $1.88 estimate. North America retail was the focus of the quarter with Amazon having a banner holiday season as the company handily exceeded expectations on this front with a monster Black Friday/Cyber Monday being a major catalyst as Amazon captured roughly 47% of all e-commerce spending during holiday season based on our estimates. International also handily beat which speaks to the company's "land and expand" strategy paying dividends yet again this quarter with strong momentum heading into 2018. As evidenced

Daniel H. Ives
917.210.3220
daniel.ives@gbhinsights.com

this quarter Bezos & Co. have an "iron grip" on e-commerce spending which is showing no signs of slowing down into 2018. While the company does not reveal Prime membership numbers, we believe the company has roughly 90 million Prime members now in its unmatched consumer fortress. Prime growth remains the key jewel for Amazon going forward as cross-selling around Whole Foods customers and putting up more walls/barriers around its growing Prime customer base is a major ingredient in Amazon's ability to fend off competition. International growth on Prime will also be another catalyst that we expect to play out in 2018 and should help further drive better than expected e-commerce retail growth in the year ahead. On another note, AWS revenue of $5.11 billion beat the Street at $4.97 billion as this remains a pillar of cloud strength along with what we saw from Microsoft last night in this two horse race for enterprise cloud success. **We maintain our Highly Attractive rating and $1,500 price target.**

- **Near-term investments for long-term success-the right strategy.** While near-term there is a major focus on significant investments around fulfillment, Prime, Echo/Alexa, AWS, and integrating the Whole Foods acquisition into the fold which could depress margins over the next few quarters with 2018 expense guidance front and center, we believe this is "near term pain for long-term gain" as Amazon has a unique window of opportunity to double down on its consumer and enterprise initiatives for 2018 and drive significant growth/cash flow for the coming years as Bezos & Co. further diversifies the Amazon franchise globally. We believe 1Q guidance was better than whisper numbers and will be a feather in the cap for bulls tomorrow morning. More details around the Whole Foods acquisition strategy and cross-sell opportunities, AWS strength, HQ2 timing, and margin guidance will be focus areas for investors on tonight's call and could be a swing factor on the stock in the near-term with margins key. In a nutshell, Amazon remains one of our favorite secular tech growth stories for FY18 as our GBH Tech Tracker survey/analysis and these robust

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results and 2018 outlook support the Amazon consumer growth thesis, coupled by cloud strength on the AWS segment which is still in the early innings of playing out among enterprises globally on the secular cloud theme.

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