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Company Update

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Regulation and Uncertainty Remain Black Clouds Over FANG Names; All Eyes on the Beltway and Trump's Next Move

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The last few weeks has been a frustrating time for investors in FANG names as the "1-2 punch" of bad news between the Facebook Cambridge Analytica debacle and President's Trump raising the ante on his boxing match vs. Amazon has heightened the risk profile around regulation and government involvement potentially on the horizon for the tech space. For investors in Facebook and Amazon these are two totally distinct regulatory issues which both have wide ranging ramifications, yet together the confluence of these events has proven to be a significant worry for the Street around FANG names, sending a negative ripple effect across tech stocks while quickly compressing multiples given the uncertainty abound. These coming weeks and months will be a defining period for tech stocks and particularly these FANG names as a Street fight between the bulls and bears remains front and center around multiples, risk profiles, regulatory crosshairs, and fundamental strength heading into 1Q earnings season. Fundamentals in the near-term have essentially taken a backseat to the "regulatory albatross" that represents a potential game changing set of actions and policy changes that could create a much more difficult and complex investing landscape for FANG names with the Beltway and Trump laser focused on a host of issues around data privacy/content, advertising transparency, e-commerce tax payments around third-party sellers and state sales taxes, and potentially lingering anti-trust swirling concerns around Amazon. While Facebook and Amazon appear to be front and center in this regulatory storm, the impact from these potential actions and growing noise from politicians, regulators, and President Trump have wide reaching ripple effects across the tech space and have muddied the waters and created uncertainty around a changing risk profile for the overall tech sector. In a nutshell, the FANG names and the Beltway continue to be on a "collision course" in the eyes of the Street, which has been a major blow to the multiples and risk profiles of these names over the past few weeks with investors wondering what is the next shoe to drop out of the Beltway. To this point, we continue to believe the noise and ever-changing headlines coming out the Beltway is creating a black cloud over FANG names in which ultimately the bark will be worse than the bite with the fundamental impact to these names "manageable", and thus would be buyers of FANG names during this period of volatility and regulatory uncertainty.

Further thoughts on the Trump and Amazon tussle. With Trump's tweet about Amazon focused on tax issues and the US Post Office, coupled by media reports that Trump is "obsessed" with Amazon and is exploring anti-trust, regulatory, and potential tax ramifications/changes for Bezos & Co, the Street is now fearful that the long-awaited Trump vs. Amazon battle could finally be on the horizon. The Street is having fears and a high level of angst about reports that Amazon and Bezos has a "bullseye on their backs" with the Trump administration now in the cross hairs, which appears to be gaining steam even with Trump comments/tweets over the weekend reinforcing these issues. Trump has not been secretive about Amazon worries with the US Post Office tweet kicking off a few months ago and last week's news adding gasoline to the fire that Amazon could see more regulation ahead and the stock is seeing significant pressure and volatility accordingly. While it appears the state taxes on collecting from third parties is the current focus of Trump around Amazon as this is viewed to be an unfair advantage vs. competitors along with the US Post Office relationship and distribution arrangement, the Street concerns go broader than these specific issues. The lingering worry is that Trump and influencers within the Beltway could present potential blockades around Amazon expanding further into healthcare/generic drugs and other consumer areas over the coming year on the broader "anti-trust concerns" thesis which has been lingering in the background. While ultimately this is out of Trump's jurisdiction the worries are that regulatory threats could shape some of the decisions coming out of Amazon and Bezos over the coming months, although we continue to believe Bezos has become a MacGyver-like business leader that is already plotting on the white board potential scenarios, roadblocks, and opportunities around expanding into the healthcare vertical in 2H2018 and beyond while further driving the Amazon consumer flywheel. While it's now a hand holding time for Amazon given this new regulatory potential threat with Trump front and center, we believe the reality of these worries altering the company's business model, distribution/logistics strategy, and future tax structure are moderately low and we would be buyers of the name at current levels. **We maintain our Highly Attractive rating and $1,850 price target.**

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Facebook and Zuckerberg navigating hurricane-like headwinds. With news that Mark Zuckerberg will appear and testify in front of Congress (April 12 likely the date) in light of the Cambridge debacle, we view this as another step in the right direction for Facebook to try to calm the public, user, and regulatory choppy waters in this data leak situation. While this will not be a fun experience for Zuckerberg and his team going in front of Congress, it is a necessary smart strategic step for Facebook to head to the Beltway as the public fury continues to grow around the Cambridge data leak which represents the darkest chapter in the company's 14 year history. We note the FTC further investigating Facebook's data collection practices, along with various other lawsuits and states/attorney generals getting into the mix, added further agita to the Cambridge inferno that has created a dark cloud over Facebook's stock the past few weeks. This has just created more worries around the nightmare PR minefield that Facebook and Zuckerberg has encountered post the Cambridge Analytica debacle over the past few weeks which has unleashed a 14% sell off in shares, regulatory chatter/noise coming from the Beltway and EU, Zuckerberg testifying in front of Congress in mid-April, the launch of an expansive FTC investigation, and a #Delete Facebook user campaign which appears to be gaining steam worldwide. With a data leak of 50 million+ users potentially exposed in the Cambridge Analytica situation and growing worldwide criticism of Facebook's handling of this situation, we would characterize this as a "defining period" for Facebook, Zuckerberg, and the Street's ability to navigate through this hurricane-like storm with the company's business model still well intact.

Ending some third-party data partnerships and new safeguards/tweaks to Facebook's privacy policies being announced over the past week are just the tip of the iceberg in our opinion of self-regulated changes coming to Facebook's platform over the coming months in light of Cambridge. While many will fret around near-term user growth/defections and advertising worries with the noise growing louder over the coming weeks, we ultimately believe Facebook can still manage

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this risk during this hand holding period, however this dark chapter has opened up a Pandora's box of bad news that will clearly weigh on shares in the near-term. In a nutshell, 1) this is either a golden buying opportunity to own a unparalleled social media user base of 2 billion+ and advertising fortress of $50 billion annually, ~30% top-line grower the next few years, with $10+ of earnings power in 2020 and a fair value valuation range we believe is between $210 to $240 per share in a year OR 2) the Cambridge fiasco represents a seminal negative moment that will change the future business model and growth trajectory of Facebook with a modest/significant regulatory oversight on the horizon and therefore fair value is in the $150-$170 range. While this is a fluid situation and Zuckerberg & Co. will be heavily tested over the coming months as they navigate this treacherous situation and we will also be keeping a close eye on user defections/engagement and advertising trends through consumer surveys in our GBH Tech Tracker during this crucial period, we ultimately believe Facebook will emerge from this crisis with minimal/moderate regulatory changes and limited financial damage to its user base and advertising kingdom as we remain positive on the name with a compelling risk/reward in shares at current levels. To this point, we believe in a worst case scenario Facebook has roughly $5 billion of annual advertising revenue or 10% of overall revenues "at risk" given the myriad of lower engagement, user growth worries, advertising softness, and regulatory oversight, which is a tough pill to swallow for investors when analyzing risk however this is a "manageable number" in our opinion that the Facebook model could absorb and potentially neutralize over time given its arsenal of monetization engines (e.g. Instagram). While the stock could be range bound over the coming months as Facebook and Zuckerberg walk regulators, users, and advertisers through its data privacy/content procedures and making sure the Cambridge issue will never be repeated, we believe the stock should ultimately make the climb back to the $180-$200 range as the dust settles over the next few quarters with fundamentals remaining on track, despite this clear white knuckle period that lies ahead. **We maintain our Highly Attractive rating and $225 price target.**

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