

Company: Alphabet Inc	Ticker: GOOGL	Current Price: \$ 1103	Industry: Technology - Internet	
Target Price: \$1400	TTM P/E: 61.94	Beta: 1.13	Market Cap: \$770.852B	
Stop Loss: \$952(15%)	Forward P/E: 22.83	Credit Rating: AA+ (S&P)	Avg Vol (3M): 1.86m	
52 Week High/ Low: \$824 / \$1198	EPS: \$18.00	Rating Outlook: Stablera	Dividend Yield: N/A	

Company Background:

Alphabet is a collection of businesses -- the largest of which, of course, is Google. It also includes businesses that are generally pretty far afield of our main Internet products such as Access, Calico, CapitalG, GV, Nest, Verily, Waymo, and X.

Industry Outlook:

Alphabet is involved in a variety of business which makes the industry outlook particularly difficult. Looking at their main source of revenue, Advertising, and it's outlook however, we see tremendous upside with Alphabet. Their largest competitor in this space in Facebook, and together they control more than 70% of all online advertisements. Alphabet is in a much better position than Facebook however to continue growing as they also control the entire ecosystem through which ads are delivered via their Chrome web browser which has a penetration rate of greater than 55% as well as their Android OS mobile operating system which is run on more than 85% of all mobile devices. By controlling the ecosystem they can make certain restrictions to the outside ads that are displayed, such as auto-playing video ads, which will in turn drive more advertising dollars towards Alphabet in addition to enhancing the user experience. Looking at the outlook for some of the Other Bets, such as Nest, the Home Automation market is poised to see tremendous growth as Millennials continue purchasing homes, and they should expect a CAGR of 19%. Waymo is said to be leading the pack in terms of autonomous vehicle software, so regardless of how Alphabet chooses to leverage that, either via licensing the software or entering the Ride Hailing market themselves, it is sure to provide a bountiful return for investors.

Investment Thesis:

Our recommendation is a buy with a target price of \$1400 (27% upside). Alphabet was hit hard with the one-two punch of an earnings call On February 1st, followed shortly thereafter by the Market Correction on Feb 2-8. The earnings results, while showing strong growth, the company opted to significantly increase their tax burden for FY2017 which had a severely negative impact on EPS and Net Income. This was obviously terrible news for those already holding the equity however combined with the correction it represents a very opportunistic entry point. With revenue growth continuing to expand in future years, and overall Profit soaring, Alphabet is in a strong position to be able to expand their current offerings, as well as invest in 'Other Bets' to diversify their revenue streams. Whether that means organic growth through additional R&D for subsidiaries like Nest and Waymo, or inorganic growth via acquisitions ranging from a ride-sharing application to a life-sciences company. Alphabet is willing to take a chance on anything it thinks can drive future revenue and help advance the population they serve

Investment Risks:

- Other bets, and specifically Waymo do not provide a sufficient first-mover advantage, leaving Alphabet behind
- Failure of Alphabet to innovate for "next" product or service. Competition is fierce and a lack of innovation can drive the stock price lower.
- Antitrust litigation force Alphabet to divest some of their other holdings outside of the core Advertising business.
- The Overreliance of advertising revenue. While Other Bets are helping to diversify earnings, 86% of all revenue is a result of advertising.
- New Regulations that disrupt how Alphabet operates its core businesses, such as General Data Protection Regulation being implemented in the EU can continue to have a negative impact.

Most recent quarter financial highlights (July- Sept 2017):

- 2017 revenues of \$110.9 billion, up 23% year on year, and fourth quarter revenues of \$32.3 billion, up 24% year on year.
- The Board of Directors authorized the repurchase of \$8B worth of stock.
- The recent tax act resulted in a one-time transition tax of \$9.9B to repatriate foreign earning as well as deferred tax impacts. This drove EPS (\$-4.35) and Net Income (\$-3B) significantly down and resulted in an effective tax rate of 138% for 2017
- Operating Income continues to rise from \$6.6B in 2016 to \$7.6B in 2017.

Financial Performance:

Millions USD	2013	2014	2015	2016	2017	2018 Est	2019 Est
Revenue	55,519	66,001	74,989	90,272	110,855	106,784	124,905
Operating Profit	33,565	40,688	46,825	55,134	65,272	77,592	90,479
Net Income	13,181	13,746	16,074	19,657	25,424	36,495	42,663
Revenue Growth %	20.6%	18.9%	13.6%	20.4%	22.8%	-3.7%	17.0%
EBITDA%	35.09%	33.11%	32.57%	33.08%	32.29%	48.23%	48.24%
Operating Profit %	60.46%	61.65%	62.44%	61.08%	58.88%	72.66%	72.44%
Net Income Margin	23.74%	20.83%	21.43%	21.78%	22.93%	34.18%	34.16%
D/E	0.02	0.02	0.01	0.01	0.01	n/a	n/a
EPS	19.45	19.99	23.17	28.09	35.00	48.69	60.02
PE Ratio	28.81	26.55	33.57	28.21	30.10	22.87	18.55
Current Ratio	4.58	4.69	4.67	6.29	5.14	n/a	n/a
ROE	16.01	14.79	14.12	15.02	8.69	n/a	n/a
ROA	12.44	11.77	11.82	12.37	6.94	n/a	n/a
Dividend P/S	0	0	0	0	0	0	0
FCF	11,301	11,417	16,622	25,824	23,907	31,774	38,074

Discounted Cash Flow

	2012-17	2018-22
Avg Revenue growth	19.3%	10%
Avg EBITDA Margin	33.24%	48.2%
Avg Net Income Margin	22.12%	34.2%
Avg Debt/Equity	0.005%	0.005%
Avg FCF / EBIDTA Margin	67.69%	62.44%
Cost of Debt		2.7581%
Tax Rate		36.4%
Cost of Equity		9.68%
WACC		9.64%
Perpetuity growth rate		2.5%

Analyst Opinion

Buy:38	Hold: 5	Sell:0
Target Price Range	1000-1475	Avg. 1277.56

Source: Bloomberg

Relative Valuation

	Facebook	Amazon	Apple	Netflix	Industry Median*
P/E	28.86	325.35	18.08	213.07	30.94
P/B	7.33	23.39	4.71	17.23	7.33
Dividend Yield	n/a	n/a	1.45%	n/a	1.45%
Revn Grth	47.09%	30.8%	6.28%	32.41%	30.8%
NI Grth	78.54%	-5.49%	10.39%	219.74%	29.34%
Operating Margin	49.69%	2.31%	26.67%	7.51%	26.05%
Debt / Equity	0%	159.32%	86.3%	181.45%	86.3%
Market Cap	520B	717B	880B	123B	717B
Revenue TTM	40.65B	177.87B	238.54B	11.69B	110.86B
Net Income TTM	15.92B	3.03B	50.52B	558.93B	12.66B
FCF TTM	17.48B	7.79B	54.91B	-1.99B	17.48B

Total Return

	GOOGL	FDN (Internet ETF)	S&P 500
YTD	3.46%	10.83%	1.64%
2017	32.93%	37.5%	19.33%
Last 2 Years	54.97%	90.8%	40.56%
Last 5 Years	178.06%	193.8%	83.8%

CSR Characteristics

	GOOGL	Industry
Governance Disclosure Score	57.14	n/a
ESG Disclosure:	42.15	n/a
Social Disclosure Score	19.3	n/a
Environmental Disclosure Score	45.74	n/a

Data: Bloomberg data of FY 2016 (CSR)

* Resource: Bloomberg, all data updated to the latest quarter except for Revenue, Net Income, and FCF