

## Alphabet

## Cost focus not one and done, more layoffs

Maintain Rating: BUY | PO: 166.00 USD | Price: 142.08 USD

## Layoffs continue in Year 2 of cost management

Alphabet has reportedly eliminated hundreds of positions from its core engineering division, Google Assistant (voice-operated virtual assistant), and hardware division that makes Pixel phone, Fitbit watches and Nest thermostat. Most of the employees affected in the hardware team included those working on augmented reality projects. In the statement, Alphabet said "We're responsibly investing in our company's biggest priorities and the significant opportunities ahead." Our Take: We think many of these jobs will be replaced by AI engineers.

## Cost discipline could entail more layoffs in 2024

According to a report by Information (in late Dec'23), Alphabet is also planning to reorganize its ad sales unit (~30,000 employees) as a result of company's recent advances in AI and strong advertiser adoption of automated tools such PMax. The report suggests many of the jobs in the ad sales unit could become redundant because of new AI/ML tools that can automatically suggest and create new ads. We would expect Alphabet to shift some S&M and G&A jobs to engineering in 2024.

## Maintaining expense discipline key for sentiment

Alphabet has indicated an intention to grow revenues faster than expenses and, given growing cost of sales expense, we expect further reorganization efforts to keep headcount growth to low/mid single digits. For 2024, Street estimates Alphabet will add ~12,000 employees (up 6% y/y) but potential reorganization could change the trajectory of headcount growth. Assuming a cost of \$300k per head, each 1,000 headcount saved could add \$250mn in after tax earnings or \$0.02 to EPS. More importantly, stock sentiment turned more negative after 3Q results which included elevated R&D and G&A costs, and evidence of new expense savings initiatives could bring back the expense savings EPS upside case.

## Ad recovery, AI &amp; reduced costs likely to drive EPS upside

We remain positive on Alphabet and expect strong 4Q Search and YouTube growth to indicate ad recovery remains on track. Also, search upside could help partially address the top concern on the stock, in our view, that the value of search may be eroded by AI provided information on other sites. We also think Street may be underestimating the complexity of AI queries, the advantages of scale for AI, and potential monetization benefit over time. At the stock price of \$143.67, Google's core business is valued at 14x core 2025 EPS in our SOTP, which we see as an attractive discount to the S&P at ~17x. Risks for 2024 include any indications of erosion of search queries from AI usage elsewhere, increasing regulatory headwinds (DMA/DSA enforcement in Europe), adverse judge ruling in the ongoing DOJ search distribution case or Google Play case, and LLM integration disruption to search revenues due to lower ad loads and monetization. 4Q headline expense risks include Sunday Ticket and legal settlement costs. Maintain Buy and \$166 PO.

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**Refer to important disclosures on page 3 to 6. Analyst Certification on page 2. Price Objective Basis/Risk on page 2.**

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## Stock Data

Price (NAS / NAS)	142.08 USD / 143.67 USD
Price Objective	166.00 USD / 166.00 USD
Date Established	11-Dec-2023 / 11-Dec-2023
Investment Opinion	B-1-9 / B-1-9
52-Week Range	88.58 USD - 145.22 USD
Market Value (mn)	1,870,761 USD
Free Float	99.6%
Average Daily Value	4104.88 USD
Shares Outstanding (mn)	13,167.0 / 13,167.0
BofA Ticker / Exchange	GOOGL / NAS
BofA Ticker / Exchange	GOOG / NAS
Bloomberg / Reuters	GOOGL US / GOOGL.OQ
ROE (2023E)	35.2%
Net Dbt to Eqty (Dec-2022A)	3.0%
ESGMeter™	High

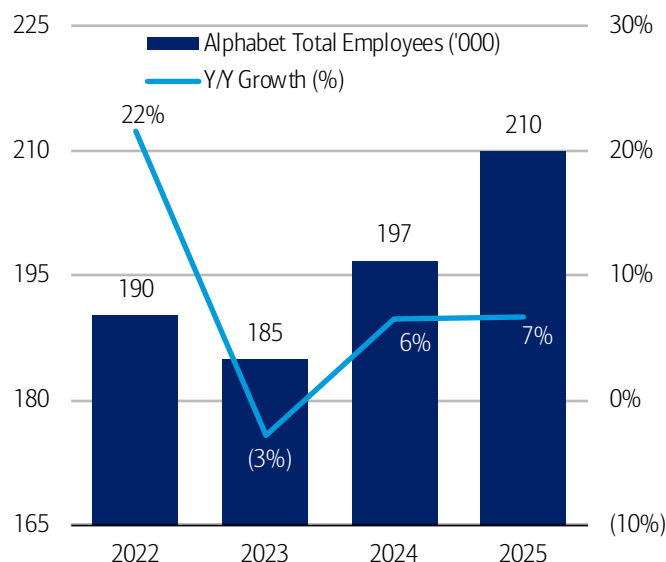
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TPU: Tensor processing unit  
LLM: Large Language model  
R&D: Research and development  
SGE: Search Generative Experience  
GCP: Google Cloud Platform  
ROI: Return on Investment  
AI: Artificial Intelligence  
ML: Machine Learning  
PMax: Performance Max  
DMA: Digital Marketing Act  
DSA: Digital Service Act  
DOJ: Department of Justice  
S&M: Sales and Marketing  
G&A- General & Administrative

# Alphabet Headcount & Opex/Employee

## Exhibit 1: Alphabet Total Employees (Street Estimates, '000)

In 2024, Alphabet is expected to add 12K employees.

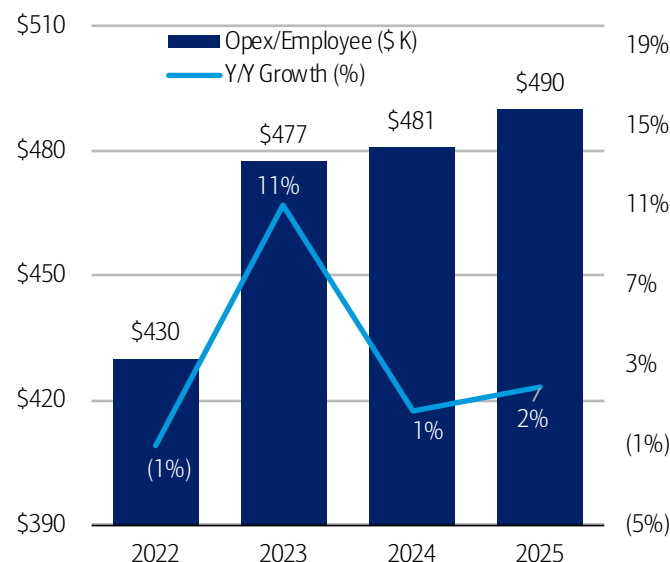


Source: Visible Alpha and Company Filings

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## Exhibit 2: Total Opex/Employee (Street Estimates, '\$ 000)

Alphabet Opex/employee is expected to grow 1% y/y to \$481K.



Source: Visible Alpha and Company Filings

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## Price objective basis & risk

### Alphabet (GOOGL / GOOG)

Our price objective of \$166/\$166 is based on 20x 2024E core Google GAAP EPS plus cash. Alphabet has traded at an average multiple of 22x GAAP P/E over the last ten years and we think our multiple is reasonable vs. history given expectations for slower, but still 10%+ revenue growth in future years.

Risks for the stock include: 1) Still volatile macro and geopolitical backdrop may impact ad spend in 4Q, 2) LLM integration in search may take longer than expected or negatively impact search revenues, 3) concerns related new regulatory framework in the European Digital Markets Act (DMA), 4) adverse judge ruling on the ongoing DOJ search distribution trial, 5) potential for increasing Capex and lower FCF given AI focus.

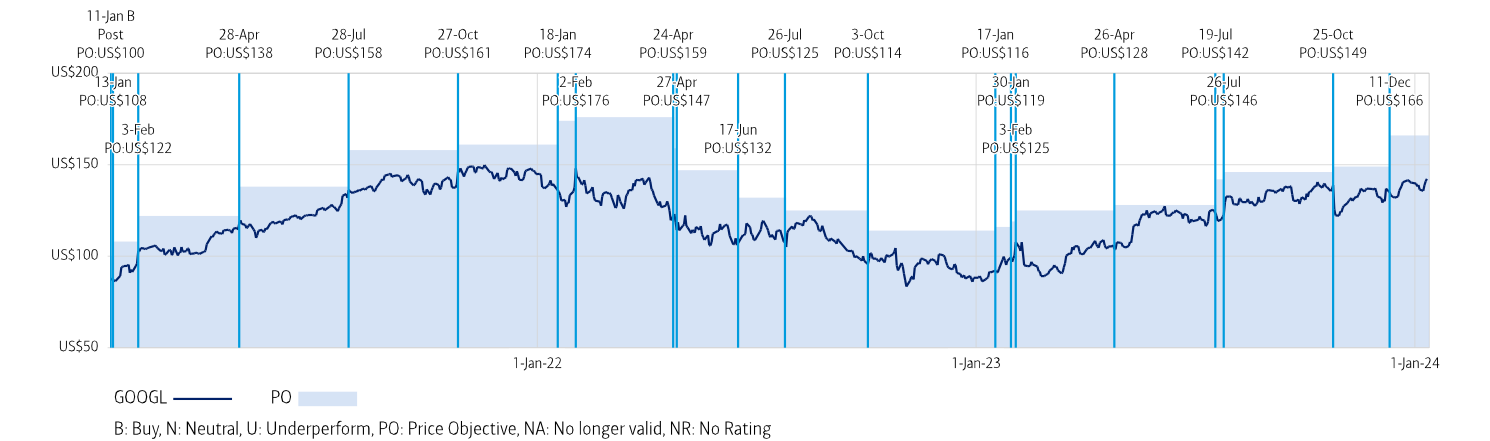
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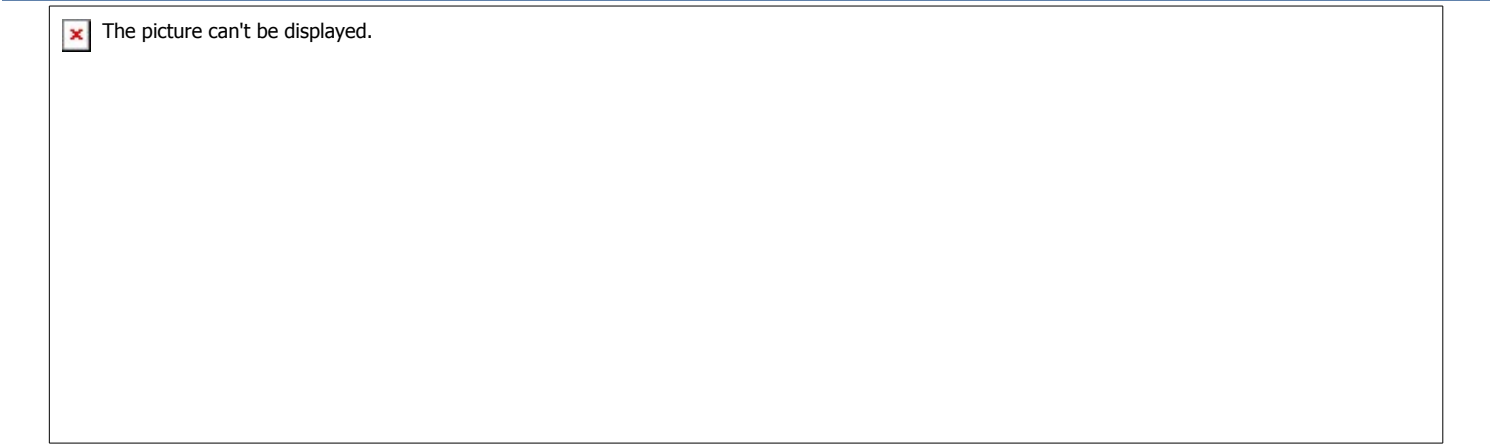
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### Alphabet A (GOOGL) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

### Alphabet C (GOOG) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

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Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

### Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
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Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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