

Company Name: Alphabet Inc
Company Ticker: GOOGL US
Date: 2018-02-01
Event Description: Q4 2017 Earnings Call

Market Cap: 774,899.61
Current PX: 1119.20
YTD Change(\$): +65.80
YTD Change(%): +6.246

Bloomberg Estimates - EPS
Current Quarter: 12.031
Current Year: 50.701
Bloomberg Estimates - Sales
Current Quarter: 24055.500
Current Year: 105590.407

Q4 2017 Earnings Call

Company Participants

- Ellen West
- Ruth Porat
- Sundar Pichai

Other Participants

- Eric J. Sheridan
- Heather Bellini
- Douglas T. Anmuth
- Brian Nowak
- Anthony DiClemente
- Daniel Salmon
- Colin Alan Sebastian
- Michael B. Nathanson
- Ken Sena
- Stephen Ju
- Justin Post
- Benjamin Schachter

MANAGEMENT DISCUSSION SECTION

Ellen West

Financial Measures

During this call, we will present both GAAP and non-GAAP financial measures

A reconciliation of GAAP to non-GAAP measures is included in today's earnings press release

Ruth Porat

We had a fantastic 2017 with total revenues of \$110.9B, up 23% over 2016 and operating income of \$28.9B, up 22% year-on-year, excluding the EC fine

Our momentum reflects a relentless focus on users, advertisers and enterprise customers, as well as the benefits of our commitment to long-term investing

For Q4, revenues of \$32.3B were up 24% year-on-year

The ongoing very strong performance in sites revenue, in particular, reflects the combined benefits of innovation and secular growth with mobile search again leading the way

Healthy growth in network revenues was again led by our programmatic business

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Substantial growth in other revenues, namely hardware, cloud and play, continues to highlight the benefits of our investments

Our outline for today's call is, first, I'll review the quarter on a consolidated basis for Alphabet, focusing on y-over-y changes

In order to facilitate comparisons of this quarter's results to prior periods, we have also provided the tax affected line items, excluding the impact of the U.S. tax legislation enacted at the end of 2017

You can see the components in our earnings press release

Second, I will review results for Google and then Other Bets

I will then conclude with our outlook

Sundar will then discuss business and product highlights, after which we will take your questions

Financial Results

Regional Revenues

- Starting with the summary of Alphabet's consolidated financial performance for the quarter
- Total revenues of \$32.3B were up 24% y-over-y and strong across all regions:
- U.S. revenues were \$15.4B, up 21% y-over-y
- EMEA revenues were \$10.3B, up 24% y-over-y
- In fixed FX terms, EMEA grew 22%, reflecting strengthening of both the euro and the British pound
- APAC revenues were \$4.7B, up 30% vs. last year and up 32% in fixed FX terms, reflecting weakening of the Japanese yen
- Other Americas revenues were \$1.9B, up 31% y-over-y and up 30% in fixed FX terms, reflecting strengthening of the Canadian dollar

Revenue Contributors

- On a consolidated basis, total cost of revenues, including TAC, which I'll discuss in the Google segment results, was \$14.3B, up 34% year-on-year
- Other cost of revenues on a consolidated basis was \$7.8B, up 34% y-over-y, primarily driven by Google-related expenses
 - Specifically cost associated with our data centers and other operations, including depreciation, hardware-related costs for our expanded Made by Google family of products and content acquisition costs, primarily for YouTube

OpEx Stock-Based Compensation and Headcount

- Operating expenses were \$10.4B, up 19% y-over-y, in particular, reflecting an increase in marketing spend given the holiday season
- Stock-based compensation totaled \$1.8B
- Headcount at the end of the quarter was 80,110, up 2,009 people from last quarter

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- As in prior quarters, the majority of new hires were engineers and product managers
- In terms of product areas, the most sizable head count additions were once again made in cloud for both technical and sales roles, consistent with the priority we place on this business

Operating Income and Margin

- Operating income was \$7.7B, up 15% vs. last year and the operating margin was 24%
- Other income and expense was \$354mm
- We provide more detail on the line items within OI&E in our earnings press release

Net Income and EPS

- Our provision for income taxes on a reported basis includes \$9.9B for items associated with the U.S. tax legislation, resulting in a reported net loss of \$3B and loss per diluted share of \$4.35
 - Excluding the impact of the U.S. tax legislation, our effective tax rate was 15%
- Our net income was \$6.8B and earnings per diluted share were \$9.70

CapEx and Operating Cash Flow

- Turning now to CapEx and operating cash flow
- Cash CapEx for the quarter was \$4.3B
- Operating cash flow was \$10.3B with FCF of \$6B
- We ended the quarter with cash and marketable securities of approximately \$102B

Segment Financial Results

Google Segment

Revenue Contributors

- Let me now turn to our segment financial results; starting with the Google segment
- Revenues were \$31.9B, up 24% y-over-y
- In terms of the revenue detail, Google Sites revenues were \$22.2B in the quarter, up 24% y-over-y, led again by mobile search, complemented by solid growth from desktop search and strong performance from YouTube
- Network revenues were \$5B, up 13% year-on-year, reflecting the ongoing momentum of programmatic and AdMob
- Other revenues for Google were \$4.7B, up 38% y-over-y, fueled by hardware, Cloud and Play

Total Traffic Acquisition Costs and Advertising Revenues

- Finally, we continue to provide monetization metrics to give you a sense of the price and volume dynamics of our advertising businesses

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- You can find the details in our earnings press release
- Total traffic acquisition costs were \$6.5B or 24% of total advertising revenues and up 33% y-over-y
- The increase in sites TAC as a percentage of sites revenues, as well as network TAC as a percentage of network revenues continues to reflect the fact that our strongest growth areas, namely mobile search and programmatic, carry higher TAC

Total TAC

- Total TAC, as a percentage of total advertising revenues, was up y-over-y, reflecting primarily an increase in the sites TAC rate, which was modestly offset by a favorable revenue mix shift from network to sites
 - The increase in the sites TAC rate y-over-y was driven by changes in partner agreements and the ongoing shift to mobile, which carries higher TAC because more mobile searches are channeled through paid access points
- The underlying trend affecting the network TAC rate y-over-y continues to be the shift to programmatic, which carries higher TAC

Stock-Based Compensation and Operating Income

- Google stock-based compensation totaled \$1.7B for the year, up 1% y-over-y
- Operating income was \$8.8B, up 11% vs. last year and the operating margin was 27%
- Accrued CapEx for the quarter was \$3.8B, reflecting investments in production equipment, facilities and data center construction

Other Bets Business

- Let me now turn and talk about Other Bets
- I'll cover results for the full year 2017 because it remains most instructive to look at financials for Other Bets over a longer time horizon as discussed on prior calls
- Results for the quarter are in our earnings release

Revenues and Operating Loss

- For the full year 2017, Other Bets revenues were \$1.2B, up 49% vs. 2016, primarily generated by Nest, Fiber and Verily
- Operating loss was \$3.4B for the full year 2017 vs. an operating loss of \$3.6B in 2016
- Other Bets accrued CapEx was \$507mm, down from \$1.4B in 2016, primarily reflecting a reduced investment in Fiber

Nest Products

- We're pleased with our progress across Other Bets
- A couple of updates

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- Nest turned in a strong holiday performance in Q4 across an expanded family of products in energy, safety and security
- In 2017, Nest products also became available in 12 new countries, more than double the number in 2016

Verily

- Verily wrapped up its first field study, seeking to reduce the transmission of diseases through mosquitoes with positive results, and just last week, Onduo, a joint venture between Verily and Sanofi, began a limited commercial launch of its diabetes management platform

Waymo

- At Waymo, progress is accelerating
- For example, Waymo surpassed 4mm miles of driving in the real world, taking only six months to achieve the last million miles compared to about 18 months for our first million miles
- And in November, Waymo announced that it is the only company to have a fleet of driverless cars on public roads that are completely autonomous without anyone in the driver seat

Business Priorities and Long Term Outlook

Let me close with some observations on our priorities and longer-term outlook

Our 23% revenue growth in 2017 was powered in particular by the ongoing extraordinary performance of our sites business

Mobile and Desktop Search

- Both mobile and desktop search continue to grow and benefit from our approach to innovation with strong momentum, as we identify additional opportunities to enhance the user and advertiser experience
- As we've consistently emphasized, alongside the continued momentum in our advertising business, we are focused on building a second wave of growth within Google over the medium and long term, which includes the rapidly growing revenue businesses in Google; Cloud, hardware and YouTube

Cloud

- With respect to Cloud, we are seeing the benefits of a fully featured enterprise offering and an expanded go-to-market team, bringing our advantages in infrastructure, data analytics, security and machine learning to more customers
- And we're pleased with the momentum in our hardware business in 2017, driven by an expansion in both our product line and geographic availability

Other Bets Businesses

- Finally, as we look further into the future for our third wave of growth, we remain excited about the longer-term potential for our Other Bets businesses

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- Overall, operating income was up 22% y-over-y in 2017, excluding the impact of the EC fine, although there was obviously fluctuation in the rate of operating income growth quarter-to-quarter
- Within cost of revenues, the biggest component is traffic acquisition cost, reflecting our strong revenue growth in mobile search and the fact that mobile search carries higher TAC than our desktop business
 - While we expect sites TAC to continue to increase as a percentage of sites revenue reflecting ongoing strength in mobile search, we anticipate that the pace of y-over-y growth in sites TAC, as a percentage of sites revenue, will slow after Q1 2018
- Within OpEx, we are keenly focused on prioritization in order to optimize the resources we're investing for longer-term growth
- As I discussed on last quarter's call, marketing spend in Q4 is significantly elevated, in particular supporting hardware, but also across Cloud and YouTube

Investments

- For 2018, we remain excited about the investments we are making to drive the next phase of growth in our big bets in Google, in Cloud, hardware and YouTube, and our machine-learning efforts, which are powering innovation across our businesses
- You'll see us continue to support our priority areas with increased head count, which will remain concentrated in R&D
- With the closing of our deal with HTC earlier this week, for example, we've added 2,000 employees to support our hardware business

SBC

- With respect to SBC, we've completed the transition to a single annual compensation cycle for employees with a full year equity refresh grant to employees in Q1 2018
- Our biannual grant to SVPs will also occur in Q1, and you will see the combined step-up in our first quarter results
- For our Other Bets in 2018, we will continue to calibrate the magnitude and pace of investment appropriate to their individual execution path

Capital Allocation

- Finally, our framework for capital allocation is unchanged from our prior discussions
- The primary use of cash continues to be to support organic growth in the business
- We're excited about the significant opportunities we've identified in our businesses and continue to invest appropriately
 - We then layer in a sensitivity analysis regarding potential M&A as well as CapEx, in particular, computing infrastructure to support the needs of these growing businesses
- The most sizable catalyst for added investment in compute power include the expanding application of machine learning efforts across Alphabet, as well as additional requirements for Google's cloud, search and YouTube businesses
 - This framework further considers complementary uses such as the share repurchase

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- After taking these potential investments into account, our board has decided to extend our share repurchase program up to an additional \$8.6B of Class C capital stock

Conclusion

- In conclusion, 2017 was another great year, and we are very excited about the opportunities ahead

Sundar Pichai

Business Perspective

Our teams are off to a great start in 2018

This year is special as it will mark 20 years since Google was founded

A lot has changed, but our mission, organizing the world's information and making it universally accessible and useful, remains the best guide for the next 10 years

Technology is an incredibly dynamic industry

Investments

- We've been laying a foundation for the next decade as we pivot to an AI first company, powering the next generation of Google products, like the Google Assistant
- And we have been making substantial investments in our three biggest bets:
 - Cloud
 - YouTube
 - And hardware
- These bets have enormous potential, and already, they are showing real momentum and gaining traction

Google Cloud

- Today, I'll start by sharing some of the exciting progress in these three big bets
- First, Google Cloud; Google Cloud, which includes Google Cloud Platform and G Suite has reached meaningful scale
- And I'm excited to share today that it's already \$1B per quarter business
 - In fact, we believe that Google Cloud Platform, based on publicly reported data for the 12 months ending December 2017, is the fastest growing major public cloud provider in the world

Strategic Customer Deals

- We're also increasingly doing larger, more strategic deals with customers
- In fact, a number of deals worth over \$1mm across all cloud products more than tripled from 2016 to 2017

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- The strength of our products and the value of working with Google is increasingly clear to partners and customers

Partnership Collaborations

- In Q4, we forged new and deepened existing partnerships with industry leaders, including:
 - Cisco, for open hybrid environments
 - Salesforce, for customer insights and productivity
 - And SAP, for AI and data insights across their products
- These collaborations span our entire companies from engineering integration to marketing programs to joint sales, and they cover Google Cloud Platform, G Suite and Google Analytics
- We also saw accelerating customer traction, and our wins included global brands like:
 - Bed Bath & Beyond
 - Dentsu Aegis Network
 - Keller Williams
 - Mattel
 - And Tyco Retail Solutions
- And underscoring the increasing importance of Google Cloud to the enterprise, we surpassed another new milestone, 4mm paying customers on G Suite

YouTube

- Next, YouTube
- Every month, more than 1.5B people come to YouTube to watch their favorite content on channels ranging from The Ellen Show, which has more than 22mm subscribers, to the NBA with over 8mm subscribers, to SciShow, a really popular educational channel with more than 4.5mm subscribers
 - In fact, there are over 1B learning-related video views everyday on YouTube, I learned that this week
- With all this great content, people are thinking of YouTube more as a key part of their TV viewing experience
- For Tuesday night's State of the Union, more partners used YouTube to live stream the address than ever before, generating 5mm live views
- And just yesterday, we announced a partnership with Major League Soccer's, LA Football Club
- YouTube TV will be the exclusive home to watch all locally televised English language matches in addition to their original programming and content
- YouTube TV is now also available on Roku
- There is great momentum around the world with localized versions of YouTube now in 90 countries in 80 different languages

YouTube Go App

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- Just this morning, we announced that we are expanding the popular YouTube Go app to over 130 countries around the globe
- The app has great data usage transparency and controls built in, which is especially useful for people living in regions with limited connectivity

New Licensing Deals

- In Q4, we also strengthened our relationship with the music industry, signing new licensing deals with Sony Music Entertainment and Universal Music Group
- We also partnered with Ticketmaster to help fans buy tickets to see their favorite artist perform live

Hardware Business

- Third, our growing hardware business
- Our Made by Google hardware products were very popular this holiday season
- Device shipments in Q4 have more than doubled y-over-y
- Our retail partners also saw strong performance
- Our devices are available in stores like:
 - Best Buy
 - Target
 - And Walmart
- I'm especially excited about the popularity of our Google devices for the home, like the Google Home Mini, Max and Chromecast
- In the last year, we have sold tens of millions of these devices and counting
- I want to call out the great work of our marketing and design teams
- Our hardware is beautiful individually and as a family, and people love discovering the unique features like the built-in Google Assistant
- Earlier this week, we officially closed our deal with HTC, which will bring great talent to drive even more innovation in the years to come

Google Assistant

- Turning to our efforts in machine learning
- Our AI research and innovation leads the world
- Our mission to better organize the world's information has been transformed by these technologies with our search products and the Google Assistant at the heart
- There's great momentum around the Google Assistant, as we bring it to more people on more devices
- It's now available on more than 400mm devices, including speakers like Google Home, as well as Android phones and tablets, iPhones, headphones, televisions, watches and more

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- People love to use the Assistant on all these devices
- There was a lot of excitement around the Google Assistant at CES from partners and consumers, where we brought the Assistant to new surfaces, like smart displays from brands like JBL and Lenovo, as well as Android Auto, which is now available in more than 400 car models from brands like GM, Hyundai, and Volvo

Photography Advancements

- One area that's really benefiting from our advancements in AI is photography
- The Pixel 2 phone is the leader in video rankings by industry standards with smoother and clearer videos, thanks to machine learning and our video stabilization technique
 - And Google Photos continues to go from strength to strength
- On New Year's Eve alone, over 3B photos and videos were uploaded to Google Photos
- More broadly, we want everyone to be able to use machine learning for their own needs
- We recently gave Google Cloud customer's access to AutoML, which makes it far easier to build complex new enrollments
- Since it launched a few weeks ago, over 10,000 customers have already signed up to try it

Computing and Advertising Platforms

- Lastly, I'll give a quick update on our computing and advertising platforms
- First, Android; to provide a better, more tailored experience for our next billion users, we made Android Oreo Go edition available for our device partners
- This year, we expect to see Go devices from dozens of manufacturers and with great support from mobile operators and app developers around the world
 - I'm confident that this will bring the power of smartphones to many more people for the first time
- Google Play is also growing well
- Just last week, we introduced audiobooks, so you can now catch up on your favorite books any time on multiple devices
- And in Latin America, number of unique monthly buyers on Google Play grew by over 50% y-over-y in 2017
- Chromebooks also continue to gain momentum and traction
- Third-party research tells us that fourth quarter sales of consumer Chromebooks in the U.S. grew by over 70% y-over-y

Advertising Platforms

- Moving to our advertising platforms, which help large and small businesses
- As shoppers turn to their mobile phones this holiday shopping season, Google was central to helping them discover new brands, compare products and find the best deals

Mobile Shopping Experience Redesigned

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- We redesigned the mobile shopping experience on Google, bringing more product information to the forefront like reviews and ratings
- We are also making the payments experience simpler, safer and more consistent
 - We brought our payments efforts together as a new Google Pay, which shoppers can use to pay online in stores and across Google products like Chrome and the Play Store
- Companies like Airbnb and Instacart are using Google Pay to speed up mobile check out
- And HotelTonight found that customers using Google Pay are 65% more likely to complete their bookings

App Promotion Campaigns

- We also have really strong momentum in app promotion ads
- The majority of our app promotion campaigns are now using universal ad campaigns, which is part of our focus on simplifying the advertiser experience
- Additionally, we introduced a new playable ad format in Google Play that allows users to sample games before they install
- Ads and Google Play are performing really well for developers
- And our app promotion business on YouTube is flourishing

Major Initiatives

- We launched major initiatives, such as store visit measurement and location-based ad formats, to drive online to off-line commerce
- We're focused on making sure YouTube is a great place for users and advertisers, while helping creators earn money from popular content

Changes to Advertising on YouTube

- In addition to the significant work we are doing to protect users and stop abuse on the platform, just a few weeks ago, we announced changes to advertising on YouTube, including stricter monetization criteria, new manual reviews for all videos in Google Preferred, and simpler controls for marketers
- The feedback we have received from advertisers and creators so far has been really positive
 - So as you can see, we are making great strides in our biggest bets, and I'm proud of the work we are doing across the company

Business Contributions

- I'm also incredibly proud that as Google grows, we are making significant contributions to our partners, the economy and our local communities
- Our business continues to benefit our partners around the world
- This includes news publishers, app developers and YouTube creators, who we share revenue with
- Over the last four years, our partners have earned over \$100B, that's incredible, and we are working on new ways to drive even more value to our partners

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New Offices and Data Centers

- In the U.S. specifically, we have offices and data centers across 21 states, and we plan to hire thousands of people across the U.S. this year
- Last year in the U.S, we grew faster outside the Bay Area than in the Bay Area
- To support this growth, we'll be making significant investments in offices across nine states, including Colorado and Michigan
- We'll also be building or opening five big new data centers in the U.S

Grow with Google Initiative

- And with digital skills and high demand by employers, our Grow with Google initiative will help jobseekers and small businesses gain education and skills to help them succeed
- Just a couple of weeks ago, we announced that we are creating an IT support certification program that will give thousands of people scholarships and job opportunities
- More than 10,000 people have already signed up, which is amazing

Recognition

I want to thank all our employees, Google users, partners and advertisers around the world

I couldn't be more excited about what's in store for all of us this year

QUESTION AND ANSWER SECTION

<Q - Eric J. Sheridan>: Maybe two, one for Sundar, one for Ruth. Sundar, coming out of CES and the success you had with Google Home and the Google Assistant during the holiday period based on the blog post you guys put out, can you identify some of the key investments in either partnerships, or hardware, or capabilities that you're targeting over the next one to two years to make sure the momentum around Assistant is sustained?

And then, Ruth, looking at cost of goods sold, that came in quite a bit higher than we thought and you were lapping a one-time charge, if we have it right, vs. the year ago period. Maybe you could talk a little bit about some of the pressures in cost of goods sold that were either seasonal or maybe a new normal in terms of a higher level going forward. Any color there would be really appreciated. Thanks, everyone.

<A - Sundar Pichai>: On the Google Assistant and Google Home, we have a – very excited about the momentum we saw in CES. It actually reflects work we have been doing for a while. Google Assistant in some ways brings together all the technology we've been building for years, and it's an extension and it's supported by Google Search as well.

We're also thinking about our capabilities broadly beyond just one device alone. And that's what we are doing here across phones, across all surfaces. So, that's something big we are focused on. And the second is, we've always built ecosystems, be it Android, or Chrome, or Chromebooks. We work with many, many partners and scale up things, right? And so, we are leveraging those best practices and trying to build this in a way in which the entire ecosystem can ship product to the Google Assistant and generate value. So, I think the framework is great. And long term, our investments in AI will directly manifest those capabilities for users through the Google Assistant. So, I'm very bullish on it.

<A - Ruth Porat>: And then in terms of gross margins, it obviously reflects our product mix. And as you know well, the TAC rate for each of sites and network, as a percentage of revenue lines, does continue to increase because they're

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our strongest growth areas, namely mobile search and programmatic, and so carry higher TAC.

But as I indicated in my opening comments, we do estimate that the year-on-year increase in the sites TAC rate will slow after Q1 2018. And then the other thing to note, other cost of revenue does reflect the seasonality of hardware, having increased both the number of products in the Made by Google family, as well as continuing to expand geographically in Western Europe and APAC, you can see that reflected here.

<Q - Heather Bellini>: Two quick questions. One for Ruth and Sundar. I guess, Ruth, just a follow-up on your comments there. The partner agreements, which you just cited, is there any color you could give us on how these typically work? And what I mean by that is, are they typically multi-year deals, on average? And how do we think about these impacting the rate of change in tax since you were talking about the pace of growth in TAC as we look out, call it, in year two if these are multi-year deals?

And then, for Sundar, I guess, I wanted to follow-up a little bit with what we saw at CES. But how do you think about voice? And given the significant number of devices in the market, how do you think in the future about traffic acquisition strategies on these devices as you look five years down the road? Is there any reason to think that the strategies might be different that you're going to follow as you look ahead than what we've seen over the past, call it, since the advent of the iPhone? Thank you.

<A - Ruth Porat>: So on your first question, there's not much really that I'm going to be able to add there. I mean, given the ongoing momentum in our mobile search business, this does continue to be relevant as you look forward, given mobile carries higher TAC. But the rate, as for your question, has also reflected changes in partnership agreement. So, all factors considered, we expect the year-on-year increases will slow after Q1 2018. And as I said on many of these calls, we're very pleased to have a very strong position in a rapidly growing market, and that momentum does continue.

I guess, the only other thing to add is that Q4 TAC, as a percentage of revenue, does benefit from the fact that Q4 is a seasonally strong quarter for YouTube. So quarter-on-quarter changes are less insightful because CAC is distinct from TAC. It's not in this number, but not much more to add there. Pass it to Sundar.

<A - Sundar Pichai>: And Heather, on voice, we are very excited by voice. We obviously see it being adopted strongly in countries like India. It's actually a significant part of just mobile search queries in general. And things like Google Assistant and doing Google Home kind of really accelerates the trend. But – we definitely see more multi-modality. So as you saw, we also announced many smart displays at CES. And I think that will be an exciting trend as well.

So we'll bet on all of that. In general, I think about we want to be there for users when they need us and we want to serve everyone. This is why we work across the ecosystem. We do first party devices. We do it globally. And so, we are committed to doing that well. So, I think it will be an extension of how we have approached search from day one and trying to serve everyone. And so I don't, overall, see a big shift.

<Q - Douglas T. Anmuth>: Some big news earlier this week, just in terms of Waymo with FCA talking about delivering thousands of minivans to Waymo later in the year. So I was hoping, Ruth, you could just talk to us more about the timing for that business and how we should think about the economic model there as you move to operations and deployment phase?

And then, secondly, the cash, now obviously much more accessible in terms of what is held overseas. Can you just you talk more about your plans there? Obviously, bigger buyback there, but still not meaningful in terms of the overall size of the company? Thanks.

<A - Ruth Porat>: Thanks. Sure. So first on Waymo, we do remain very excited about the opportunity with Waymo and our continued progress on multiple fronts, in particular the rider program in Phoenix we're excited about and we're expanding our testing to more states.

In November, we announced that Waymo's self-driving TAC reached a major milestone, becoming the only company to have a fleet of driverless cars on public roads that are completely autonomous. And that builds on our more than

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4mm test miles driven in the real world in seven states, 25 U.S. cities where we're currently driving self-driving I should say, 10,000 miles every day with billions of miles and simulation and robust testing at our private facility.

So, more to your question, we do continue to explore a range of options beyond the program we're piloting in Phoenix including ride sharing and personally used vehicles, logistics, deliveries and working with cities to help them address public transportation objectives.

That being said, our first commercial application is the ride service that we will launch in 2018 that would be open to members of public in Phoenix and riders will be able to use our Waymo app to hail one of our fully self-driving cars without a driver at the wheel, so very excited about that.

And then in terms of cash, I think the main point as we think about it is there's no change in our approach to our capital allocation framework. We've consistently been focused on long-term investing and we talked a lot about that already on this call and our framework has been therefore very consistent. The priority, the first use is organic. It's investing in the many opportunities that we have.

And the second is strategic and we do remain active with smaller M&A deals, in particular to support our cloud business and hardware. The HTC deal, which we just closed, is a good example of that.

Third is CapEx. And we continue to invest in machines to support growth we see across Google, but in particular supporting cloud, search, YouTube and all that we're doing in machine learning. And then, finally, that leaves return of capital. And when we considered all of that that's what led us to extend – to have the board extend the share repurchase program, which we announced a couple of years ago. And we'll let you determine what that number represents in true Google fashion. But it's just a modest increase to what we've been doing previously.

<Q - Brian Nowak>: I have two. The first one Ruth, you called out desktop search I think for the second straight quarters being relatively strong. Could you just talk about some of the drivers of the strength of desktop, and how do you think about the sustainability of continued strong desktop growth into 2018 and beyond?

The second one, kind of a question on search query volume; there's often speculation and question marks around how consumer behavior is changing in e-commerce and whether Google is still capturing as many e-commerce searches. Could you just talk to what you're seeing in retail search query volumes and search user growth within e-commerce in the United States?

<A - Sundar Pichai>: Overall, look, we – obviously search is very broad. And even when you talk about commercial thing we serve across many, many categories including things like from travel to hotels, and to services, to products and so on. So we are very, very comprehensive.

And obviously e-commerce is evolving a lot. And we continue to invest there. Google Shopping is doing well. And we work hard to make sure we bring the best experience possible, which is why as it evolves with Search and Assistant we partner with companies like Walmart for example to make it much easier to buy products and so on. So, we invest a lot there. You're right consumer behavior is changing, but we're comfortable given the breadth of how we do things and how that – how we are focused on user experience there.

<A - Ruth Porat>: Then on your question on desktop. There really isn't one particular item to call out here and that's why last quarter, I tried to walk through the process that our team goes through and the way they look at innovations really stepping back and recognizing that the way we all use smartphones and desktop is continuing to evolve. And so therefore, there's utility and challenging assumptions about evolving user behavior and advertiser preferences and that opens new lines of inquiry, which benefits not just mobile, but also desktop. And desktop did deliver solid revenue growth. It does remain an important form factor for certain more complex tasks such as planning vacations or assessing insurance options. And we're pleased with the ongoing strength. I'll leave it to you to do any of the forecasting, but we just view it as yet another valuable form factor, and are really pleased with the performance there.

<Q - Anthony DiClemente>: One for Sundar and one for Ruth. Sundar, on YouTube, you mentioned the 1.5B people come to YouTube. Any other information you can give us there on user growth or engagement trends would be great? Anything on time spent, I mean particularly as YouTube becomes more mature and mobile video, particularly North

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America gets more competitive. And then, also on YouTube, anything around new products or features driving the monetization or ad business?

And then, Ruth, just a question on the growth and marketing spend in Q4. I think you said that Q4 was significantly elevated. Should we interpret that to mean that the growth rate in selling and marketing y-over-y should decelerate off Q4?

And then, just related to that, you're getting a good return on investment from this marketing spend, particularly when you think about media mix and all the spend that we've seen on TV, as compared to digital marketing. Thanks a lot.

<A - Sundar Pichai>: Look, on YouTube, we are continuing to see great momentum maybe one area, which for example highlights how well it's doing is if you think about YouTube on TV, people actually weren't watching YouTube on the big screen. Our growth has been significant there, and so increasingly people use YouTube for – we see it being used across every possible use case.

And I said it earlier in the call, every day we get over 1B views on educational content alone. People use it to go catch up on sports, music, entertainment. And so, you can think about the breadth of – historically, YouTube has been very strong on mobile and continues to be strong on mobile. It's doing particularly well in the next billion user market. So, growth last year was very strong there, which is why we supported it with investments like YouTube Go, and we are seeing it now grow well beyond mobile, especially in the living room, so, lot of momentum there.

<A - Ruth Porat>: And then in terms of sales and marketing, as I said, it particularly supported hardware, but was also supporting cloud and YouTube, and as Sundar and I have said these are important Google growth areas for us and we are investing to support growth in the business.

The elevated levels this quarter did reflect both seasonality and strategic decision to invest in these brands. And so we view it as a very important part of the overall investment and what we view as very sizeable opportunities, and it's both supporting the brand and the momentum, therefore, going into 2018. But this is very specific product focus as well.

<Q - Daniel Salmon>: Sundar, I'll go with a European theme. First, curious to hear your thoughts on the potential impact of GDPR maybe both on your own sites and properties, and how any business practices may need to be adjusted for that, but also for tools like customer match that your advertisers may use.

And then second, I'll take a shot at it. Any updates on your dialogue with EU officials and regulators on the proceedings there? Thank you.

<A - Sundar Pichai>: Good question, I was just in Europe last week. It was exciting to be there. There's clearly momentum we feel in terms of how Europe is doing, and we are very committed to the region. We are opening new offices there. We announced a AI center. We are committed to hiring more engineers and supporting staff there. So it's an important market for us.

On things like GDPR, we want to be – we have been thoughtfully engaged there. I think it's important to put privacy first for European citizens and we're very supportive of the work that's underway there, and we are committed to complying with GDPR across all the services that we provide in Europe.

There's still time. As a reminder, it doesn't go into effect until May or so. And we are working to make sure all our products are ready and we'll work hard to make the transition well. In terms of, again, with the European Commission, we have long had constructive conversations. We are understanding their concerns and responding with thoughtful changes, and we'll continue engaging in a thoughtful way.

<Q - Colin Alan Sebastian>: First, Sundar, your comments on Google Cloud were upbeat, and I wonder how much of the momentum there is related to machine-learning capabilities offered as a service. If you could frame just how important that is for the Cloud business overall.

And then, as a follow-up on Google Home or the voice-based Assistant, if there's any update in how you're thinking about monetization from a transactional perspective, transactional model with perhaps retail partners or do you see an

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ad-based model emerging there as well? Thank you.

<A - Sundar Pichai>: On the first thing, Colin, on Cloud, particularly the last quarter, we obviously brought AutoML to our Google Cloud customers. To me that shows the rate at which we are bringing our internal advances. Just a year ago, I remember reviewing with the team and they first showed me the AutoML work. We spoke about it at Google I/O. And it's pretty cutting-edge work. And to turn it back around and to provide it for everyone in the world, I think that shows the power of what we can do with Google Cloud and get our state-of-the-art and get it to everyone.

I think the momentum there, obviously, is due to our strength in machine learning, the kind of open agile development environment we provide security and then the combination with G Suite. But above all, I think, we've always – we've been doing Cloud now for 19 years because Google itself was built on a cloud platform. But where the momentum is really coming from is over the past two years we have put a lot of effort to make sure we are enterprise scale ready. So now we can handle any type of enterprise, any kind of regulatory complexity, security complexity and so on. And that's evident in the business wins we are seeing. So, we are signing customers who are very large across the board, globally, and I think that's driving a lot of momentum there.

On your question on Google Home and voice-based Assistant and how we're thinking about monetization, there are a lot of interesting ideas internally. So, teams are excited about trying new things. We see a lot of potential. But the guidance I've given the teams is to be squarely focused on user experience.

We are really getting started. I think these are going to be powerful technologies. But the areas where we clearly feel all of us fall short for doing right by users and getting the expectation – matching their expectation. So, you'll see us focused on user experience there for a while to come.

<Q - Michael B. Nathanson>: I've one for Sundar and one for Ruth, both on YouTube. So, first question was, as Google Preferred kicks up a little heat on the types of qualities that makes the cut for your videos, do you feel that you have to take a more active stance in looking at what is in Google Preferred – sorry, YouTube Preferred, and how are you going to go about that?

And then for Ruth, the past year was one where we heard a lot about brand safety. And I wonder when you look back at the YouTube results in 2017, is there any noticeable signs of maybe a shift in ad spending from some of the brands who are making those complaints? So, those are my questions.

<A - Sundar Pichai>: Thanks, Michael. I probably can talk about both, as they're related. We obviously want to make sure YouTube has a great experience for users, content creators and advertisers, because it supports content creators. And we took a lot of steps last year, but particularly in December, we adopted a new rigorous approach, and that's a much more stringent standards for creators. For example, they need 1,000 subscribers to be eligible for monetization.

We are manually reviewing Google Preferred videos. We obviously use machine learning to support that a lot, and they both go hand in hand. We've provided improved controls for marketers and we're also working with trusted third-party vendors to assess brand suitability. So, it's a comprehensive approach to make sure all of this works well.

And so while there have been concerns and we – but we are working really hard to address them and respond strongly. And so, I think, we are focused on the long-term opportunity here and I think we are setting ourselves up well for the years ahead.

<Q - Ken Sena>: So just a question on – searches seem to becoming more qualified through travel as far as filtering the price that people want to pay, locations, amenities, et cetera. Is there any trend that goes along with that in terms of maybe depressing search volume growth, to some extent, because of the more filtered aspect?

And then secondly, does the higher qualification trend tie in at all to the shifts towards programmatic and in terms of other parties that might be involved or the discussion that we've had around TAC?

And then maybe two, if – just as a follow up, if you can provide just a little bit more color on Google Pay in terms of what might be different in this round vs. previous attempts? Thanks.

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<A - Sundar Pichai>: Maybe I'm not fully sure I understood all the specifics there, but at a high level, as people are on-the-go, they are traveling, et cetera, if anything, I think search is more invaluable than ever before. All the work we do in local searches applies incredibly when you travel, the properties we have like Google Maps, etcetera, go along with it. So overall, I think, they all add up to a better user experience and hence a better opportunity for us.

Google Pay turns out to be an important part of all of this. As we move from just answers to helping users complete actions over time, including transactions, the ability to complete the transaction is an important part of it, and which is why making sure Google Pay in a unified way works as seamlessly as possible is a big part of our long-term strategy.

<Q - Stephen Ju>: So Sundar, I think, Ruth cited hardware in the prepared remarks as the largest contributor in Q4 for the other revenue line. As you look at the roadmap going forward, you acquired the HTC engineers to bring that team in-house. So it looks like for the first time you have an integrated hardware and a software team under one roof.

So, how do you think your product development pace and strategy will change for smartphones and other devices going forward? And also, does it make sense to bring the Nest team to be more integrated into core Google, as well given the drive to increase the touch points for all the Google products to other form factors? Thanks.

<A - Sundar Pichai>: Thanks Stephen. Great question. You're right that, part of the reason we are so excited about being able to bring this world-class team in-houses, while we've been working together already, we've had to straddle a company boundary to do that. But now having them as Googlers, will really make that integrated development, which is so critical for us to do it better. We bring a unique approach to hardware. The combination of AI plus software, plus hardware, so being able to get those teams working together I think will really drive the pace forward. And the best example of that is you see the advances we have made with both still and video photography on our phones.

And the Nest team is very, very closely aligned with the Google hardware team. We work hard to realize lot of synergies there. We already share a lot of our go-to-market efforts and we increasingly are collaborating on product development as well. So we collaborate closely, and I'm excited at the possibilities there as well.

<Q - Justin Post>: First, for Sundar. It didn't feel like there is many visible search changes this year as far as coverage or ad formats. So, would love to hear your thoughts on search innovation pipeline as you look out to 2018 and key growth drivers going forward.

And then, Ruth, in the prepared remarks, there was a lot of comments on investment in your medium-term business growth drivers, offices, data centers and other areas. And just wondering if you view 2018 upcoming as an investment year or kind of more of the same of what we've seen over the last couple of years? Thank you.

<A - Sundar Pichai>: Justin, when you think about search, one of the ways that I encourage you to think – we think about user journeys. And so a lot of the innovation that we are doing has gone on to not just an individual query in how we respond, but how we think about what a user is trying to accomplish over a series of sessions. Are you trying to plan a trip and how do we do it better. Do you have a health-related area where you're trying to learn more about it, and how do we help you through that. And so, it's not always just changing a specific format, but understanding context better and bringing you that information through a journey.

And I think so, there's lot of innovation that's happening in that direction. And also underlying is what I said earlier, it's not just providing the answers, how do you help them get to that information and act on it. And so, maybe you found something and you want to call that place, or maybe you're trying to order a birthday gift, and we actually want to go a step further and help you buy that gift. So that's along the lines. And the innovation is happening across Search and Assistant in an integrated way.

<A - Ruth Porat>: And then in terms of your investment question, we've consistently been investing across Alphabet. And we've tried to be very clear about our investment priorities, all with a view to supporting healthy long-term growth that goes back to the inception of the company.

The year-on-year op inc growth that you've seen does include these sustained investments for all the areas that Sundar and I have talked about; for the year, up 22% vs. last year. Obviously, a lot of variability in growth quarter-to-quarter.

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And we just continue to be focused on doing the right things to support growth of the business. Q4 does reflect the obvious seasonality. And again, we continue to look across the various products their needs and try and prioritize so that we can remain committed to long-term growth.

<Q - Benjamin Schachter>: Just a couple of questions. Can you discuss the evolution of the business model for Waymo? You're launching the ride-hailing service in Phoenix. You've worked with manufacturers. You talked about other models. But when you think about the sort of 5 to 10-year view of that, what will the primary business model look like?

And separately, can you talk about what is interesting from a strategic point of view about the video game business? You're making some key hires there. And just wondering what you think Google can bring to that industry that would be innovative? Thanks.

<A - Ruth Porat>: So on Waymo, really not much more to add. We're really pleased after years of work on technology, where it was really about safety, safety, safety, and developing the technology and the platform. And now we're in a position where we have this opportunity to let people use and benefit from what we've developed. So I think that safety has been a key driver and the opportunity for cities has been really exciting what it means about optimizing resource base that they have. So, it's still very early days, and we're just – we're pleased with all the progress the teams' made. But it would be getting ahead of ourselves to go further out than we've laid out here.

<A - Sundar Pichai>: On the video gaming side, I think, look, we are – we today have a lot of momentum in these areas, both with YouTube as a platform, Google Play. So, these are assets that's really worked well. And we'll continue investing there, nothing new or interesting to share with you at this time.

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