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TECHNOLOGY

Is Google Stock A Buy As AI Investments Aim To Drive Ad, Cloud Growth?



REINHARDT KRAUSE | 09:30 AM ET 08/05/2023

Amid a possible bubble in artificial intelligence stocks, is the valuation of Google-parent **Alphabet (GOOGL)** a worry? Not if rising AI investments for GOOGL stock yield improved advertising and cloud computing growth, analysts say.



Despite mounting competition in artificial intelligence and internet search, Google stock has advanced 46% this year. That's better than the 34.6% jump in the Nasdaq composite. One worry is that investor appetite for **AI stocks** could drive a market melt-up.

Alphabet reported **second-quarter earnings and revenue** that beat expectations amid rising investments in artificial intelligence. With 19% earnings growth in the June period, Google stock ended a four-quarter string of year-over-year declines.

In addition, the company said Chief Financial Officer Ruth Porat will assume the newly created role of President and Chief Investment Officer effective Sept. 1. Porat will continue to serve as CFO through the 2024 capital planning process as the company finds a successor.

One concern for GOOGL stock is new competition in internet search.

GOOGL Stock: AI Battle Rages

Google aims to counter **Microsoft's (MSFT)** investment in **artificial intelligence startup OpenAI** by making its own **generative AI tools** available to software developers. One big question is whether integrating chatbot AI technology into search queries will lower Google profit margins.

"While Microsoft and OpenAI were first to introduce text-generative AI with ChatGPT, we note that Google has been using large language/AI models to enhance search results for users and enable smart bidding for advertisers," Truist analyst Youssef Squali said in a note to clients.

He added: "To better compete on the enterprise software side, Alphabet is integrating AI into its Cloud offering, providing tools and APIs for developers, creators and partners to help grow their businesses. Also, Google is integrating AI into Gmail and Docs."

At the Google I/O 2023 developers event on May 10, Alphabet showcased how generative AI will be integrated into search, maps, Workspace, photos, cloud computing and Android devices. Google discussed how **advertising will evolve** as generative AI is added to search.

At Google Marketing Live on May 23, Alphabet announced AI tools to allow advertisers to essentially synthesize a unique text or display ad, in real time, based on the user's query and advertiser data supplied to Google.

Google Stock: Pichai Pay Jumps

Google's board of directors has authorized an additional \$70 billion in stock repurchases. In the first quarter, the company repurchased \$14.6 billion of its own stock.

According to JP Morgan, Alphabet has been increasing its stake in **GitLab (GTLB)**. Google Ventures in May bought \$19.7 million of GTLB shares. Google Ventures and Alphabet now own 3.4% of GitLab, which offers software programmers an open source app development platform.

Amid pressure to cut expenses, Alphabet disclosed that Chief Executive Sundar Pichai's pay jumped to \$226 million in 2022, due to a big stock award.

Meanwhile, Alphabet has stepped up cost cutting.

Google stock on Jan. 20 said it will cut 12,000 jobs, or roughly 6% of its global workforce, adding to a growing wave of layoffs among U.S. technology companies. The layoffs follow a hiring spree at the company.

The U.S. Department of Justice on Jan. 24 filed antitrust charges against Google, leaving open the question of whether the search giant will have to divest some of its ad business in order to satisfy regulators. The DOJ claims Google's dominance in digital advertising harms competition.

GOOGL Stock: Justice Department Files Suit

The lawsuit marks the DOJ's second antitrust case versus the internet giant in just over two years. The DOJ in October 2020 filed an antitrust lawsuit charging that Google has monopolized internet search and search-related advertising. That case is scheduled to go to trial in September.

YouTube Chief Executive Susan Wojcicki in February announced her departure. She was replaced by long-time YouTuber Neal Mohan.

Meanwhile, lawmakers and courts are closing in on fundamental changes to **Section 230 of the Communications Decency Act**. The law has shielded internet companies from liability for content on their sites for nearly three decades.

The internet giant completed a 20-for-1 split for shares of Google-parent Alphabet after the market close on July 15 2022.

In the long run, however, the GOOGL stock split could pave the way for the tech giant to enter the Dow Jones Industrial Average. Google stock could be more attractive to retail investors.

Due to its huge cash holdings, Google stock has shrugged off three fines totaling \$9.3 billion levied by the European Union on antitrust grounds.

Boosting Ad Business Through E-Commerce

Alphabet aims to boost its advertising business through **e-commerce-related internet search**. At the same time, it hopes to chip away at **Amazon.com's (AMZN)** dominance in product search.

Google's internet search business will hold up better than other advertising formats, such as social media, analysts say.

Google has rolled out the **Performance Max advertising platform**. It automates buying across YouTube, internet search, display, Gmail, maps and other applications. Performance Max lets advertisers manage campaigns across all Google ad inventory. Advertisers that use the tools convert more shoppers into buyers, Google says.

The big picture: Google stock this year faces more difficult year-over-year growth comparisons in 2023 as the coronavirus emergency fades.

In a near-term boost for its advertising business, Google has delayed phasing out internet cookies to 2024. Also, in early 2022, Alphabet said it expected a "meaningful increase" in 2022 capital spending, reflecting investments in computer servers in internet data centers and construction of office space.

Google Stock: Artificial Intelligence Prowess

Most investors still know the company as Google, even though the internet search giant reorganized as holding company Alphabet in 2015. The restructuring move separated Google's core internet advertising business from so-called moonshots, such as autonomous vehicles and the Verily Life Sciences unit.

In March 2022, Google spun off its quantum computing technology group as a separate company.

Google stock's strength in artificial intelligence spans digital advertising, the Google Cloud Platform, YouTube and consumer hardware products. GOOGL stock is just one **artificial intelligence stock** to watch.

At a Google developers conference in mid-May, the company demonstrated how it uses AI tools in a wide range of applications, including Google Workspace, Google Maps, virtual reality, and voice-based search.

After a long run, GOOGL stock has dropped out of the **IBD Leaderboard**. The Leaderboard is IBD's curated list of leading stocks that stand out on technical and fundamental metrics.

Big Tech Stocks Face Regulatory Headwinds

With the Android mobile operating system built into devices sold worldwide, the Play Store has been a revenue growth driver.

A federal judge ruled in September 2021 that **Apple (AAPL)** must allow mobile app developers to steer consumers to outside payment methods. Google's policies also are under scrutiny.

Google in 2021 said service fees at its Play Store would drop to 15% from 30%. The move reduced revenue.

Under Pichai, Google has improved transparency. Google began disclosing cloud computing financial metrics with its fourth-quarter report in fiscal 2020. But the cloud business has yet to turn a profit. And YouTube's profitability still remains a mystery.

Google Stock Fundamentals

Google earnings for the June quarter came in at \$1.44 a share, up 19%, as operating margins expanded for the first time since the fourth quarter of 2021.

The company said gross revenue rose 7% to \$74.60 billion, compared with \$69.7 billion a year ago. Analysts had predicted Google earnings of \$1.34 per share on revenue of \$72.84 billion.

Capital spending in the second quarter rose to \$6.9 billion, up from \$6.3 billion in the first quarter. Further, Google repurchased \$14.97 billion of its own stock during the period.

Also, advertising revenue rose 3% to \$58.14 billion vs. estimates of \$57.39 billion.

Meanwhile, YouTube ad revenue rose 4% to \$7.66 billion during the second quarter. Analysts had estimated YouTube ad revenue of \$7.42 billion. Google said cloud computing revenue rose 28% to \$8.03 billion vs. estimates of \$7.87 billion.

Waymo Autonomous Vehicle Business

A key question for investors is how much should Google's self-driving-car project Waymo and "Other Bets" such as the Verily Life Sciences unit figure into valuation.

In early 2018, some Google stock analysts projected Waymo's long-term valuation in a range of anywhere from \$75 billion to \$125 billion. **Expectations for autonomous vehicles**, though, have been sharply lowered.

Waymo in 2021 raised \$2.25 billion in funding from outside investors. including private equity firm Silver Lake, the Canada Pension Plan Investment Board and Abu Dhabi's Mubadala investment arm.

While Google did not disclose Waymo's valuation in the funding round, reports said it was only \$30 billion. It could be lower now.

Google Stock: Cloud, Hardware, Security Acquisitions

Another question is the performance of Google's hardware business. It's battling Apple in smartphones and Amazon in smart-home appliances.

Also, Google's acquisition of smartwatch maker Fitbit closed in January 2022. The \$2.1 billion purchase should help Google make a push into the health and fitness market, analysts say.

Google's cloud computing business, meanwhile, faces tough rivals in Amazon and Microsoft. Google brought in Thomas Kurian, a former **Oracle (ORCL)** executive, to improve performance in the corporate market.

Bulls say Google Cloud Platform is taking share as it focuses on security, open source software and data analytics.

In 2019, Google **purchased data analytics firm Looker** for \$2.6 billion in cash. Santa Cruz, Calif.-based Looker's analytics platform uses business intelligence and data visualization tools.

More acquisitions to boost Google's cloud business could be coming, analysts say. Google acquired cybersecurity firm **Mandiant (MNDT)** for \$23 per share in an all-cash \$5.4 billion deal.

Google Stock: Is It A Buy Now?

GOOGL stock jumped 65% in 2021. But in 2022 Google shares dropped 39%.

Meanwhile, Google's **Relative Strength Rating** stands at 89 out of a best-possible 99, according to **IBD Stock Checkup**. The best stocks tend to have an RS rating of 80 or better.

Google stock owns an Accumulation/Distribution Rating of B. That rating analyzes price and volume changes in a stock over the past 13 weeks of trading.

Further, shares hold an IBD Composite Rating of 98 out of 99. The best growth stocks have a Composite Rating of 90 or better.

As of Aug. 4, Google stock holds a 127.10 buy point from a **cup-with-handle base**. GOOGL stock trades in a 5% buy zone that extends to 133.45.

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