

**LARRY PAGE, CEO** \$1 COMPENSATION

**SERGEY BRIN, CO-FOUNDER** \$1 COMPENSATION

**ERIC SCHMIDT, CHAIRMAN** \$200-300K COMPENSATION, 1 YEAR OF \$100 MM BONUS

HEADQUARTERS: MOUNTAIN VIEW, CA

32,000 EMPLOYEES

FOUNDED: 1998 **GOOGLE INC.**

BUSINESS IN 50+ COUNTRIES, 100+ LANGUAGES

Global tech leader focused on improving ways people connect with information. Does this mainly through their search engine google.com  
Mission is to organize the world's information and made it universally accessible & useful

**SEARCH:** maintains a vast index of the internet, their search technologies sort through it for relevant & useful results

**ADVERTISING:** AdWords with search, AdSense with the rest of the internet; Mobile Ads is the way of the future; Google Local is for locales

**O/S & PLATFORMS:** Android- free mobile platform for any device maker; Chrome & Chrome O/S browsers; Google+ has 100 MM users

**ENTERPRISE:** Google Apps- Gmail, Google Docs, Google Calendar, Google Maps, & Google Earth (basically all combined is *cloud computing*)

**FAST GROWER**  
**EQUITY BOND DCA**  
#1 GLOBAL SEARCH ENGINE  
**VALUATION:**  
FAIR VALUE = \$317-360 B (\$974-1,109/SHARE)  
DISCOUNT = \$190-198 B (\$585-610/SHARE)

\$Billion	2011	2010	2009	2008	2007	2006
Shares Outstanding (MM)	325	322	318	315	313	311
Sales	37.91	29.32	23.65	21.80	16.59	10.60
Cost of Goods Sold	-13.19	-10.42	-8.84	-8.62	-6.65	-4.23
<b>Gross Profit</b>	<b>24.72</b>	<b>18.9</b>	<b>14.81</b>	<b>13.18</b>	<b>9.94</b>	<b>6.37</b>
R&D	-5.16	-3.76	-2.84	-2.79	-2.12	-1.23
Sales & Marketing	-4.59	-2.8	-1.98	-1.95	-1.46	-0.85
General & Administrative	-2.58	-1.83	-1.56	-1.69	-1.22	-0.72
<b>Operating Income</b>	<b>12.38</b>	<b>10.51</b>	<b>8.42</b>	<b>6.74</b>	<b>5.14</b>	<b>3.58</b>
Net Interest	0.44	0.29	-0.04	0.21	0.53	0.43
Tax	-2.59	-2.29	-1.86	-1.63	-1.47	-0.93
<b>Net Income</b>	<b>10.23</b>	<b>8.51</b>	<b>6.52</b>	<b>5.32</b>	<b>4.2</b>	<b>3.08</b>
Operating Cash Flows	11.96	9.8	7.67	6.41	4.59	2.98
Capital Expenditures	-3.44	-2.2*	-0.8	-2.36	-2.4	-1.9
<b>Free Cash Flows</b>	<b>8.52</b>	<b>7.60</b>	<b>6.87</b>	<b>4.05</b>	<b>2.19</b>	<b>1.08</b>

Dividends/Repurchases	-	-0.5	0.1	-0.1	-	2.33
Net Borrowings	0.7	3.46	-	-	-	-
Net Acquisitions	-1.9	-2.9*	-0.1	-3.3	-0.9	-0.4
<b>Operating Margin</b>	<b>32.7%</b>	<b>35.8%</b>	<b>35.6%</b>	<b>30.9%</b>	<b>31.0%</b>	<b>33.9%</b>
Capital Employed	13.02	10.30	8.69	9.46	6.28	3.40
Return On Capital Employed	95.1%	102%	96.9%	71.2%	81.8%	106%

### Earning Power:

**\$10.5 B earning power, 18-22% growth per year**

- Margins seem to be generally stable, even with the large R&D expense on self-driven cars and other interesting (wacky) projects
- \$10.5 B in earnings is from capex being much more than depreciation expense, income statement seeming to be a more accurate measure of earning power, & Q1 2012 earnings already up 24% year-over-year
- Last 6 years, company grew revenue 29%/yr and earnings 28%/yr
- So for expected future growth of 18-22%/yr, I underestimated historical growth rates and it seems Google can still grow more into the future. The U.S. is 47% of revenue- Google can get much more global and will continue to grow as the internet grows.

### Capital Structure:

**\$45.4 B cash & investments**

**No Net Debt**

- \$3.5 B overall debt, \$30.7 B "healthy debt allowance"

**No Pension**

**\$45.4 B "Cash"**

\*For FY 2010, there was a \$1.8 B amount included in capex that was for a building in New York; I saw this as more of an acquisition expense than a capital expenditure. Therefore I include it in acquisitions instead of capex.

“Don't be evil.”

February 2012

**Concluding Remarks:**

Man, what a company. The culture is perfect, employees are fiercely loyal, it doesn't directly require capital to incrementally grow its business (a priceless thing that very few businesses can claim), and it's still innovating with a bunch of bizarre projects that may make them even wealthier someday (self-driven cars...). With 46% of sales in the U.S., there is still a huge growth opportunity internationally. And despite “competing” with many different companies (Apple, Yahoo!, Microsoft, Facebook, etc.), there is no close 2<sup>nd</sup> best search engine out there. Google is so good at what they do that no one can seem to keep up. It seems like a very durable competitive advantage to me, especially after reading *In the Plex*. I'd highly recommend it. Oh, and good luck to Keith, my friend who started working at Google. What a great place to be. Enjoy California my friend. I own this one.

**History:**

- 1995-1997: Larry & Sergey meet at Stanford, collaborate on search engine *BackRub* using PageRank
- 1998: google.com launches
- 2000: AdWords - advertisers pay to place ads on Google and/or on any site, uses pay per click to determine cost
- 2003: AdSense – ad publishing where website signs up for Google ads on site, paid a portion of ad revenue
- 2004: Gmail – now among most popular email accounts
- 2006: YouTube acquisition for \$1.65 B (cheap!)
- 2008: DoubleClick acquisition for \$3.1 B, allowing for a “super cookie” to track users' activity online

**RISKS:**

1. Intense Competition- technology is among the fastest-moving and brutally competitive industries
2. 98% of Revenue From Ads- Google has defined the online ad market, let's hope that doesn't change
3. Regulatory Scrutiny- U.S. Government seems out to get Google, but so far no big enforcement actions
4. IP Fights/Lawsuits- the technology industry fights bitterly over patents and it's starting to get expensive
5. Security- people need to be able to trust Google with all the information they safeguard
6. Larry, Sergey, and Eric- are a lot of the company's intangible wealth, let's hope they live long and prosper

**General Information:**

- Takes lot of pride in their culture, works hard to recruit top talent & keep them happy. They still cherish their roots and encourage workers to be independent thinkers; has very little organizational structure.
- LOT of related party transactions – donations to Stanford; various Google Ventures investments

**Competition:**

- Search Engines- Yahoo! & Bing (Microsoft)
- Vertical Search Engines- Kayak, Amazon, eBay, Monster
- Social Networks- Facebook, Twitter
- Other forms of ads- TV, radio, print
- Mobile Apps- iPhone (Apple)

**News in Recent Years:**

- 2010: Google Instant; saw continued push toward “digital economy” helping their core business
- 2011: Larry Page takes over as CEO in April, launched Google+ in June, massive increase in Android for smartphones (more market share than the iPhone), \$12.5 B Motorola acquisition announced in August

Class A + B shares worth same, B has 10X voting rights

Larry, Sergey, & Eric own 18.5% of stock, control 65.9% of voting rights together

Peers:

- |                |                    |            |
|----------------|--------------------|------------|
| - Amazon       | - <u>HP</u>        | - Oracle   |
| - Apple        | - <u>IBM</u>       | - Qualcomm |
| - <u>Cisco</u> | - Intel            | - Disney   |
| - eBay         | - <u>Microsoft</u> | - Yahoo!   |

(Underlined if I've covered)

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