FAANGM Monthly – May 22

Still attractive despite economic uncertainty

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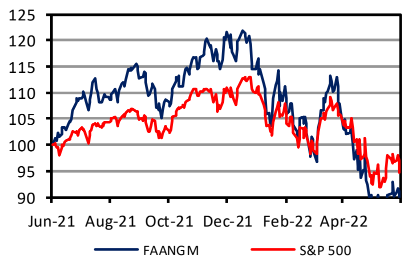
OVERWEIGHT

- The FAANGM declined 3.1% in May, slightly worse than the Nasdaq's drop of 1.7%. The S&P 500 was flat for the month. AAPL was the laggard, losing 5.6%, with NFLX the best performer, gaining 3.7%.
- Slowing consumer demand, and a tighter labour market, continue to present overhangs for big tech, especially for AAPL and AMZN. We continue to see uncertain legislative headwinds for both GOOGL and META, with a new bipartisan bill introduced in the Senate. NFLX continues to churn out exciting content for its subscribers, while also managing its expenses. MSFT continues to benefit from increasing digitalisation tailwinds, albeit with some short-term FX headwinds.
- We remain OVERWEIGHT on FAANGM as they remain at attractive valuations – 29x forward PE vs average of 31x. We believe that worries over contracting margins, slower consumer demand, and rising inflation, have largely been priced into the market. Long-term secular tailwinds from digital advertising, increasing cloud adoption, and increasing global digitalisation remain intact.

PRICE PERFORMANCE (%)

31 May 2022	1MTH	3MTH	YTD
META INC	(3.4)	(8.8)	(44.0)
APPLE INC	(5.6)	(10.6)	(17.3)
AMAZON INC	(3.3)	(21.7)	(27.7)
NETFLIX INC	3.7	(49.9)	(67.1)
ALPHABET INC	(0.6)	(15.9)	(21.9)
MICROSOFT CORP	(2.0)	(9.2)	(19.5)
FAANGM	(3.1)	(13.9)	(24.2)
S&P 500	0.0	(5.5)	(13.3)
NASDAQ	(1.7)	(11.2)	(22.5)

RETURNS VS. S&P 500



Source: Bloomberg, PSR

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Review

Meta Platforms Inc (META US, BUY, TP US$312)

- **Cutting spending in Reality Labs segment.** In an effort to reduce expenses in line with its expense guidance, Meta has reportedly been cutting spending in its Reality Labs segment, and has also been slowing down hiring. These cost cutting measures are not company specific, but seem to be affecting most companies across the tech sector, with slowing growth outlook as the key reason for this.
- **New Senate Bill could force Meta to break up ad business.** Lawmakers in the US have introduced a new bipartisan bill in the Senate, named The Competition and Transparency in Digital Advertising Act, in one of the most aggressive attempts to controlling big tech companies. This act aims to target conflicts of interest in ad tech, and would prevent companies that process more than US$20bn a year in ad revenue from taking part in more than one part of the digital ad ecosystem. This could spell trouble for digital ad dominators Alphabet and Meta, which could be forced to divest parts of its business if the bill is passed.

Comment: Slowing down of hiring and other cost cutting measures is no surprise, as was reiterated in the company's 1Q22 earnings call. A more sustainable and measured approach to expenses should also help the company's margins in the future. Scrutiny from US lawmakers is intensifying with the latest bipartisan bill introduced in the Senate, as it attempts to reign in more control over big tech.

Apple Inc (AAPL US, BUY, TP US$214)

- **Modest reacceleration in App Store spending and downloads.** Halfway through 3Q22, Apple's global App Store revenue has already risen 7% YoY, with total downloads on iPhones and iPads up 5% YoY. App Store revenue grew only 6% YoY in the previous quarter.
- **Flat iPhone production, increasing labour costs.** Reports have come out that Apple is looking to keep its iPhone production relatively flat for this year – roughly 220mn units, indicating that there could be headwinds in the overall consumer electronics environment. At the same time, the company is also raising its pay for store and corporate employees, citing a tighter labour market as the reason for this.

Comment: Some good news for Apple as it starts seeing a reacceleration in higher margin App Store revenues. Waning consumer demand for products and a tighter labour market continue to exert downward pressure on Apple's margins.

Amazon Inc (AMZN US, BUY, TP US$3,130)

Comment: Rising inflation, tougher comps vs a pandemic-inflated 2021, and weak earnings across other online retailers sent Amazon's stock down to its 52-week lows in May, as investor sentiment turned even more negative over worries of slowing consumer demand.

Netflix Inc (NFLX US, BUY, TP US$427)

- **Laying off 150 employees due to cost cutting**. Netflix laid off about 150 employees (~1.5% of total workforce) as it begins its cost cutting measure mentioned during its 1Q22 earnings call. Slowing revenue growth and plans to maintain steady margins were cited as reasons for the pull back in spending.
- **"Stranger Things" smashes records**. The heavily anticipated new season of "Stranger Things" smashed viewership records over the long Memorial Day weekend in the US, topping the charts with 287mn hours viewed in just 3 days – the previous record for an English-language series was set Season 2 of "Bridgerton" which streamed 193mn hours in its first weekend.

Comment: Netflix's plans to pull back spending by laying off employees was expected, as mentioned in their 1Q22 earnings call, as the company tries to maintain its profitability moving forward. The continued success of Netflix Original productions reiterates the company's ability to generate quality content for its subscribers.

Alphabet Inc (GOOGL US, BUY, TP US$3,493)

- **Google Cloud partnering with AMD to aid workloads.** Alphabet announced that it was partnering with Advanced Micro Devices (AMD) to aid in supporting AMD's chip-design workload, as well as enhancing AMD's data centers. As part of the deal, AMD will leverage on Google Cloud's storage, networking, and machine learning capabilities to improve its own hybrid and multi-cloud strategies for its chip design requirements.

Comment: The partnership with AMD continues to enhance Google Cloud's credibility and effectiveness in providing quality cloud solutions for enterprises, and is one of the main reasons why we expect its Cloud segment to continue its high growth moving forward.

Microsoft Corp (MSFT US, BUY, TP US$410)

- **FX headwinds weighing on 4Q22 outlook.** Microsoft marginally reduced its 4Q22 outlook to account for unfavorable foreign currency movements observed through May. Management now anticipates total revenue to be in the range of US$51.9bn to US$52.7bn (prev. US$52.4bn to US$53.2bn). Additionally, Microsoft now expects diluted EPS to be in the range of US$2.24 to US$2.32 in 4Q22 (prev. US$2.28 to US$2.35). Microsoft generates more than 50% of its revenues from international markets.

Comment: Our investment thesis remains unchanged since these dynamics are beyond Microsoft's control. We believe that strong corporate demand for Microsoft's higher-end licenses will continue to grow amid rising cybersecurity concerns. Azure will continue to benefit from digital transformation and cloud migration trends, while reopening of offices is driving the Office Commercial user growth from small and medium sized businesses.

Recommendation

We remain OVERWEIGHT on the FAANGM. Our preferred picks are still GOOGL and MSFT. Increasing corporate demand for GOOGL's high-margin Cloud services should continue to push revenue growth for the segment. For MSFT, revenue growth is still expected to be very strong, even as it reduces guidance marginally due to FX headwinds.

Company	1 Mth Perf.	3 Mth Perf.	YTD Perf.	Share Px (US$)	Mkt. Cap. (US$ mn)	PSR Rating	PSR Target Px (US$)	PE Yr 0	PE Yr + 1	PE Yr + 2	P/BV Yr 0	Dividend Yield	ROE Yr 0	EV/ EBITDA	EBITDA Margin
FAANGM															
Meta Platforms	-8%	-6%	-48%	175.57	475,149	BUY	312.00	12.1	14.1	12.2	3.9	0.0%	29.1%	7.6	47.7%
Apple Inc	-4%	-11%	-23%	137.13	2,219,474	BUY	214.00	23.4	22.1	21.4	33.0	0.6%	149.3%	16.3	33.3%
Amazon.com Inc	3%	-25%	-34%	109.65	1,115,624	BUY	3,130.00	33.4	48.3	26.5	8.3	0.0%	18.0%	15.8	14.1%
Netflix Inc	5%	-46%	-70%	182.94	81,275	BUY	427.00	15.9	15.8	14.8	4.6	0.0%	32.9%	12.7	22.9%
Alphabet Inc	-1%	-14%	-23%	2,223.23	1,463,997	BUY	3,493.00	19.3	17.6	15.0	5.8	0.0%	30.8%	11.1	36.4%
Microsoft Corp	-1%	-10%	-25%	252.99	1,892,121	BUY	410.00	30.9	26.4	23.6	11.6	0.9%	48.7%	18.7	49.8%
	-2%	-14%	-27%		7,247,640			25.2	25.8	20.8	15.9	0.4%	69.7%	15.2	36.1%

Source: Bloomberg, 10 Jun 2022, PSR

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