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Alphabet Inc.

Reddit Didn't Do It: Initiating at Neutral

Alphabet lost roughly $500bn of market value on 29 October, a record one-day loss for the company, and the story that has stuck is that Reddit's results proved AI is killing Google Search. The order of events says otherwise. Alphabet fell 12.6% on 29 October on its own third-quarter print; Reddit reported after that day's close and fell ~30% on 30 October. Reddit's slump is a consequence of Google's AI answers, not the cause of Google's sell-off. What the market sold was cash flow: 3Q26 capex of $51.4bn exceeded operating cash flow of $42.3bn, management said 2027 capex will "increase significantly", and Alphabet has raised ~$61bn of equity this year. Search still grew 12%, on 8% more paid clicks and 4% higher prices per click: volume, not a squeeze. **Wrong suspect, right worry: we initiate at Neutral with a Dec-27 price target of $310.**

- **Initiating at Neutral, Dec-27 PT $310.** Our PT blends three Dec-27 sum-of-the-parts scenarios (Table 1). Base (50%): Services at 18x and Cloud at 26x FY28E after-tax operating income, with investments at a 25% haircut, for $321/share. Bull (25%): AI Mode monetises close to classic search and Cloud converts its backlog faster, for $434. Bear (25%): AI answers take paid clicks and Cloud margins compress, for $159. **After the sell-off the market pays ~18x 2027E earnings for Services once Cloud and the investment book are valued, close to our own base case:** a fair price for a slower search business, not the death of one.
- **Search is a volume story; the clicks being lost are the publishers'.** In 3Q26 paid clicks rose 8% and cost per click 4%; over nine months, 11% and 4%. Price explains about a third of growth, not the "inorganic squeeze" alleged. Growth did slow, from +19% in 1Q and +17% in 2Q to +12%, mostly on currency by management's account, with AI Mode monetising below classic search. The click loss is real but lands on the open web: Pew finds users click a result in 8% of visits with an AI summary vs 15% without.
- **The real debate is capex, and the backlog answers only half of it.** Capex reached $132bn in 9M26 against a $195-205bn guide, and 2027 will be "significantly" higher; we model $270bn. On our numbers FCF is negative in 2026E and 2027E, funded by ~$76bn of net new debt and ~$61bn of equity this year, with buybacks suspended. Cloud backlog reached $560.8bn (3.6x a year ago) at a 36.2% Cloud margin, but ~$200bn of it is one customer, Anthropic. Until 2027 capex is known, we stay on the sidelines.

Neutral

GOOGL, GOOGL US
Price (30 Oct 26): $279.84
Price Target (Dec-27): $310.00
Initiation of coverage

Internet & Cloud Platforms

K2 Capital Limited
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Quarterly Forecasts (FYE Dec)

Operating income ($ mn)

	2025	2026E	2027E
Q1	30,606A	39,696A	43,255
Q2	31,271A	40,770A	44,426
Q3	31,228A	40,576A	44,214
Q4	35,934A	44,324	48,298
FY	129,039A	165,366	180,194

Search vs. Spend Dashboard

3Q26 metric	3Q26	3Q25	Chg
Paid clicks, y/y	+8%	+7%	+1pp
Cost per click, y/y	+4%	+7%	-3pp
Search & other, y/y	+12%	+15%	-3pp
Cloud backlog ($bn)	560.8	155.0	+262%
Capex ($bn)	51.4	24.0	+114%
Free cash flow ($bn)	(9.1)	24.5	nm

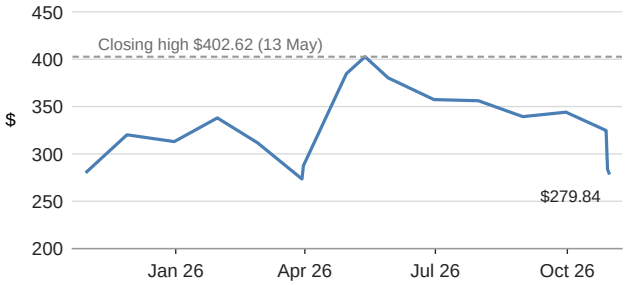
GOOGL **-12.6%** on 29 Oct (results 28 Oct); RDDT **~-30%** on 30 Oct (results 29 Oct). GOOGL is -30% from its 13 May closing high of $402.62.

Sources for: Search vs. Spend Dashboard: Alphabet 3Q26 Form 8-K, 10-Q and earnings call; share price moves as reported by Trefis and Decrypt. All other tables are company data and K2 Capital estimates.

See page 10 for analyst certification and important disclosures.

K2 Capital Limited and its personnel may hold positions in, and may trade, securities discussed in this report, including positions inconsistent with its rating. Investors should consider this report as only a single factor in making their investment decision.

Price Performance



	YTD	1m	3m	12m
Abs	-10.6%	-18.7%	-21.4%	-0.5%
Rel	-21.3%	-17.8%	-22.6%	-11.3%

Company Data

Shares O/S, Class A, B and C (mn)	12,290
52-week closing range ($)	273.50-402.62
Market cap ($ mn)	3,439,234
Exchange rate	1.00
Cash & marketable securities, 30-Sep-26 ($ mn)	265,098
o/w marketable equity incl. SpaceX ($ mn)	90,400
Long-term debt, 30-Sep-26 ($ mn)	125,102
Quarterly dividend ($)	0.22
Unused buyback authorisation ($ mn)	69,500
Employees, 30-Sep-26	204,757
Next results	Early Feb 2027 (4Q26)

Key Metrics (FYE Dec)

$ in millions	FY25A	FY26E	FY27E
Financial Estimates			
Revenue	402,836	496,711	586,836
Google Cloud revenue	58,705	109,905	170,353
Operating income	129,039	165,366	180,194
Net income (GAAP)	132,170	237,862	147,486
Diluted EPS (GAAP)	10.81	19.23	11.72
Core EPS (ex. investment gains)	8.76	11.13	11.98
Cashflow from operations	164,713	179,149	239,486
Capex	(91,400)	(199,953)	(270,000)
FCF	73,313	(20,804)	(30,514)
Margins and Growth			
Revenue growth y/y	15.1%	23.3%	18.1%
Cloud revenue growth y/y	35.8%	87.2%	55.0%
Operating margin	32.0%	33.3%	30.7%
Core EPS growth y/y	16.9%	27.0%	7.7%
Ratios			
Capex / revenue	23%	40%	46%
Net cash, incl. marketable equity	80,296	123,946	89,042
Valuation			
P/E, core (x)	31.9x	25.1x	23.4x
FCF yield	2.1%	(0.6%)	(0.9%)
Dividend yield	0.3%	0.3%	0.3%

Summary Investment Thesis and Valuation

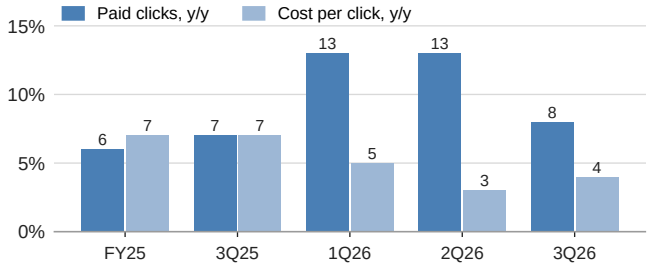
Investment Thesis

Alphabet is two businesses being priced as one anxious one. Google Services earned $39.2bn of operating income in 3Q26 at a 40.7% margin, with search revenue up 12% on more paid clicks. Google Cloud, now 24% of revenue, doubled its sales at a 36.2% margin with a $560.8bn backlog behind it. The 29 October sell-off attached a third story, that AI answers will hollow out search, to a quarter whose real problem was cash: capex of $51.4bn, negative free cash flow and a promise of more in 2027. We think the market has the evidence wrong but the price about right. Search monetisation is holding, though growth has slowed; the click loss so far lands on publishers such as Reddit. Against that, free cash flow is negative through 2027E on our numbers, depreciation is rising ~50% a year and no one yet knows the 2027 capex figure. We rate shares Neutral.

Valuation

Our $310 Dec-27 PT is a probability-weighted sum of the parts on FY28E (Table 1). Base (50%): Services at 18x and Cloud at 26x after-tax operating income, Alphabet-level costs at the Services multiple, Other Bets incl. Waymo at $60bn, SpaceX, Anthropic and other stakes at 30-Sep carrying value less 25%, and YE27E net cash ex. investments, for $321. Bull (25%): 21x and 32x, for $434. Bear (25%): 2028 search revenue falls 4% and the multiples compress to 13x and 16x, for $159. The shares trade on 23.4x our 2027E core EPS.

Search Growth Is Mostly Volume



$ in billions, 30-Sep-26	
Cash & marketable securities	265.1
o/w SpaceX (sale-restricted)	75.2
o/w other marketable equity	15.2
Non-marketable equity securities	135.2
Long-term debt	(125.1)
Net cash, incl. marketable equity	140.0
Debt issued, net of repayments, 9M26	76.3
Equity issued, 9M26 (incl. preferred, $12.4bn ATM)	~61
Share repurchases, 9M26	0.0

Source: Company filings (3Q26 Form 8-K, 10-Q and earnings call), Digrin, Trefis and K2 Capital estimates. Rel. performance vs S&P 500. Price history: month-end closes (Digrin), the 52-week closing low and high (Trefis) and closes on 28-30 Oct 2026. Chart: y/y growth in paid clicks and cost per click as disclosed (FY25: full year). Core EPS: operating income taxed at 17%, excluding gains and losses on equity securities.

- **3Q26 Summary.** Revenue rose 25% to $127.6bn, just short of the $128.0bn consensus: Search & other +12% to $63.4bn, YouTube ads +9% to $11.2bn, Network +1%, subscriptions, platforms and devices +11% to $14.3bn and Cloud +103% to $30.7bn. Operating income rose 30% to $40.6bn (31.8% margin), with Cloud's margin at 36.2% vs 23.7%. Net income fell 24% to $26.5bn and EPS of $2.12 missed the $3.02 consensus on an $8.7bn mark-to-market loss on equity securities, mainly SpaceX. Paid clicks +8%, cost per click +4%; TAC 20.0% of advertising revenue. Employees 204,757 (+7.7%). See Figure 1.
- **Capex and Funding Update. (1)** Capex was $51.4bn (40% of revenue), taking 9M26 to $132.0bn. The 2026 guide of $195-205bn was held, after rising from $175-185bn in February and $180-190bn in April; it implies $63-73bn in 4Q. **(2)** Management said 2027 capex will "increase significantly"; we model $270bn. **(3)** Operating cash flow fell to $42.3bn, so free cash flow was -$9.1bn, the second negative quarter running. **(4)** In 9M26 Alphabet raised $85.2bn of debt and repaid $8.9bn (long-term debt $125.1bn vs $46.5bn at end-2025), sold $49.6bn of common and mandatory convertible preferred stock in June, and $12.4bn through a $40bn at-the-market programme whose proceeds are mainly earmarked for employee equity tax withholding. There were no buybacks, leaving $69.5bn of authorisation unused. **(5)** Net cash was $140.0bn at 30 September, but $90.4bn of the cash line is marketable equity, mostly sale-restricted SpaceX stock. **Excluding investments, we estimate net cash falls from $49.6bn at September to roughly zero (-$1.4bn) by end-2027.**

Table 1: Alphabet Dec-27 PT Methodology (Sum of the Parts)

$ in millions, except per share; FY28E is the NTM year at Dec-27

	Bull	Base	Bear
FY28E Google Services revenue	451,344	443,036	412,576
Services operating margin	41.5%	39.5%	35.0%
x P/E on after-tax operating income	21x	18x	13x
Google Services value	**3,264,773**	**2,614,491**	**1,558,093**
FY28E Google Cloud revenue	247,011	229,976	195,906
Cloud operating margin	38.0%	35.0%	28.0%
x P/E on after-tax operating income	32x	26x	16x
Google Cloud value	**2,493,038**	**1,737,010**	**728,456**
Alphabet-level costs at Services P/E	(644,910)	(552,780)	(399,230)
Other Bets incl. Waymo	120,000	60,000	0
Equity investments, less haircut	225,630	169,222	112,815
YE27E net cash ex. investments	(1,358)	(1,358)	(1,358)
Target Equity Value	5,457,172	4,026,585	1,998,776
YE27E diluted shares (M)	12,560	12,560	12,560
Value per Share	**$434.49**	**$320.59**	**$159.14**
Scenario Probability	25%	50%	25%
Dec-27 Price Target (probability-weighted)		**$310.00**	
Return Potential (ex. dividends)		*11%*	

Source: Company reports, K2 Capital estimates. After-tax operating income at a 17% tax rate. Equity investments are the 30-Sep-26 carrying values of marketable ($90.4bn, incl. SpaceX $75.2bn) and non-marketable ($135.2bn) equity securities; the haircut covers tax on gains, sale restrictions and mark-to-market risk. Other Bets: Waymo raised $16bn at a $126bn valuation in Feb-26; Base applies a discount to Alphabet's share. Diluted shares add ~60M for the mandatory convertible preferred ($18.0bn carrying value) and assumed at-the-market issuance. Net cash uses long-term debt.

Figure 1: Alphabet Earnings Trends

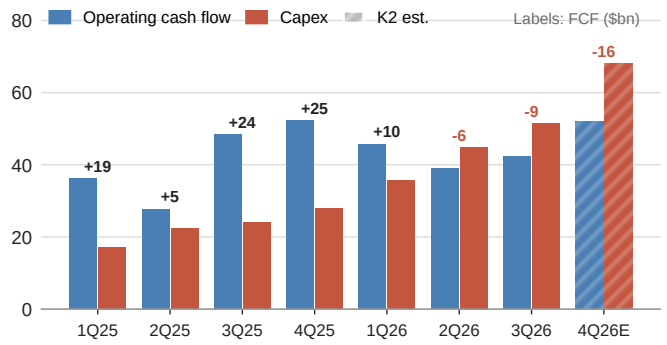
$ in millions, except where stated

$ in millions	3Q25	4Q25	1Q26	2Q26	3Q26
Google Search & other	**56,567**	**63,073**	**60,399**	**63,271**	**63,350**
y/y	*14.5%*	*16.7%*	*19.1%*	*16.8%*	*12.0%*
Paid clicks y/y | cost per click y/y	*+7% | +7%*	*n/d*	*+13% | +5%*	*+13% | +3%*	*+8% | +4%*
YouTube ads	10,261	11,383	9,883	11,055	11,207
Google Network	7,354	7,828	6,971	7,303	7,455
Subscriptions, platforms and devices	12,870	13,578	12,384	12,911	14,290
Google Cloud	**15,157**	**17,664**	**20,028**	**24,768**	**30,709**
y/y	*33.5%*	*47.8%*	*63.4%*	*81.8%*	*102.6%*
Total revenue (incl. Other Bets, hedging)	**102,346**	**113,828**	**109,896**	**119,796**	**127,577**
y/y	*15.9%*	*18.0%*	*21.8%*	*24.2%*	*24.7%*
Google Services operating income	33,527	40,132	40,589	39,544	39,157
margin	*38.5%*	*41.9%*	*45.3%*	*41.8%*	*40.7%*
Google Cloud operating income	3,594	5,313	6,598	8,814	11,121
margin	*23.7%*	*30.1%*	*32.9%*	*35.6%*	*36.2%*
Other Bets and Alphabet-level	(5,893)	(9,511)	(7,491)	(7,588)	(9,702)
Operating income	**31,228**	**35,934**	**39,696**	**40,770**	**40,576**
margin	*30.5%*	*31.6%*	*36.1%*	*34.0%*	*31.8%*
Diluted EPS (GAAP, $)	2.87	2.82	5.11	9.11	2.12
Cloud backlog ($bn)	155.0	240.0	>460	514.0	560.8
Operating cash flow	48,414	52,402	45,790	39,069	42,290
Capex	(23,953)	(27,804)	(35,674)	(44,924)	(51,355)
Free cash flow	**24,461**	**24,598**	**10,116**	**(5,855)**	**(9,065)**

Source: Company reports (Forms 8-K, 10-Q and 10-K), K2 Capital calculations. Paid clicks and cost per click as disclosed; n/d: 4Q25 not disclosed separately (FY25: paid clicks +6%, cost per click +7%). EPS includes gains and losses on equity securities: gains of $36.9bn in 1Q26 and ~$99bn in 2Q26, a loss of $8.7bn in 3Q26, chiefly SpaceX.

Figure 2: Capex Has Overtaken Operating Cash Flow

$ in billions; 4Q26E is a K2 estimate



Source: Company reports, K2 Capital estimates. 4Q26E capex of $68bn sits within the $63-73bn implied by the 2026 guide.

Figure 3: Dec-27 Value per Share: Services vs. Cloud Multiple

P/E on FY28E after-tax operating income; base case otherwise

Services P/E \ Cloud P/E	16x	20x	26x	30x	35x
12x	$213	$234	$266	$287	$314
14x	$231	$252	$284	$305	$332
16x	$249	$270	$302	$324	$350
18x	$267	$289	**$321**	$342	$368
20x	$286	$307	$339	$360	$387
22x	$304	$325	$357	$378	$405

Source: K2 Capital estimates. Red: more than 10% below the current price; amber: within 10%; green: more than 10% above. Each turn on the Services multiple is worth ~$12/share; each turn on Cloud ~$5.

Wrong Suspect: The Order of Events

The sequence in the brief (Reddit reports, then Google sells off) is the reverse of what happened, and the difference matters because it changes what the sell-off was about. Alphabet reported after the close on Wednesday 28 October, hours after the Federal Reserve held rates at 3.75-4.00%. Its shares fell 12.6% the next day to $283.82, a record ~$500bn one-day loss of market value, as investors focused on $51.4bn of quarterly capex, negative free cash flow, an EPS miss driven by the SpaceX mark and the guide to a "significant" increase in 2027 capex. Reddit reported after the close on 29 October and fell ~30% on 30 October, as its CEO said Google referrals were falling; Alphabet fell a further 1.4% to $279.84 that day. **Reddit's quarter is evidence about what AI answers do to publishers. It is not evidence about Google's revenue, which had been public for two days.**

Figure 4: Three Days in October

Date (ET)	Event	Market reaction
Wed 28 Oct, 2:00pm	FOMC holds the fed funds target range at 3.75-4.00%.	UST 10Y ~4.9%.
Wed 28 Oct, after close	**Alphabet 3Q26:** revenue +25% to $127.6bn (consensus $128.0bn); EPS $2.12 vs $3.02 on an $8.7bn equity-securities loss, mainly SpaceX; Cloud +103%; Search & other +12%; capex $51.4bn vs OCF $42.3bn; FCF -$9.1bn; 2027 capex to "increase significantly".	GOOGL lower after hours.
Thu 29 Oct	Brokers cut targets but stay well above the price: Piper Sandler $345, J.P. Morgan $375, BofA $380, KeyBanc $385. Focus: capex, FCF and the search slowdown.	**GOOGL -12.6%** to $283.82, a record ~$500bn loss of market value; S&P 500 -0.3%, Nasdaq -1.4%.
Thu 29 Oct, after close	**Reddit 3Q26:** revenue +53% to $895M, but US DAUq -2% and 4Q revenue guide of $1.00-1.03bn below ~$1.05bn consensus. CEO: Google search referrals fell by more than one million a week on average in October.	RDDT lower after hours.
Fri 30 Oct	Reddit's fall is widely attributed to Google's AI search features.	**RDDT ~-30%** to ~$90; GOOGL -1.4% to $279.84.

Source: Alphabet and Reddit 3Q26 results; Federal Reserve; Trefis, Decrypt, Investing.com and MarketBeat as reported. GOOGL 28-Oct close implied by the 12.6% fall.

Figure 5: Checking the Brief, Claim by Claim

The brief says	What the record shows	Verdict
"Google sold off after Reddit's earnings call"	Alphabet reported on 28 Oct and fell 12.6% on 29 Oct. Reddit reported after the close on 29 Oct and fell ~30% on 30 Oct, when Alphabet fell 1.4%.	**Order reversed**
"Reddit dropped ~30%"	Down ~30% on 30 Oct to ~$90, and ~44% over the week.	**Correct**
"Reddit's CEO says Google's AI isn't sending traffic"	Steve Huffman: "The AI mode does not drive traffic, not for us and not to anybody as far as I know."	**Correct**
"AI is destroying Google Search"	Search & other +12% y/y in 3Q26 to a record $63.4bn, on 8% more paid clicks. Growth did slow, from +19% in 1Q and +17% in 2Q.	**Not yet in the numbers**
"Search is growing inorganically by squeezing customers"	3Q26: paid clicks +8%, cost per click +4%; 9M26: +11% and +4%. Volume, not price, drove roughly two-thirds of growth.	**Not supported**
"Wall Street analysts know search is in trouble"	Post-results target cuts (to $345-385) centred on capex and FCF; every one sits 23-38% above the $279.84 close.	**Mischaracterised**
"Pure-play AI such as Nebius is the better bet"	NBIS is up ~84% YTD but fell 34.7% in October and 31.1% in July; it rides the same capex cycle, with more leverage to it.	**Not a hedge**
"My portfolio is up 170%"	No holdings, dates or benchmark are given.	**Unverifiable**

Source: Alphabet 3Q26 Form 8-K and earnings call; Reddit 3Q26 results and call; broker notes as reported by MarketBeat and Investing.com; Nebius share prices; K2 Capital.

Follow the Clicks: Who Loses When Google Answers

AI answers change who gets the click, not yet whether Google gets paid. When an AI Overview or AI Mode answers a question, the user stays on Google and the publisher that supplied the answer loses the visit. That is why the damage shows up first at Reddit, news sites and review pages, and why Google's own paid clicks still rose 8% in 3Q26. The risks to Google are second order and slower, but they are real: paid-click growth has slowed from 13% in 1H26 to 8%, AI Mode (now above 1 billion monthly users) monetises below classic search, chat assistants compete for commercial queries, and a thinner open web leaves AI answers with less to draw on. Figure 6 sets out the evidence; Figure 7 sizes what it would take to break search.

Figure 6: The Click Evidence

Source	Finding	Who loses
Pew Research Center (Jul-25)	Users who saw an AI summary clicked a traditional result in 8% of visits vs 15% without one; 1% clicked a link inside the summary.	Publishers (organic clicks)
Agarwal and Sen (randomised trial)	Exposure to AI Overviews cut clicks to external sites by 39.8%.	Publishers (organic clicks)
SparkToro and Datos	~68% of Google searches end without a click to the open web.	Publishers; Google keeps the user
Reddit 3Q26 (29-Oct)	Google search referrals fell by more than one million a week on average in October; US DAUq -2%; CEO: AI Mode "does not drive traffic".	Publishers dependent on Google referrals
Alphabet 3Q26 (28-Oct)	Paid clicks +8% y/y (1Q26 and 2Q26: +13%) and cost per click +4%; Search & other +12% to $63.4bn.	Not yet Google's ad clicks, though growth has slowed

Source: Pew Research Center (July 2025); Agarwal and Sen; SparkToro and Datos; Reddit and Alphabet 3Q26 results; K2 Capital.

Figure 7: What It Would Take to Break Search

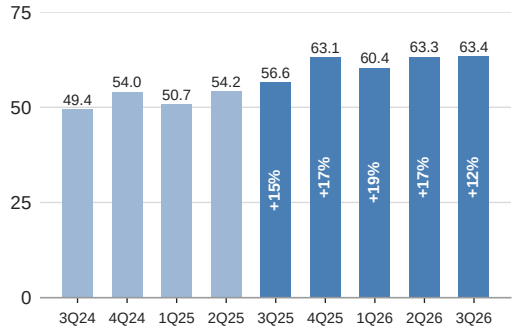
FY28E Search & other revenue at risk | Dec-27 value per share at risk

		AI monetisation vs. classic search		
AI share of commercial queries	**100%**	**85%**	**70%**	**55%**
20%	-	(3%) | -$8	(6%) | -$16	(9%) | -$24
35%	-	(5%) | -$14	(10%) | -$28	(16%) | -$42
50%	-	(8%) | -$20	(15%) | -$40	(22%) | -$59
65%	-	(10%) | -$26	(20%) | -$52	(29%) | -$77

Source: K2 Capital estimates. Base-case FY28E Search & other revenue of $296.3bn; lost revenue taken at a 75% decremental margin, taxed at 17% and capitalised at the base-case 18x. Green: under 6% of search revenue; amber: 6-15%; red: above 15%.

Figure 8: Search & Other Revenue

$ in billions; label: y/y growth



Source: Company reports.

Reddit is a canary, not a verdict. Publishers depend on organic clicks; Google is paid on ad clicks, which sit above and alongside AI answers and are still growing. For search to break, AI surfaces must take a large share of *commercial* queries and monetise well below classic search at the same time. If half of commercial queries moved to AI surfaces monetising at 70% of today's rate, ~15% of FY28E search revenue would be at risk, about $40/share of value. For scale, the 29 October fall took ~$41/share off the price. We see no evidence of a hit that size yet, but the stock now discounts a meaningful one, which is why we see it as fairly priced on search rather than cheap.

The Real Debate: Capex, Cash and Dilution

If search is not the problem, the 29 October reaction still needs explaining, and the explanation is in the cash flow statement. Alphabet's 2026 capex guide has been raised twice (Figure 8) and 3Q26 capex of $51.4bn was 40% of revenue. Management has guided 2027 "significantly" higher; we assume $270bn. On our model free cash flow is -$20.8bn in 2026E and -$30.5bn in 2027E before turning roughly neutral in 2028E (Figure 9), so the build is being funded by the balance sheet and by new shareholders: ~$76bn of net new debt this year, ~$61bn of equity and no buybacks. The offset is demand that is already contracted. Cloud backlog reached $560.8bn, 3.6x a year earlier (Figure 10), and Cloud now earns a 36.2% operating margin, so unlike the leveraged neoclouds Alphabet is not funding assets that earn less than its cost of capital. **The risks are payback period and concentration: roughly $200bn of the backlog is a single customer, Anthropic.**

Figure 8: The 2026 Capex Guide, Raised Twice

Guidance date	2026 capex guide	Context
Feb-26 (4Q25 results)	$175-185bn	vs $91.4bn in 2025 and $52.5bn in 2024
Apr-26 (1Q26 results)	$180-190bn	Cloud backlog nearly doubles q/q to >$460bn; 2027 to increase significantly
Jul-26 (2Q26 results)	$195-205bn	Raised again after $49.6bn equity raise in June; backlog $514bn
Oct-26 (3Q26 results)	$195-205bn (held)	9M26 $132.0bn; implies $63-73bn in 4Q; 2027 to increase significantly

Source: Alphabet earnings releases and calls.

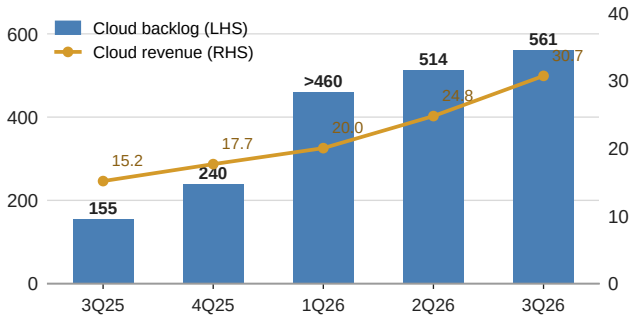
Figure 9: The Funding Bridge

$ in billions	FY25A	FY26E	FY27E	FY28E
Operating cash flow	164.7	179.1	239.5	285.1
Capex	(91.4)	(200.0)	(270.0)	(280.0)
Free cash flow	**73.3**	**(20.8)**	**(30.5)**	**5.1**
Acquisitions (Wiz, Intersect in 2026)	-	(34.1)	0.0	0.0
Dividends (incl. preferred)	(10.0)	(11.2)	(12.4)	(12.9)
Share repurchases	(45.4)	0.0	0.0	0.0
Equity issued	0.0	63.9	8.0	8.0
Net debt issued	35.7	76.3	30.0	15.0
Long-term debt, end of year	**46.5**	**125.1**	**155.1**	**170.1**
Net cash, end of year	**80.3**	**123.9**	**89.0**	**89.3**

Source: Company reports, K2 Capital estimates. FY26E equity issued includes ~$61bn raised in 9M26 (incl. preferred). Net cash includes marketable equity securities.

Figure 10: Cloud Backlog vs. Quarterly Cloud Revenue

$ in billions



Source: Company reports. Backlog is Google Cloud remaining performance obligations; 1Q26 disclosed as "over $460 billion".

Side Note: Pure-Play Is Not a Hedge

The brief prefers "pure-play AI" such as Nebius. Nebius is a neocloud: it rents NVIDIA GPU capacity, much of it to Microsoft and Meta under multi-year contracts, so it sits on the same capex cycle that hit Alphabet on 29 October, with more leverage to it and no search franchise to fund it. Its shares have risen this year but fell by about a third in both July and October. Swapping Alphabet for Nebius does not hedge the risk to search; it concentrates the risk to AI capex. We cannot verify the brief's "170%" portfolio claim and would not treat it as evidence either way.

Total return	YTD	Oct-26
Nebius (NBIS)	+84%	-34.7%
Alphabet (GOOGL)	-10.6%	-18.7%
S&P 500	+10.7%	-0.9%

Source: Share prices to 30-Oct-26 as reported (NBIS July 2026: -31.1%); Digrin; K2 Capital calculations.

Investment Thesis, Valuation and Risks

Alphabet Inc. *(Neutral; Price Target: $310.00)*

Investment Thesis
Alphabet fell 12.6% on 29 October on its own results, not on Reddit's, and the evidence for the popular explanation, that AI is destroying Google Search, is not in the numbers: search revenue grew 12% in 3Q26 on 8% more paid clicks and 4% higher prices per click. AI answers are taking clicks from publishers first, which is what Reddit's ~30% fall reflects. What the market is right to worry about is cash: capex of ~$200bn this year and significantly more in 2027, negative free cash flow through 2027E on our numbers, rising depreciation and equity issuance. The $560.8bn Cloud backlog, earned at a 36.2% margin, makes that a question of payback rather than of value destruction, but it is concentrated, and after the sell-off the shares price Services at ~18x 2027E earnings, in line with our base case. We rate shares Neutral.

Valuation
Our $310 Dec-27 PT is a probability-weighted sum of the parts on FY28E: a base case (50%) with Services at 18x and Cloud at 26x after-tax operating income ($321/share), a bull case (25%) at 21x and 32x ($434) and a bear case (25%) in which search revenue declines and the multiples fall to 13x and 16x ($159). The PT implies 11% upside, in line with our expectation for the market. We rate shares Neutral.

Risks to Rating and Price Target
Upside risks: paid-click growth re-accelerates as AI Mode ads scale; 2027 capex comes in below fears or Cloud converts its backlog faster than we model; Cloud margins hold above 35% as depreciation builds; buybacks resume; SpaceX gains. Downside risks: AI assistants take share of commercial queries, or AI Mode keeps monetising well below classic search; 2027 capex rises faster than Cloud revenue; Anthropic, ~$200bn of backlog, reduces or re-prices its commitment; remedies in the US search and ad-tech cases; further equity issuance at lower prices; a lower SpaceX share price; and a stronger dollar.

What Would Make Us Wrong?
We would move to Underweight if two or more of the following occur:

1. Paid clicks decline y/y for two consecutive quarters (3Q26: +8%), the first sign that AI answers are displacing ad clicks rather than organic ones.

2. Cost per click outgrows paid clicks for two consecutive quarters while Search & other grows below 8%: the "squeeze" in the brief would then be real.

3. 2027 capex is guided above ~$300bn (our model: $270bn) without Cloud backlog growing faster than capex, or Cloud margin falls below 25% for two quarters (3Q26: 36.2%).

4. Anthropic shifts a material share of its compute commitment elsewhere, or any single customer exceeds 40% of Cloud backlog (today ~36%).

We would move to Overweight if both of the following occur:

5. Paid-click growth returns to 10% or more with management reporting AI Mode monetisation close to classic search.

6. 2027 capex is guided at or below ~$250bn, or backlog converts fast enough to return FCF to positive in 2027.

Signposts
18 Nov: FOMC minutes. 9 Dec: FOMC decision. Early Feb 2027: 4Q26 results, the first 2027 capex figure and AI Mode monetisation. Through 1H27: Anthropic compute deals; SpaceX sale restrictions; US ad-tech ruling.

Alphabet Inc.: Summary of Financials

Income Statement - Annual	FY24A	FY25A	FY26E	FY27E	FY28E
Google Search & other	198,084	224,533	256,400	276,912	296,296
YouTube ads	36,147	40,367	44,439	47,994	51,833
Google Network	30,359	29,791	29,635	29,043	28,171
Subs., platforms & devices	40,340	48,026	54,657	60,669	66,736
Google Cloud	43,229	58,705	109,905	170,353	229,976
Other Bets and hedging	1,859	1,414	1,675	1,866	2,332
Revenue	**350,018**	**402,836**	**496,711**	**586,836**	**675,345**
Google Services	121,263	139,404	161,674	163,774	174,999
Google Cloud	6,112	13,910	38,573	57,920	80,492
Other Bets	(4,444)	(7,515)	(8,046)	(8,500)	(9,000)
Alphabet-level activities	(10,541)	(16,760)	(26,835)	(33,000)	(37,000)
Operating income	**112,390**	**129,039**	**165,366**	**180,194**	**209,491**
Other income (incl. equity gains)	7,425	29,787	127,278	(2,500)	(4,500)
Pre-tax income	**119,815**	**158,826**	**292,644**	**177,694**	**204,991**
Tax	(19,697)	(26,656)	(54,782)	(30,208)	(34,848)
Net income (GAAP)	**100,118**	**132,170**	**237,862**	**147,486**	**170,143**
Diluted EPS (GAAP)	8.04	10.81	19.23	11.72	13.49
Core EPS (ex. investment gains)	**7.49**	**8.76**	**11.13**	**11.98**	**13.89**
DPS	0.60	0.83	0.87	0.90	0.93
Diluted shares (wtd)	12,447	12,227	12,334	12,480	12,520

Balance Sheet & Cash Flow Statement	FY24A	FY25A	FY26E	FY27E	FY28E
Cash & marketable securities	95,657	126,843	249,048	244,144	259,396
Non-marketable securities	37,982	68,687	135,230	135,230	135,230
PP&E (net)	171,036	246,597	431,327	649,327	857,327
Other assets	145,581	153,154	230,157	230,157	230,157
Total assets	**450,256**	**595,281**	**1,045,762**	**1,258,858**	**1,482,110**
Long-term debt	10,883	46,547	125,102	155,102	170,102
Other liabilities	114,289	133,469	197,738	201,738	205,738
Total liabilities	**125,172**	**180,016**	**322,840**	**356,840**	**375,840**
Shareholders' equity (incl. preferred)	325,084	415,265	722,922	902,018	1,106,270
Total liabilities & equity	**450,256**	**595,281**	**1,045,762**	**1,258,858**	**1,482,110**
Net cash (incl. marketable equity)	84,774	80,296	123,946	89,042	89,294
Cash flow from operations	**125,299**	**164,713**	**179,149**	**239,486**	**285,143**
o/w Depreciation	15,311	21,100	31,455	52,000	72,000
Capital expenditure	(52,535)	(91,400)	(199,953)	(270,000)	(280,000)
as % of sales	*15%*	*23%*	*40%*	*46%*	*41%*
Acquisitions	(2,931)	-	(34,103)	0	0
Share repurchases	(62,222)	(45,400)	0	0	0
Dividends (incl. preferred)	(7,363)	(10,000)	(11,217)	(12,390)	(12,890)
Equity issued	0	0	63,893	8,000	8,000
Debt issued, net	(1,300)	35,664	76,343	30,000	15,000
Free cash flow	**72,764**	**73,313**	**(20,804)**	**(30,514)**	**5,143**

Income Statement - Quarterly	1Q26	2Q26	3Q26	4Q26E
Google Search & other	60,399	63,271	63,350	69,380
YouTube ads	9,883	11,055	11,207	12,294
Google Network	6,971	7,303	7,455	7,906
Subs., platforms & devices	12,384	12,911	14,290	15,072
Google Cloud	20,028	24,768	30,709	34,400
Other Bets and hedging	231	488	566	390
Revenue	**109,896**	**119,796**	**127,577**	**139,442**
Google Services	40,589	39,544	39,157	42,384
Google Cloud	6,598	8,814	11,121	12,040
Other Bets	(2,100)	(1,799)	(2,047)	(2,100)
Alphabet-level activities	(5,391)	(5,789)	(7,655)	(8,000)
Operating income	**39,696**	**40,770**	**40,576**	**44,324**
Gains (losses) on equity securities	36,915	99,025	(8,660)	0
Other income, net	801	(1,042)	439	(200)
Pre-tax income	**77,412**	**138,753**	**32,355**	**44,124**
Tax	(14,834)	(26,560)	(5,887)	(7,501)
Net income (GAAP)	**62,578**	**112,193**	**26,468**	**36,623**
Diluted EPS (GAAP)	5.11	9.11	2.12	2.92
Core EPS (ex. investment gains)	**2.69**	**2.75**	**2.72**	**2.96**
Diluted shares (wtd)	12,238	12,309	12,368	12,420
Capex	(35,674)	(44,924)	(51,355)	(68,000)
Free cash flow	**10,116**	**(5,855)**	**(9,065)**	**(16,000)**

Ratio Analysis	FY24A	FY25A	FY26E	FY27E	FY28E
Operating margin	32.1%	32.0%	33.3%	30.7%	31.0%
Google Services margin	39.8%	40.7%	42.0%	39.5%	39.5%
Google Cloud margin	14.1%	23.7%	35.1%	34.0%	35.0%
Net profit margin (GAAP)	28.6%	32.8%	47.9%	25.1%	25.2%
Revenue y/y	-	15.1%	23.3%	18.1%	15.1%
Search & other y/y	-	13.4%	14.2%	8.0%	7.0%
Google Cloud y/y	-	35.8%	87.2%	55.0%	35.0%
Core EPS y/y	-	16.9%	27.0%	7.7%	15.9%
Capex / sales	15.0%	22.7%	40.3%	46.0%	41.5%
ROE (GAAP)	30.8%	31.8%	32.9%	16.4%	15.4%
P/E, core (x)	37.3x	31.9x	25.1x	23.4x	20.1x
P/E, GAAP (x)	34.8x	25.9x	14.6x	23.9x	20.7x
P/BV (x)	10.6x	8.3x	4.8x	3.8x	3.1x
FCF yield	2.1%	2.1%	(0.6%)	(0.9%)	0.1%

Source: Company reports, K2 Capital estimates.
Note: $ in millions (except per-share data). Fiscal year ends Dec. o/w - out of which. FY24A-FY25A and 1Q-3Q26 are actuals; FY26E includes 4Q26E. Core EPS is operating income taxed at 17%, excluding gains and losses on equity securities and other income. FY26E balance sheet rolls forward from 30-Sep-26 (marketable equity, incl. SpaceX, held flat); no investment gains or losses are forecast. FY25A acquisitions not shown; FY25A debt issued is the change in long-term debt. Depreciation excludes amortisation of intangibles.

Analyst Certification: The research analysts of K2 Capital Limited responsible for this report certify that (1) the views expressed in this report accurately reflect their personal views about the subject company and its securities, and (2) no part of their compensation was, is or will be directly or indirectly related to the specific rating or views expressed in this report.

Important Disclosures

Ratings: Overweight: over the duration of the price target, we expect the stock to outperform the total return of the S&P 500. Neutral: we expect the stock to perform in line with it. Underweight: we expect the stock to underperform it. Price targets are set for the period stated and are based on the methodology and risks described in this report.

Date	Rating	Price ($)	Price Target ($)
05-Nov-26	N (initiation)	279.84	310.00

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Sources and methodology: Prices are as of the close on 30 October 2026 and no information after that date is used. Company data are from Alphabet's earnings releases for 1Q26-3Q26 (3Q26: Form 8-K, Exhibit 99.1, 28 October 2026) and calls, its Forms 10-Q for 2026 and Form 10-K for 2025, and its June 2026 equity capital raise announcement. Other sources include Reddit's 3Q26 results and call (29 October 2026); the Federal Reserve FOMC statement (28 October 2026); Pew Research Center (July 2025); Agarwal and Sen's randomised study of AI Overviews; SparkToro and Datos; Waymo's February 2026 funding announcement; share price data from Digrin and Trefis; and reporting by Reuters, Bloomberg, CNBC, Decrypt, MarketBeat, Investing.com, Futurum, StockTitan and sec-api.io. Estimates, scenario values and sensitivities are K2 Capital's and are subject to change without notice.

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