

November, 17, 2017

## Akamai Technologies, Inc. : AKAM

Joshua Weiss

**Sector:** Information Technology

**Industry:** Internet Software and Services

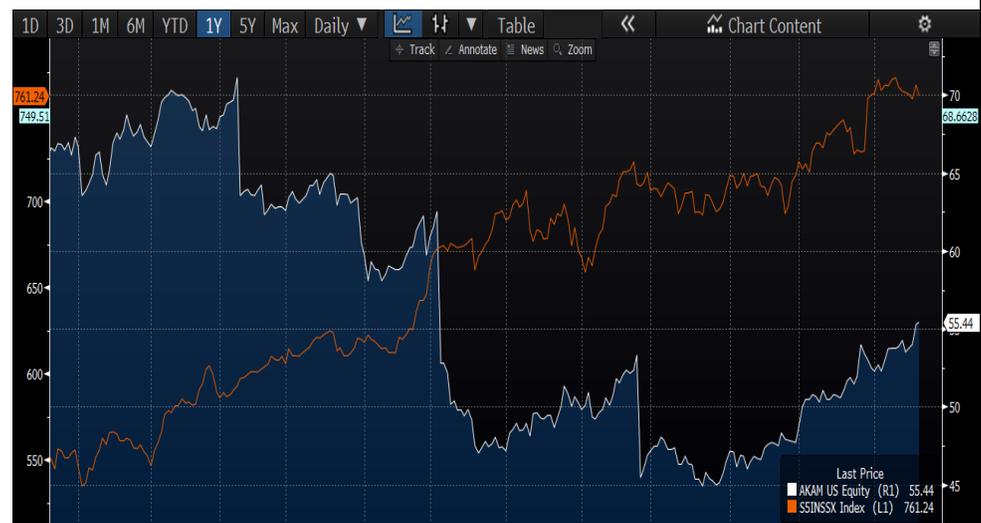
**Current Price:** \$55.26

**Target Price:** \$78.66

**Company Description:** Akamai Technologies Inc. is the global leader in Content Delivery Network services. Their goal is to provide services for customers to be as fast, reliable and secure their information as best as they possibly can.

### BUY

Current Price: \$55.26  
 Target Price: \$78.66  
 Market Cap: 9.38B  
 WACC: 9%  
 ROIC: 7.22%  
 Avg Volume: 2.21M  
 EBITDA margin: 31.6%  
 Operating Margin: 19.64%



### Thesis:

Akamai Technologies Inc. is a company that has a diverse portfolio with information software and services. They provide cloud networks for companies to operate on while also having fast and secure services to protect customer's information from hackers. With an EBITDA margin of 31.6% and an operating margin of 19.64% being at the top of their industry, it shows that they retain the most money from each dollar of revenue. In Q4 the acquisition of Nominum and in the future gaining of market share from their OTT focus, Akamai Technologies Inc. is priced low at \$55.26 and is a buy.

### Catalysts:

- A lot of online traffic in Q4 due to e-commerce customers surfing the web for the holiday seasons. Expecting to see slight increases in revenue from acquisitions.
- Will start to see an impact on revenue from their acquisitions, especially from Nominum.
- Gain market share on the OTT focus as there is higher traffic volume.

## Company Performance

Akamai Technologies is split up into three divisions and all of these divisions have a different part in four solutions. In the 3<sup>rd</sup> quarter earnings call, the CEO, Tom Leighton said that they had a great quarter due to the continuous rapid growth of their security offerings and a very strong traffic acceleration in their Media Business. Akamai Technologies reported revenue in the 3<sup>rd</sup> quarter of \$621 million. This was above the high-end of their guidance range and was a 6% increase from the 3<sup>rd</sup> quarter of 2016. The Cloud Security section of their portfolio was the fastest growing part of their whole business with a total of \$121 million in revenue and a growth of 27% year-over-year. As of September 30, 2017 AKAM had an EBITDA margin of 31.6% and an EPS of \$1.86. They have also reported a Gross profit of \$1,606.4M, which is the same gross margin percentage in the 9 months of 2017 as all of 2016. In 2016, they have an operating margin as a company of 19.64% which although is a decrease by 2% from 2015, it is a growth of 7.5% in year-over-year growth. They have negative growth in gross margin, EBITDA margin, Operating margin and Net income margin. This is not bad because although they are all negative, this is due to a very poor performance in 2015 and all of these 4 margins have been increasing and are almost positive year-over year growth. With the company continuing to beat their EPS and revenue and keeping a mid-30% EBITDA margin, I believe that this will allow the company to increase their growth margins to positive. With all these growth margins becoming positive it will drive the company's revenue and stock price up as the company continues to grow at a steady rate.

Revenue, Adj	859.8	1,023.6	1,158.5	1,373.9	1,577.9	1,963.9	2,197.4	2,340.0	2,455.7
Growth %, YoY	8.7	19.1	13.2	18.6	14.8	24.5	11.9	6.5	6.6
Gross Profit, Adj	609.8	720.2	704.8	844.0	1,066.8	1,352.9	1,471.8	1,531.0	1,606.4
Margin %	70.9	70.4	60.8	61.4	67.6	68.9	67.0	65.4	65.4
EBITDA, Adj	347.3	397.6	456.0	524.8	600.9	740.5	770.6	806.2	776.1
Margin %	40.4	38.8	39.4	38.2	38.1	37.7	35.1	34.5	31.6
Net Income, Adj	144.7	170.8	198.8	208.3	294.9	338.3	333.1	342.7	325.7
Margin %	16.8	16.7	17.2	15.2	18.7	17.2	15.2	14.6	13.3

## Management/Ownership

The current CEO of Akamai Technologies was one of the co-founders in 1998, Dr. Tom Leighton. He served as the Chief Scientist from 1998 to 2013 when he was finally promoted to CEO. Through the time he has been CEO, the company has transitioned from a Content Delivery Network to one of the most trusted cloud delivery and cybersecurity platforms. Since he became CEO, the company's revenue and profit has grown 70%. Jim Benson operates as the VP and CFO for Akamai. He is the director for all the company's accounting, tax, treasury, business finance and corporate services activities. He use to be the CFO at HP and joined Akamai in 2009. When he joined in September of 2009, the price of the stock was \$19.68 and within a year as CFO the company's stock grew to \$50.18. Since 2014, as a whole Acamai has had stock base compensation grow from around \$21 million to \$31 million. This can prove to do well for the company as employees will work harder to have the company do better because they will receive compensation based on how the company is doing.

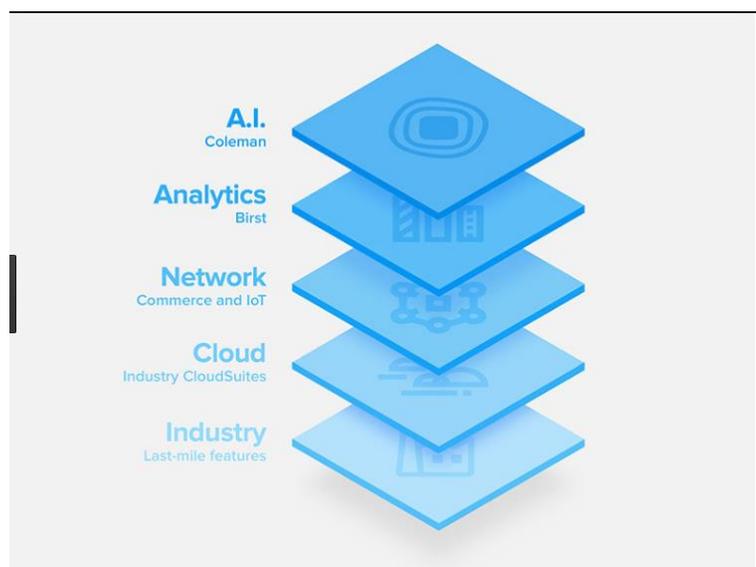
From the beginning of the year, the company has not had that much change in ownership. They have had an increase in since January, 2017 in hedge fund manager ownership from 4.3% to 5% today. This is showing us that many investors see potential in the company to grow and they are starting to purchase the stock.

Combining this information with a short interest of 3.27 days, tells us that the investors are not shorting this company and if they are only holding the short for 3 and a quarter days at a time. The majority of the company's ownership is through Investment Advisor at 83.2% of their total ownership. Besides the top two, the other ownership types have not changed much in the past year.

Ownership Type	11/12/17	Curr ↓	Change	
11) Investment Advisor	83.56	83.20	-0.36	<input checked="" type="checkbox"/>
12) Hedge Fund Manager	5.41	4.99	-0.42	<input type="checkbox"/>
13) Bank	2.41	2.88	+0.47	<input type="checkbox"/>
14) Individual	2.65	2.63	-0.02	<input type="checkbox"/>
15) Pension Fund	2.13	2.13	0.00	<input type="checkbox"/>
16) Government	1.24	1.23	-0.01	<input type="checkbox"/>
17) Insurance Company	0.88	1.17	+0.29	<input type="checkbox"/>
18) Sovereign Wealth Fund	1.09	1.08	-0.01	<input type="checkbox"/>
19) Brokerage	0.31	0.31	0.00	<input type="checkbox"/>
20) Holding Company	0.08	0.14	+0.06	<input type="checkbox"/>
21) Corporation	0.12	0.11	-0.01	<input type="checkbox"/>

## Industry

The Industry Software and Services industry as a whole has been growing massively and it does not look like it is going to slow down. Software services revenue year over year has been growing at 35%. This looks like it is going to continue to grow as new software continues to be processed and integrated. Internet revenue year over year growth is growing at 25.1%. This is due mainly from the big 6 platforms continuing acceleration growth and does not look like as it is going to slow down as alphabet, amazon, apple, facebook, Microsoft and Netflix are continuing to show massive revenue growth and profits. Software by itself has been having revenue growth year over year of 10.7% due to new technologies coming out and a high volume usage of these new software technologies. Lastly, Systems and PC hardware revenue growth year over year has been 9.7%. This growth for the industry although is the smallest through these four sections is still vital for the industry as a whole as these software and hardware cannot operate without having the system and PC hardware to operate in.



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## Segments

Akamai is broken down into three divisions and four solutions. The three divisions are their web division customers, media division customers and their enterprise and carrier division customers. The web division customers revenue is \$328M which is up 14% from quarter three of 2016. Most of this segment is made up of their Cloud Security offerings which is 53% of this divisions revenue. One thing that will drive this segment to continue to grow at low digit 10% is the bot manager premier. The BMP uses an artificial intelligence to distinguish the machines from the human users. It can detect the ways that a human touches the screen, presses a key or even how the human moves with a mouse. They already had 70 customers that are willing to use BMP and predict more people will be willing to use it as they believe that billions of dollars are lost due to credential abuse annually from bot hacking. The second division is their Media Division customers which has been receiving the most focus out of all the divisions. They had a total revenue of \$273M which was down 1% YOY but is up 3% that is excluding the impact of the large internet platform customers. They saw the most YOY traffic growth in Q3 since 2015. This is very good because they were working hard to increase traffic growth. The last division is their smallest which is Enterprise and Carrier Division. This division has basically hit its mature stage and only accounts for \$20M of their revenue and is up 1% from a strong quarter three in 2016.

The four solution categories are performance and security solutions, cloud security solutions, media delivery solutions, and services and support solutions. The largest solution is the performance and security solutions with a total revenue for the third quarter of \$381M. This was a growth of 10% year over year and although this has declined over the years due to their media division not using their performance solutions as much, they still predict to see steady growth throughout the next few years. The Cloud Security solutions is their fastest growing solutions and their flagship product. They had a third quarter revenue of \$121M, which was up 27% year over year. This is mainly due to the Kona Site Defender. The Kona Site Defender examines all the traffic coming to a website and determines its safety. It can be used as a virtual patching layer in front of websites and apps which is what allows customers to be protected. This is growing rapidly due to many financial hacks across the USA, which showed millions of peoples financial information. The third solution is the Media Delivery Solution which had a third quarter revenue of \$183M which was down 3% YOY. The growth although is negative, was improvement from the second quarter which was driven from the acceleration of media traffic. The smallest solution category is their services and support solutions which has a revenue of \$57M. This is a growth of 12% year over year. Through all these divisions and solutions, Akamai will be driven by their Nominum acquisition and their cloud security segment to drive their margins back to positive percentages.

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## Competitors

Akamai compared to their competitors are one of the largest companies. Although the sales 1 year growth vs there competitors is less than the median, they beat most of their competitors in all the other categories. Their

EBITA margin for the past three years is best in class at 35.74%, while the second best company is at 26.44%.

They also are best in class for operating margin for one year and operating margin for the past 3 years. The operating margin for the past year is at 20.16% which means for

Name (BICS Best Fit)	Sales 1 Yr Growth	Gross Margin	Gross Margin 3 Yr	Operating Margin	Operating Margin 3 Yr	EBITDA Margin	EBITDA Margin 3 Yr	EPS Before XO 1 Yr	Return on Equity	Return on Capital
Median	16.82%	66.77%	67.24%	7.12%	7.16%	16.68%	12.78%	-50.04%	6.71%	6.22%
100) AKAMAI TECHNOLOGIES INC	6.49%	65.43%	67.10%	20.16%	22.24%	31.60%	35.74%	0.56%	11.31%	10.06%
101) SPLUNK INC	42.12%	79.89%	82.55%	-35.00%	-41.88%	-22.02%	-38.70%	-20.45%	-34.29%	--
102) PEGASYSTEMS INC	9.90%	68.11%	68.49%	5.42%	7.92%	7.15%	11.74%	-25.53%	10.81%	--
103) ACI WORLDWIDE INC	-3.85%	55.76%	55.28%	8.93%	12.82%	24.15%	22.19%	50.68%	11.25%	6.72%
104) PROGRESS SOFTWARE CORP	7.36%	83.79%	85.53%	17.43%	17.99%	33.64%	26.44%	-564.71%	6.71%	6.22%
105) GTT COMMUNICATIONS INC	41.28%	47.48%	43.44%	8.91%	6.40%	24.78%	18.63%	-74.55%	-8.66%	--
106) LIMELIGHT NETWORKS INC	-1.57%	42.41%	40.45%	-6.93%	-12.75%	9.21%	-0.47%	-195.83%	-10.12%	-9.95%
107) SERVICENOW INC	38.29%	71.33%	67.37%	-10.92%	-16.51%	-0.29%	-10.47%	-116.54%	-42.28%	-18.95%

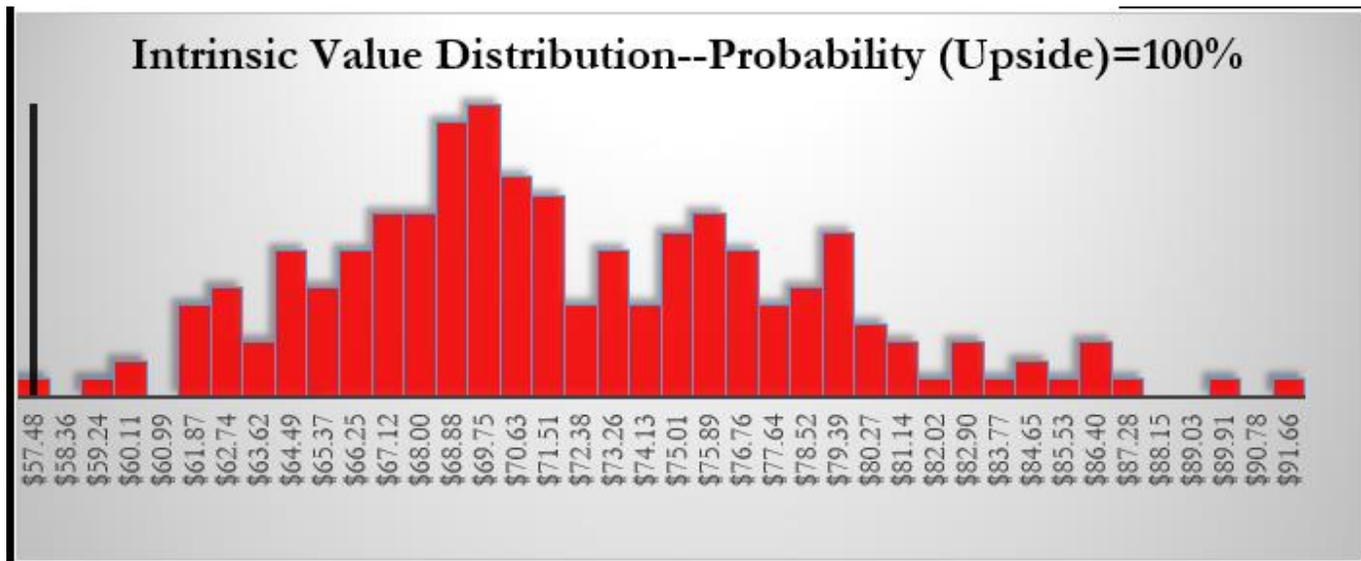
every dollar of revenue, \$.20 is left over after paying off all the costs. This is higher than all their other competitors which shows us that they retain more money per dollar after costs than all their competitors.

Compared to the two companies that are larger than them, Splunk inc. and Servicenow inc., Akamai has a positive ROE at 10.1% while these companies have negative ROEs. They also have a 1 year revenue growth less than the median of the industry. However, most of these companies that are growing at 35-40% revenue growth also have a negative Earning per share for the past year. The median for the industry is -6.40% while Akamai Technologies has a one year Earning per share 5.21%. Although they do not lead in every category for the industry versus their competitors, they are first in class in what I believe is the two main categories which is EBITDA margin and Operating margin and in the other categories they have steady growth.

## What if Analysis

Upside scenario:

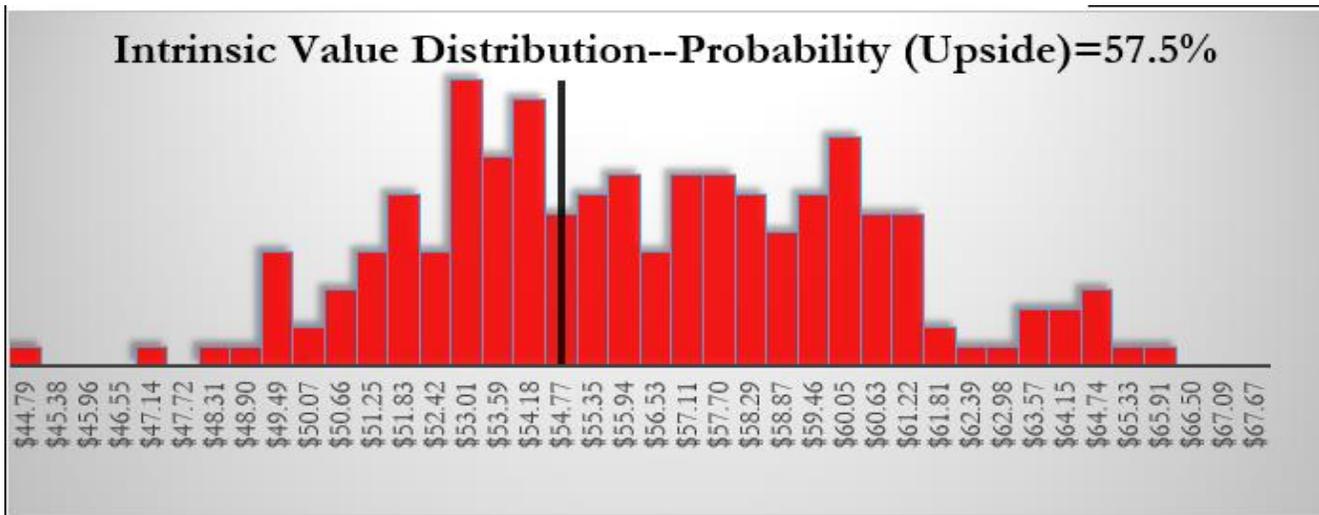
With my one-year target price of \$78.66, I believe that the only thing that will change in this company will be



their revenue and operating cost. With assumptions of forecasted revenue growth being 10% for the next quarter and 4 years after due to the acquisition of Nominum having a direct increase of revenue of 3%. This will have a steady 10% revenue growth for the next 4 years after I believe and than slowly decline to a 6% revenue growth rate for the long-term. Operating cost will also be cut by a couple of percent to 60% for the long term as they continuation of implementing and acquiring new companies will cut their costs by a little. With these assumptions, we would see a 42.35% return if it reached the one-year target price.

Downside Scenario:

If the company stayed at a revenue growth rate of 6% for the next 10 years and had their operating margin increase to 70% from 62.1% they would have a negative one year return of -.24%. With these assumptions of revenue and operating cost coming from if the implementation of Nominum does not do as well as they hoped and has no effect on the company’s revenue at all. There operating cost could increase to 70% if they make another acquisition that does not work out as well as they thought and causes there operating costs to go up instead of down.



## Conclusion

Akamai Technologies Inc although is not at the top of their industry in every category, they are the most well rounded. They lead the industry vs their competitors in EBITDA margin and Operating margin, which are the two main margins that show how much money they retain per dollar of revenue. With the acquisition of Nominum and anticipating EBITDA margin to increase by a couple of percentages, I believe Akamai Technologies in underpriced and is a certain buy.

**Akamai Technologies, Inc.**  
**(AKAM)**

**CENTER FOR GLOBAL FINANCIAL STUDIES**

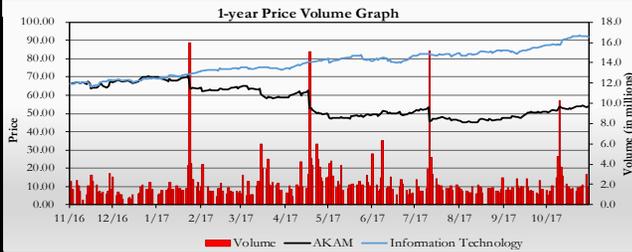
**BULLISH**

Analysis by Joshua Weiss  
11/17/2017

Current Price: **\$55.26**  
Divident Yield: **0.0%**

Intrinsic Value: **\$70.42**  
Target Price: **\$78.66**

Target 1 year Return: 42.35%  
Probability of Price Increase: 100%

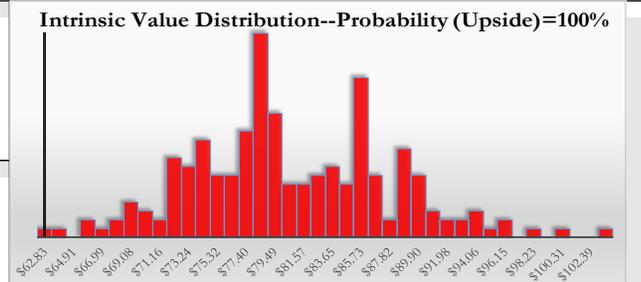


<b>Description</b>	
Akamai Technologies, Inc. provides cloud services for delivering, optimizing, and securing content and business applications over the Internet in the United States and internationally.	
<b>General Information</b>	
Sector	Information Technology
Industry	Internet Software and Services
Last Guidance	November 3, 2015
Next earnings date	February 7, 2018
Estimated Country Risk Premium	7.01%
Effective Tax rate	24%
Effective Operating Tax rate	24%

<b>Market Data</b>	
Market Capitalization	\$9,347.33
Daily volume (mil)	2.76
Shares outstanding (mil)	169.15
Diluted shares outstanding (mil)	173.85
% shares held by institutions	116%
% shares held by investments Managers	76%
% shares held by hedge funds	5%
% shares held by insiders	2.91%
Short interest	5.63%
Days to cover short interest	5.11
52 week high	\$71.64
52-week low	\$44.65
Volatility	33.60%

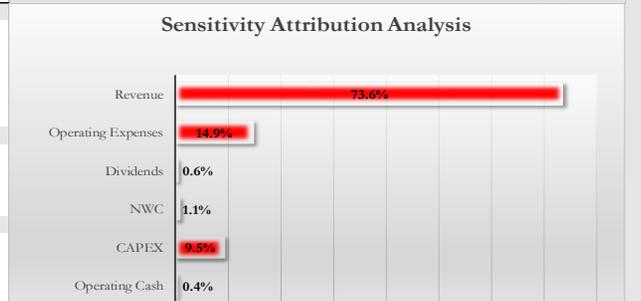
<b>Past Earning Surprises</b>		
Quarter ending	Revenue	EBITDA
9/30/2016	2.11%	-21.55%
12/31/2016	1.89%	-26.20%
3/31/2017	0.75%	-24.99%
6/30/2017	0.65%	-31.10%
9/30/2017	1.70%	-31.30%
Mean	1.42%	-27.03%
Standard error	0.3%	1.9%

<b>Peers</b>	
Red Hat, Inc.	
Twitter, Inc.	
eBay Inc.	
Limelight Networks, Inc.	
GoDaddy Inc.	
2 Global, Inc.	
Symantec Corporation	
TrueCar, Inc.	



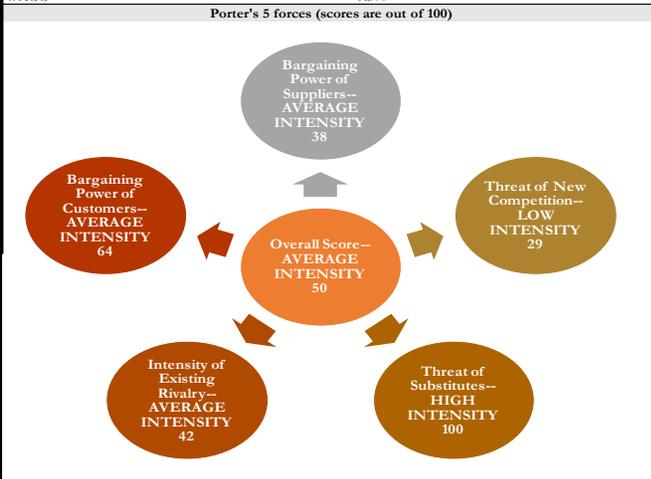
<b>Management</b>		<b>Position</b>	
Leighton, F.	Co-Founder, CEO & Director	<b>Total compensations growth</b>	<b>Total return to shareholders</b>
McConnell, Rick	President & GM of Web Divisi	235.49% per annum over 5y	-5.84% per annum over 5y
Benson, James	Executive VP & CFO	6.3% per annum over 4y	7.86% per annum over 4y
Blumofe, Robert	Executive VP of Platform & G	26.4% per annum over 5y	-5.84% per annum over 5y
Wheaton, William	Chief Strategy Officer	15.56% per annum over 2y	5.62% per annum over 2y
Kalia, Kumud	Chief Information Officer	N/M	N/M
		N/M	N/M

<b>Profitability</b>		<b>AKAM (LTM)</b>		<b>AKAM (5 years historical average)</b>		<b>Peers' Median (LTM)</b>	
Return on Capital (GAAP)	15.6%	17.28%	10.96%	10.96%	10.96%	11.63%	11.63%
Operating Margin	23%	22.38%	11.63%	11.63%	11.63%	0.94	0.94
Revenue/Capital (GAAP)	0.67	0.77	0.77	0.77	0.77	20.2%	20.2%
ROE (GAAP)	11.5%	11.3%	11.3%	11.3%	11.3%	21.3%	21.3%
Net margin	17.3%	18.4%	18.4%	18.4%	18.4%	0.95	0.95
Revenue/Book Value (GAAP)	0.67	0.62	0.62	0.62	0.62		



<b>Invested Funds</b>		<b>AKAM (LTM)</b>		<b>AKAM (5 years historical average)</b>		<b>Peers' Median (LTM)</b>	
Cash/Capital	16.0%	25.7%	26.8%	26.8%	26.8%	-9.8%	-9.8%
NWC/Capital	5.2%	6.6%	6.6%	6.6%	6.6%	49.9%	49.9%
Operating Assets/Capital	50.8%	44.3%	44.3%	44.3%	44.3%	33.0%	33.0%
Goodwill/Capital	28.1%	23.4%	23.4%	23.4%	23.4%		

<b>Capital Structure</b>		<b>AKAM (LTM)</b>		<b>AKAM (5 years historical average)</b>		<b>Peers' Median (LTM)</b>	
Total Debt/Market Capitalization	0.19	0.10	0.44	0.44	0.44	5.3%	5.3%
Cost of Existing Debt	2.9%	3.0%	3.0%	3.0%	3.0%	BBB	BBB
CGFS Rating (F-score, Z-score, and default Probability)	BBB	BBB	BBB	BBB	BBB	9.4%	10.5%
WACC	9.3%	9.4%	9.4%	9.4%	9.4%		



<b>Revenue Growth Forecast</b>	
Period	Revenue Growth Forecast
Base Year	7%
9/30/2018	10%
9/30/2019	10%
9/30/2020	10%
9/30/2021	10%
9/30/2022	10%
9/30/2023	8%
9/30/2024	8%
9/30/2025	8%
9/30/2026	6%
9/30/2027	6%
Continuing Period	2%

<b>Valuation</b>	
<b>NOPAT Margin Forecast</b>	
Period	Revenue to Capital Forecast
Base Year	0.56
9/30/2018	0.57
9/30/2019	0.55
9/30/2020	0.53
9/30/2021	0.52
9/30/2022	0.51
9/30/2023	0.47
9/30/2024	0.44
9/30/2025	0.41
9/30/2026	0.39
9/30/2027	0.37
Continuing Period	0.34

<b>Return on Capital Forecast</b>	
Period	Return on Capital Forecast
Base Year	13.7%
9/30/2018	10.9%
9/30/2019	10.8%
9/30/2020	11.0%
9/30/2021	11.4%
9/30/2022	15.2%
9/30/2023	13.9%
9/30/2024	13.1%
9/30/2025	12.4%
9/30/2026	11.6%
9/30/2027	11.0%
Continuing Period	9.9%

<b>WACC Forecast</b>	
Period	Price per share Forecast
Base Year	\$70.63
9/30/2018	\$78.61
9/30/2019	\$86.62
9/30/2020	\$94.91
9/30/2021	\$103.49
9/30/2022	\$112.63
9/30/2023	\$121.92
9/30/2024	\$131.50
9/30/2025	\$141.44
9/30/2026	\$151.53
9/30/2027	\$162.49
Continuing Period	