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HEDGEYE

INTERNET & MEDIA

INVESTMENT IDEAS – 2Q15 UPDATE

July, 2015

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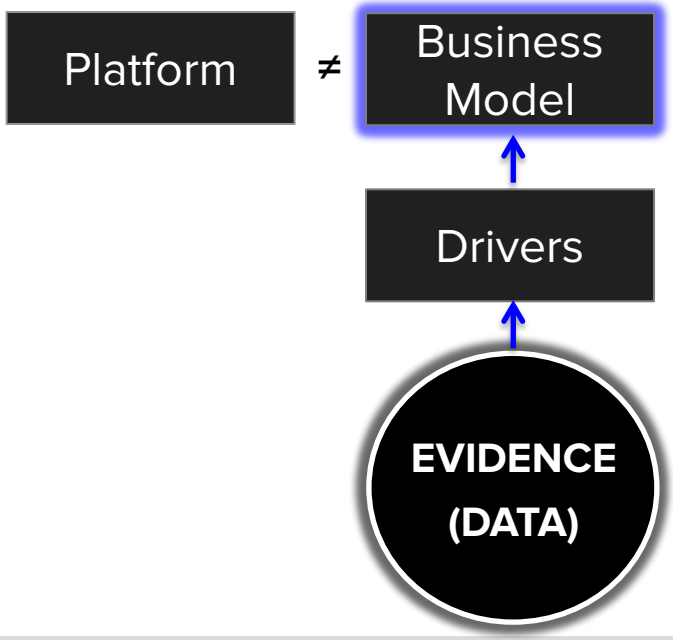
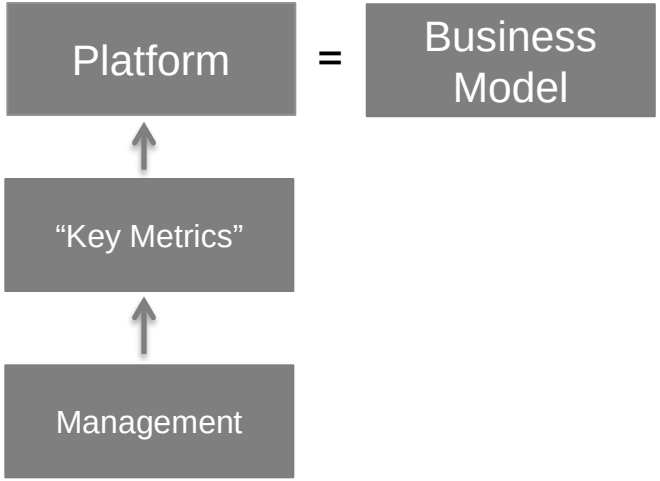


TRADITIONAL SELL-SIDE



OUR FOCUS IS THE BUSINESS MODEL, NOT THE PLATFORM

There's a difference between the platform, and how the company monetizes the platform (the Business Model). We focus on the latter, and do not defer to mgmt to tell us what drives it. We focus on the data.

BETTER DATA = BETTER THESIS

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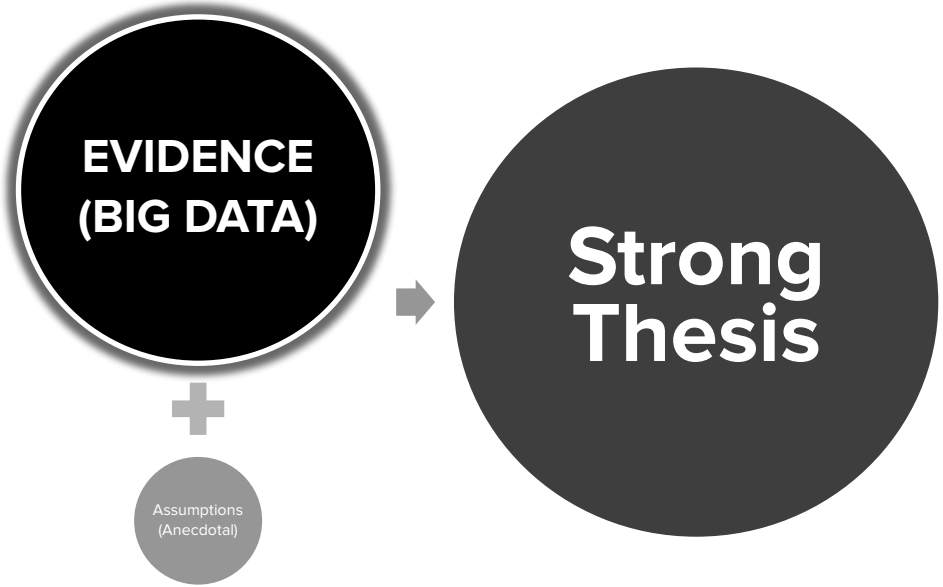

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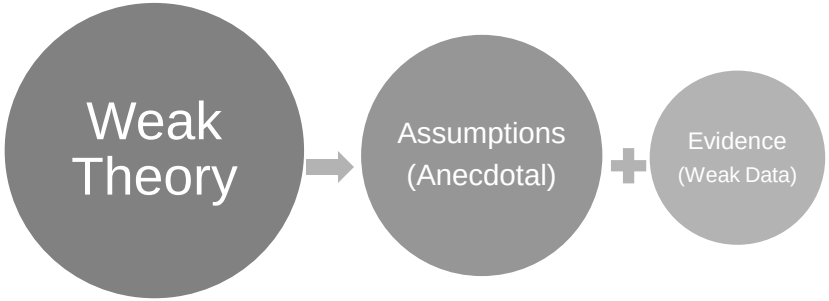


WE LET THE DATA TELL THE STORY

The data drives the thesis, not the other way around. That is our edge. We avoid saying anything unless we have the data to back it up, and we don't make up stories when don't have the answer.

LNKD LONG THESIS

LNKD: LONG THESIS SUMMARY

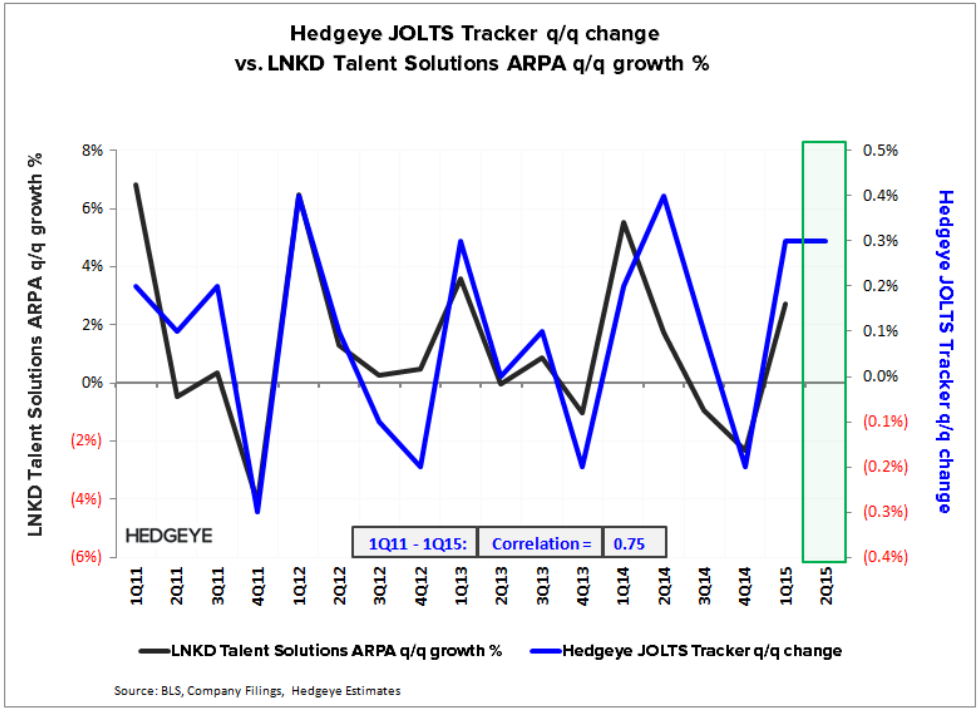
1. **Business Model**: Product portfolio is primarily varying levels of paywalls to its member profiles; Virtual moat provides premium pricing/high margins.

2. **Analysis:** ARPA is key, and the selling environment is tied to macro. Early penetration its core Talent Solutions TAM. Continues to reinvest in business.

3. **Outlook:** 1Q15 not nearly as bad as market reaction. Account transition issue due to a massive salesforce investment into an accelerating macro tailwind

4. **Setup**: Management used soft 1Q15 results to rebase full-year consensus expectations, which are now inline with guidance for first time in over a year.

5. **Duration**: Depends on macro and/or consensus



REBASED EXPECTATIONS + DISCOUNT = ENTRY POINT

LNKD is a name we have liked for a while, but couldn't pull the trigger on at new 52-wk highs and consensus estimates consistently tracking ahead of guidance. Overreaction to 1Q15 print gives us our entry point.

LNKD: KEY POINTS

1

REAL PLATFORM, REAL CASH

LNKD's value comes from its database of professional profiles, which likely can't be replicated at comparable scale. That moat has led to a premium-priced product portfolio that produces the margins/cash flow necessary to consistently reinvest in its business/expand its TAM

2

EMPLOYEE'S MARKET = GROWING OPPORTUNITY

Wee see Talent Solutions as the swing factor, and the bulk of that TAM is not in account volume (LCS customers), but in up-selling those accounts (ARPA). Historically, that up-sell becomes much easier for LNKD as the burden to fill open positions intensifies, which is currently the case.

3

TRANSITION = INVESTMENT

Outside of Fx, much of the 1Q weakness was due to its salesforce account transition, which was actually a major investment into an accelerating macro tailwind. The 2015 guidance cut captured that transitory impact, but also rebased consensus estimates to allow for upside.

PRODUCT PORTFOLIO = PAYWALLS

LNKD: NETWORKING PRODUCT COMPARISON							
SEGMENT==>	TALENT SOLUTIONS			PREMIUM SUBSCRIPTIONS			
PRODUCT==>	Recruiter			Sales Navigator		Individual	
Price/Feature	Corporate	Small Business	Recruiter Lite	Team	Individual	Business Plus	Job Seeker
Monthly Price	n/a	n/a	**$120**	**$100**	**$80**	**$60**	**$30**
Annual Price	**$9,000**	**$4,800**	**$1,200**	**$1,200**	**$780**	**$576**	**$360**
InMails	150	50	30	30	15	15	3
Collaboration	x	n/a	n/a	x	n/a	n/a	n/a
Search Radius	500	500	100	?	n/a	n/a	n/a
Project Folders	x	n/a	n/a	n/a	n/a	n/a	n/a
ATS linking	x	n/a	n/a	n/a	n/a	n/a	n/a
Candidate/Lead Tracking	x	x	x	x	n/a	n/a	n/a
Enhanced Who's Viewed	x	x	x	x	x	x	x
Unlimited Profile Search	All	3rd	3rd	3rd/Team	3rd	3rd	3rd
Lead Recommendations	x	x	x	x	x	n/a	n/a
Featured Applicant	n/a	n/a	n/a	n/a	n/a	n/a	x

Source: LinkedIn, Hedgeye Estimates

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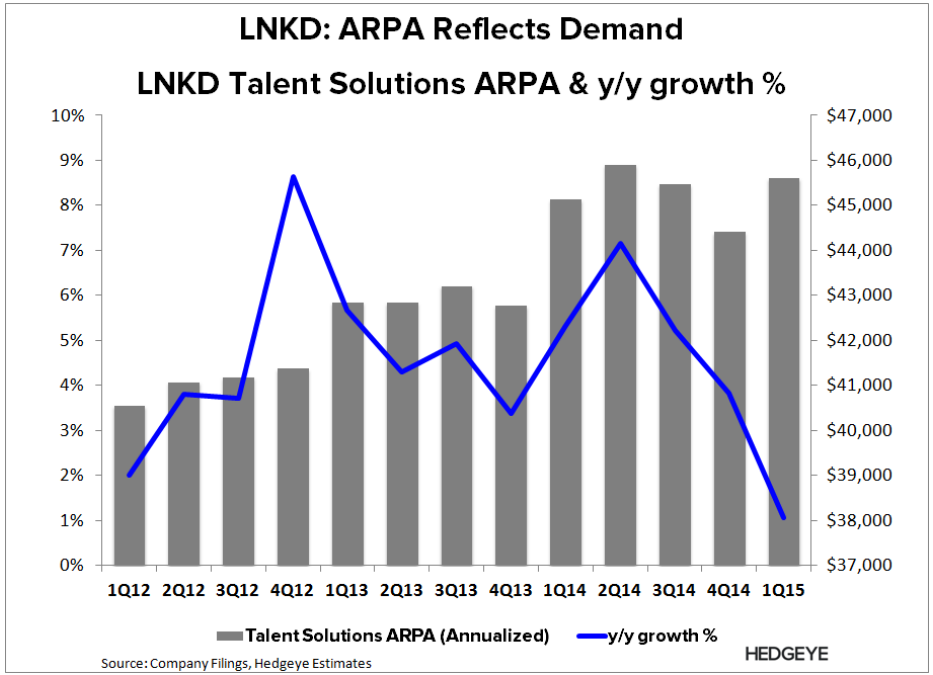
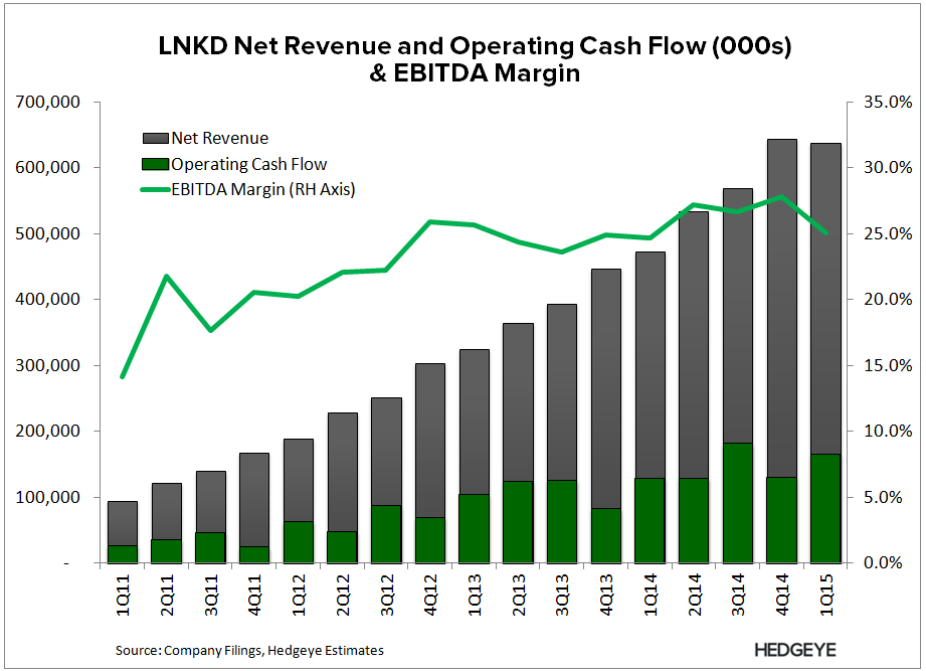
PRICING IS BASED ON VARYING LEVELS OF ACCESS TO MEMBER PROFILES

LNKD's flagship product is its Recruiter product, which provides the highest level of access (search & outreach) to its member profiles. LNKD also offers scaled-down products to address the lower end of the market.

PRICING POWER + DEMAND = CASH





ARPA IS MULTIPLES OF PREMIUM PRODUCT, SUGGESTING SOLID DEMAND

LNKD's Corporate Solutions Customers (LCS) pay roughly 5x it highest-priced product; suggesting a healthy level of demand for its products suite, and a proven opportunity to up-sell its new accounts.

THE UP-SELL DEFINES ITS TAM

LNKD US Private Employer Economic Sensitivity Analysis: Recruiter Platform

Total Enterprises & Seats based on Monthly Hiring Needs (Min, Max, & Current Rates)

Metrics by Employment Size (Headcount)			JOLTS Hiring Rates			Average Monthly Hires[1]			Enterprise TAM (> 3 Hires)[2]			Required Seats (3 Hires)[3]			Required Seats (4 Hires)[3]		
Employees	Firms	Avg Payroll	Trough	Peak	Current	Trough	Peak	Current	Trough	Peak	Current	Trough	Peak	Current	Trough	Peak	Current
0-99	5,601,330	$271,909	3.3%	4.6%	3.9%	-	-	-	-	-	-	-	-	-	-	-	-
100-499	80,341	$8,855,159	3.1%	4.8%	4.3%	4	6	5	45K	80K	80K	64K	143K	130K	34K	75K	69K
500-4,999	15,092	$68,702,344	2.2%	3.6%	3.3%	17	28	25	15K	15K	15K	82K	130K	118K	61K	97K	88K
5,000 +	1,730	$1,135,744,362	1.1%	2.7%	1.6%	138	339	201	2K	2K	2K	80K	196K	116K	60K	147K	87K

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ENTERPRISE TAM (#)			EMPLOYER SEAT TAM (#)					
62K	97K	97K	226K	468K	364K	155K	319K	244K

US Human Resource Professionals Penetration %[4]					
37%	77%	59%	25%	52%	40%

US EMPLOYER SEAT TAM ($)					
$2.0B	$4.2B	$3.3B	$1.4B	$2.9B	$2.2B

US EMPLOYER SEAT TAM PENETRATION %					
21%	10%	13%	31%	15%	20%

Notes

1) Monthly Hiring Needs applies to "Knowledge Workers" only (est. 60% of workforce)
2) Enterprise TAM are enterprises hiring more than 3 employees/month
3) Required Seats are based on how may positions a hiring manager can fill/month
4) Based on ~612K Employer-Based HR Professionals, excludes Employment Services (BLS-May 2014)
5) This analyis is for the **Recruiter Product Only** (estimate of 50% of Talent Solutions Revenue)

Source: Company Reports, BLS, Hedgye Estimates

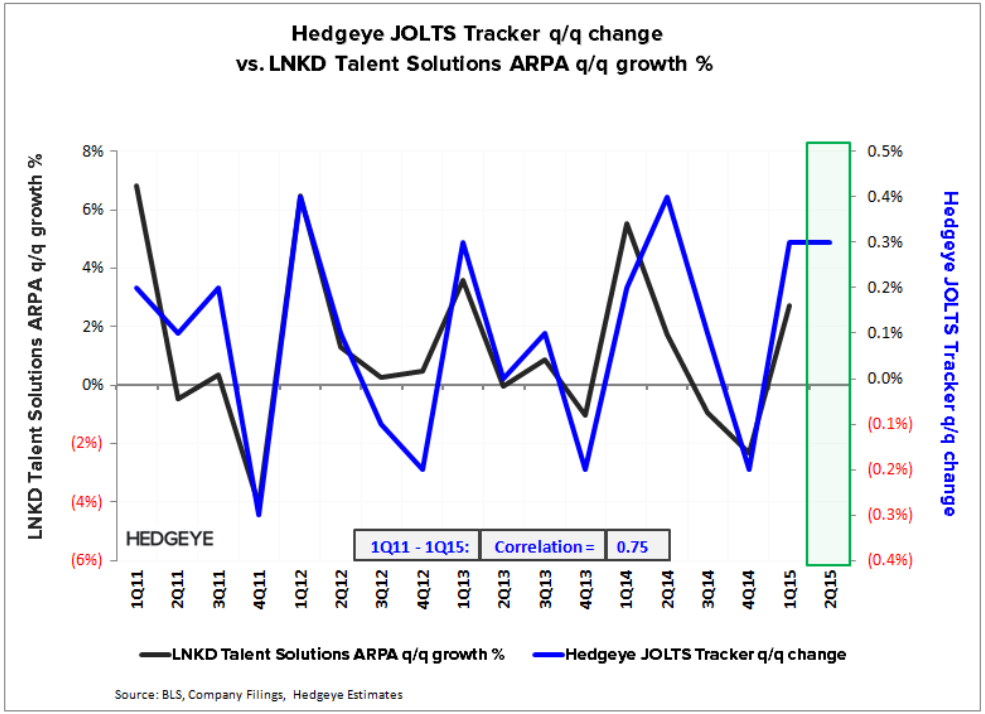
KEY POINTS

1. **TAM Favors ARPA**: The bulk of LNKD's TAM is not in account volume, but in up-selling those accounts via additional licenses (aka seats).
2. **Macro Drives ARPA**: The selling environment improves as the burden to fill open positions intensifies (i.e. upsell becomes easier)
3. **Ripe Selling Environment:** Hiring rates are elevated, but not yet at historical peak levels.
4. **Low Penetration:** LNKD is somewhere between 10% to 31% penetrated in US depending on the selling environment.

AND MACRO DRIVES THE SELLING ENVIRONMENT…

This analysis refers specifically to LNKD's flagship Recruiter product under fairly restrictive assumptions (see notes in table). The Key Points above collectively tell us ARPA matters most, and macro is key…

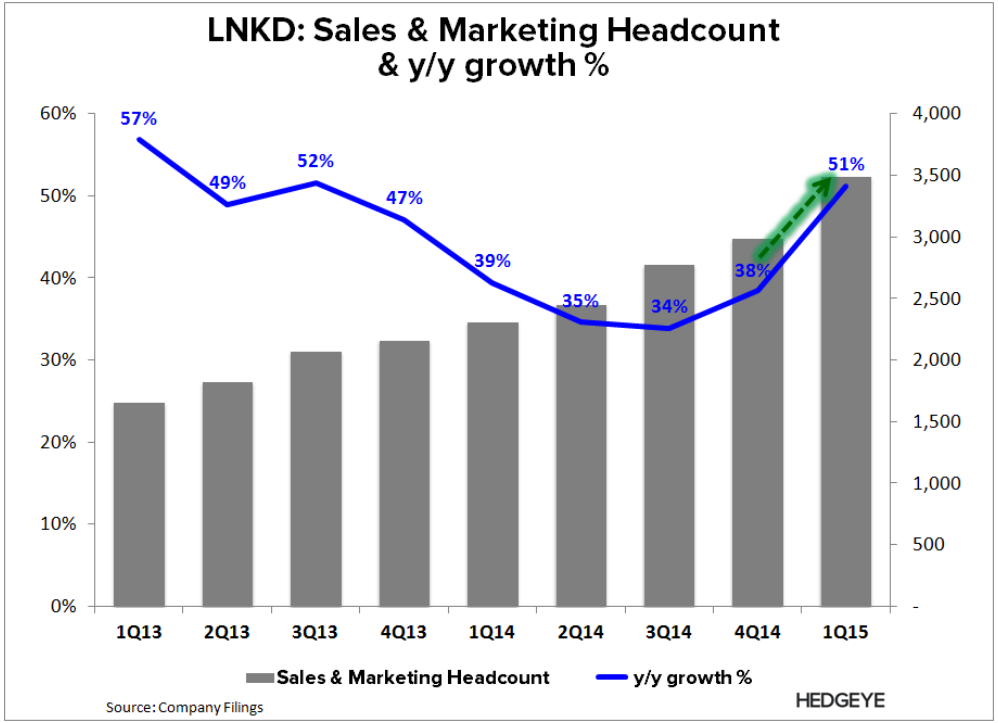
MACRO MOVING IN RIGHT DIRECTION



TRACKER SUGGESTS SELLING ENVIRONMENT CONTINUES TO IMPROVE

ARPA is key, so we built a tracker to tell us which way it's going. The relatively tight correlation combined with the marginal seasonality in both metrics confirms that ARPA is driven macro, which continues to improve.

TRANSITION OR INVESTMENT?



Notes

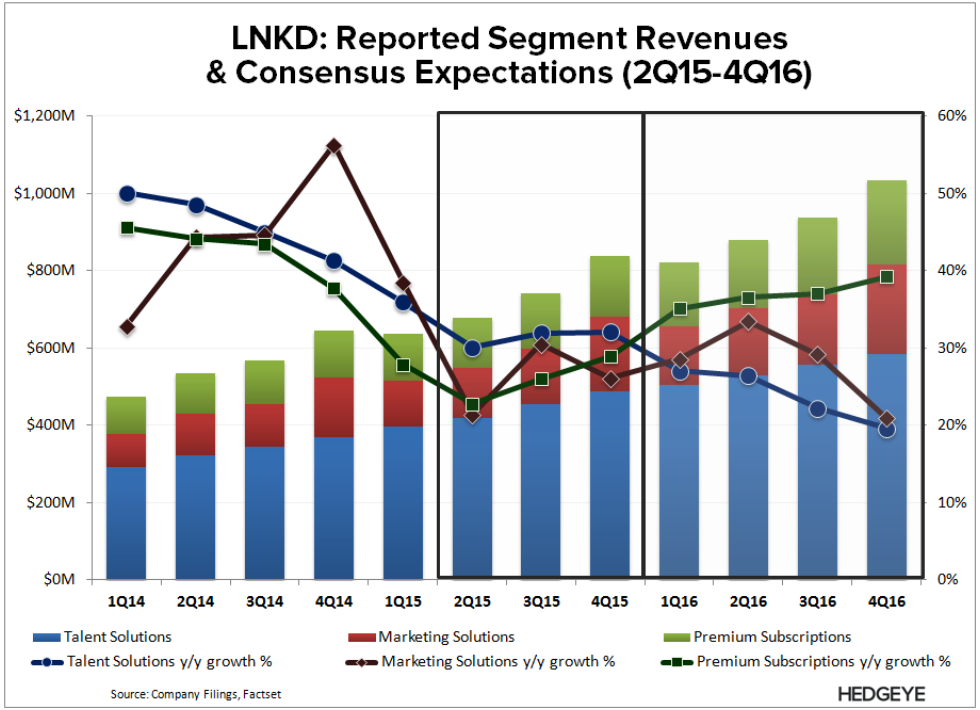
1. **Account Transition**: Management stated on its 1Q15 call that roughly 60% of its Accounts now have a new sales rep.

2. **Salesforce Ramp:** Management didn't effectively emphasize why the transition occurred in the first place. The 1Q15 increase in its salesforce was its largest since 3Q13

RAMPING INTO AN IMPROVING SELLING ENVIRONMENT

The account transition that spooked the street in 1Q15 was due to a massive investment in its salesforce. Given the afformentioned macro tailwinds, we see that ramp as a coiled spring.

GUIDANCE CUT = BREATHING ROOM



2015 Guidance Cut: Notes

+$20M-$25M: Lynda Acquisition Revenue (net deferred revenue write-off)

-$50M: Heightened Fx headwinds (EUR/USD)

-$30M: Operational issues, primarily in Marketing Solutions (display advertising) and Talent Solutions (salesforce account transitions)

MGMT USED SOFT 1Q15 RESULTS TO REBASE 2015 ESTIMATES

LNKD cut 2015 guidance despite coming in above its 1Q15 guidance. The bulk of LNKD's $30M-$50M guidance cut came from Fx, the balance primarily from Marketing Solutions, which is now captured in consensus estimates

TALENT SOLUTIONS = SWING FACTOR

LNKD 2015 Talent Solutions Revenue Scenario Analysis						
ARPA y/y growth	Net New LCS Customers (y/y growth %)					
	0%	2%	4%	6%	8%	10%
5.0%	$1,802,306	$1,805,643	$1,808,981	$1,812,318	$1,815,655	$1,818,992
4.5%	$1,795,611	$1,798,932	$1,802,254	$1,805,575	$1,808,897	$1,812,218
4.0%	$1,788,916	$1,792,222	$1,795,527	$1,798,833	$1,802,138	$1,805,444
3.5%	$1,782,221	$1,785,511	$1,788,800	$1,792,090	$1,795,380	$1,798,669
3.0%	$1,775,526	$1,778,800	$1,782,074	$1,785,347	$1,788,621	$1,791,895
2.5%	$1,768,831	$1,772,089	$1,775,347	$1,778,605	$1,781,863	$1,785,121
2.0%	$1,762,136	$1,765,378	$1,768,620	$1,771,862	$1,775,104	$1,778,346
1.5%	$1,755,441	$1,758,668	$1,761,894	$1,765,120	$1,768,346	$1,771,572
1.0%	$1,748,747	$1,751,957	$1,755,167	$1,758,377	$1,761,587	$1,764,798
0.5%	$1,742,052	$1,745,246	$1,748,440	$1,751,635	$1,754,829	$1,758,023
0.0%	$1,735,357	$1,738,535	$1,741,714	$1,744,892	$1,748,070	$1,751,249

Consensus	$1,758,051

	4Q14	1Q15
Net New LCS Customers (y/y%)	21.0%	6.6%
Average Revenue Per Account (y/y%)	5.3%	1.1%

Source: Factset, Hedgye Estimates

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REBASED CONSENSUS ESTIMATES NOT ASKING FOR MUCH

LNKD should exceed consensus estimates barring a sharp deceleration in **BOTH** of its core growth drivers, which were depressed by the account transition, and Fx pressure that should abate in 2H15 on easier comps.

LNKD: TRACKING THE LONG

Setup: We're getting long at a discount on rebased expectations while LNKD is making a considerable investment into an accelerating macro tailwind. We expect meaningful upside to 2015 estimates. The question is whether mgmt approaches 3Q guidance cautiously on the 2Q15 release. If so, we may eat a some near-term downside in exchange for a better setup heading into 2016 depending on the selling environment and consensus estimates; either could push us out of the name.

What We're Keying In On: ARPA, which is where the bulk of its TAM lies, but also the driver most sensitive to economic fluctuations. Our Macro team contends that the US economy is late cycle. If we notice any material negative inflections in our JOLTS tracker, it could mean the beginning of a deteriorating selling environment, which would put LNKD's core driver at risk.

Risks to Thesis: Mgmt conservatism on 3Q15 guidance, deteriorating macro trends, consensus estimates.

Timeline

- **1Q15:** Hedgeye wasn't covering
- **2Q15:** Strong 2Q Revenues beat, inline full-year raise with 3Q15 guidance edging above consensus.
- **3Q15:** Setup depends on JOLTS tracker and consensus estimate revisions; either could push us out of the name
- **4Q15**: Too early to tell. Reassess setup post 3Q15 print.

NOT A SLEEPY LONG, SETUP CAN TURN ANY GIVEN QUARTER.

The main risks are a negative inflection in the macro environment, or consensus upping estimates too much on a good print(s) and pushing us out of the name. In short, we may only be in this position for 1-2 quarters

P SHORT THESIS

P: SHORT THESIS SUMMARY

1. **Business Model**: Advertising-focused model. P must pay for every song it streams, regardless of whether it is serving ads on those listener hours.

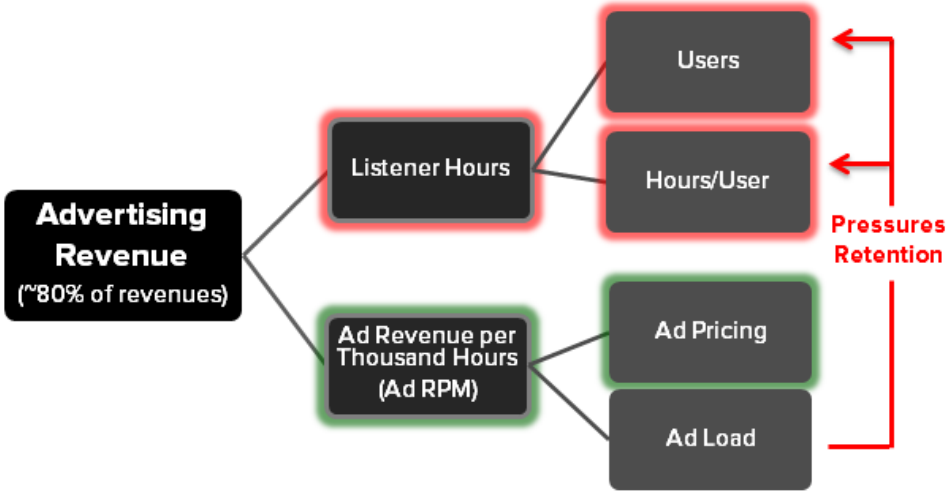
2. **Analysis:** Increasing monetization has led to heighted attrition. More importantly, P's model may not survive the Web IV outcome (royalty rates).

3. **Outlook:** We're expecting users to decline y/y by 2H15. Regarding Web IV, P may lose the one debate that it can't (bifurcated royalty rates).

4. **Setup**: Expecting light 3Q15 guidance and Weak 2Q15 user metrics. Web IV will be an overhang, decision to go against them (December).

5. **Duration**: Exit between 4Q15 and 1H16

P Advertising Revenue Drivers



CHALLENGING BUSINESS MODEL, WHICH MAY NOT SURVIVE WEB IV

P's core growth drivers are working against each other. Increasing ad load (monetization) is pushing the user away. More importantly, P's model is only sustainable if it gets its way on Web IV; that doesn't appear likely

P: KEY POINTS

1

NOT MUCH BREATHING ROOM

P guided light for 2015, which was the prudent move, but consensus is calling for accelerating ad revenue growth through 4Q15; a tall order given that its core advertising growth drivers are working against each other. 3Q/4Q guidance may disappoint.

2

USERS TO DECLINE Y/Y IN 2015

P has churned through more accounts than it has retained since 1Q11. Our survey work suggests that P has exhausted much of its TAM, and new user growth moving forward will not be able to offset attrition for that much longer. Needless to say, declining users would be a sentiment killer.

3

WEBCASTER IV = POWDER KEG

P's doesn't have the operating leverage necessary to absorb a rate increase and sustain its business model at the same time. Our review of the Web IV CRB filings and prior Webcaster proceedings suggest P is going to lose the one debate that it can't (bifurcated rates).

3Q/4Q GUIDANCE MAY DISAPPOINT

P: 2H15 ADVERTISING REVENUE SCENARIO ANALYSIS (000s)					
Y/Y Growth: Listener Hours vs. Ad Revenue Per Thousand Hours (RPM)					
Advertising	Listener Hours (Ad-Supported)				
RPM	0%	5%	10%	15%	20%
10.0%	$455,818	$478,609	$501,400	$524,191	$546,982
12.5%	$466,178	$489,486	$512,795	$536,104	$559,413
15.0%	$476,537	$500,364	$524,191	$548,018	$571,844
17.5%	$486,897	$511,241	$535,586	$559,931	$584,276
20.0%	$497,256	$522,119	$546,982	$571,844	$596,707
22.5%	$507,616	$532,996	$558,377	$583,758	$609,139
25.0%	$517,975	$543,874	$569,773	$595,671	$621,570
30.0%	$538,694	$565,629	$592,563	$619,498	$646,433

Consensus 2H15 Ad Revenue	$545,823

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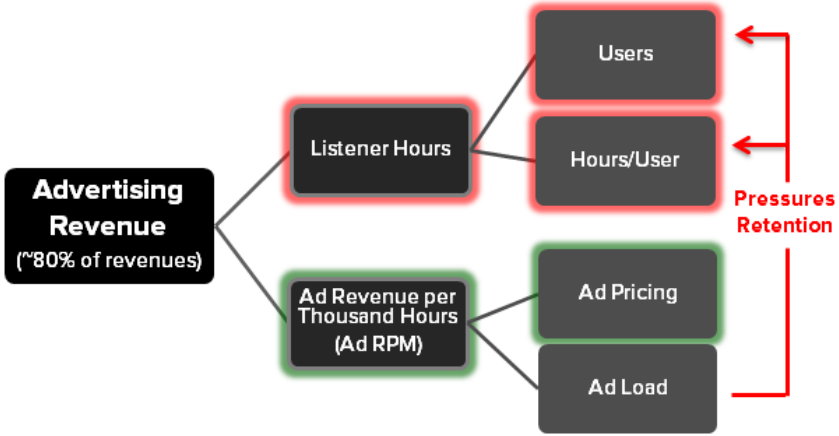
Source: Factset, Hedgeye Estimates

1Q15 GROWTH (Y/Y%)	
Listener Hours	11%
Advertising RPMs	15%

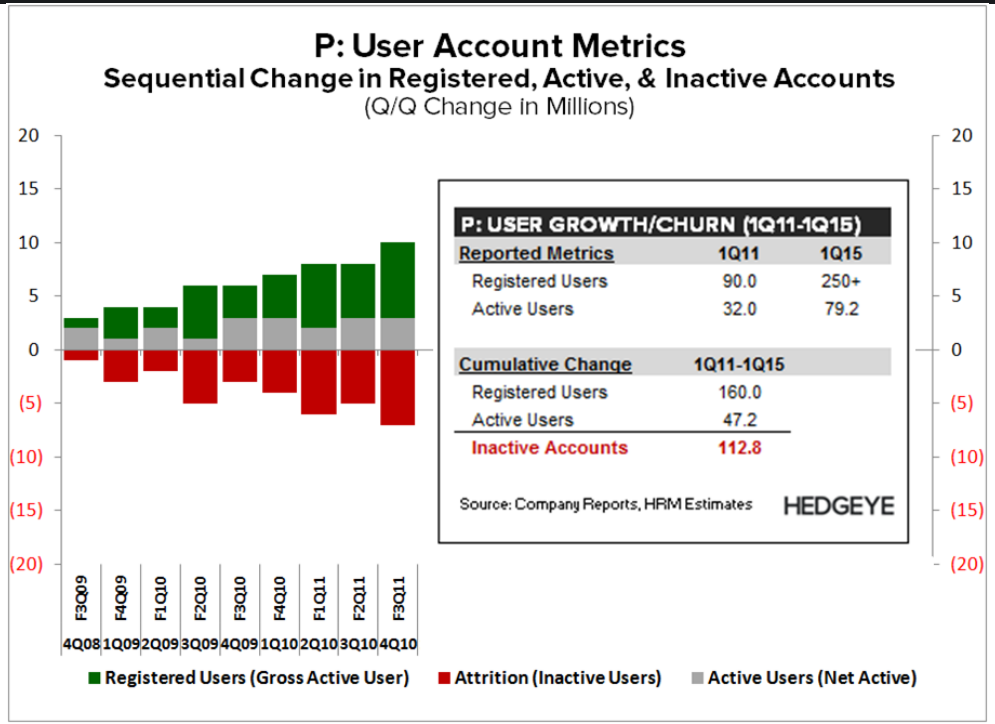
P Advertising Revenue Drivers



DESPITE LIGHT GUIDANCE, CONSENSUS NOT GIVING P MUCH BREATHING ROOM

Consensus is calling for accelerating ad revenue growth through 4Q15. We're expecting listener hours to slow into the single-digits, which means increasing ad load and local ad mix (pricing) must pick up the slack.

P HAS SERIOUS ATTRITION ISSUES



P: USER GROWTH/CHURN (1Q11-1Q15)		
Reported Metrics	1Q11	1Q15
Registered Users	90.0	250+
Active Users	32.0	79.2
Cumulative Change	1Q11-1Q15	
Registered Users	160.0	
Active Users	47.2	
Inactive Accounts	112.8	

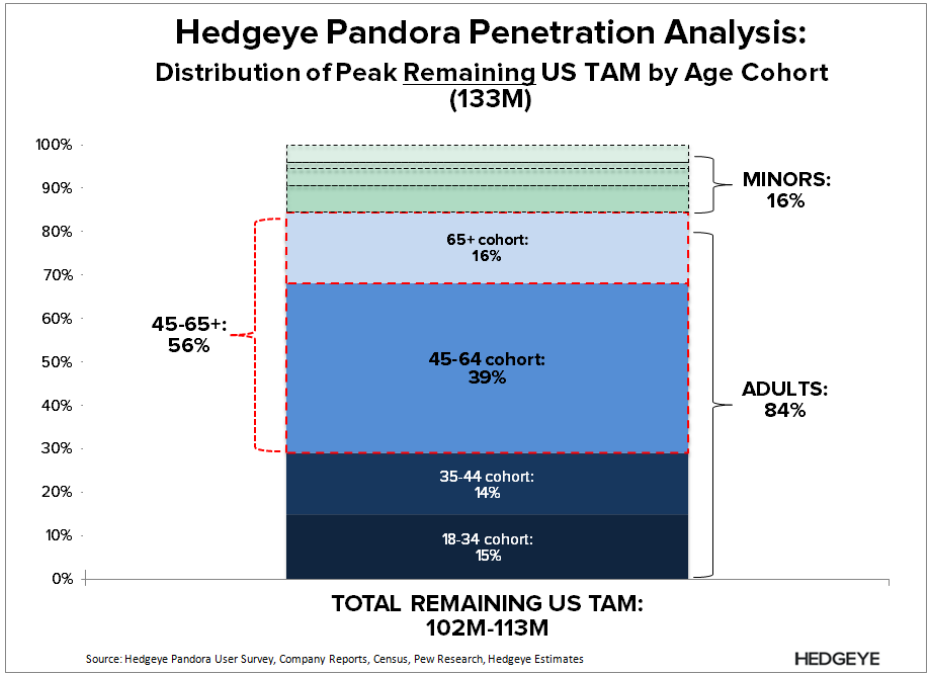
METRIC NOTES

1. P switched its method for reporting registered users in 2Q11 (from an actual # to "+" format)
2. We can't explicitly calculate its quarterly attrition rate after 1Q11, but we estimate it has averaged in the mid-to-high teens as percentage of its active users, or roughly 10.5M per quarter
3. We can calculate its cumulative attrition, which is at least 71% between 1Q11 and 1Q15 (~113M inactive out of 160M registered).

INTERNAL METRICS TELL DAUNTING STORY, BUT NOT THE WHOLE STORY

P's reported metrics suggest it has churned through more accounts than it has retained since 1Q09. However, some users have multiple accounts, which we need to account for…

WHY USERS DECLINE Y/Y IN 2015?



P: 2015 PENETRATION SCENARIO ANALYSIS

PENETRATION OF REMAINING TAM BY THE END OF 2015

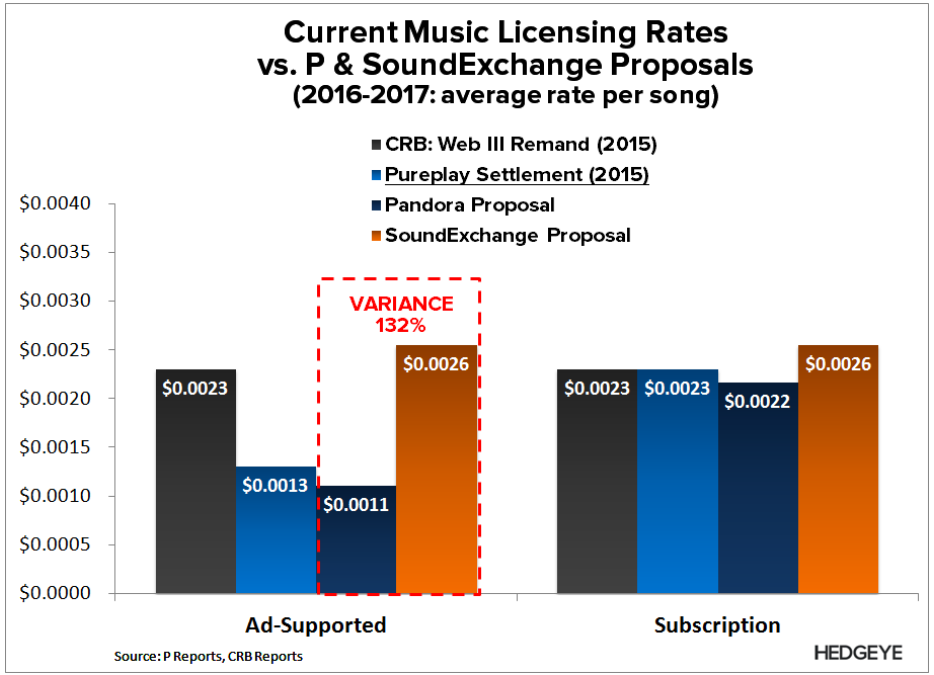
Remaining TAM	Quarterly Attrition					
	10M	11M	12M	13M	14M	15M
102M	49%	54%	59%	63%	68%	73%
107M	47%	52%	56%	61%	66%	70%
108M	46%	51%	55%	60%	65%	69%
113M	44%	49%	53%	58%	62%	66%

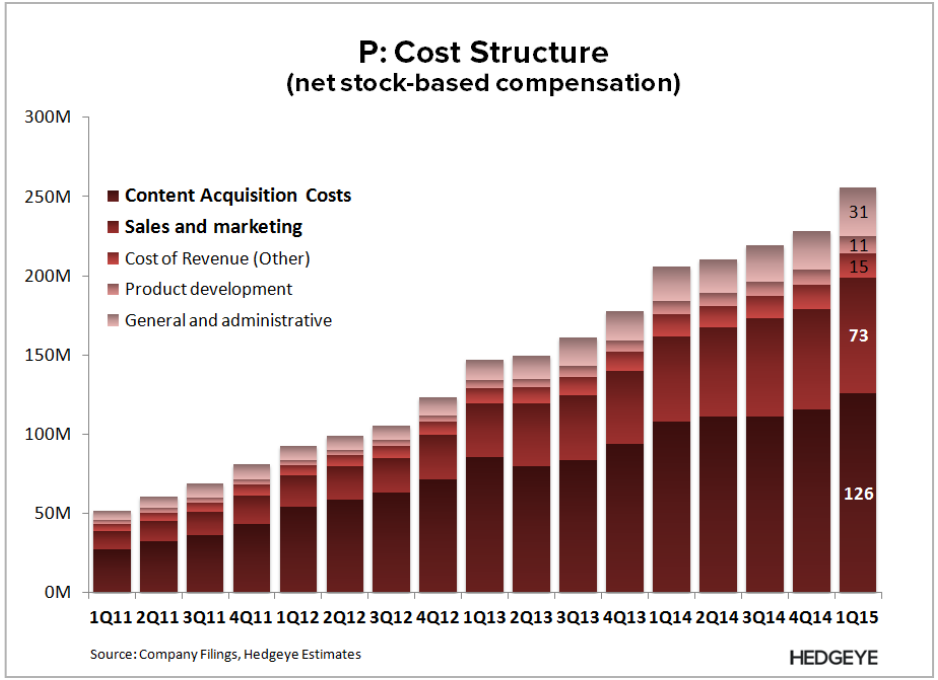
Source: Hedgeye Pandora User Survey, Company Reports, Census, Pew Research, Hedgeye Estimates

BECAUSE WE DON'T BELIEVE THIS WILL HAPPEN

The right table details how much of P's remaining TAM needs to be penetrated in order to maintain it's current user base over the 5-Qtr period starting 3Q14. Compare that to the chart on the left, and decide for yourself.

WEBCASTER IV: WORLDS APART

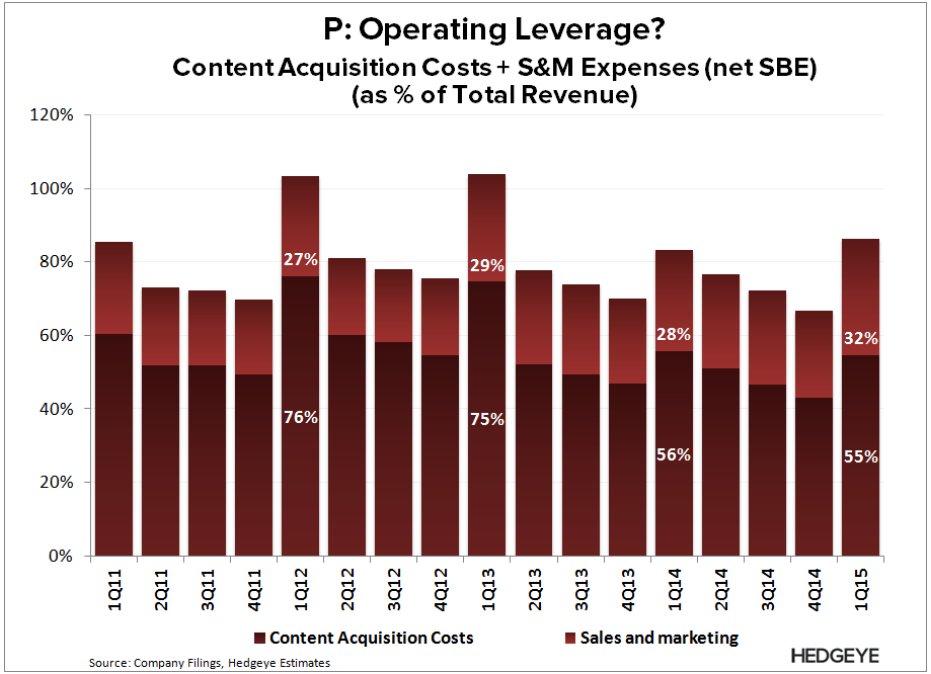


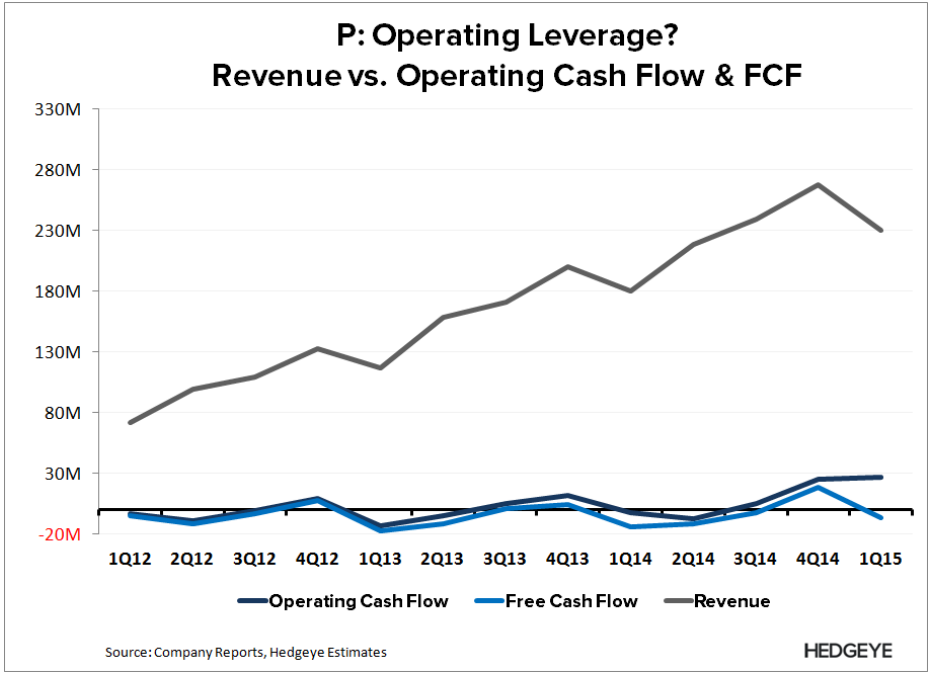


A COMPROMISE ISN'T GOOD ENOUGH…

We estimate that almost 90% of P's listener hours are streamed to ad-supported users, so the variance in proposals is a big deal. The midpoint of the two ad-supported proposals translates a 42% rate increase.

P HASN'T REALLY ACHIEVED LEVERAGE

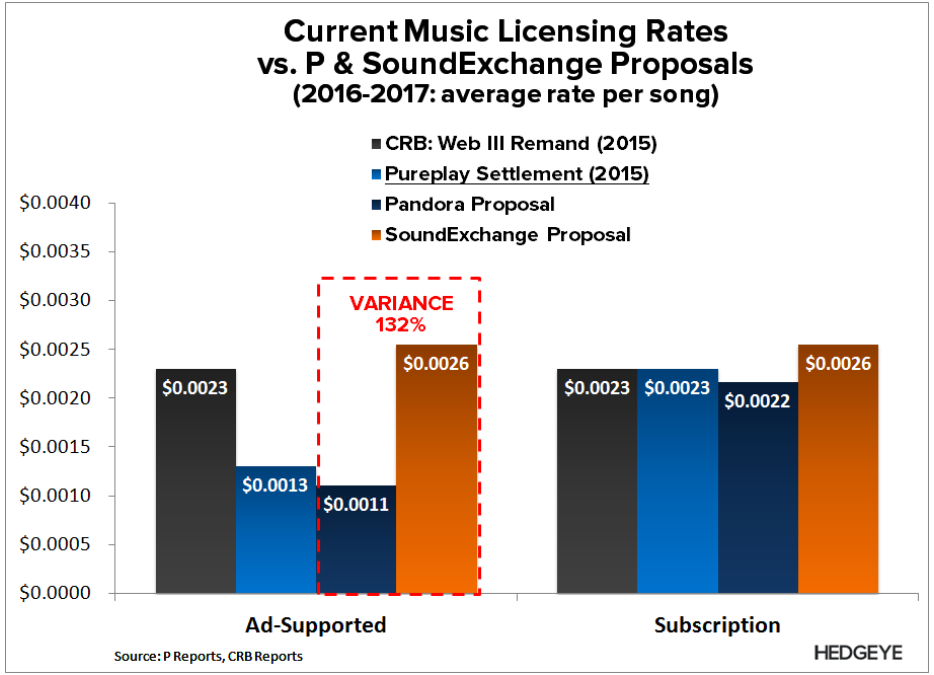




P'S MODEL CAN'T ABSORB ANYTHING BUT A BEST CASE SCENARIO

Whatever leverage P has achieved on the content side was paid for salesforce & marketing expenses. P's model can't absorb even a small royalty rate hike, especially since it struggles to generate cash flow as it is.

WEB IV: P LOSING THE KEY DEBATE



1. **Pureplay Settlement is Irrelevant**: The current bifurcated rate setup was borne out of the Pureplay Agreement, which prohibited the incorporated rates from ever being included as a benchmark in any rate-setting procedure.

2. **Existing Benchmarks May Be Irrelevant**: P will have difficulty using any existing agreement with bifurcated rates as precedent since it would be tough to argue that these rates were not a derivative of the Pureplay Agreement. SX has provided witness testimony suggesting as much.

3. **P's Business Model is Irrelevant**: Quote from the judges of the Web III Remand. *"The Act instructs the Judges to use the willing buyer/willing seller construct, assuming no statutory license. The Judges are not to identify the buyers' reasonable other (non- royalty) costs and decide upon a level of return (normal profit) sufficient to attract capital to the buyers."*

BIFURCATED RATE STRUCTURE: P HAS NO LEG TO STAND ON

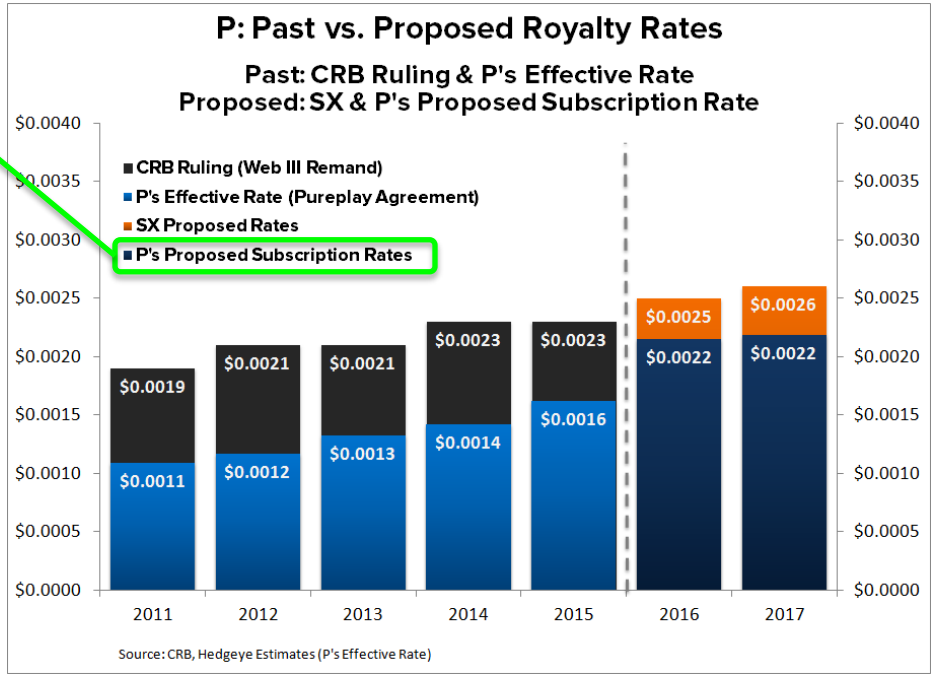
The purpose of Web IV is to determine what willing buyers/sellers would agree to in a competitive market outside the shadow of statutory rates. More importantly, the copyright owner takes priority.

WEB IV: P'S BEST CASE SCENARIO?

P: WEB IV SCENARIO ANALYSIS: TOTAL EBITDA (2016-2017)						
REVENUE VS. HOURS (2015-2017 CAGR)						
SCENARIO	P's Proposed Subscription Rates Applied to All Hours					
HOURS	Revenue					
	24.0%	23.0%	22.0%	21.0%	20.0%	19.0%
17.0%	($148M)	($182M)	($215M)	($247M)	($279M)	($311M)
16.0%	($113M)	($146M)	($179M)	($212M)	($244M)	($276M)
15.0%	($78M)	($111M)	($144M)	($177M)	($209M)	($241M)
14.0%	($43M)	($77M)	($110M)	($143M)	($175M)	($206M)
13.0%	($10M)	($43M)	($76M)	($109M)	($141M)	($172M)
12.0%	$24M	($10M)	($43M)	($75M)	($107M)	($139M)
11.0%	$57M	$23M	($10M)	($42M)	($74M)	($106M)
10.0%	$89M	$56M	$23M	($10M)	($42M)	($74M)
9.0%	$121M	$88M	$55M	$22M	($10M)	($42M)
8.0%	$153M	$119M	$86M	$54M	$22M	($10M)
7.0%	$184M	$150M	$117M	$85M	$53M	$21M

Source: P reports, CRB Filings, Hedgeye Estimates

HEDGEYE



Note: The wider the gap between revenues and hours, the greater the reliance on ad pricing and **ad load,** which could exacerbate **attrition**

P WOULD STILL NEED TO BLOW UP ITS BUSINESS MODEL

The takeaway is not just the potential cash burn, but what would be required to avoid it, and P's limited margin of error to do so. The cost of getting it wrong is too severe to not proactively revamp its entire business model.

P: TRACKING THE SHORT

Setup: Working against P. 1Q15 likely the best print of the year, 3Q15 guidance could disappoint on consensus assumption for accelerating ad revenue. Deteriorating user metrics and the overhang from Web IV will keep a lid on the stock, especially as we move through the year since declining users become more likely, and Web IV draws closer. If we're wrong on users/hours, then the setup into 2016 become much worse.

What We're Keying In On: Listener Hours. Web IV is all that really matters now. The setup into 2016 becomes much worse if P enters the year with a larger listener-hour base. The more active users/hours P has, the more bearish we become. The other factor is S&M % of Revenues; whether P can achieve leverage on its salesforce.

Risks to Thesis: Web IV rates are significantly below Web III rates (however unlikely), or street misinterprets outcome.

Timeline

- **1Q15:** Strong Revenue beat, inline raise, but weakening user metrics
- **2Q15:** Beat Revenues, inline raise, but light 3Q15 Guidance, and dissapointing user growth.
- **3Q15:** Declining users more likely, potentially light 4Q15 guidance, Web IV draws closer (12/15)
- **4Q15**: Declining users even more likely. New strategic priorities post Web IV will take street by surprise.

ASYMMETRIC SETUP TO THE DOWNSIDE

The only real positive is upside to 1H15 results. Even if we're wrong on 2015 revenue growth, the setup gets progressively worse with both growing pressure on user metrics and Web IV ruling drawing closer.

YELP SHORT THESIS

YELP: SHORT THESIS SUMMARY

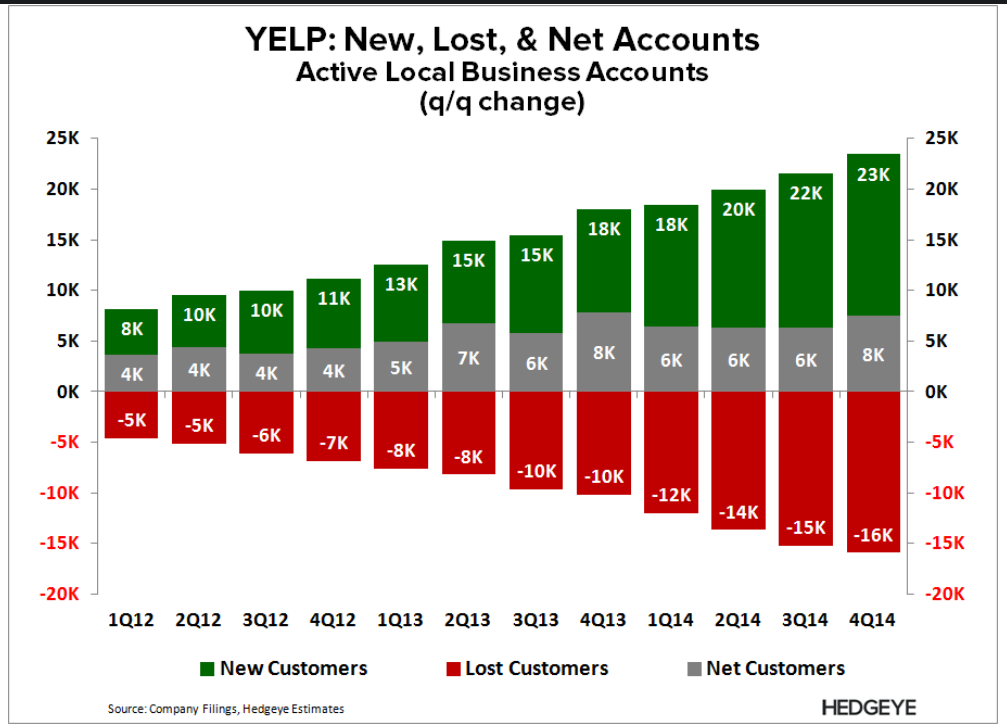
1. **Business Model**: Primarily selling ad packages to local businesses. YELP must hire enough new sales reps to drive new account growth in excess of its rampant attrition (the majority of its customers).

2. **Analysis:** YELP's Business Model is only sustainable if its TAM is large enough to support; it's not. Worse, growing its salesforce now an issue.

3. **Outlook:** Attrition will exert a greater impact on its model moving forward. YELP's financials suggest that this has already started.

4. **Setup:** Expecting light 2Q15 Local Advertising Revenue and pending 2015 guidance cut.

5. **Duration:** Depends on consensus 2016 estimates



RAMPANT ATTRITION + LIMITED TAM = DEATH OF A BUSINESS MODEL

YELP's attrition risk will always grow with its account base. The burden of new account growth will become more challenging against a limited TAM, leading to a precipitous slowdown in growth, and eventually declines.

YELP: KEY POINTS

1

ABSURD ATTRITION TO GET WORSE

We estimate that YELP is losing the majority of its local advertising customers on an annual basis. Baring a seismic shift in its business model, the risk will increase each year

2

TAM IS A FRACTION OF WHAT'S ADVERTISED

Estimates vary for YELP's total addressable US market, YELP has estimated as high as 27M....In reality, we estimate its closer to 3M in a best-case scenario. More importantly, YP.com's 600K account base is not the low-hanging fruit as mgmt suggests, it's a pipe dream.

3

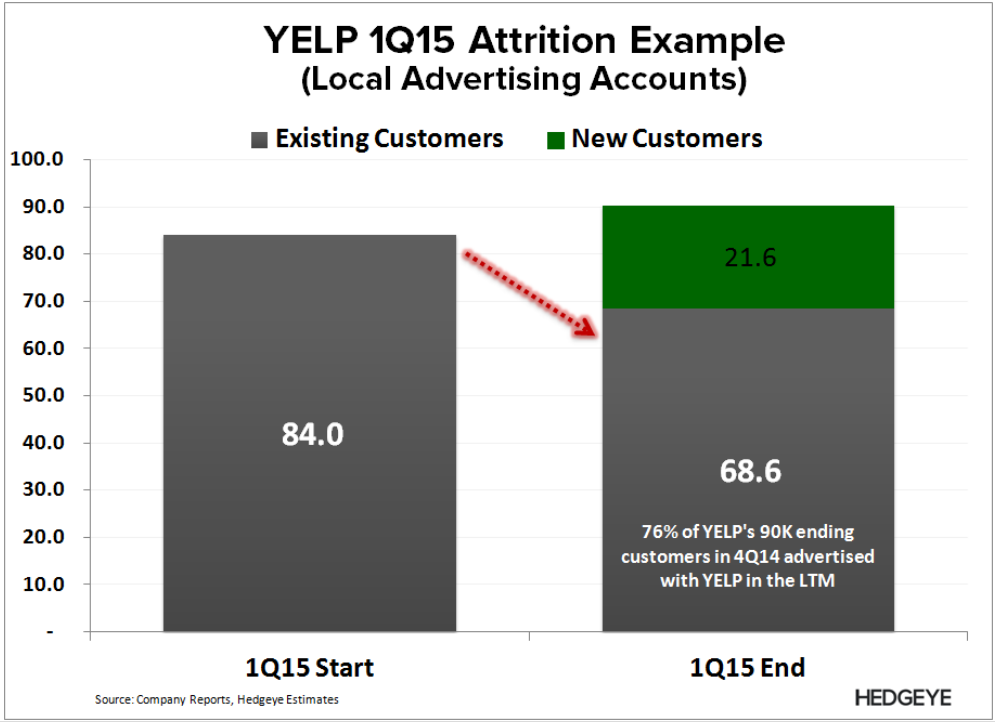
THE MODEL IS ALREADY BREAKING DOWN

YELP's business model isn't sustainable, and we're already seeing signs that it's breaking down. Most recently its inability to grow its salesforce. The fact that this is even remotely an issue suggest this story is to turn much sooner, and get much uglier, than we initially expected.

ATTRITION EXAMPLE

1Q15 EXAMPLE (Local Advertising)

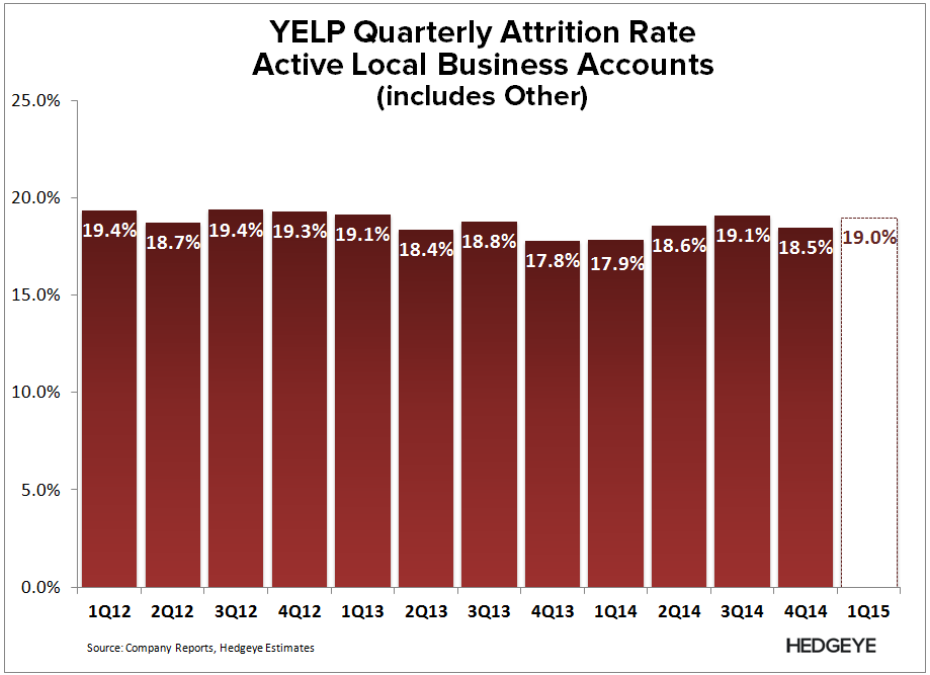
1. 4Q14: YELP had **84K customers**
2. 1Q15: YELP had **90K customers**
3. 1Q15 **Customer Repeat Rate** was **76%**
   - 1Q15 Repeating Customers: **69K** (90K x 76%)
   - 1Q15 New Customers: **22K** (94K x 24%)
4. YELP had 84K customers in 4Q14, but only 69K repeating customers in 1Q15, so it **lost ~15K** customers **(69K-84K)** , or **18.4%** of its customers from 4Q14.

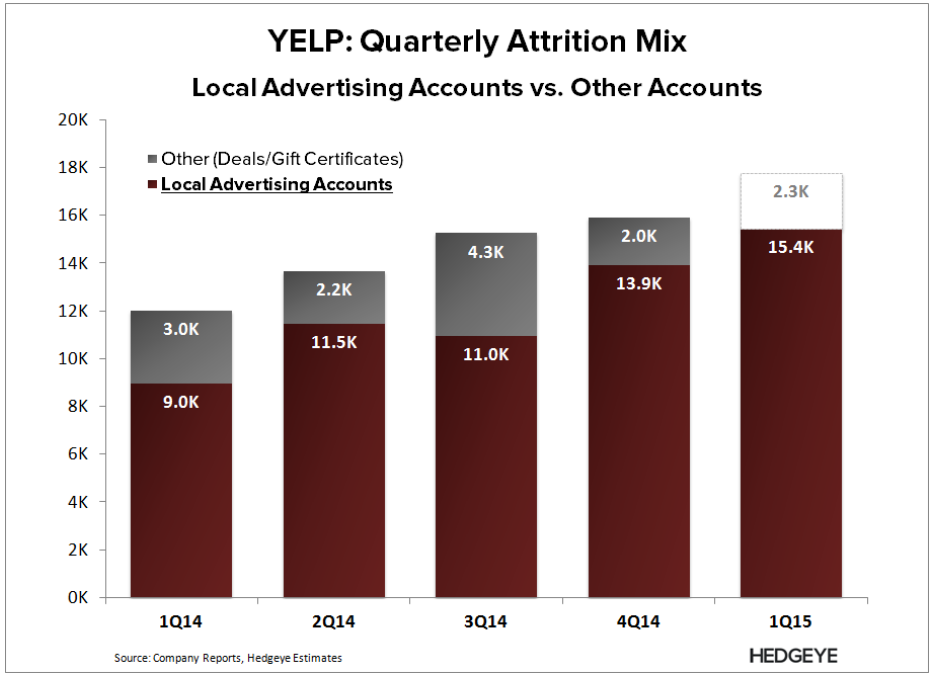


THE CUSTOMER REPEAT RATE IS A MEASURE OF MIX, NOT RETENTION

Any time YELP's Repeating Customers (calculated using its stated Repeat Rate) are less than its Local Advertising Accounts from the prior quarter, it lost customers.

ATTRITION IS A RECURRING THEME

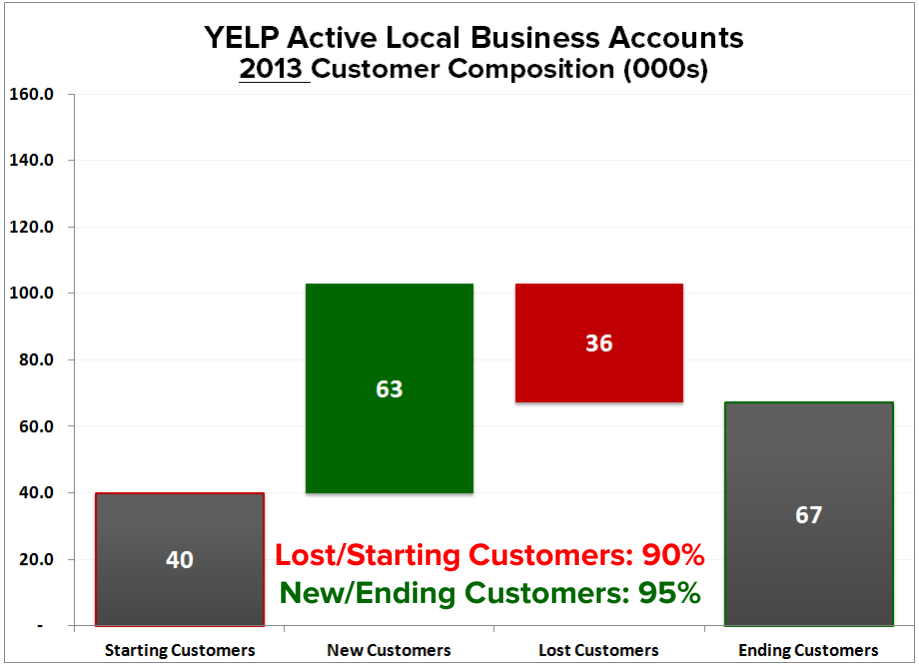


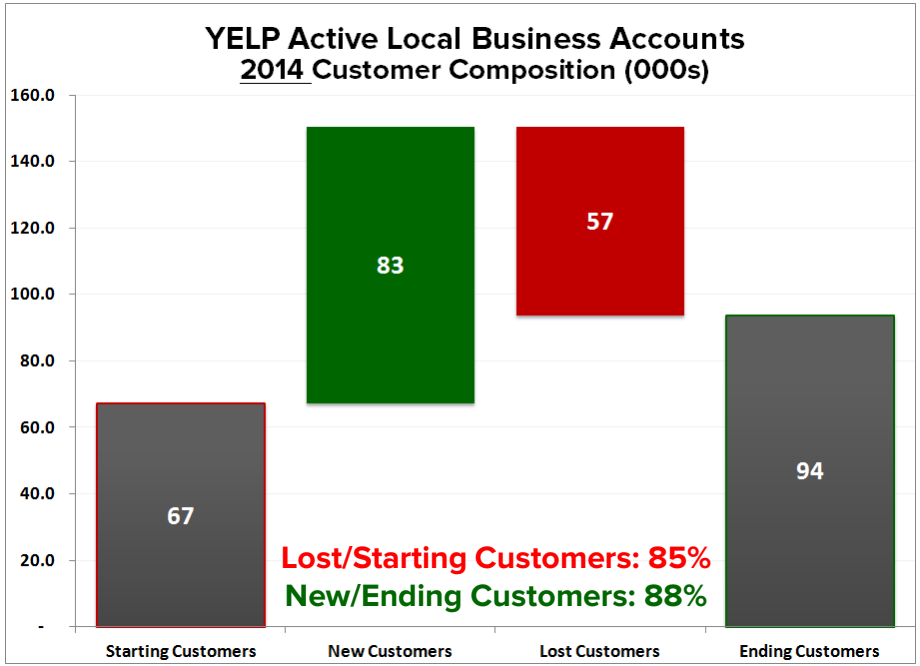


THE MAJORITY OF WHICH COMES FROM ITS CORE LOCAL ADVERTISING

YELP stopped reporting its Active Local Business Accounts in favor of a new metric called Local Business Accounts. Management broke our time series, but essentially conceded that attrition is coming from its core.

ANNUAL ATTRITION IS ABSURD





HEDGEYE

YELP LOSING ALMOST ALL ITS CUSTOMERS ANNUALLY

Since most of YELP's contracts are on annual terms, it is losing the majority of its customers annually, while its ending customer base is comprised almost entirely of new accounts signed during the course of the year.

YELP'S ADDRESSABLE US MARKET...

Criteria for Advertising with YELP

1. **Affordability:** Minimum cost $3,600 annually
2. **Retail:** vs. B2B

Composition of US Market (27M Total Businesses)

1. **Affordability**: 75% earn < $100K in annual revenue
2. **Retail**: 47% are primarily B2B companies

YELP Estimate for US Local Business Opportunity

NOT ALL BUSINESSES ARE APPLICABLE

YELP's audience is primarily retail (our survey suggests 70% use exclusively for restaurants); B2B companies aren't likely to advertise. Most earn less than 100K, so YELP's smallest ad program would be prohibitive.

DATA SOURCE: CENSUS, COMPANY REPORTS (27 TAM ESTIMATE FROM YELP MAY 2012 INVESTOR CONFERENCE PRESENTATION)

TAM MUCH SMALLER THAN IMPLIED

YELP TOTAL ADDRESSABLE MARKET ANALYSIS

CROSS SECTION OF BUSINESSES WITH AVAILABLE INCOME & APPLICABLE INDUSTRIES

YELP Market	Industry	Firms with Annual Sales Of...										
		All Firms	+ 100K	< 5K	5K - 10K	10-25K	25-50K	50-99K	100-250K	250-500K	500K-1M	> 1M
	Agriculture, forestry, fishing and hunting	258,779	44,382	59,856	38,316	54,106	34,177	27,942	23,847	9,002	5,908	5,625
	Mining, quarrying, and oil & gas extraction	122,352	37,190	24,813	14,665	19,705	12,491	13,488	14,455	7,567	5,256	9,912
	Utilities	24,050	6,492	6,053	2,983	4,003	2,608	1,911	2,083	1,212	822	2,375
	Construction	3,413,632	1,012,982	502,782	361,705	639,959	490,589	405,615	408,238	223,891	164,691	216,162
	Manufacturing	614,631	296,102	91,254	55,847	72,394	50,854	48,180	68,011	52,599	46,986	128,506
	Wholesale trade	732,222	386,636	86,722	53,873	77,317	62,036	65,638	83,198	60,573	59,053	183,812
YELP	**Retail trade**	2,671,836	809,107	694,526	348,795	391,792	228,053	199,563	249,560	175,031	142,044	242,472
	Transportation and warehousing	1,253,095	339,817	142,551	125,635	237,192	216,174	191,726	215,068	49,447	31,139	44,163
	Information	380,486	80,157	102,611	56,703	67,731	39,567	33,717	29,909	15,634	12,249	22,365
YELP	**Finance and insurance**	1,017,680	311,690	181,279	114,716	161,614	125,917	122,464	139,298	76,033	43,967	52,392
YELP	**Real estate and rental and leasing**	2,615,937	693,396	303,790	290,036	513,537	426,286	388,892	368,463	173,694	101,380	49,859
	Professional, scientific, and technical svcs	3,789,002	869,350	842,257	514,457	665,377	471,532	426,029	424,242	187,785	117,295	140,028
	Admin & support, waste, remediation svcs	2,122,906	296,679	585,822	418,031	484,303	202,914	135,157	121,590	67,146	46,052	61,891
YELP	**Educational services**	600,778	59,378	274,418	106,412	92,526	41,568	26,476	22,571	12,298	8,720	15,789
YELP	**Health care and social assistance**	2,368,801	602,506	475,426	389,519	474,650	249,246	177,454	183,107	147,500	131,760	140,139
YELP	**Arts, entertainment, and recreation**	1,235,766	125,419	482,636	216,969	222,710	114,698	73,334	55,911	27,198	19,225	23,085
YELP	**Accommodation and food services**	776,722	410,303	79,235	57,711	80,391	64,157	84,925	140,140	106,275	81,793	82,095
YELP	**Other services (except public admin)**	3,120,566	396,310	641,158	543,124	835,014	437,483	267,477	207,599	94,617	55,698	38,396
	Uncharacterized	7,581	2,189	-	844	1,161	1,245	2,142	1,333	441	258	157
	Totals	**27,126,822**	**6,780,085**	**5,577,189**	**3,710,341**	**5,095,482**	**3,271,595**	**2,692,130**	**2,758,623**	**1,487,943**	**1,074,296**	**1,459,223**
	YELP Markets (Total Firms)	**14,408,086**	**3,408,109**	3,132,468	2,067,282	2,772,234	1,687,408	1,340,585	1,366,649	812,646	584,587	644,227

Data Source: Census.gov

? HEDGEYE

27 MILLION...OR A SUSPECT 3 MILLION?

We pulled the Census data where YELP is getting its TAM estimate, and we filtered it by companies with more than 100K in revenue and those that cater to YELP's audience. **3.4 million is still ambitous.**

YP'S TAM IS A PIPE DREAM

SMALL BUSINESS ADVERTISING COMPANIES
Customers vs. Service Offering Comparison

	YELP	YP	DXM
US CUSTOMERS	**94K**	**575K**	**580K**
ADVERTISTING/MARKETING SERVICES			
Local Search Ads	x	x	x
Videos	x	x	x
Transactional (Orders/Deals/Reservations)	x		
Website Design/Hosting		x	x
Listings & Reputation Mangement		x	x
Direct Mailing		x	x
Search Engine Marketing		x	x
Search Engine Optimization			x
Yellow Pages Ads		x	x

Source: YELP reports, company websites

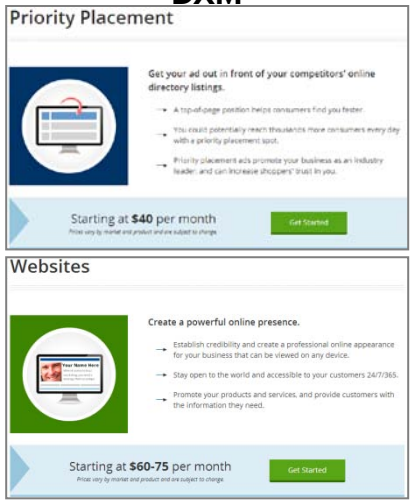
HEDGEYE

YELP

Packages to Fit Your Budget
Yelp Local business advertising packages typically range from $300 to $2,200 per month, depending on how aggressively you want to attract customers. Each package includes a dashboard to track your results in the program.

YP.com

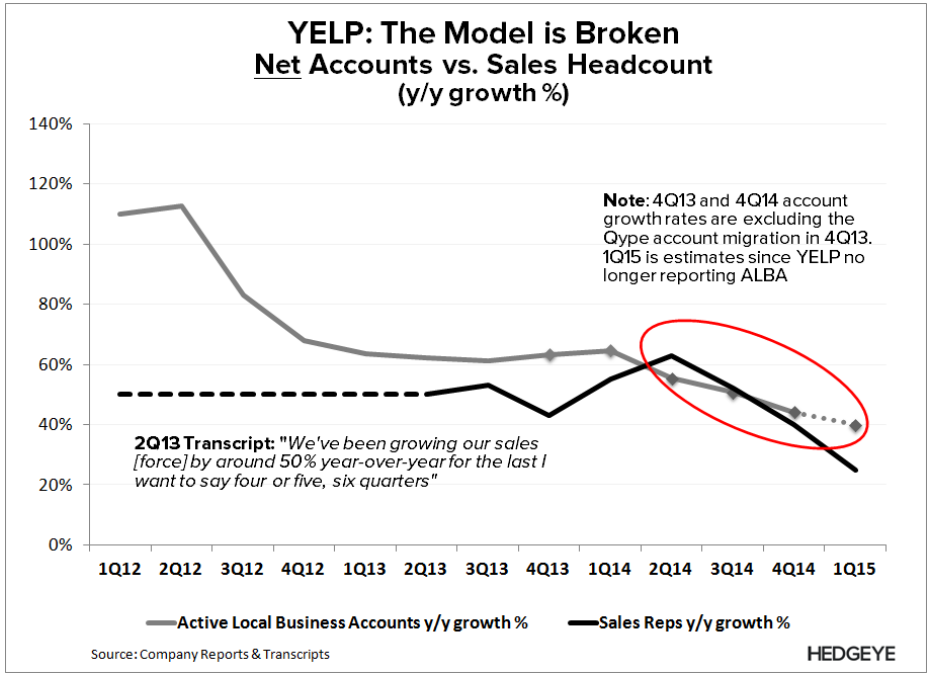
DXM

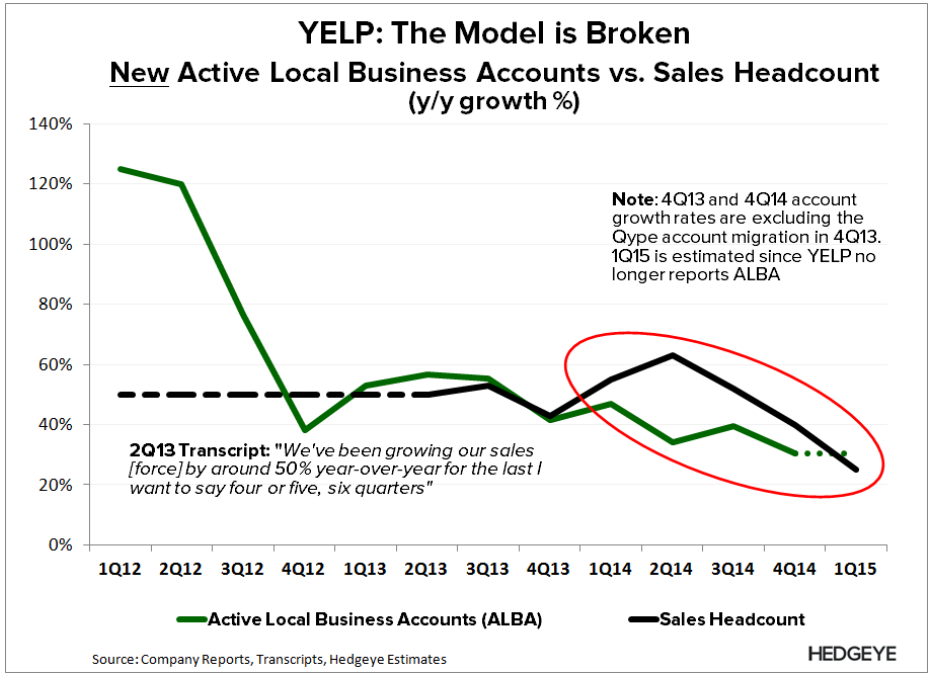


FEWER PRODUCTS – B2B EXPOSURE + HIGHER PRICE = SMALLER TAM

YELP has implied that YP's account base is the low-hanging fruit. Yet, the breadth of **YELP's offering** is **far more limited**, and often **more expensive;** meaning their TAMs aren't remotely comparable.

THE DEATH OF A BUSINESS MODEL

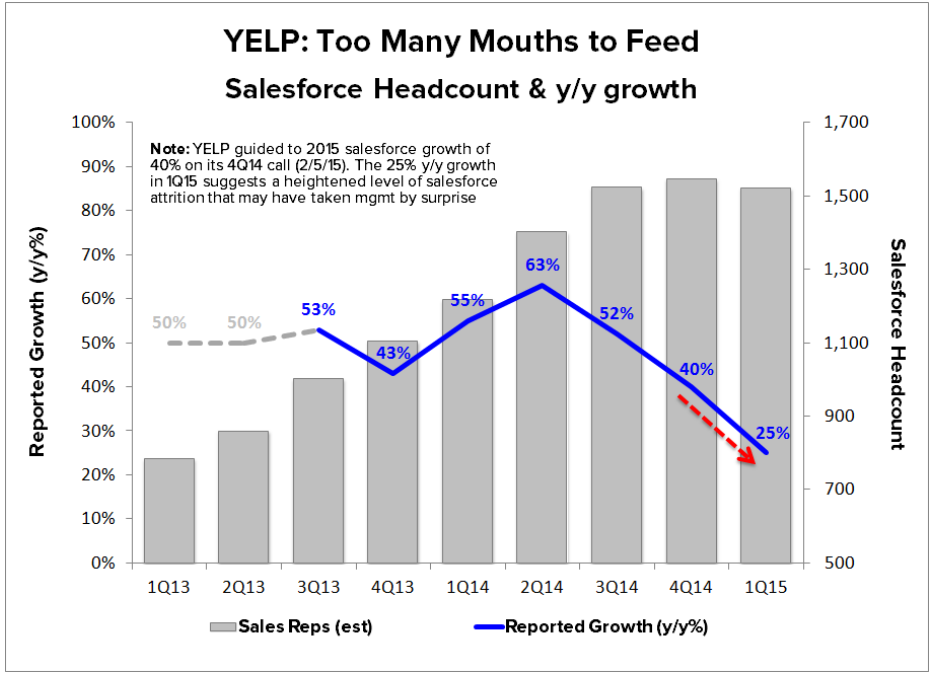


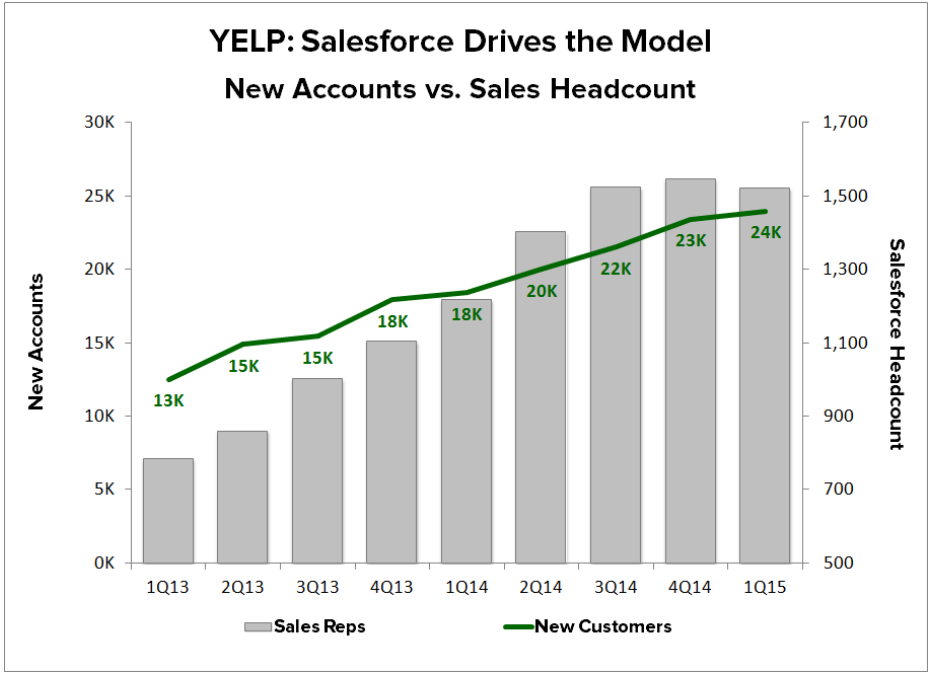


SALESFORCE OUTGROWING THEIR PRODUCTIVITY

YELP's attrition issues have gone unnoticed because its aggressive salesforce increases have driven enough new account growth to compensate. That story is over, which means the model is broken…

SALESFORCE CHURN = GAME OVER





THE FACT THIS IS EVEN REMOTELY AN ISSUE IS A MAJOR RED FLAG

The entire model is predicated on hiring enough new reps to drive new account growth in excess of its rampant attrition. If YELP can't do that consistently, it's basically game over.

2015 ESTIMATES BEYOND LOFTY

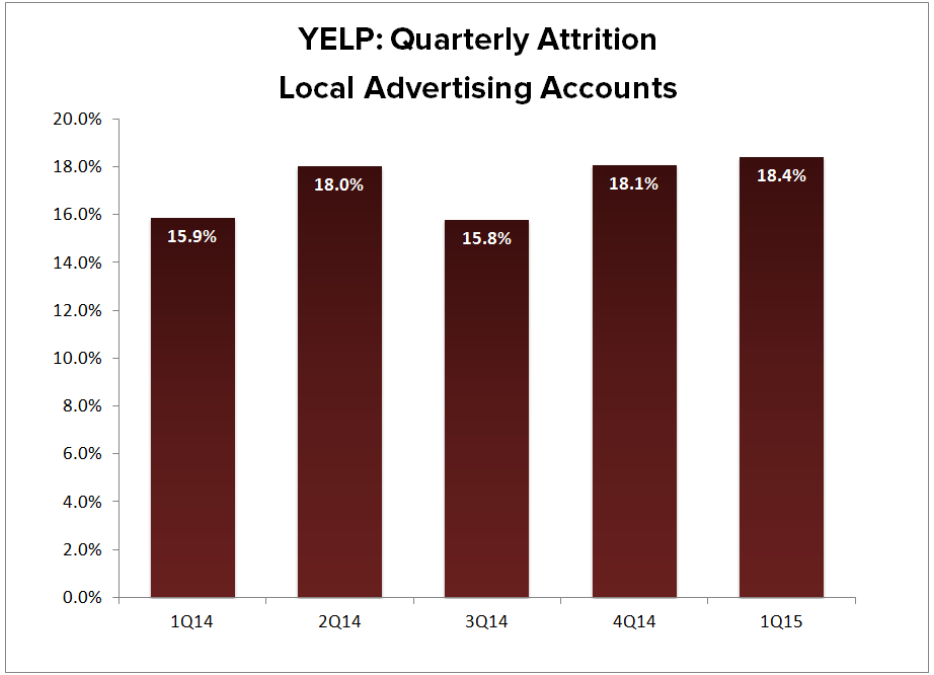
YELP 2015 Local Advertising Revenue Scenario Analysis					
New Acct	Quarterly Attrition Rate				
y/y growth	15.0%	16.0%	17.0%	18.0%	19.0%
30.0%	$461M	$454M	$447M	$440M	$434M
35.0%	$466M	$459M	$452M	$445M	$438M
40.0%	$471M	$464M	$457M	$450M	$443M
45.0%	$476M	$469M	$461M	$454M	$447M
50.0%	$481M	$473M	$466M	$459M	$452M
55.0%	$485M	$478M	$471M	$464M	$457M

HEDGEYE

Consensus	$466M

	1Q15
New Account Growth (y/y)	36.4%
Quarterly Attrition	18.4%

Source: Factset, Hedgeye Estimates



BECAUSE THEY WON'T CONSIDER YELP'S ATTRITION ISSUES

YELP would need to produce historically low Attrition Rates **and** accelerate its new account growth considerably over 1Q15 levels despite decelerating salesforce growth and declining productivity

YELP: TRACKING THE SHORT

Setup: YELP's model is breaking down, and mgmt is doing whatever it can to disguise what's really going on (i.e. M&A & evasive disclosure). The story took a major turn for the worse when its salesforce declined q/q in 1Q15 (Hedgeye estimate); it model can't afford any slippage there. Further management didn't do themselves any favors by maintaining 2015 guidance off the 1Q miss and light 2Q guidance in hopes of a takeout. We're expecting a 2Q miss on Local Advertising and mgmt to cut 2015 guidance.

What We're Keying In On: Salesforce, primarily size, secondarily productivity. Both speak to the size of YELP's TAM and the viability of its model. The former is the bigger issue; if YELP can't consistently grow its salesforce (net of churn), then the story is going to turn much quicker, and get much uglier than we initially expected.

Risks to Thesis: Upside from ancillary businesses, longer tail from acquired revenues. Buy-side consensus.

Timeline

- **1Q15:** Beat Revenues on Inorganic Upside, 2Q15 Release ahead of the Street, Consensus raises estimates
- **2Q15:** Miss Local Advertising Estimates, 3Q15 Guidance Release Disappoints, cuts 2015 guidance
- **3Q15:** Really depends on the 2Q15 release and how consensus trends thereafter
- **4Q15**: We may cover ahead, if not before, if consensus 2016 revenue growth rate slips to sub-30% rate (currently 34%)

SHOOTING ITSELF IN THE FOOT (AGAIN)

YELP should have rebased expectations on the 2015 guidance release, and had an another opportunity to do so on the last print. Now mgmt has raised the 2H15 bar while the model is unraveling.

TWTR SHORT THESIS

TWTR: SHORT THESIS SUMMARY

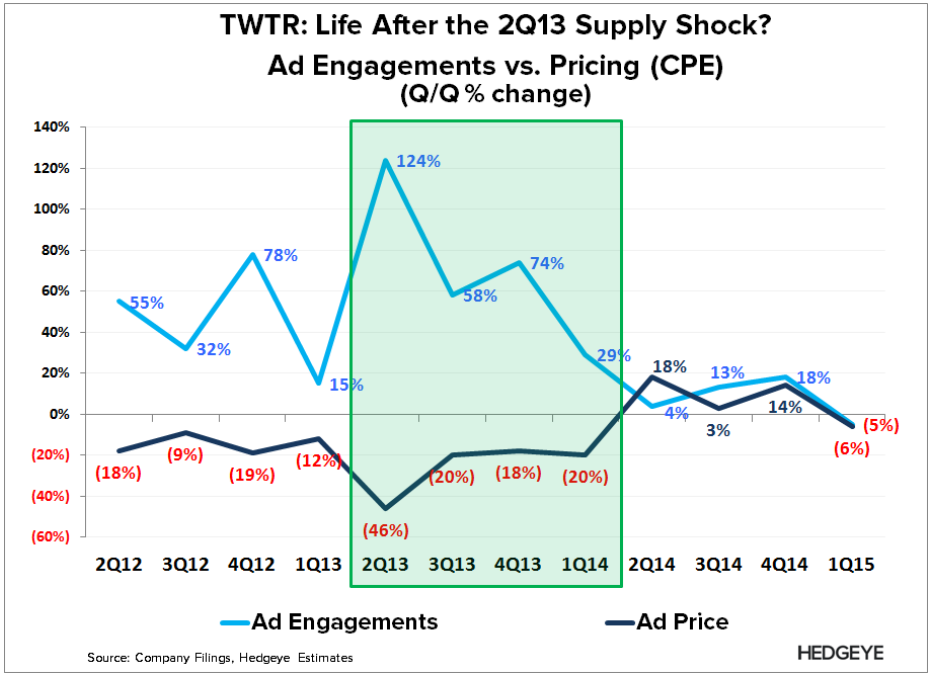
1. **Business Model**: TWTR runs CPC ad model, which requires user interaction with ads to generate revenue.

2. **Analysis:** We suspect surging ad load has been driving ad monetization, but pushing MAUs away, putting mgmt in a box vs. street expectations.

3. **Outlook:** Mgmt already slashed 2015 guidance, but concentrated the cut into 1H15. Consensus Ad Revenue estimates through 4Q16 still lofty.

4. **Setup:** We upside 1 quarter of upside in this print. Question is when mgmt rebases expectations again

5. **Duration:** 2016 guidance or earlier (mgmt?)



CAT IS OUT OF THE BAG…

TWTR missed 1Q revenue and cut 2015 guidance, most of cut centered on 1H15. We don't believe mgmt has answer to life after the 2Q13 Supply Shock, especially in relation to consensus expectations.

TWTR: KEY POINTS (SHORT)

1

MANAGEMENT IS IN A BOX

We suspect there is a perverse relationship between TWTR's revenue and user growth, with surging ad load driving revenue growth, yet pushing the user away at the same time. If TWTR experiences weakness on either front, the street will punish the stock for it.

2

ESTIMATES AREN'T AS LOFTY...BUT STILL LOFTY

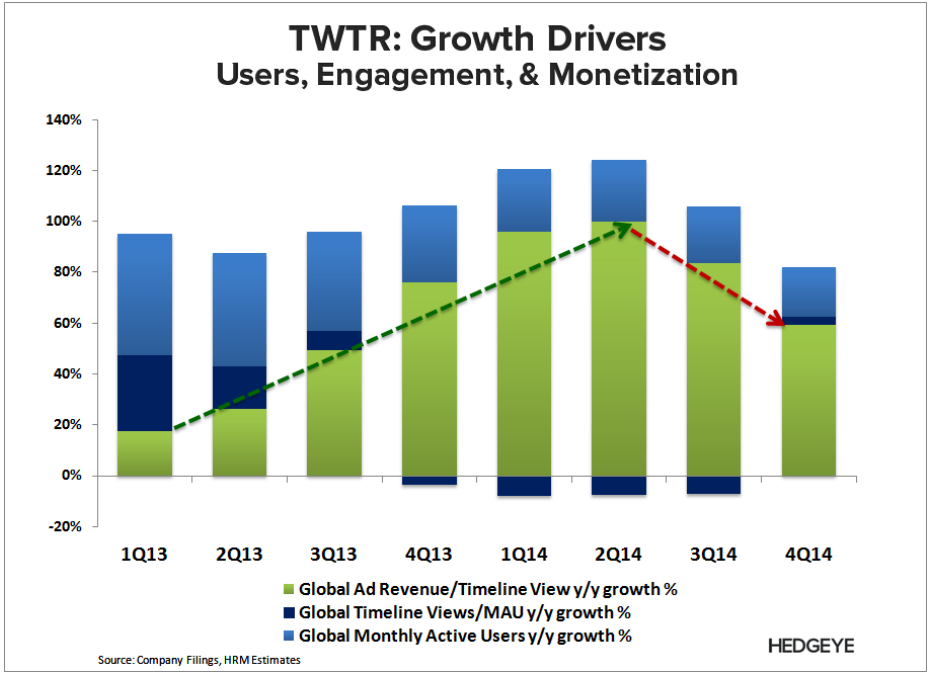
Management slashed 2015 guidance, concentrating most of the reduction into 1H15. The setup isn't as tough into the 2Q15 print if it can sustain its CPE tailwind. However, 2016 is still a stretch; consensus is looking for ad revenue growth to hover at a +50% rate through 4Q16.

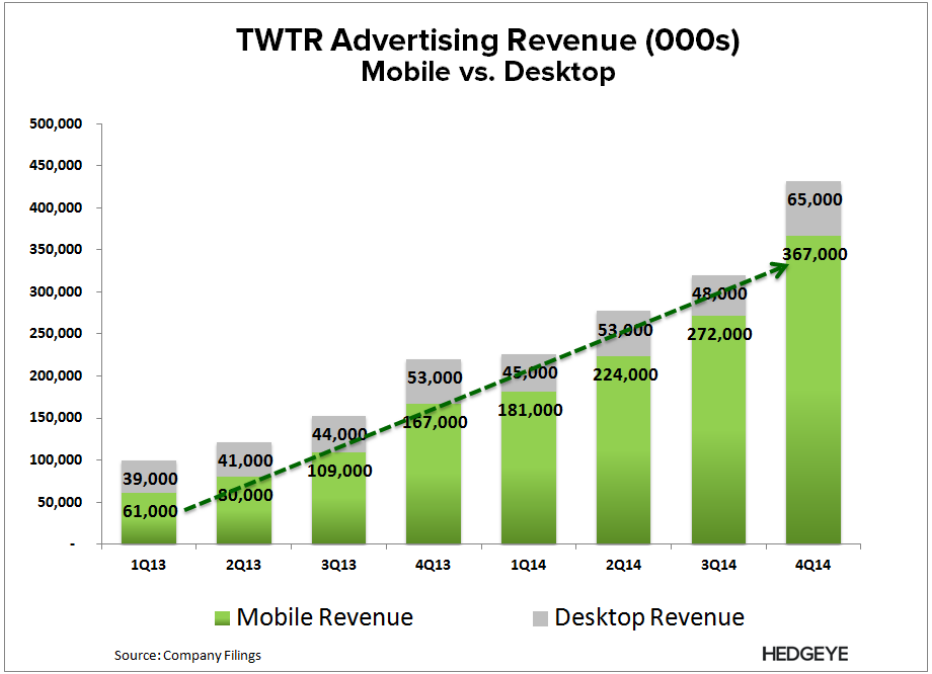
3

STAYING SHORT TILL MGMT CORRALS CONSENSUS

Granted, the easy money has been made, and expectations have been marginally rebased, but not enough. If management doesn't get a hold of the sell-side, it's walking into another blow-up. We'll stay short through 2016 guidance unless it grabs the consensus by the horns

TWTR'S GROWTH DRIVERS

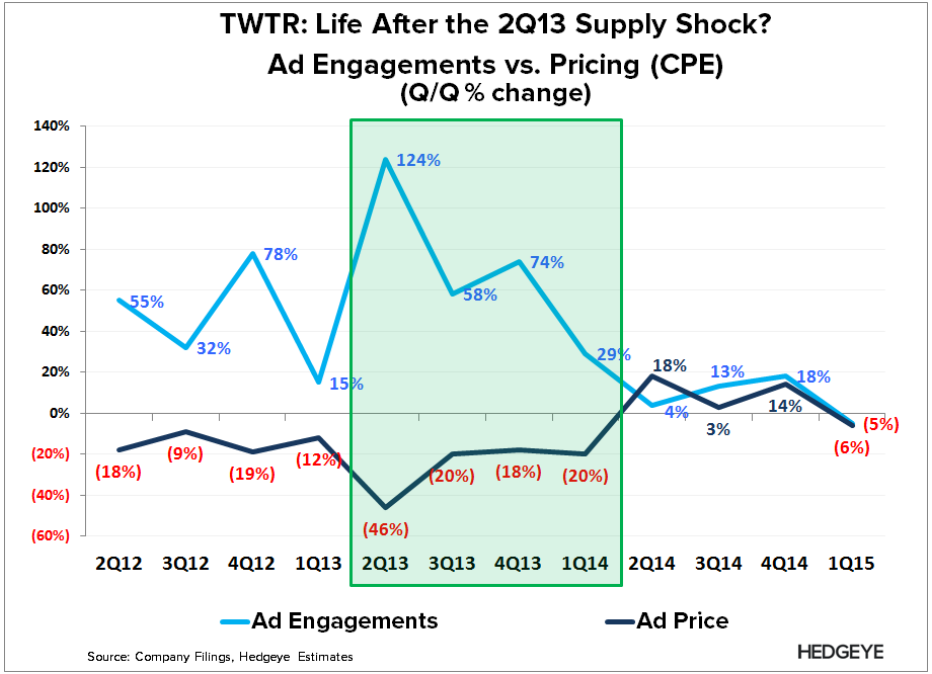




MOBILE MONETIZATION HAS BEEN DRIVING THE MODEL

Monetization has been a surging growth driver for TWTR, which has been driven primarily by mobile. Everything looks great until we understand what's been driving the model…

AD LOAD IS DRIVING MONETIZATION

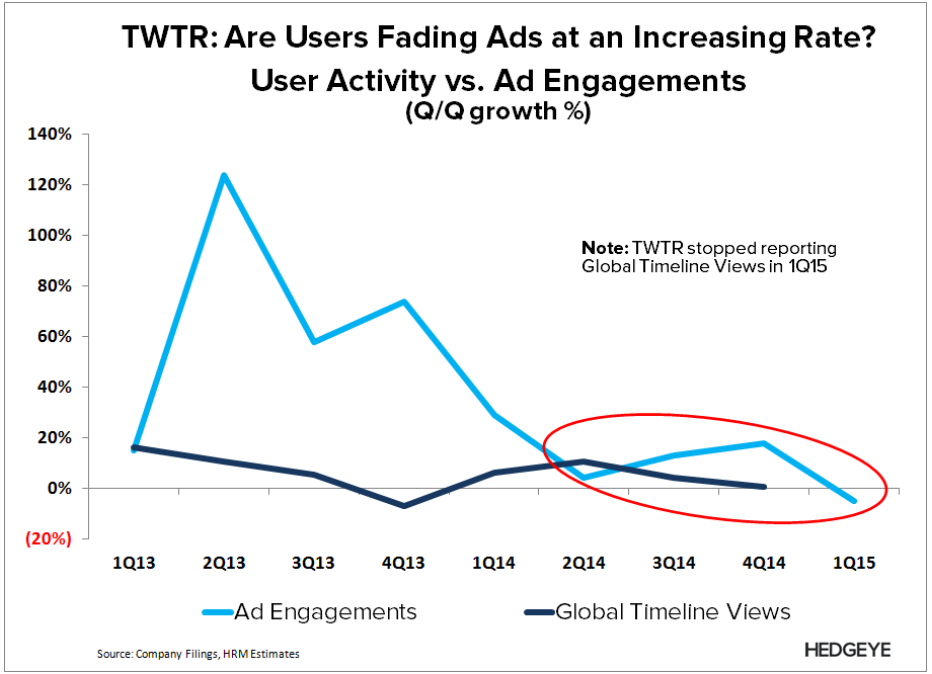


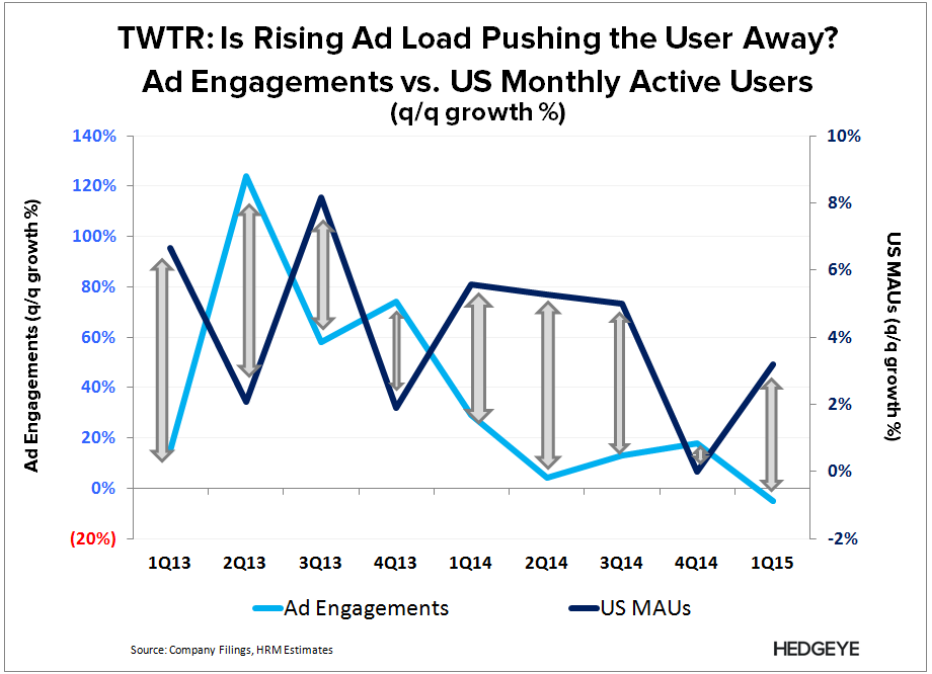
TWTR S-1/A MD&A (11/4/2013): *The decreases in cost per ad engagement over these periods* ***[3Q12-3Q13]*** *were primarily due to an* ***increase in supply of advertising inventory available in our auctions****, which was partially offset by increased demand for our Promoted Products.* ***Supply of advertising inventory increased as we expanded the distribution of our Promoted Products to our mobile applications and additional markets outside of the United States in 2012****. The increase in advertising inventory provided us with additional opportunities to place ads on our platform*

AND THERE IS ONLY SO MUCH THAT CAN INCREASE

TWTR's ad engagements have risen as cost has declined; suggesting supply has been the main lever of ad engagements. TWTR's S-1 essentially confirms our thesis. This cannot continue indefinitely…

MONETIZAION STRATEGY IS FAILING

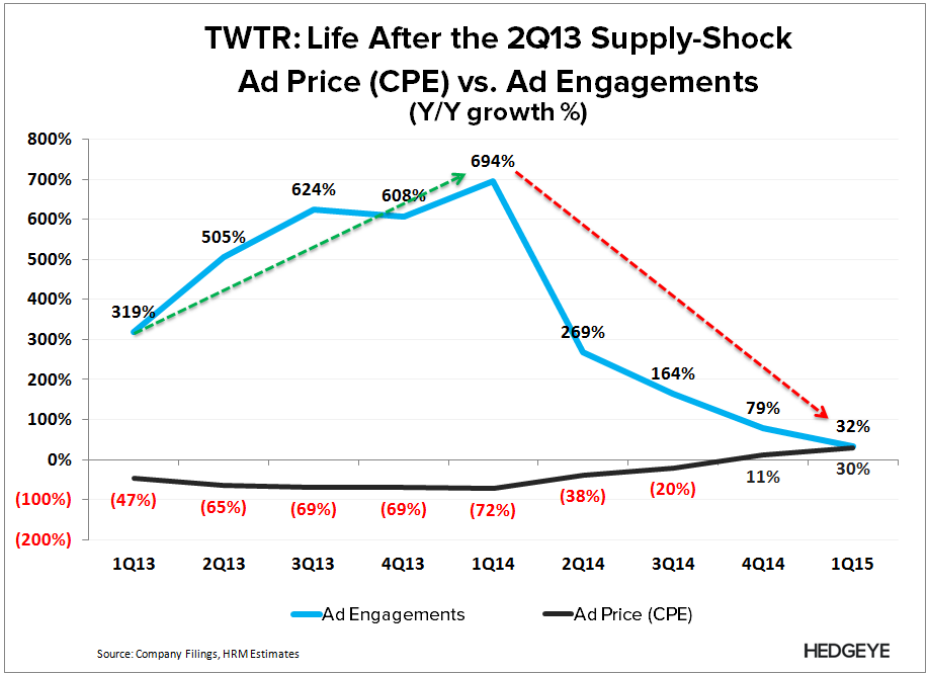


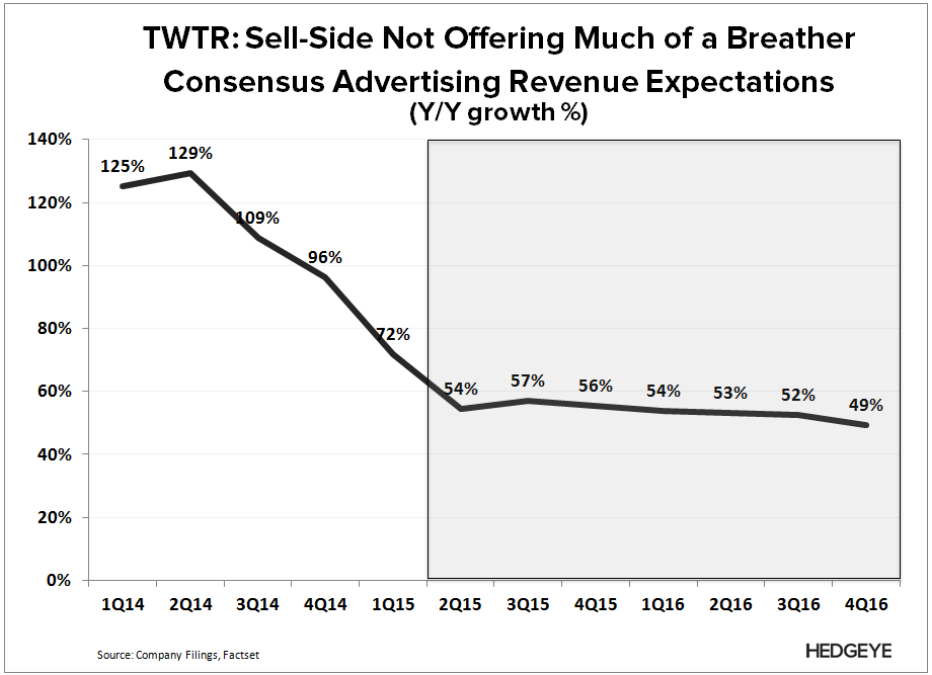


USERS ARE FADING RISING AD LOAD, IF NOT LEAVING ALTOGETHER

TWTR will not see a proportionate increase in ad engagements with rising ad load if users are fading ads at a growing rate. Even worse, it appears rising ad load may be pressuring user retention.

NOT OUT OF THE WOODS YET





MGMT IS WALKING THE PLANK UNTIL IT GETS THE SELL-SIDE UNDER WRAPS

Even with the new-found CPE tailwind, which is an underappreciated positive, mgmt will be hard-pressed to sustain a 50% growth rate through 2016 with ad engagements falling off a cliff.

TWTR: TRACKING THE SHORT

Summary: TWTR already cut 2015 guidance, so easy money has been made. But now the question is when management gets the sell-side under control. TWTR can't hit 2016 advertising revenue estimates, and 4Q15 may be a stretch as well. That said, we TWTR needs to drastically rebase expectations again, and we're staying short until it does

What We're Keying In On: CPE and Ad Engagements/MAU, which collectively will tell us whether mgmt has an answer to life after the 2Q13 Supply Shock. If those factors can both move in the same direction, it's a completely different story.

Risk to Thesis: Could get run over on 2Q15 release, but any upside would be short lived.

Timeline

- **1Q15:** Could miss 1Q15 Ad revenue, 2Q15 guidance could disappoint (depends on disclosure & M&A plan)
- **2Q15:** TWTR bought some breathing room on the guidance cut, question how it approaches 3Q guidance
- **3Q15:** Not sure, setup likely changes off the 2Q print
- **4Q15**: We doubt TWTR guides to $3.3B in 2016 revenue, which implies steady +50% ad revenue growth through 4Q16.

STAYING SHORT UNTIL MANAGEMENT CORRALS CONSENSUS

Easy money has been made. But the setup hasn't changed that much over the NTM. It all depends on how management chooses to address the street moving forward (manage expectations or appease).

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BABA BEARISH THESIS

BABA: BEARISH THESIS SUMMARY

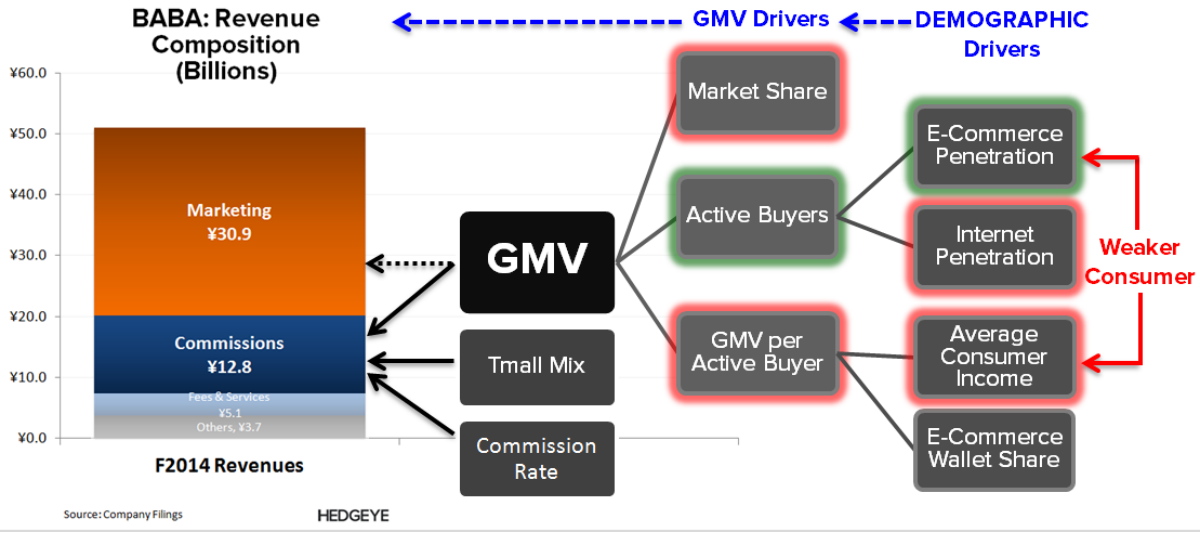
1. **Business Model**: The majority of BABA's revenues (~85%) are tied to its Gross Merchandise Value (GMV)

2. **Analysis:** Chinese consumer demographic analysis suggests the Upper Class is driving BABA's GMV.

3. **Outlook:** BABA's user growth will come from a progressively weaker consumer, which will pressure its entire model.

4. **Setup:** [Covered] Consensus not asking for much in F1Q16, gets worse after through, esepcially with YHOO Spinco in 4Q15.

5. **Duration:** depends on consensus & mgmt



WE COVERED THE SHORT, F1Q16 SETUP GOING AGAINST THE BEARS

Fundamental thesis still holds: The influx of a weaker consumer will lead to declining avg spending and decelerating GMV/revenue growth; particularly within its core marketing segment (this has already started).

BABA: KEY POINTS

1

HOSTAGE TO THE CHINA GROWTH STORY

BABA is too large to control its own destiny. BABA has dominant share in China's e-commerce market. BABA will become increasingly dependent on the demographics of the Chinese consumer, which creates a new set of challenges for the company.

2

GROWTH WILL COME AT A PRICE

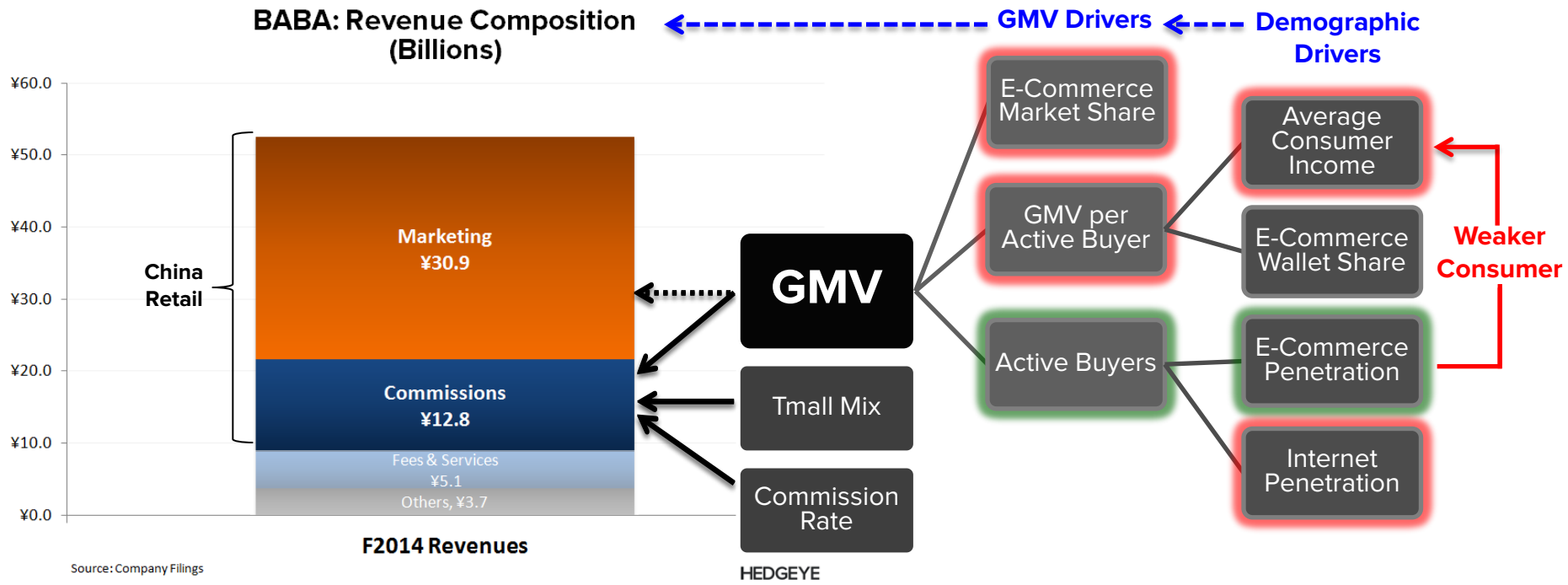
BABA's active buyer growth moving forward will come from a much weaker consumer, which will pressure both GMV growth (Average GMV) and pricing on the ads vendors run on BABA's sites. The latter falls within BABA's Marketing segment, which represents the majority of its revenues.

3

BUT ESTIMATES HAVE COME IN

Consensus responded to the F3Q15 blow-up by slashing estimates in the subsequent two quarters (F1Q16 included). Combine that with the recent sell-off = Cover and watch. The YHOO SpinCo remains a bearish catalyst, but if BABA can manage expectations, we'll stay away.

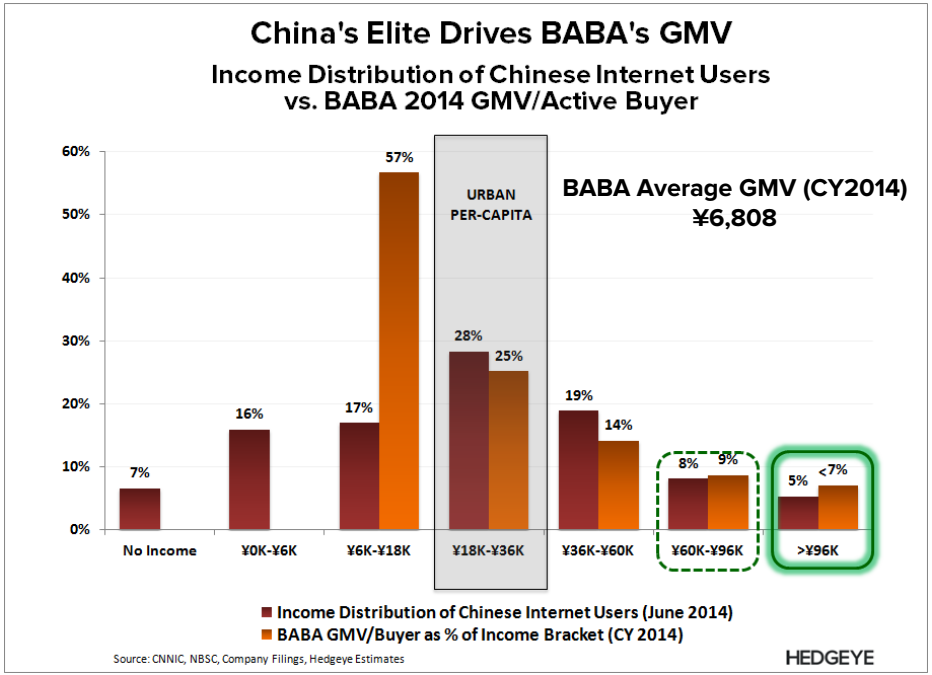
GMV DRIVES BABA'S BUSINESS MODEL



THE CHINA GROWTH STORY WILL PRESSURE ITS GMV MOVING FORWARD

BABA already has dominant market share, so its GMV growth moving forward will become increasingly hostage to the China growth story (particularly demographics), which has less to bear from here...

CHINA'S ELITE DRIVES BABA'S GMV



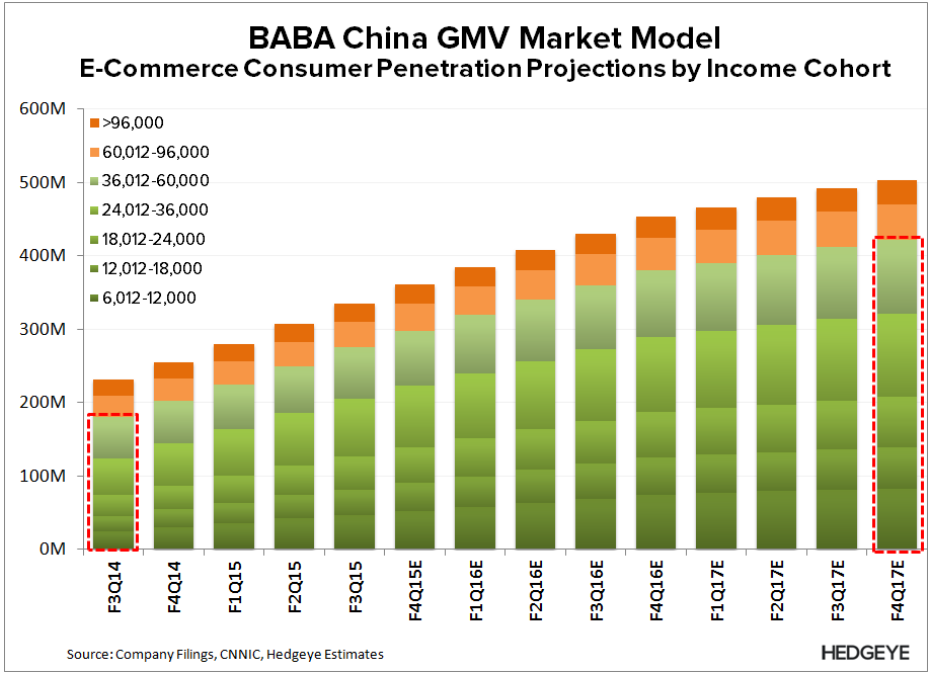
BABA F2Q15 Earnings Call (Maggie Wu): "*Let me share with you some color on this average spending per buyer. As I said that the longer customers stay with us, the more they're going to spend annually on our platform. I'll give you an example*"

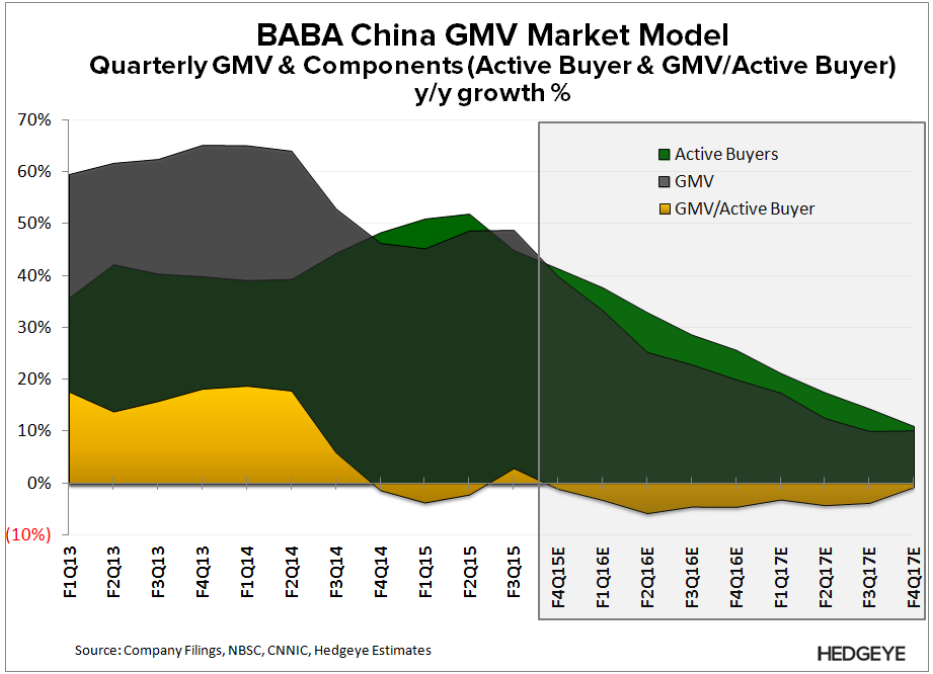
- *"The customer who stayed with us for a* ***year's time, their average annual spending level is somewhere around RMB 1,000****"*
- *"And for the ones who stayed with us for* ***five years' time, their spending level is somewhere around RMB 15,000****"*
- *"And then for the ones who stayed around* ***10 years, their levels is going to above RMB 30,000****"*

AVERAGE GMV + COHORT COMMENTARY → UPPER CLASS DRIVES BABA'S GMV

Wallet share gains will be tied upper class appetites moving forward, and those gains need to strong enough to mitigate the dilutive impact of new user growth to sustain average GMV (next section).

AVERAGE SPENDING (GMV) TO DECLINE

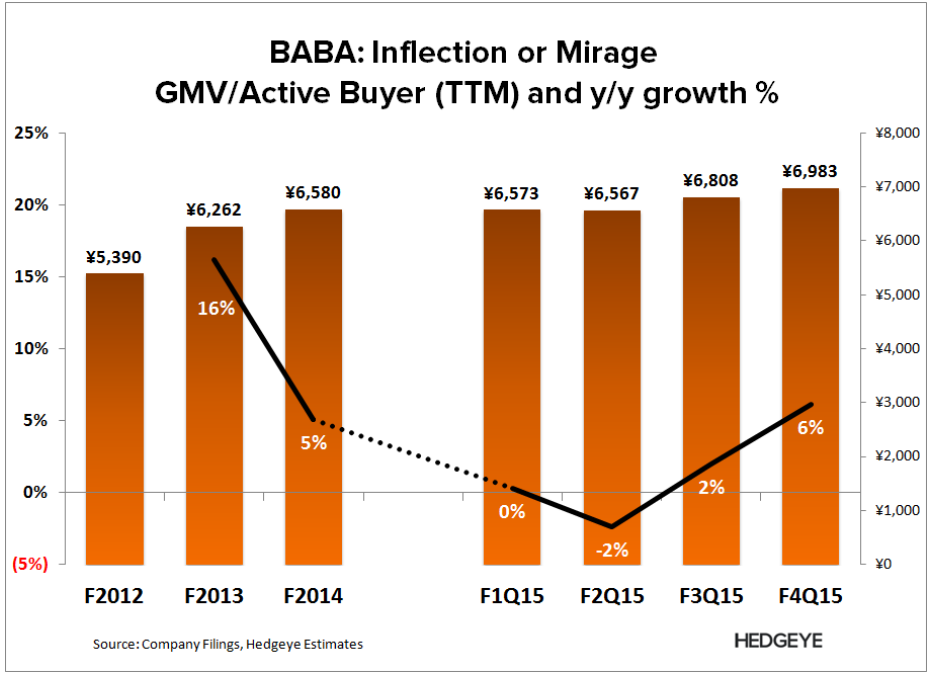


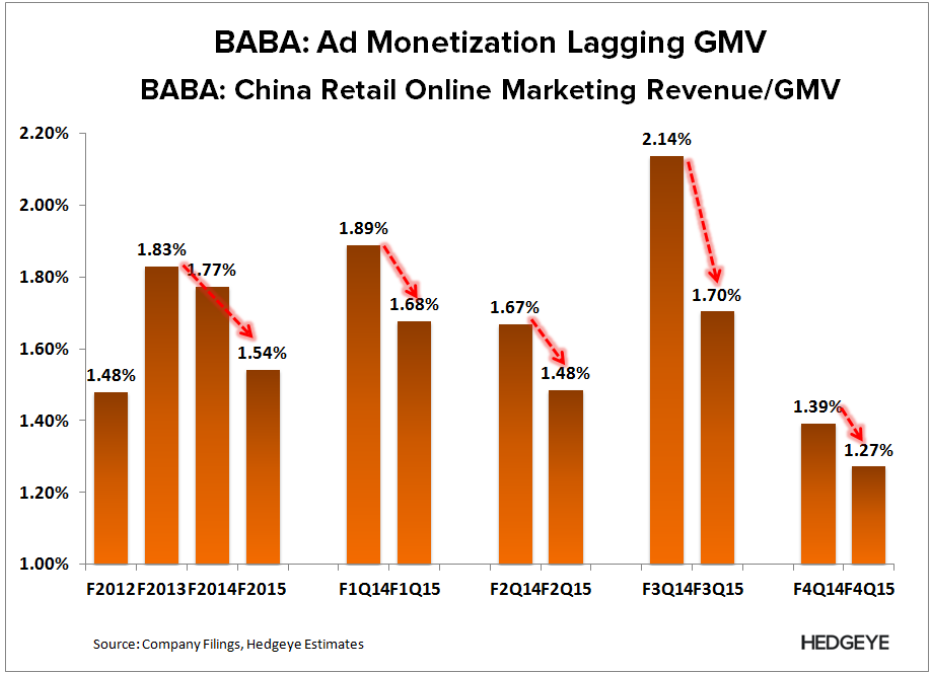


TURNING WHAT WAS A MASSIVE TAILWIND INTO A SECULAR HEADWIND

Our model is driven off of demographic projections of e-commerce penetration and spending by income cohort. The growing mix of lower-income consumers will pressure GMV, which will pressure ad rates as well…

THIS HAS ALREADY STARTED

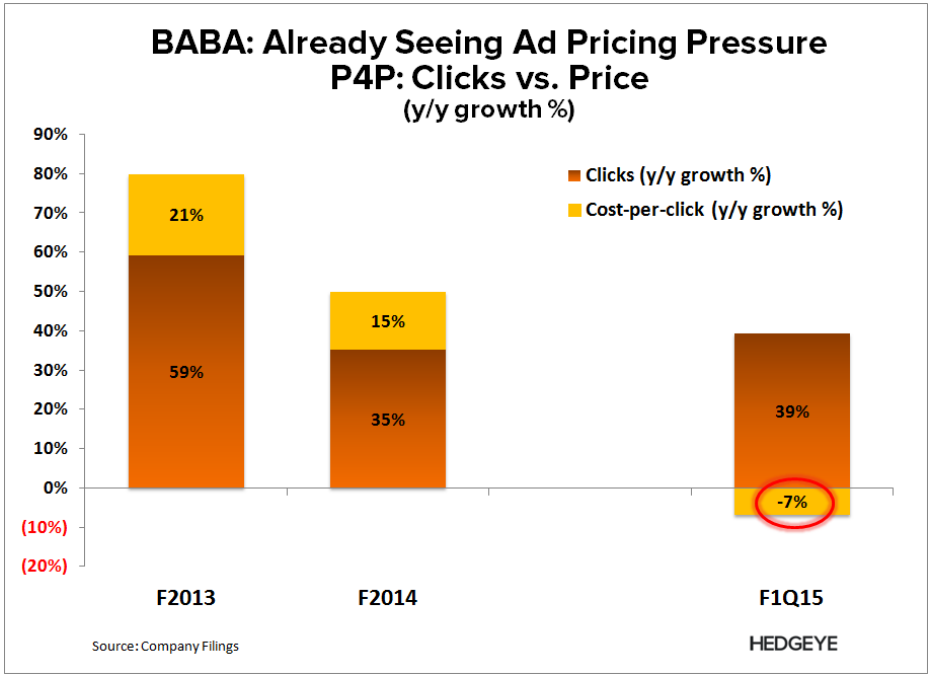




WEAKER BUYER → SLOWING AVERAGE SPEND → WANING ADVERTISING DEMAND

BABA's monetization rate includes commission revenue, so this dynamic isn't as evident in its reported monetization rate. So why isn't advertising keeping pace with GMV?

AD PRICING IS UNDER PRESSURE



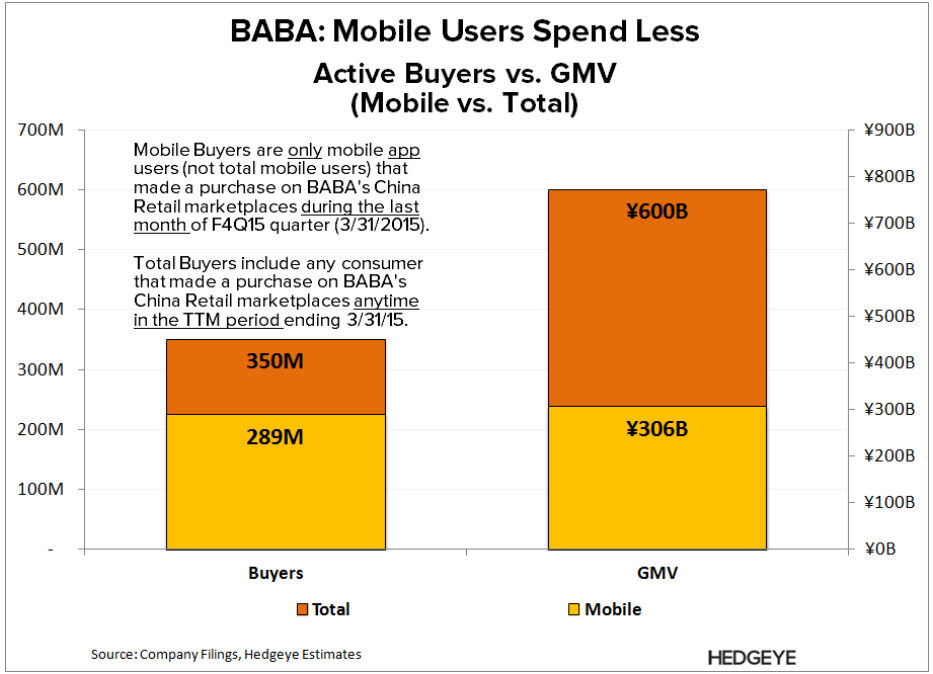
BABA F-1 COMMENTARY: F1Q15 (CY 2Q14)

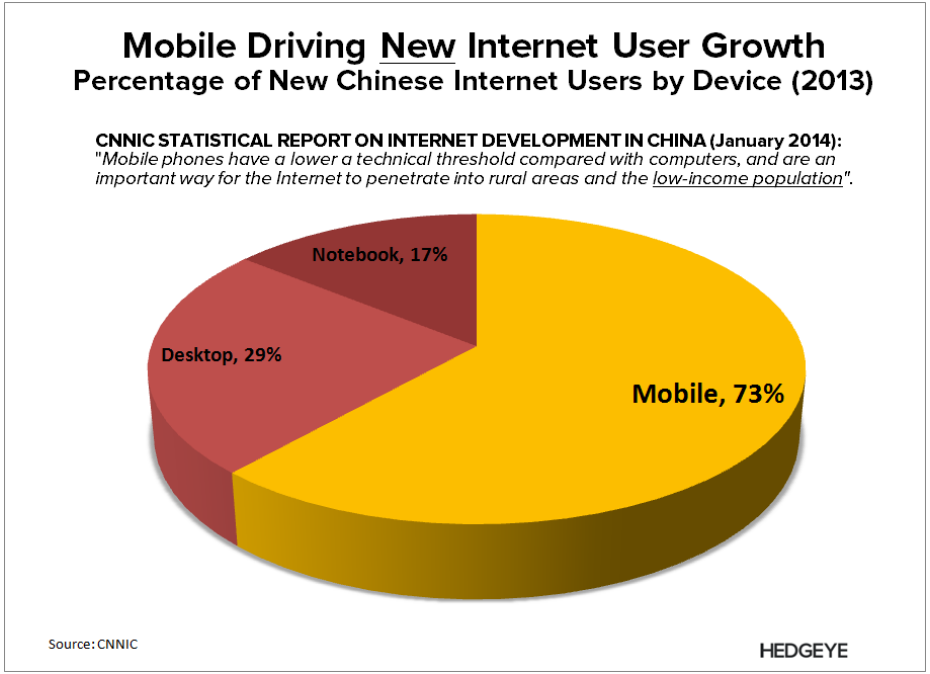
*"The increase in online marketing services revenue during this period was primarily driven by a 39.2% increase in the number of clicks attributable to our P4P marketing services, which was partially offset by a 6.9% decrease in the cost-per-click paid by our merchants, reflecting a higher proportion of **mobile marketing services**, for which our merchants currently pay a lower cost-per-click than for marketing services placed through personal computer interfaces"*

MOBILE IS TO BLAME

What was a tailwind is now a headwind. We suspect the reason why vendors are not paying comparable rates for mobile is because they have experienced lower conversion off their mobile ad clicks.

MOBILE = WEAKER CONSUMER

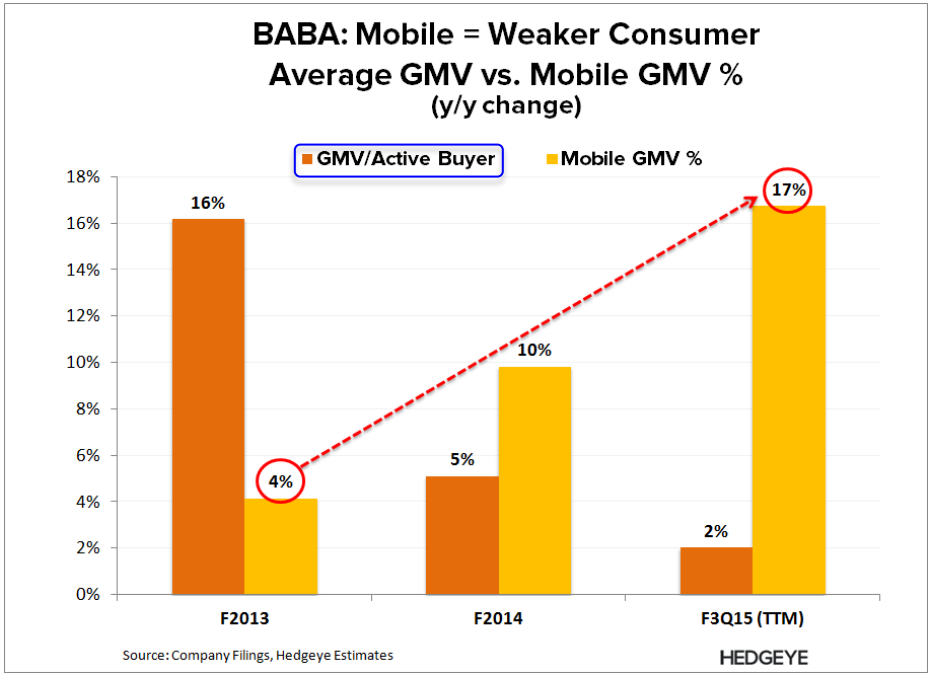


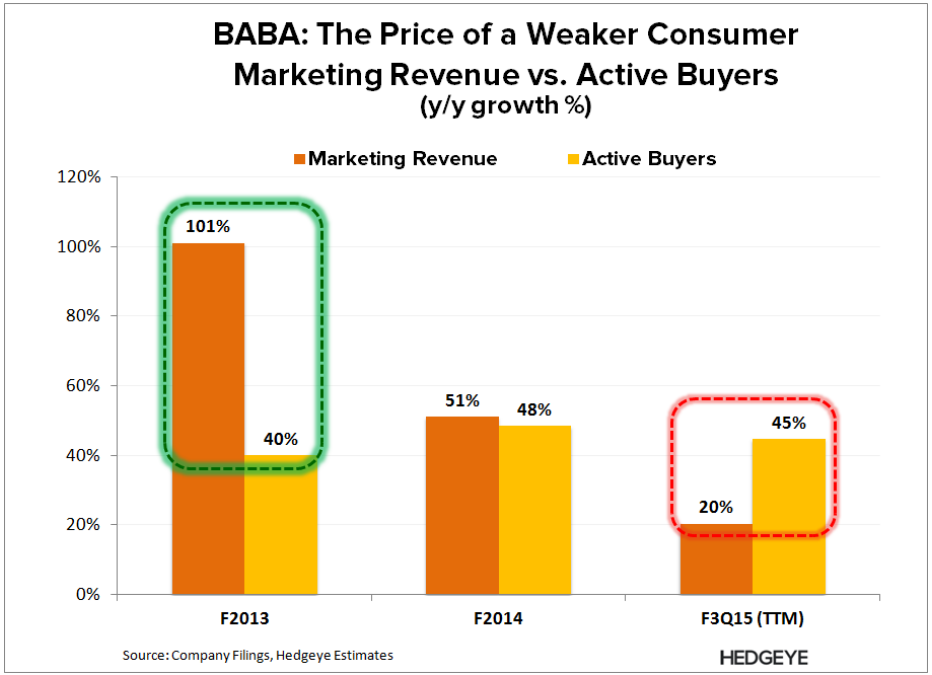


MOBILE IS NOT LONG-TERM OPPORTUNITY, IT'S A SECULAR HEADWIND.

Mobile consumer represent the majority of BABA's consumers, yet the minority of its GMV. As more mobile users join the platform, the more pressure on average spending (GMV)

WEAKER BUYER = PRICING PRESSURE

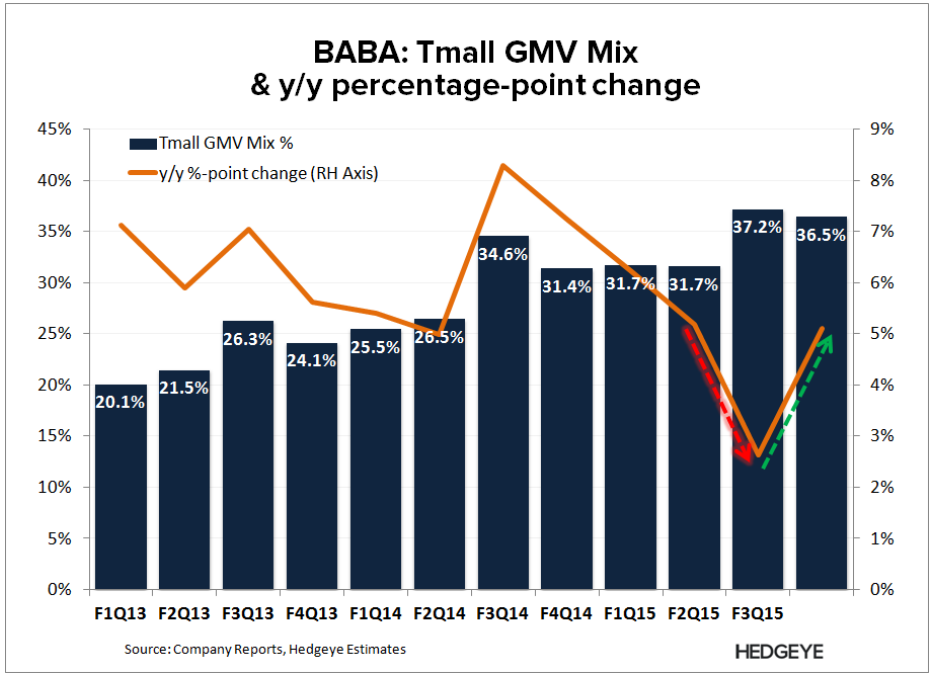


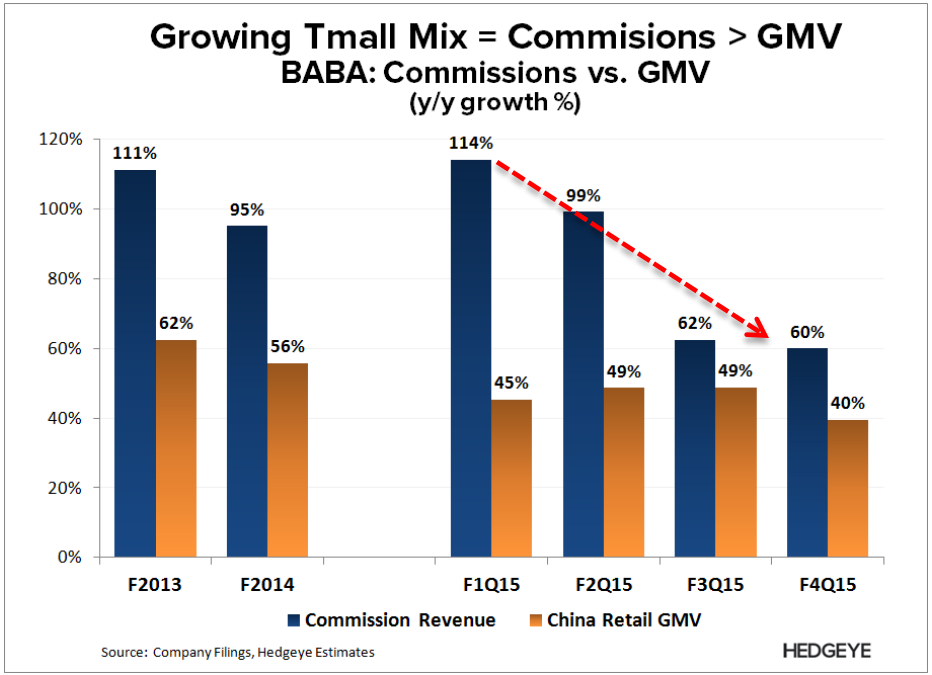


MARKETING: SECULAR DECLINE IN AVG GMV = SECULAR AD PRICING PRESSURE

Slowing Average GMV has already led to marketing revenue growth failing to keep pace with user growth; this dynamic will only get worse. **Weaker consumer → Worse Ad Conversion/ROI → Ad Pricing Pressure.**

CAN'T TRUST TMALL MIX





COMMISSIONS: TMALL MIX IS NOT AN UNBRIDLED TAILWIND ANYMORE

Tmall Mix Shift has been driving commission growth in excess of GMV; partially mitigating weakness in its Marketing segment. That should continue near-term, but not to the same historical magnitude.

BABA: TRACKING THE STOCK

Setup: Currently favors the bulls with the recent sell-off and subdued F1Q16 estimates. But the fundamental thesis hasn't changed. BABA's model is facing secular pressure from the influx of a weaker consumer, which will leading to a precipitous slowdown in both GMV and revenue growth. Further, the sell-side is still confusing mobile weakness as a longer-term opportunity rather than a secular headwind. We believe BABA needs to produce consistent upside to sustain its valuation; we don't believe that's possible.

What We're Keying In On: Consensus. The sell-side isn't giving BABA much breathing room starting in F2Q16. Consensus concentrated its downward revisions off the F3Q15 release into the following two quarters.

Risks to Thesis: Adequate Disclosure, New acquisitions, artificially inflated reported metrics (fraud)

Timeline

- **F4Q15:** inline to slight top-line miss. Our tracker suggests Tmall Mix and Commission growth will slow further
- **F1Q16:** favoring the bulls with subdued consensus estimates and recent sell-off with Chinese stocks
- **F2Q16:** potential top-line miss on slowing GMV and take-rate growth, consensus estimates decline (question is how much)
- **F3Q16**: depends on consensus, YHOO Spinco could be a major headwind.

EXPECTATIONS IS THE BIG QUESTION

Consensus is still asking too much from BABA through F2017. With a F1Q16 top-line beat, we expect estimates to track even higher, We're expecting the setup to get tougher starting in F2Q16

PLEASE REACH OUT WITH ANY QUESTIONS, OR TO DISCUSS FURTHER

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