WHAT'S HOT: CLOUD COMPUTING: ARE SHARE PRICES HEADING TOWARD ZERO, OR IS IT AN OPPORTUNITY TO CONSIDER?

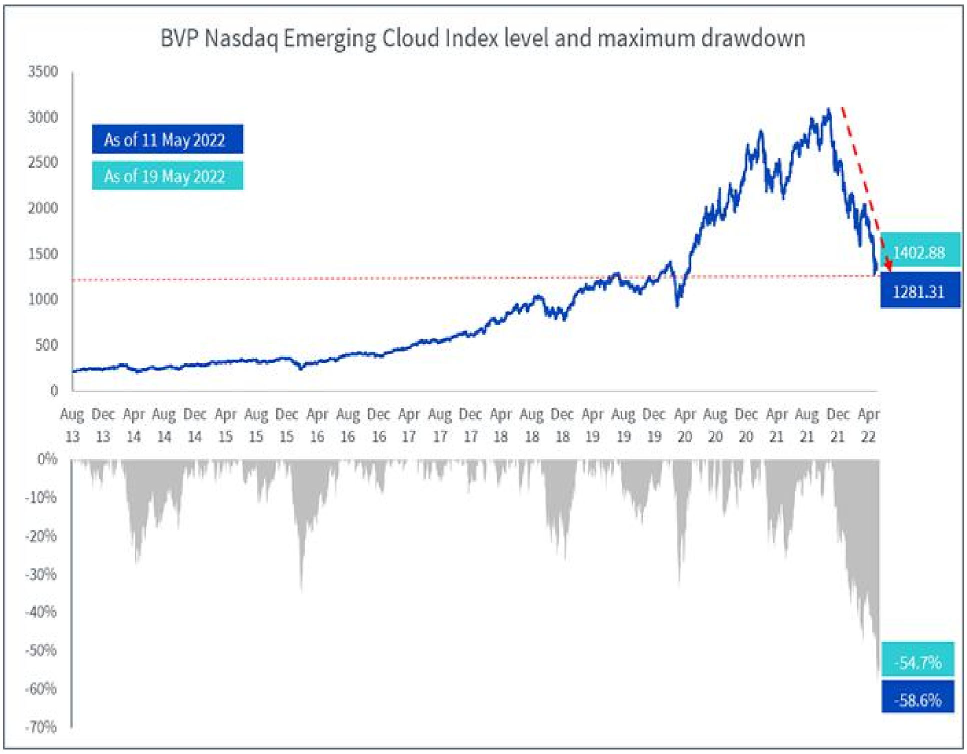
Christopher Gannatti – Global Head of Research, WisdomTree.,Elvira Kuramshina – Associate Director, Quantitative Research
20 May 2022

Cloud Computing: Are Share Prices Heading Toward Zero, or is it an Opportunity to consider?

The drawdown in many stocks focused on cloud computing software has been, in a word, unbelievable. In basically one month's time, from 11th April to 11th May, the BVP Nasdaq Emerging Cloud Index—a group of cloud-oriented companies—has lost roughly 30% of its value.
In Figure 1, we see:

- The drawdown of the BVP Nasdaq Emerging Cloud Index (EMCLOUDN) from the peak in November 2021, when the U.S. Federal Reserve began to discuss removing liquidity from the market in a serious way, has been more than 50%.
- From 9th November 2021 to 11th May 2022, the period of 'maximum drawdown' to date, we had a 58.6% drop over 126 days.
- On 11th May 2022, EMCLOUDN closed below levels observed first time in July 2019.

Figure 1: The Drawdown in Cloud Computing Share Prices has been intense



Source: WisdomTree, Bloomberg. Period from 16 August 2013 to 19 May 2022. The BVP Nasdaq Emerging Cloud Index is presented on a 'net' basis when referencing dividend reinvestment. The index began live calculation on 02 October 2018, so values before this date represent backtested data. You cannot invest directly in an index.

Historical performance is not an indication of future results and any investments may go down in value.

The primary question, knowing this, comes back to the following, which we can simplify down to two outcomes.

1. Cloud computing as a delivery mechanism through which customers subscribe to software is the wrong business model, and customers will vote with their wallets and go towards something different.

1. Customers are at least equally excited and, if not even more excited, about cloud computing as a delivery mechanism through which they can subscribe to software.

Company Results Support Outcome #2 over Outcome #1

While we can never guess the future with certainty, the evidence that we can interpret today would tend to indicate that Outcome #2 has a higher probability of becoming true.

The big players are still growing—FAST.

- One of the risks we monitor in cloud computing regards the biggest players shifting from engines of growth to something more like ‘utilities’—the concept being that everyone able to adopt cloud computing has done so, so the future growth stabilises.

- Amazon Web Services (AWS) indicated revenue growth of 37%, to a figure of $18.4 billion[1].

- Microsoft indicated that the part of its cloud business most directly comparable to AWS grew revenues at 46% year-over-year. It should be noted that it only had 7% market share in 2016, so getting to 20% in this short time has been impressive[2].

- Google Cloud indicated year-over-year revenue growth of 44%, to a figure of $5.8 billion[3].

M&A Activity is Still Active

While it is true that not every cloud-focused company is involved in M&A, even amidst the share price performance turmoil of 2022, companies are still active.

Google Cloud has announced its intention to buy Mandiant, a cybersecurity firm, for $5.4 billion. The rationale is to provide its cloud customers with more robust cybersecurity solutions at a time when this is at the forefront of many customers’ minds[4].

Shopify has announced its intention to buy e-commerce fulfilment specialist Deliverr for $2.1 billion[5].

Conclusion: The Cloud Business Model is Still Robust Amidst Substantial Lowering of Equity Valuations

Some of us might have thought that there has been so much discussion about Western central banks shifting policy from extremely ‘easy’ to extremely focused on mitigating the risk of runaway inflation that this must have been priced into equity markets. The recent behaviour of software-oriented cloud computing companies would tell us something different—adjustments are clearly still being made. Our bottom line is this—these subscription-oriented businesses are still largely growing their revenues, even if that growth is nowhere near what would have been seen during the pandemic period in 2020. Those with a time horizon of the next few months may have an extremely uncertain outcome. Those with a time horizon in the range of 5, 7 or 10 years—as long as the cloud business model continues to find favour—may see this downdraft as an interesting opportunity.

Sources

[1] Herrera, Sebastian. “Amazon Posts First Quarterly Loss Since 2015 as Costs, Rivian Stake Weigh on Results.” Wall Street Journal. 28 April 2022.

[2] Tilley, Aaron. “Microsoft Earnings Rose Last Quarter With Demand for Cloud Services.”

Wall Street Journal. 26 April 2022.

[3] Bobrowsky, Meghan. “Alphabet Earnings Show Slowing Sales Growth on Digital-Ad Tumult.” Wall Street Journal. 26 April 2022.

[4] Bobrowsky, 2022.

[5] Marchese, Adriano. “Shopify to Buy E-Commerce Fulfilment Specialist Deliverr for $2.1 Billion.” Wall Street Journal. 5 May 2022.

Related products

+ WisdomTree Cloud Computing UCITS ETF - USD Acc (WCLD/KLWD)

View the online version of this article here.

Important Information

Marketing communications issued in the European Economic Area ("EEA"): This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

Marketing communications issued in jurisdictions outside of the EEA: This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as "WisdomTree" (as applicable). Our Conflicts of Interest Policy and Inventory are available on request.

For professional clients only. The information contained in this document is for your general information only and is neither an offer for sale nor a solicitation of an offer to buy securities or shares. This document should not be used as the basis for any investment decision. Investments may go up or down in value and you may lose some or all of the amount invested. Past performance is not necessarily a guide to future performance. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

The application of regulations and tax laws can often lead to a number of different interpretations. Any views or opinions expressed in this communication represent the views of WisdomTree and should not be construed as regulatory, tax or legal advice. WisdomTree makes no warranty or representation as to the accuracy of any of the views or opinions expressed in this communication. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

This document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public offering of shares or securities in the United States or any province or territory thereof. Neither this document nor any copy hereof should be taken, transmitted or distributed (directly or indirectly) into the United States.

Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any affiliate, nor any of their respective officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.