Ten Questions
Internet Execs Should Ask & Answer

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Question Focus Areas

1) Globality
2) Mobile
3) Social Ecosystems
4) Advertising
5) Commerce
6) Media
7) Company Leadership Evolution
8) Steve Jobs
9) Ferocious Pace of Change in Tech
10) Closing Thoughts
1. **Globality**

*Do you know which players in which countries do what you do better (or at least differently) than you do?*

*Do you study / implement it?*
Top Internet Markets – 46% of Users in 5 Countries – China, USA, Brazil, India, Russia

USA
240MM users, +4% Y/Y
76% penetration*

Brazil
76MM users, +3% Y/Y
39% penetration*

Russia
60MM users; +31% Y/Y
42% penetration*

China
384MM users; +29% Y/Y
29% penetration*

India
61MM users; +18% Y/Y
5% penetration*

2009 - 1.8B Global Internet Users, +13% Y/Y(1); 18.8T Minutes Spent, +21% Y/Y(2)

Note: *Penetration is per 100 inhabitants.
Source: 1) Internet user stats per International Telecommunications Union; 2) time spent data per comScore global 12/09.
## Top Mobile Internet Markets – ~670MM 3G Subscribers (+37% Y/Y), CQ2

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>CQ2:10 3G Subs (MM)</th>
<th>3G Penetration</th>
<th>3G Sub Growth Y/Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>USA</td>
<td>136.6</td>
<td>48%</td>
<td>31%</td>
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<td>2</td>
<td>Japan</td>
<td>106.3</td>
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<td>Italy</td>
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<td>57</td>
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<td>France</td>
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<tr>
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<td>Australia</td>
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<td>31</td>
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<td>Poland</td>
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<td>Russia</td>
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<td>5</td>
<td>81</td>
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<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>CQ2:10 3G Subs (MM)</th>
<th>3G Penetration</th>
<th>3G Sub Growth Y/Y</th>
</tr>
</thead>
<tbody>
<tr>
<td>16</td>
<td>Malaysia</td>
<td>7.9</td>
<td>26%</td>
<td>32%</td>
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<tr>
<td>17</td>
<td>Canada</td>
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<td>Saudi Arabia</td>
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<td>Turkey</td>
<td>6.8</td>
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<tr>
<td>20</td>
<td>South Africa</td>
<td>6.7</td>
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<td>Portugal</td>
<td>5.7</td>
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<td>23</td>
<td>Netherlands</td>
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<td>33</td>
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<td>Austria</td>
<td>5.1</td>
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<td>25</td>
<td>Israel</td>
<td>4.9</td>
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<td>Philippines</td>
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<td>Greece</td>
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<td>29</td>
<td>Singapore</td>
<td>3.9</td>
<td>55</td>
<td>41</td>
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<tr>
<td>30</td>
<td>Romania</td>
<td>3.8</td>
<td>13</td>
<td>20</td>
</tr>
</tbody>
</table>

### Global 3G Stats:
- Subscribers = ~670MM
- Penetration = 14%
- Growth = 37%

Note: 3G includes CDMA 1x EV-DO and Rev. A / B, WCDMA, HSPA; Source: Informa WCIS+, Morgan Stanley Research.
Unusually High Level of Global Innovation – Facebook & Tencent Learning From Each Other’s Playbooks

**Facebook**
- Largest Social Network in English-Speaking Countries – 620MM visitors, +51% Y/Y in 9/10
- Real Identity – Sharing among real-world friends / pictures / events

**Tencent**
- Largest Social Network in China – 637MM active IM users, +31% Y/Y in CQ3
- Virtual Identity – $1.4B virtual goods revenue (from users customizing their avatars / purchasing game items…) in 2009, +94% Y/Y

Source: Facebook, comScore (global unique visitors for Facebook), Tencent.
2. Mobile

Ramping faster than any ‘new new thing’ – is your business leading or lagging?
Apple iPhone + iTouch + iPad Ramp – The Likes of Which We Haven’t Seen Before

iPhone + iTouch vs. NTT docomo i-mode vs. AOL vs. Netscape Users
First 20 Quarters Since Launch

Note: *AOL subscribers data not available before CQ3:94; Netscape users limited to US only. Morgan Stanley Research estimates ~65MM+ netbooks have shipped in first 11 quarters since launch (10/07). Source: Company Reports, Morgan Stanley Research.

Data as of CQ3:10.
Mobile Operating Systems –
Attackers (Apple & Google) Driving Market Excitement & Momentum

Global Unit Shipment Share of Smartphones by Operating System,
Symbian (Nokia) / BlackBerry (RIM) / iOS (Apple) / Android (Google) / Others, 1Q06 – 3Q10

Note: iOS excludes iPod Touch and iPad shipments as they are not smartphones. *Others include Windows Mobile, Palm OS & WebOS, Linux and other proprietary smartphone OSes. Call outs on the left side represent market shares in CQ1:06; call outs on the right side represent market shares in CQ3:10. Source: Gartner.
Smartphone > PC Shipments Within 2 Years – Implies Very Rapid / Land Grab Evolution of Internet Access

Global Unit Shipments of Desktop PCs + Notebook PCs vs. Smartphones, 2005 – 2013E

2012E: Inflection Point
Smartphones > Total PCs

Note: Notebook PCs include Netbooks. Source: Katy Huberty, Ehud Gelblum, Morgan Stanley Research. Data and Estimates as of 11/10
Japan Social Networking Trends Show How Quickly Mobile Can Overtake Desktop Internet Access – Mixi Mobile Page Views = 84% vs. 17% Four Years Ago

Note: Mixi is one of Japan’s leading social networking sites on PC and mobile with 22MM registered users as of 10/31/10. It monetizes mobile usage via sales of avatars, customized homepages and other premium services.

Source: Company reports, Morgan Stanley Research
3. Social Ecosystems

Would you rather be Apple, Google or…Facebook?
Will their future directions help / hurt your business?
Facebook / Apple / Google = Platforms of Different Types...Each with Rapid Innovation

Facebook

- 620MM users +51% Y/Y
- 550K+ Apps
- 500MM+ Downloads

Apple iPhone / iTouch / iPad

- 120MM+ users +111% Y/Y
- 300K+ Apps
- 6.5B+ Downloads

Google

- 940MM users +11% Y/Y
- CQ3: CPCs +2% Q/Q
- Paid Clicks +16% Y/Y

Source: PC World, comScore (global user data for Facebook and Google as of 9/10), Facebook, Apple, Google (as of CQ3).
4. Advertising

Ripe for innovation –

will your business benefit?
Media Time Spent vs. Ad Spend Still Out of Whack
Internet / Mobile (upside…) vs. Newspaper / Magazine / TV (downside…)

% of Time Spent in Media vs. % of Advertising Spending, USA 2009

0% 10% 20% 30% 40% 50%
% of Total Media Consumption Time or Advertising Spending

Print  Radio  TV  Internet

Time Spent: 12%  16%  31%  28%
Ad Spend: 26%  9%  39%  13%

~$50B Global Opportunity

Morgan Stanley

Note: Time spent data per NA Technographics (2009), ad spend data per VSS. Internet advertising opportunity assumes online ad spend share matches time spent share, per Yahoo!. Source: Yahoo! Investor Day, 5/10.
Advertising Dollars Follow Eyeballs – Ad Revenue per User = $46 in 2009E vs. $0 in 1994E

<table>
<thead>
<tr>
<th></th>
<th>1995E</th>
<th>2009E</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global Internet Ad Revenue</td>
<td>$55MM</td>
<td>$54B</td>
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<tr>
<td>Ad Revenue per User</td>
<td>$9</td>
<td>$46</td>
</tr>
<tr>
<td>Global Internet Users</td>
<td>6MM</td>
<td>1.2B</td>
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</tbody>
</table>

Source: Global online ad revenue per Juniper Communications (1995), ZenithOptimedia (2009). Internet users per MS estimate (1995) and comScore (2009). We note that comScore reports a lower global Internet user # than International Telecommunications Union.
**Facebook’s 620MM Users (+51% Y/Y) + Under-Monetized ‘Like’ Connections Offer Significant New Ad Opportunities**

<table>
<thead>
<tr>
<th>Rank</th>
<th>Top 20 Brands / Products</th>
<th># of People Who Like This (Millions)</th>
<th>Equivalent TV Shows*</th>
<th>TV CPM Range ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Texas Hold’em Poker (Zynga)</td>
<td>27.2</td>
<td>American Idol</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Facebook</td>
<td>25.2</td>
<td>NCIS</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>YouTube (Google)</td>
<td>19.6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Starbucks</td>
<td>16.9</td>
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<td></td>
</tr>
<tr>
<td>5</td>
<td>Coca-Cola</td>
<td>16.7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>Mafia Wars (Zynga)</td>
<td>14.4</td>
<td></td>
<td></td>
</tr>
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<td>7</td>
<td>Oreo (Kraft)</td>
<td>13.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>Skittles (Mars)</td>
<td>12.4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td>Red Bull</td>
<td>11.1</td>
<td>The Good Wife</td>
<td></td>
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<tr>
<td>10</td>
<td>Disney</td>
<td>10.3</td>
<td>Glee</td>
<td>~$25</td>
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<tr>
<td>11</td>
<td>Victoria’s Secret (Limited Brands)</td>
<td>9.1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>12</td>
<td>Converse All Star</td>
<td>8.8</td>
<td></td>
<td></td>
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<tr>
<td>13</td>
<td>iTunes (Apple)</td>
<td>7.9</td>
<td></td>
<td></td>
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<tr>
<td>14</td>
<td>Windows Live Messenger (Microsoft)</td>
<td>7.6</td>
<td>Fringe</td>
<td></td>
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<tr>
<td>15</td>
<td>Pringles (P&amp;G)</td>
<td>6.7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>16</td>
<td>iPod (Apple)</td>
<td>6.6</td>
<td></td>
<td>~$20</td>
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<tr>
<td>17</td>
<td>ZARA</td>
<td>6.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18</td>
<td>NBA</td>
<td>6.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>19</td>
<td>Starburst (Mars)</td>
<td>5.9</td>
<td>Scrubs</td>
<td></td>
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<tr>
<td>20</td>
<td>Dr Pepper</td>
<td>5.8</td>
<td>Vampire Diaries</td>
<td></td>
</tr>
</tbody>
</table>

*Note: Facebook’s user figure reflects global unique visitors in 9/10, per comScore. Top 20 brand / product pages ranked by # of people who opted in to ‘like’ the page, excludes ‘people’ (like Vin Diesel / Lady Gaga) and ‘activities’ (like ‘I ♥ Sleep’). Data as of 11/10/10. *Equivalent TV shows based on # of total viewers during the 2009 – 2010 season. Source: Facebook, Nielsen Media Research, comScore.
Twitter’s 102MM Users (+74% Y/Y) Increasingly in Touch with Brands + Media Players

<table>
<thead>
<tr>
<th>Rank</th>
<th>Top 20 Brands</th>
<th># of Twitter Followers</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Oprah</td>
<td>4.5MM</td>
</tr>
<tr>
<td>2</td>
<td>CNN Breaking News</td>
<td>3.6MM</td>
</tr>
<tr>
<td>3</td>
<td>New York Times</td>
<td>2.7MM</td>
</tr>
<tr>
<td>4</td>
<td>Google</td>
<td>2.6MM</td>
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<tr>
<td>5</td>
<td>E! Online</td>
<td>2.5MM</td>
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<tr>
<td>6</td>
<td>The Onion</td>
<td>2.4MM</td>
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<td>7</td>
<td>People Magazine</td>
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<td>8</td>
<td>Time Magazine</td>
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<td>9</td>
<td>NBA</td>
<td>2.1MM</td>
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<td>10</td>
<td>Mashable</td>
<td>2.1MM</td>
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<tr>
<td>11</td>
<td>Martha Stewart</td>
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<td>12</td>
<td>Whole Foods</td>
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<td>13</td>
<td>NPR</td>
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<td>InStyle Magazine</td>
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<td>15</td>
<td>NFL</td>
<td>1.8MM</td>
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<tr>
<td>16</td>
<td>BBC Click</td>
<td>1.8MM</td>
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<tr>
<td>17</td>
<td>Zappos!</td>
<td>1.8MM</td>
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<tr>
<td>18</td>
<td>Good Morning America</td>
<td>1.7MM</td>
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<tr>
<td>19</td>
<td>Woot</td>
<td>1.6MM</td>
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<td>20</td>
<td>CBS News</td>
<td>1.6MM</td>
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</tbody>
</table>

Note: Twitter user figure reflects global unique visitors to Twitter.com in 9/10, per comScore. Top 20 brands ranked by # of followers, excludes celebrities like Ashton Kutcher and Britney Spears. Data as of 11/05/10. Source: TwitterCounter.com, comScore.
Online Ad CPM Dislocation?

Share of Total USA Online Display Ad Units + CPM, by Top Publisher Categories – 3/10

- Retail: 2% (CPM: $2.59)
- Business / Finance: 2% (CPM: $2.72)
- Lifestyles: 2% (CPM: $2.70)
- Online Gaming: 2% (CPM: $6.35)
- Sports: 3% (CPM: $5.63)
- News / Information: 8% (CPM: $4.53)
- eMail: 10% (CPM: $2.69)
- Entertainment: 11% (CPM: $0.89)
- Portals: 21% (CPM: $0.55)
- Social Networking: 27% (CPM: $0.00)

Source: comScore presentation “Insights into Online Display Advertising Growth” (6/10).
Where are the Great Online Ads?
Apple / Google / Yahoo! / Facebook / Twitter / Others Say ‘Watch This Space!’

AdAge Top 25 Advertising Campaigns in Twentieth Century

<table>
<thead>
<tr>
<th>Rank</th>
<th>Company</th>
<th>Commercial</th>
<th>Ad Agency</th>
<th>Year</th>
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<tbody>
<tr>
<td>1</td>
<td>Volkswagen</td>
<td><em>Think Small</em></td>
<td>Doyle Dane Bernbach</td>
<td>1959</td>
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<tr>
<td>2</td>
<td>Coca-Cola</td>
<td><em>The pause that refreshes</em></td>
<td>D'Arcy Co.</td>
<td>1929</td>
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<td>3</td>
<td>Marlboro</td>
<td><em>The Marlboro Man</em></td>
<td>Leo Burnett Co.</td>
<td>1955</td>
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<tr>
<td>4</td>
<td>Nike</td>
<td><em>Just do it</em></td>
<td>Wieden &amp; Kennedy</td>
<td>1988</td>
</tr>
<tr>
<td>5</td>
<td>McDonald’s</td>
<td><em>You deserve a break today</em></td>
<td>Needham, Harper &amp; Steers</td>
<td>1971</td>
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<td>6</td>
<td>DeBeers</td>
<td><em>A diamond is forever</em></td>
<td>N.W. Ayer &amp; Son</td>
<td>1948</td>
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<td>Absolut Vodka</td>
<td><em>The Absolut Bottle</em></td>
<td>TBWA</td>
<td>1981</td>
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<td>8</td>
<td>Miller Lite Beer</td>
<td><em>Tastes great, less filling</em></td>
<td>McCann-Erickson Worldwide</td>
<td>1974</td>
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<td>9</td>
<td>Clairol</td>
<td><em>Does she...or doesn’t she?</em></td>
<td>Foote, Cone &amp; Belding</td>
<td>1957</td>
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<td>10</td>
<td>Avis</td>
<td><em>We try harder</em></td>
<td>Doyle Dane Bernbach</td>
<td>1963</td>
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<tr>
<td>11</td>
<td>Federal Express</td>
<td><em>Fast talker</em></td>
<td>Ally &amp; Gargano</td>
<td>1982</td>
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<tr>
<td>12</td>
<td>Apple Computer</td>
<td>1984</td>
<td>Chiat/Day</td>
<td>1984</td>
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<tr>
<td>13</td>
<td>Alka-Seltzer</td>
<td>Various ads</td>
<td>Jack Tinker &amp; Partners; Doyle Dane Bernbach; Wells Rich, Greene</td>
<td>1960s, 1970s</td>
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<tr>
<td>14</td>
<td>Pepsi-Cola</td>
<td><em>Pepsi-Cola hits the spot</em></td>
<td>Newell-Emmett Co.</td>
<td>1940s</td>
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<td>15</td>
<td>Maxwell House</td>
<td><em>Good to the last drop</em></td>
<td>Ogilvy, Benson &amp; Mather</td>
<td>1959</td>
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<td>16</td>
<td>Ivory Soap</td>
<td><em>99 and 44/100% Pure</em></td>
<td>Proctor &amp; Gamble Co.</td>
<td>1882</td>
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<td>17</td>
<td>American Express</td>
<td><em>Do you know me?</em></td>
<td>Ogilvy &amp; Mather</td>
<td>1975</td>
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<tr>
<td>18</td>
<td>U.S. Army</td>
<td><em>Be all that you can be</em></td>
<td>N.W. Ayer &amp; Son</td>
<td>1981</td>
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<tr>
<td>19</td>
<td>Anacin</td>
<td><em>Fast, fast, fast relief</em></td>
<td>Ted Bates &amp; Co.</td>
<td>1952</td>
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<tr>
<td>21</td>
<td>Pepsi-Cola</td>
<td><em>The Pepsi generation</em></td>
<td>Batton, Barton, Durstine &amp; Osborn</td>
<td>1964</td>
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<tr>
<td>22</td>
<td>Hathaway Shirts</td>
<td><em>The man in the Hathaway shirt</em></td>
<td>Hewitt, Ogilvy, Benson &amp; Mather</td>
<td>1951</td>
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<tr>
<td>23</td>
<td>Burma-Shave</td>
<td><em>Roadside signs in verse</em></td>
<td>Allen Odell</td>
<td>1925</td>
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<tr>
<td>24</td>
<td>Burger King</td>
<td><em>Have it your way</em></td>
<td>BBDO</td>
<td>1973</td>
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<tr>
<td>25</td>
<td>Campbell Soup</td>
<td><em>Mmm mm good</em></td>
<td>BBDO</td>
<td>1930s</td>
</tr>
</tbody>
</table>

Source: Advertising Age.
5. Commerce

‘Wal-Mart in your pocket’…location-based services…group buying power…flash sales…deep discounts…transparent pricing…real-time alerts / ratings…virtual goods…immediate gratification…

Products must be fast + easy + fun.

Have you ever seen ‘constant improvement’ in products like we are seeing now?

Is your business keeping pace?

Do humans want everything to be like a game?

Morgan Stanley
Online Commerce Gaining Share vs. Offline – Online at ~5% of USA Retail, Mobile Should Get to Same Level Much Faster

USA eCommerce % Share\(^{(1)}\) of Total Retail Sales, CQ3:00 – CQ4:12E

Note: (1) Adjusted for eBay by adding back eBay US gross merchandise volume; Source: US Dept. of Commerce (CQ4:09), Morgan Stanley Research.

Morgan Stanley
Mobile Revolutionizing Commerce –
With Constant Product Improvements

- **Location-Based Services** – Enable real-time physical retail / service opportunities

- **Transparent Pricing** – Instant local + online price comparison could disrupt retailers

- **Discounts** – Invitation-only time-based selective sales gaining traction

- **Immediate Gratification** – OTA (over-the-air) instant digital product + content delivery

---

**Location-Based Services**
- Priceline.com iPhone App
- Finds hotel deals in your area

**Transparent Pricing**
- ShopSavvy Android App
- Comparison shopping among online + local stores

**Discounts**
- Gilt iPhone App
- Designer handbags Up to 70% Off

**Immediate Gratification**
- iTunes Store on iPhone
- Music / video / apps delivered wirelessly

Source: Company Reports, Morgan Stanley Research.
6. Media

What does the extraordinary ramp in on-demand video usage mean for your business?
Streaming Video Gaining Material Market Share of Internet / Mobile Usage

North America Downstream Fixed-Access Peak Hour* Traffic Share by Application, 9/10

- Other Traffic: 26%
- HTTP: 23%
- Netflix: 21%
- YouTube: 10%
- BitTorrent: 8%
- Flash Video: 6%
- RTMP: 6%

Downstream Traffic Share during Peak Hours, by Application (9/10)

Streaming Video Up to ~37% of Internet Traffic During Traditional “TV Hours”

North America Mobile Peak Hour* Traffic Share by Application, 9/10 vs. 1/10

- Mobile Video = 41% of Peak Hour Traffic, Up from 27% in January

Note: *Peak hours are the periods during which bandwidth utilization is heaviest. They typically occur in the evening and last 3-5 hours. (e.g., peak hours for Netflix = 8-10pm). RTMP stands for real-time messaging protocol (Instant messaging). Real-time entertainment represents streamed / buffered audio and video content. Source: Sandvine Fall 2010 Global Internet Phenomena Report, Morgan Stanley Research.
YouTube Content Growth Accelerating (+2x Y/Y) – 35 Hours of Content Added Every Minute

Source: YouTube blog, Morgan Stanley Research.
7. Internet Company Leadership Evolution

Shocking changes over just 6 years…
are you prepared for next half decade of change?
## Global Public Internet Companies – Significant Changes Over Last 6 Years

### Top Global 15 Publicly Traded Internet Companies by Market Value – 2010 vs. 2004

<table>
<thead>
<tr>
<th>Rank</th>
<th>Company</th>
<th>Region</th>
<th>Market Value ($B)</th>
<th>Revenue ($MM)</th>
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<td>JPN</td>
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</table>

**Total** | $809B | $126B | **Total** | $304B | $33B

### 2 of 2010 Top 15 Companies (Alibaba, Baidu) Went Public Post 2004

Morgan Stanley

8. Steve Jobs

What’s his ‘secret sauce’?

Does your company have it?
Steve Jobs – ‘…mind of an engineer and the heart of an artist…’

**Larry Ellison (June 2004):** Steve Jobs is the most brilliant person in our industry, and what is most remarkable about Steve, I think, is his incredible aesthetic sense. He has the mind of an engineer and the heart of an artist — that's a very unusual combination, an enormous advantage when you do consumer products. Look at the iPod...I think the iPod is a beautiful design and I think the iMac is a brilliant design. He's done a tremendous amount of innovation on the integration of hardware design and software design.

**Bill Gates (May 2007):** …We build the products that we want to use ourselves. And so he’s [Steve Jobs] really pursued that with incredible taste and elegance that has had a huge impact on the industry. And his ability to always come around and figure out where that next bet should be has been phenomenal. Apple literally was failing when Steve went back and re-infused the innovation and risk-taking that have been phenomenal.
9. **Ferocious Pace of Change - What’s Next in Tech?**

*When do consumers / enterprises & incumbents / attackers need you?*
Mobile Connectivity Drives New Ways to Do **LOTS** of Things Faster / Better / Cheaper from Palm of Hand

- **More Connected** – Real-time connectivity / 24x7 / in palm of hand…
- **More Affordable** – Wi-Fi nearly ubiquitous in many developed markets…for many / 3G tiered pricing lowers adoption barrier…
- **Faster** – Near-zero latency for boot-up / search / connect / pay…
- **Easier to Use** – User Interface revolution + location awareness provide something for nearly everyone…
- **Fun to Use** – Social / casual gaming / reward-driven marketing…
- **Access Nearly Everything** – Music / video / documents / ‘stuff’ in cloud…
- **Longer Battery Life** – Hours of continuous usage…

Morgan Stanley
Unusually High Level of Innovation - from Incumbents

- **Apple** – iPad / iPhone / iTouch / iTunes / Multi-Touch Input /
- **Google** – Android / Chrome / YouTube / Display Advertising / Web Apps / Instant + Voice Search
- **Amazon.com** – Kindle / EGM (Electronics & General Merchandise) Sales / Mobile Apps / AWS (Amazon Web Services)
- **Tencent** – Virtual Goods
- **Nintendo / Sony / Microsoft** – Motion Sensors (natural gaming input)
- **PayPal** – Mobile + Digital Goods Payments
- **Netflix** – Streaming Content
- **Salesforce.com** – Chatter (real-time enterprise collaboration platform)
Unusually High Level of Innovation - from New Attackers

- **Facebook** – Real-time Communication / Social Graph / Credits
- **Zynga** – Social Gaming / Virtual Goods / Offers (Reward-Driven Marketing)
- **Twitter** – One-to-Many Real-Time Broadcast
- **OpenTable / Yelp / Foursquare / Shopkick** – Location-Aware Mobile Services
- **Gilt / One Kings Lane / Rue La La** – Time-based ‘Flash’ Sales
- **Groupon** – Social Group Buying
- **Tapulous / Digital Chocolate / Booyah / Ngmoco:)** – Social / Mobile Gaming
- **Pandora / Spotify** – Personalized Music
Christensen studied why great companies with smart managements and substantial resources consistently lost to ‘disruptors,’ companies with simpler, cheaper, and inferior products. - Michael Mauboussin (7/10)

Two Ways Disruptive Innovation Can Happen

**Low-End Segment Strategy**
Disruptors introduce a product that is at the low end of the market and that is neither profitable for the incumbents nor in demand from the incumbents customers...

This becomes a problem as the disruptors improve their offering and move up market, eventually encroaching on the core business of the incumbent, and doing so with a lower cost structure.

*Amazon.com / Netflix / PayPal…*

**Non-Consumption Strategy**
Disruptors introduce a product that was unavailable to consumers before, effectively competing with non-consumption.

*iPhone / iPad / Facebook…*
10. Closing Thoughts –

Large companies do not typically support rapid growth rates of the magnitude that follow…

will these trends continue?
Global Public Internet Leaders –
Strong Q3 Trends…

1. **Apple ($283B market cap, $20.3B in CQ3 revenue)** - **Momentum continued as revenue grew 67% Y/Y** – iPhone units grew 91% Y/Y to 14MM, 4MM iPads shipped and Mac growth was a healthy 27% to 4MM. 80% / 65% of Fortune 500 companies have deployed (or are piloting) iPhones / iPads. User base of 50MM Macs; 61MM iPhones; 7.5MM iPads.

2. **Google ($193B, $7.3B)** - **Momentum accelerated as search quality improved and mobile usage growth extended reach:** Paid clicks up 16% Y/Y, cost-per-click up 3% Q/Q. New initiatives gaining traction: Display advertising and mobile at $2.5B and $1B gross revenue run rates. Android momentum continued to surprise on upside. Capex rose a hefty 59% Q/Q to $757MM as Google ramped investments in data centers / IT infrastructure. Base of 940MM average monthly unique users.

3. **Amazon.com ($74B, $7.6B)** - **Revenue growth remained very strong at 39% Y/Y** as EGM (electronics and general merchandise) powered up to 53% of revenue vs. slower growing media sales (+14% Y/Y). Operating margins compressed to 5.3% vs. 6.4% Y/Y owing to across-the-board investments in fulfillment (13 new fulfillment centers) / marketing / technology & content. Active customer growth remained robust (+23% Y/Y). Base of 121MM active customers.

*Note: Market cap data as of 11/12/10. Source: Company data, Factset, comScore (unique user data), Morgan Stanley Research.*
4. **Tencent ($41B, $797MM)** - Momentum continued as revenue rose 55% Y/Y, driven by IVAS (Internet Value Added Services) growth of +57% Y/Y (now ~79% of total sales) and MVAS (Mobile Value Added Services) growth of +56% Y/Y (13% of sales). Online game sales supplied the majority of IVAS growth (+67% Y/Y to 49% of total sales) as titles such as CrossFire and QQ Speed reached record usage levels (measured by concurrent users). Online ad revenue maintained healthy growth (+30% Y/Y) and continued to expand its advertiser base following the momentum gained during the World Cup in June and July. Base of 198MM average monthly unique users.

5. **eBay ($39B, $2.2B)** - PayPal payment volume rose a healthy 26% Y/Y while users grew 16% Y/Y to 91MM as merchant services (off-eBay) continued to grow at a strong rate (+40% Y/Y) and cross-border transactions maintained a healthy level of overall activity (24% of total transaction value). Marketplace sold items growth accelerated to 13% Y/Y as demand in international markets continued to pick up and the US / UK / Germany (eBay’s largest markets) benefited from a pricing change instituted in each market over the past year. Base of 222MM average unique monthly eBay users and 90.5MM active PayPal users.

6. **Baidu ($39B, $337MM)** - Paid search revenue growth accelerated to 76% Y/Y, as online advertising customers increased 26% Y/Y (to 272K, <1% of total SMEs in China, leaving room for ample upside) and advertiser ARPU rose 41% Y/Y as large corporate customers continued to increase their online marketing spend. Operating margin (56%) improved 2ppts Q/Q and 12ppts Y/Y, owing to pricing power vs. search advertising competitors and fixed-cost leverage over bandwidth and infrastructure costs. Base of 185MM average monthly unique users.

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**Note:** Market cap data as of 11/12/10.  
Source: Company data, Factset, comScore (unique user data), Morgan Stanley Research.
...Global Public Internet Leaders –
Strong Q3 Trends...

7. **Yahoo! ($22B, $1.6B)** - Display advertising revenue rose 17% Y/Y (from recession compressed levels) as ad targeting continued to improve while search-related revenue declined 7% Y/Y as the transition to Microsoft algorithmic search during the quarter impacted paid click volume. Turnaround remains on track, but bolstering user engagement on sites is key to fend off usage time erosion to the likes of Facebook. Outlook for Asian investments / assets remains compelling. Base of 616MM average monthly unique users.

8. **priceline.com ($20B, $1.02B)** - Gross bookings growth remained strong at 47% Y/Y and revenue growth continued to accelerate, reaching 37% Y/Y. International gross bookings, which increased 67% Y/Y (78% Y/Y on an FX-neutral basis), and hotel room nights (up 54% Y/Y) remained the two primary growth drivers for the company. Gross profit of $666MM (up 54% Y/Y, 67% margin) was driven primarily by international strength (international gross profit was $530MM, up 80% on an FX-neutral basis and represented 80% of total gross profit). Base of 23MM average monthly unique visitors.

9. **Alibaba.com ($10B, $219MM)** - Revenue growth remained strong at 40% Y/Y as international sales (outside China) grew 33% Y/Y (58% of total) and paying member growth continued (30% Y/Y to ~751K). Value-added services (such as keyword bidding, premium placement, and online translations) contributed 25%+ of China Gold Supplier sales and 20%+ of TrustPass revenue, up from mid-teens a year ago, and continue to improve the value proposition for suppliers. Base of 42MM average monthly unique users.

**Note:** Market cap data as of 11/12/10. 
Source: Company data, Factset, comScore (unique user data), Morgan Stanley Research.
10. **Akamai ($9B, $254MM)** - Revenue growth accelerated for the fourth straight quarter to 23% Y/Y as: 1) Media & Entertainment revenue (+26% Y/Y, 44% of total) posted strong numbers driven by increasing traffic volume from strengthening over-the-top video demand; and 2) eCommerce revenue (+24% Y/Y, 32% of total) also came in strong and should continue to grow as consumers shift retail spending online during the holiday season. Akamai’s continued investment in its unique network architecture position the company well to capitalize on the secular growth in online video, eCommerce, and cloud-based services.

11. **Netflix ($9B, $553MM)** - Very strong momentum as subscriber and revenue growth continued to accelerate – up 52% and 31% Y/Y, respectively…while subscriber acquisition cost and churn declined to their lowest levels in company history. We estimate subscriber level (at 17MM in CQ3) should surpass HBO’s USA subscriber base (MS forecast at ~30MM for YE C2012E) by CH1:12E. Netflix growth has been assisted by acceptance as a key video content source on Apple’s iPad and the company’s large and growing library of video content.

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**Note:** Market cap data as of 11/12/10.
Source: Company data, Factset, comScore (unique user data), Morgan Stanley Research.
Something You Should be Thinking About that May Not be Top of Mind
USA Federal Government – Entitlement Spending + Interest Expense are Forecast to Exceed Revenue by 2025, per Congressional Budget Office

Entitlement Spending + Interest Payments vs. Revenue as % of GDP, 1980 – 2050E

Source: Congressional Budget Office (CBO) Long-Term Budget Outlook (6/10). Note that entitlement spending includes federal government expenditures on Social Security, Medicare and Medicaid. Data in our chart is based on CBO’s ‘alternative fiscal scenario’ forecast, which assumes a continuation of today’s underlying fiscal policy. Note that CBO also maintains an ‘extended-baseline’ scenario, which adheres closely to current law. The alternative fiscal scenario deviates from CBO’s baseline because it incorporates some policy changes that are widely expected to occur (such as extending the 2001-2003 tax cuts rather than letting them expire as scheduled by current law and adjusting physician payment rates to be in line with the Medicare economic index rather than at lower scheduled rates) and that policymakers have regularly made in the past.
Near Term Good News
Consumers Expect to Celebrate the Holiday Season in 2010 ;)

Do You Plan to Celebrate a Major Winter Holiday This Year?

- 92% Yes, Plan to Celebrate
- 8% No, Do Not Plan to Celebrate

Note: Survey asked 8,767 respondents whether they planned to celebrate Christmas, Hanukkah, and/or Kwanzaa this year. Source: BIGresearch / National Retail Federation (NRF) Consumer Intentions & Actions Survey, 10/12/2010.
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Global Stock Ratings Distribution
(as of October 31, 2010)

For disclosure purposes only (in accordance with NASD and NYSE requirements), we include the category headings of Buy, Hold, and Sell alongside our ratings of Overweight, Equal-weight, Not-Rated and Underweight. Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, Not-Rated and Underweight are not the equivalent of buy, hold, and sell but represent recommended relative weightings (see definitions below). To satisfy regulatory requirements, we correspond Overweight, our most positive stock rating, with a buy recommendation; we correspond Equal-weight and Not-Rated to hold and Underweight to sell recommendations, respectively.

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Data include common stock and ADRs currently assigned ratings. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor’s existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months.
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Overweight (O). The stock's total return is expected to exceed the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
Equal-weight (E). The stock's total return is expected to be in line with the average total return of the analyst's industry (or industry team's) coverage universe, on a risk-adjusted basis, over the next 12-18 months.
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Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

Analyst Industry Views
Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.
In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.
Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.

Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index.

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