
INSIDE Q3 2023 CLOUD EARNINGS

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CONTEXT

The top three public cloud providers (Amazon, Microsoft, and Google) each released earnings last week. Let's look at the cloud-specific elements within each of their respective earnings to understand what that tells us about the state of the public cloud market.

AMAZON WEB SERVICES (AWS)

AWS reported a 12% year-over-year growth in Q3, with \$919 million in incremental quarter-over-quarter revenue. This revenue growth is among the highest in the industry.

Amazon highlighted the following during its earnings call:

- **Revenue Growth:** AWS reported \$23.1 billion in revenue for the third quarter, marking a 12% year-over-year growth. Despite its large size, AWS continues to experience substantial revenue growth.
- **Cost Optimization:** AWS customers are still optimizing their usage to improve price-performance. While cost optimization remains a factor, it's slowing down compared to previous quarters. Many customers are taking advantage of enhanced price-performance capabilities offered by AWS.
- **Investment in Generative AI:** Amazon is making significant investments in generative AI. This includes custom silicon development for training and inference with technologies like Trainium and Inferentia chips. These investments are aimed at improving the performance and efficiency of large language models (LLMs).
- **Collaborations:** AWS is collaborating with partners and companies in the generative AI space. A notable partnership is with Anthropic, a leading LLM maker, which chose AWS as its primary cloud provider. This collaboration aims to develop LLM technologies further.

- **Amazon Bedrock:** AWS introduced Amazon Bedrock, a service that provides access to LLMs from third-party providers like Anthropic, as well as Amazon's own LLMs called Titan. Bedrock allows customers to customize LLMs using their data while maintaining security and access control through a managed service.
- **Customer Adoption:** Amazon highlighted that many companies are rapidly adopting generative AI on AWS, including large enterprises like adidas, Booking.com, Bridgewater, Clariant, GoDaddy, LexisNexis, Merck, Royal Philips, and United Airlines. Additionally, AWS is seeing success with generative AI startups.
- **Future Growth:** AWS remains optimistic about its future growth, particularly in generative AI. The company believes that generative AI will become a significant source of revenue over the next several years and is focused on delivering value to customers in this rapidly evolving technology field.

Amazon president Andrew Jassy said in the earnings call that he remains optimistic about the medium and long-term prospects for AWS, citing its extensive functionality, large partner ecosystem, robust security, operational performance, and customer-focused approach. Amazon believes that as more IT spending shifts from on-premises to the cloud, there is significant growth potential for AWS.

Additionally, Amazon sees a substantial opportunity in generative AI for AWS, expecting the technology to generate tens of billions of dollars in revenue over the next few years. The company's unique and broad approach to generative AI, along with its fast-growing presence in this field, has contributed to its optimistic outlook and successful deal signings.

Overall, AWS is seeing a stabilization of its year-over-year growth rate and a notable reduction in customer optimization levels. The company attributes its optimism to its extensive functionality, robust partner ecosystem, security, customer-focused approach, and the ongoing shift of IT spending from on-premises to the cloud.

MICROSOFT AZURE

Microsoft Cloud revenue reached \$31.8 billion, growing by 24%, exceeding expectations. The gross margin percentage increased slightly year-over-year to 73%, primarily due to improvements in Azure. Company-wide gross margin dollars increased by 16%, with a gross margin percentage of 71%, partly driven by Azure and Office 365.

The discussion about Microsoft Cloud and Azure highlights the following key points:

- **Microsoft Cloud Revenue:** Microsoft reported robust performance in its cloud business, with Microsoft Cloud revenue surpassing \$31.8 billion, indicating a substantial 24% growth rate in the last quarter.

- **AI Integration:** Microsoft emphasized its strategic focus on artificial intelligence (AI), mentioning that they are rapidly integrating AI across their entire technology stack. The goal is to make AI accessible and practical for various roles and business processes, aiming to drive productivity improvements for their customers.
- **Azure's Strong Position:** Microsoft Azure, the company's cloud computing platform, is showcased as a standout performer. Azure continues to gain market share as more organizations migrate their workloads to the cloud.
- **Global Reach:** Microsoft highlighted the global footprint of Azure, with more than 60 data center regions worldwide. This extensive network allows them to provide cloud services to customers in various geographic locations.
- **AI Infrastructure:** Microsoft claimed to have the best AI infrastructure for both training and inference within Azure. This infrastructure supports AI workloads and applications, making it a competitive advantage for Microsoft in the cloud computing space.
- **AI Services Availability:** Microsoft Cloud offers access to a wide range of AI models, including frontier models from OpenAI, open-source models, and Microsoft's proprietary models. Customers can leverage these models to build their AI applications while meeting specific cost, latency, and performance requirements.
- **Azure Arc and Oracle Integration:** Microsoft mentioned the growing adoption of Azure Arc, a service that enables customers to run applications across on-premises, edge, and multi-cloud environments. Additionally, they highlighted being the only other cloud provider to run Oracle's database services, simplifying the migration of on-premises Oracle databases to Azure.
- **SAP Workloads:** Microsoft positioned Azure as the cloud of choice for running SAP workloads, with several notable companies such as Brother Industries, Hanes, Zeiss, and ZF Group running SAP on the Azure platform.

Microsoft expects Azure revenue growth to be around 26% to 27% in constant currency, with a growing contribution from AI. The Azure consumption business remains a key growth driver. The company anticipates stable Azure revenue growth for H2, assuming ongoing trends and increased contributions from AI.

In the on-premises server business, flat revenue growth is expected, driven by hybrid demand in multi-cloud environments, while Enterprise and Partner Services revenue may decline moderately.

Microsoft's Azure cloud platform continues to gain market share as more organizations migrate their workloads to the cloud. Azure boasts a comprehensive global cloud footprint with over 60 data center regions, making it one of the largest

cloud providers. It is also recognized for having a robust AI infrastructure for both training and inference.

GOOGLE CLOUD

In Q3, Google Cloud reported revenue of \$8.4 billion, a 22% increase; this is the slowest growth since at least the first quarter of 2021. This was slightly below Wall Street estimates of \$8.62 billion. Google Cloud's operating income for the quarter was \$266 million, with an operating margin of 3%.

Key points about Google Cloud from the provided text include:

- ❑ **Strong Growth:** Google Cloud reported robust growth in the third quarter, with revenues reaching \$8.4 billion, representing a 22% increase year-over-year.
- ❑ **Google Cloud Portfolio:** Google Cloud encompasses Google Cloud Platform (GCP) and Workspace collaboration tools, offering a comprehensive set of cloud services and productivity solutions.
- ❑ **AI Optimized Infrastructure:** Google Cloud provides advanced AI-optimized infrastructure that enables customers to train and deploy machine learning models at scale.
- ❑ **Vertex AI Platform:** The Vertex AI platform offers more than 100 AI models, including third-party and open-source options, allowing customers to build, deploy, and scale AI-powered applications.
- ❑ **Duet AI:** Google Cloud's Duet AI, powered by large foundation models, enhances productivity for users and is integrated into various cloud products and services.
- ❑ **Data Analysis:** Google Cloud is enabling companies to analyze both structured and unstructured data, providing a unified platform for data analysis.
- ❑ **Workspace Integration:** Duet AI is integrated into Google Workspace, offering content creation and refinement capabilities that benefit a range of companies, including Grupo Boticário, Unilever, and Warner Music.
- ❑ **Cybersecurity:** Google Cloud incorporates AI into its cybersecurity portfolio, offering generative AI-powered assistance in threat intelligence and security operations.
- ❑ **Profitable Growth:** Google Cloud is focused on profitable growth while maintaining a commitment to long-term investments in AI and technical infrastructure to support AI compute.
- ❑ **Customer Optimization:** The growth in Google Cloud revenue is partly attributed to customer optimization efforts, emphasizing cost management.

Like its public cloud competitors, Google also sees increased momentum coming from the current boom in AI infrastructure. Google Cloud offers advanced AI-optimized infrastructure to train and deploy models at scale, with over half of funded generative AI start-ups being its customers.

Google has also been steadily building its AI capabilities. Its Vertex AI platform, for example, helps customers build, deploy, and scale AI-powered applications, offering more than 100 models and tools for various use cases. The number of active generative AI projects on Vertex AI grew significantly from Q2 to Q3.

ANALYSIS

The key takeaway from the recent earnings reports of the top three public cloud providers, Amazon Web Services (AWS), Microsoft, and Google Cloud, is that the cloud market remains robust and continues to grow rapidly.

AWS, with a 12% year-over-year growth and a strong focus on generative AI, is maintaining its position as a revenue growth leader and anticipates significant potential in the cloud market's shift from on-premises to cloud-based solutions.

Microsoft's Azure platform is gaining market share and driving growth with a 24% increase in cloud revenue, highlighting the ongoing trend of cloud adoption.

Google Cloud, with a 22% increase in revenue, is making significant inroads into serving large enterprises, especially in the AI infrastructure sector, where it is attracting a growing number of generative AI start-ups. Despite the momentum, Google's cloud business is underperforming relative to its competitors while also failing to meet Wall Street expectations.

Overall, the public cloud market remains highly competitive, with each major player experiencing sustained growth and innovation. It's good to see cloud growth starting to rebound from

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