



August 9, 2022

Datadog, Inc.

Thoughts following our vNDR with management

Our view: While macro uncertainty clouds ST visibility, after a day of investor meetings, we remain bullish on the LT opportunity for Datadog to profitably consolidate share in a growing observability market. Investor's primary focus was on better trends in July and how conservative guidance is, and while management noted it's too early to extrapolate July, guidance assumes a healthy amount of conservatism based on slower trends in June. Maintain our OP rating and \$125 PT as we think DDOG remains on the short-list of disruptive ideas investors want to own in a recovery.

Key points:

What to make of improving trends in July: This was the A-topic as management noted that while they were pleased with improving customer commit/usage trends in July vs June, the macro environment remains "noisy" and "fuzzy". As such, they want to see the quarter play out before assuming one month creates a trend. The good news is that management sounded conservative in their guidance assumptions not embedding better July trends in 2H/22 expectations but rather assuming ST trends remain challenged. Regarding how this environment feels vs COVID, Q2/20 was marked by an abrupt slowdown by many of their customers while the Q2/22 slowdown was more gradual and primarily on larger customers within consumer discretionary including e-commerce and food delivery. That said, the company is coming off a quarter where they added a record 1.4K new logos (a reasonable amount self-serve) as management remains bullish on their LT opportunity to profitably consolidate observability share.

How we think about 2H/22 conservatism: Management noted ARR can be approximated by revenue * 34-36% * 12. With this math, the company exited Q2/22 with ARR of ~\$1,706M and ~\$181M of net-new ARR (+23% y/y) off a very difficult post-COVID comp. Q3/22 guidance implies net-new ARR of ~\$25M declining -84% y/y (note they did ~\$37M of net-new in Q2/20) while Q4/22 assumes net-new ARR of ~\$109M, down -53% y/y. Per guidance, the Q4/22 revenue exit growth rate is +34%, but using less conservative net-new ARR assumptions (but still negative growth) could point to a revenue exit rate in the mid-to-upper 40% with, in our view, the potential to accelerate in CY/23.

Other tidbits: 1) non-committed revenue is 20-25% of the total (portions of logs & APM) and while customers can become more efficient with logs & APM, they can't go too low given how mission critical DDOG is; 2) some customers' spend on observability is in the mid-to-high single digits as a % of cloud spend, while others are higher as we remain bullish on being tied to cloud spend; 3) their strong balance sheet and CF allows mgmt the optionality to invest and take advantage vs. competitors that pull back on spending; 4) regarding competition, it's not something management thinks about directly, but rather how to delight customers with new features / functionality; 5) mgmt remains bullish on infrastructure growth, APM and logging are ~\$750M in ARR and security continues to do very well.

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Outperform

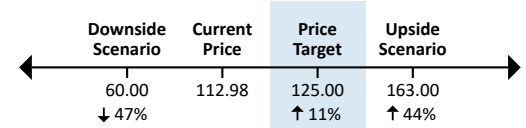
NASDAQ: DDOG; USD 112.98

Price Target USD 125.00

WHAT'S INSIDE

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Scenario Analysis*



*Implied Total Returns

Key Statistics

Shares O/S (MM):	351.6	Market Cap (MM):	39,724
Dividend:	0.00	Yield:	0.0%
		Avg. Daily Volume:	5,071,019

RBC Estimates

FY Dec	2020A	2021A	2022E	2023E
Revenue	603.5	1,028.8	1,619.2	2,186.0
EPS, Ops Diluted	0.22	0.49	0.78	1.11
P/E	NM	NM	NM	NM
	Q1	Q2	Q3	Q4
Revenue				
2021	198.5A	233.5A	270.5A	326.2A
2022	363.0A	406.1A	412.0E	438.0E
2023	478.0E	518.0E	570.0E	620.0E
EPS, Ops Diluted				
2021	0.06A	0.09A	0.13A	0.20A
2022	0.24A	0.24A	0.16E	0.13E
2023	0.25E	0.26E	0.29E	0.32E

All values in USD unless otherwise noted.

Priced as of prior trading day's market close, EST (unless otherwise noted).



Key fundamental questions

Our view

What makes Datadog unique vs peers?

The platform was built to break down the silos between development and operations (DevOps). Though starting in infrastructure monitoring, the platform is flexible enough to enable movement into natural adjacencies including APM, Logging, UX Monitoring, NPM, security, real-time business intelligence and/or ITSM.

How quickly is the competitive environment evolving?

Although many competing vendors started in a specific category, there is certainly convergence taking place, as we believe the competitive landscape is rapidly evolving and becoming increasingly competitive. That said, we believe the size of the market is large (could be \$35+ billion); we do not think it will be winner-take-all, and we realize there are several legacy vendors that are particularly vulnerable to share shift.

What does the expansion beyond observability look like?

We think one of the key items to watch is the ability to cross- and up-sell, as we think Datadog is well suited with early success from both Logging and APM. Last year, Security Monitoring and Compliance monitoring were announced, as the company has a vision of common tools across DevSecOps.



Key ESG questions

This section is intended to highlight key ESG discussion points relevant to this company, as well as our views on the outlook. Both the questions we highlight and our responses will evolve over time as the dialogue between management, analysts and investors continues to advance. We welcome any feedback on the topics.

What are the most material ESG issues facing this company?

Our view

Data privacy and security: As the threat landscape continues to evolve and increasingly sophisticated breaches come to light, adequate security controls at all levels of the software life cycle have become necessary to continue to retain and expand the customer base.

Energy consumption: While the software industry is not a particularly energy-intensive industry, its biggest source of energy consumption comes from the data centers, which account for ~1% of global electricity use.

Does the company integrate ESG considerations into its strategy?

While Datadog does not have a publicly disclosed ESG program, it has undertaken several initiatives over the years around diversity and inclusion including partnerships with Tech Ladies, She+ Geeks Out, and Lesbians Who Tech.

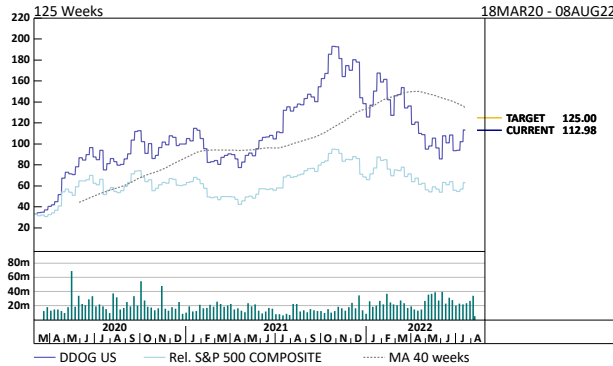
What is diversity like at the board/management level?

Management: 18% female, 82% male. Board of directors: 14% female, 86% male.



Target/Upside/Downside Scenarios

Datadog, Inc.



Source: Bloomberg and RBC Capital Markets estimates for Target

Valuation

We calculate our base-case price target of \$125 by applying a 20.7x multiple to our CY/23E revenue of \$2,186M. Our target multiple is above the expanded multiple of +40% growth SaaS peers, in our view warranted by a large and expanding TAM that leads to an attractive growth profile, as well as the opportunity for upside to growth expectations driven by maintained traction from the land-and-expand motion. Our price target supports our Outperform rating.

Upside scenario

Our upside scenario of \$163 is based on revenue growth 500 bps better each year vs. our base-case assumption. To reach this level of growth, we believe there would need to be some combination of higher cross-selling, better new customer additions, and a stable to better macro environment. We believe upside to revenue and margins could point to 25x CY/23E EV/S, or a premium to peers.

Downside scenario

Our downside scenario of \$60 is based on revenue growth 500 bps below each year vs. our base-case estimates. To reach this level of growth, we believe there would need to be a fall-off in tech spending, less success expanding into new customers, and lower renewal and expansion rates. Additionally, with a less attractive growth and margin profile, we believe the stock could receive a lower multiple. We believe downside to revenue and margins could point to 10x CY/23E EV/S, or a discount to peers.

Investment summary

On a mission to break down the traditional DevOps silos: Datadog was born in 2010 from a problem identified by its two co-founders, one of whom sat on the development side and the other on the operation side, and the realization that their teams could not understand complex systems the same way. The vision was to break down these silos and create an SaaS-based, real-time data integration platform. Today, the company has five complementary applications that leverage a common platform including Infrastructure Monitoring, APM, Logging, UX Monitoring, and NPM. We believe Datadog can continue to add incremental applications such as security, real-time business intelligence, and ITSM.

Potential growth catalysts

- The company has already seen strong adoption of Logging and APM within its Infrastructure Monitoring base of customers. Additional attach of these modules plus UX Monitoring and NPM could provide upside to estimates.
- The potential introduction of additional modules including security (SIEM), real-time business intelligence, and/or ITSM could provide upside to estimates.
- Additional customer penetration at the high end of the market.

Risks to rating and price target

- Operates in a market with competition from larger legacy competitors and new entrants.
- Business is dependent on ability to land new customers and retain and expand within the base.
- Will need to manage growth effectively to maintain customer satisfaction.
- COVID-19 could impact company operations or customer demand.



Company description

Datadog is a monitoring and analytics platform for developers, IT operations teams, and business users in the cloud age. Its SaaS platform integrates and automates infrastructure monitoring, application performance monitoring, and log management to provide unified, real-time observability of customers' entire technology stack. Datadog is used by organizations of all sizes and across a wide range of industries to enable digital transformation and cloud migration, drive collaboration among development, operations, and business teams, accelerate time to market for applications, reduce time to problem resolution, understand user behavior, and track key business metrics.

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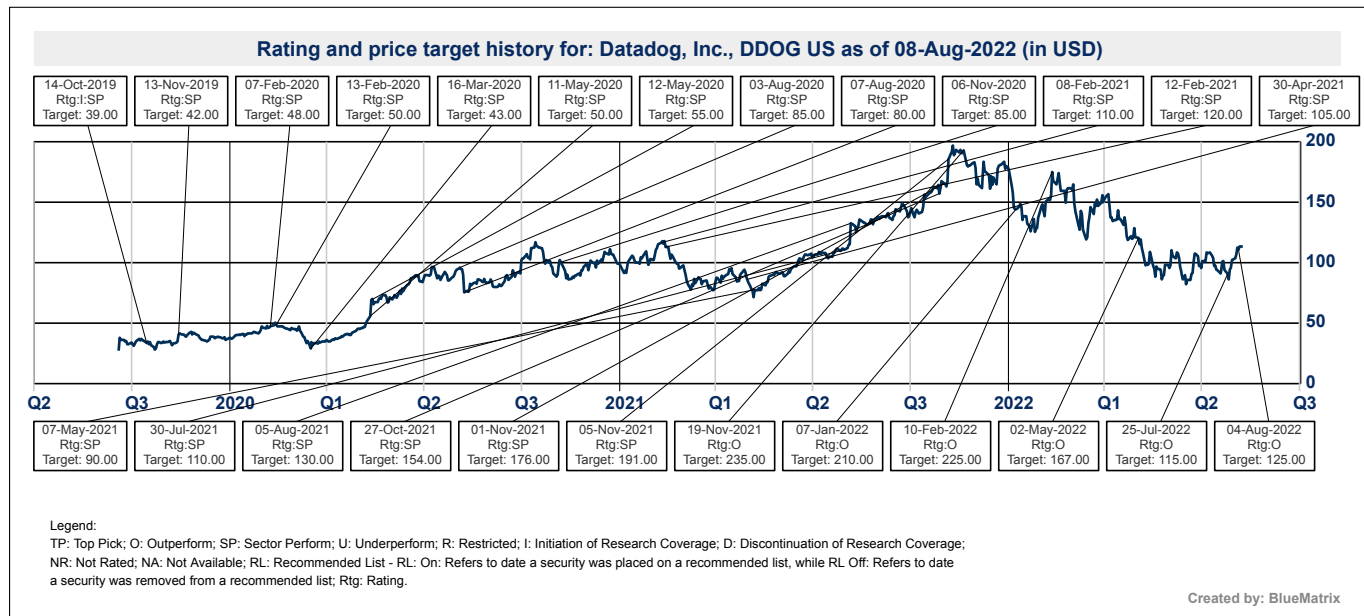
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			Serv./Past 12 Mos.	
			Count	Percent
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HOLD [Sector Perform]	560	38.44	169	30.18
SELL [Underperform]	46	3.16	6	13.04



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Datadog, Inc.

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