

GoPro: In The Early Stages Of A Beat And Raise Cycle

Consensus' expectation of a 10% growth in GoPro's action camera segment in the second half of the year (driven by the HERO5 launch) appears extremely conservative in light of similar refresh cycles undertaken by other tech companies. In our view, GoPro is likely to reach the high-end of its guidance (or even exceed it), pointing to at least 9% revenue upside.

GoPro's recent earnings were arguably encouraging as they pointed to improving ASPs (thanks to the elimination of entry-level products) and to a clean distribution channel ahead of the holiday season (inventory decreased 59% year-on-year and 36% quarter-on-quarter). But, in our view, the confirmation by management that the Karma drone would ship in time for the holiday season and that retailers' interest in the company's Karma and HERO5 products was strong was much more important.

While the stock has surged following the earnings report, we believe the rerating potential still remains significant as consensus expectations for the full year remain on the conservative side. The Street is currently standing at the low-end of GoPro's unchanged FY16 revenue guide (\$1.38bn compared to \$1.35-1.50bn) but reasonable assumptions suggest that the company could reach the high-end of its guidance or even exceed it (see our revenue model below).

First, we believe that the new drone business could bring in revenue in a \$60-120m range in the second half. According to various [sources](#), the consumer drone market should represent ~7m units in 2016 and toy/hobbyist drones should account for ~40% of the market. If we assume that Q4 accounts for 40% of these ~3m toy/hobbyist drone shipments and that GoPro grabs an initial 10% market share (or 20% in a more aggressive scenario), then the company could ship slightly more than 100K units (or 200K in the bull case) at an ASP we estimate around \$500-600.

Second, while many investors overlook the action camera business, we believe this segment should be a major source of upside in the second half of the year as GoPro refreshes its product lineup with the introduction of the HERO5. While there is traditionally no debate about a product refresh sparking revenue growth, there can be some discussions among investors about the extent of the revenue recovery.

If we assume that Karma will bring in \$60m revenue, then consensus expects the camera segment to grow 10% in the second half. This is an extremely cautious estimate in light of similar refresh cycles undertaken by other tech companies. Notably, we decided to look back at Apple's revenue numbers in [FY14 Q4](#) and [FY15 Q1](#) when the company started shipping the iPhone 6, which was arguably a major device upgrade. Over these two quarters, Apple recorded 43% revenue growth year-on-year in its iPhone segment.

Applying a similar growth rate to GoPro's action cameras revenue in the second half would lead to \$1,576m revenue for the segment in FY16 and \$1,636m revenue for the company, well above the high-end of GoPro's guidance and 19% above consensus.

GoPro Revenue Model: Bull Case (\$m)

	FY15 H2	FY16 H2	FY16
Action cameras	837	1'172	1'576
% growth	-	40%	-
Drones	0	60	60
Units ('000)	-	200	-
ASP (\$)	-	600	-
Revenue	837	1'232	1'636
Upside/downside vs. Consensus			19%

Source: AtonRâ Partners

Even a much more conservative scenario (25% growth in the camera business) would put GoPro slightly above the high-end of its guidance and 9% above consensus. Interestingly, 25% growth in the second half would be consistent with GoPro CEO's statement that the HERO5 will have "the most successful new camera launch in GoPro's history" as GoPro's segment revenue would be 14% above its FY14 H2 revenue (when the company shipped the HERO4). Once again, consensus appears way too conservative as it assumes almost no growth in FY16 H2 vs. FY14 H2.

GoPro Revenue Model: Base Case (\$m)

	FY15 H2	FY16 H2	FY16
Action cameras	837	1'046	1'450
% growth	-	25%	-
Drones	0	60	60
Units ('000)	-	100	-
ASP (\$)	-	600	-
Revenue	837	1'106	1'510
Upside/downside vs. Consensus			9%

Source: AtonRâ Partners

In conclusion, we believe that, after a couple of tough years, a beat & raise cycle is just around the corner for GoPro and remain Buyers of the stock.