

Adobe

OpenAI Sora Video Tool Threat is Overdone

Reiterate Rating: BUY | PO: 700.00 USD | Price: 549.98 USD

Sora addressing the emerging generative video category

Today, OpenAI launched a text-to-video model, dubbed Sora. The tool is being positioned as capable of developing detailed complex scenes for 'visual artists, designers and filmmakers.' At the same time, the company acknowledged that it's not perfect with regard to accuracy and look and feel. Nonetheless, Adobe's stock is trading down in the last two days on the news/pending.

A wide moat exists in Adobe's video business

While we do not dismiss competitive threats from OpenAI, (running the largest LLMs today) and other 3rd party models, we believe the reaction is overdone. Adobe's suite of video tools (consisting of Frame.io for video collaboration, Premiere for film editing and After Effects for sound effects) command a meaningful competitive moat over any open model in the core creative professional end of the market. The Adobe suite provides safeguards to prevent copyright infringement. This represents a real advantage over any open model (such as Sora), consuming public data sources which cannot provide that assurance to a creative professional, operating in an enterprise environment. We believe that Sora is a tool better suited for the consumer in social media use cases.

Adobe to unveil its own video model later this year

Sora does introduce competition in the consumer end of the market for Creative Cloud, though this segment is still an emerging opportunity for the business. 'Top of funnel' / consumer strength is a relatively new growth driver for Adobe Creative Cloud, since the launch of the entry level Creative Cloud Express offering in December 2021. Creative Cloud Suite remains the clear leader in Adobe's core creative professional segment, given the brand, breadth of offering (graphics, images, vector, video, etc.) and network effect amongst creative professionals (36 million CC subscribers in our model). We remain bullish on Adobe's ability to take share in the consumer segment (consisting hundreds of millions of users, versus tens of millions in the core creative professional), with Firefly (for text to image and vector graphic), Creative Cloud Express and eventually a generative film editing tool (to be launched later this year). The company unveiled robust generative video capabilities in beta at the Adobe Max conference in October 2022. Capabilities include but not limited to generative content, editing and multi language. We continue to view Adobe as a key AI beneficiary in the software group. Maintain Buy rating and \$700 PO.

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Equity

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Stock Data

Price	549.98 USD
Price Objective	700.00 USD
Date Established	14-Dec-2023
Investment Opinion	B-1-9
52-Week Range	318.60 USD - 638.25 USD
Mkt Val (mn) / Shares Out (mn)	250,406 USD / 455.3
Free Float	99.8%
Average Daily Value (mn)	1404.83 USD
BofA Ticker / Exchange	ADBE / NAS
Bloomberg / Reuters	ADBE US / ADBE.OQ
ROE (2024E)	45.2%
Net Dbt to Eqty (Nov-2023A)	-46.2%
ESGMeter™	High

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LLM: Large language model

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Timestamp: 16 February 2024 03:25PM EST

Price objective basis & risk

Adobe (ADBE)

Our PO of \$700 is based on an EV/FCF multiple of 31x our C25E free cash flow estimate. This represents 1.5x our 3-year mid-teens FCF CAGR, a premium to the large-cap GARP (growth at reasonable price) software group average of 1.3x. We view the premium as justified given Adobe's AI leadership position and durability of both top- and bottom-line growth.

Risks to our PO are 1) competition from point solutions and platform vendors, 2) application spending cyclicalities, and 3) future acquisitions, which could weigh on margin expansion.

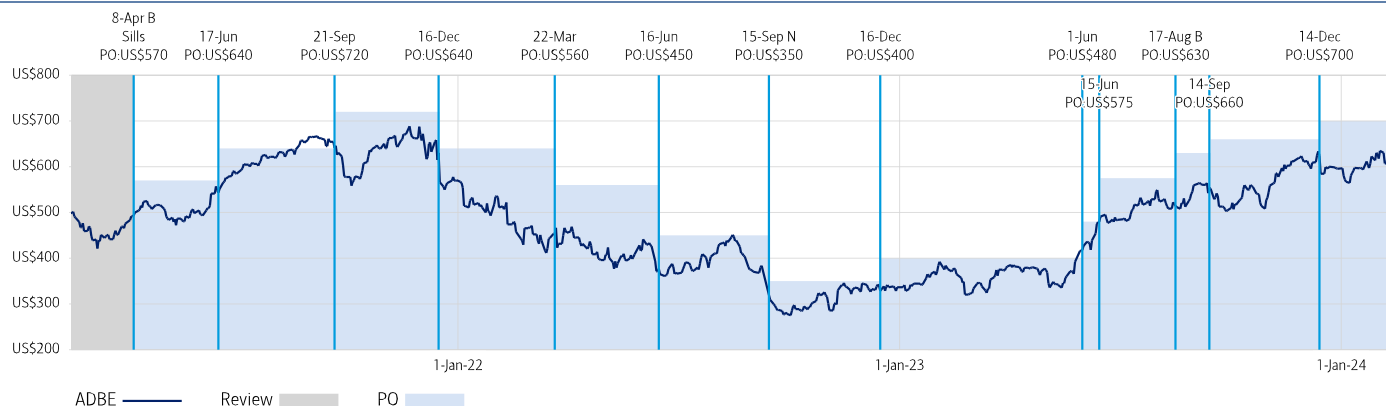
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Adobe (ADBE) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

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