

Palo Alto Networks

Battling off weak orders through discounting, bundling, and free offerings

Reiterate Rating: NEUTRAL | PO: 370.00 USD | Price: 366.09 USD

Billings weakness continues in 2Q24

2Q24 results reflected another weak billings quarter, with management flagging an environment of increased discounting, bundling, deferred payments and free deployment offerings. At the core, we note a challenging legacy firewall market, similar to trends reported by Fortinet, Check Point and Cisco. Management is aiming to offset the negative trends through bundling, but it also results in excessive discounting and pressure on growth, which is impacting Palo Alto Networks and the sector. Some products, like XDR, are seeing greater negative pricing impact; we believe SASE will also face similar negative trends, while other areas are seeing better trends, such as XSIAM. We believe the underlying secular trends remain solid, but management noted 18-24 months of pressure on billings, with weakness that will linger well into 2025. We reiterate our Neutral rating, reduce our estimates accordingly (see Financial Highlights), and reduce our PO from \$390 to \$370, now based on 12x CY25E EV/Sales (vs 14x prior to reflect the negative growth trends and pricing impacts).

Billings weakness translated into lower profit

Billings grew 15.7% vs. Street's 16.7%, with 3Q and 4Q guidance at 3% and 9.3% YoY growth vs. Street's 16.6% and 18.2%, respectively. Revenue is now expected to grow 14.2% and 10.4% YoY in 3Q and 4Q vs. Street's 18.5% and 17.3%, with EPS guided at \$1.25 and \$1.41, respectively, 5c and 13c below expectations. On the positive side, management expects FCF to remain on target, despite the impact on revenue and 4Q margins. We also flag the 50% ARR growth of Next Generation Security (NGS), reflecting Palo Alto's ability to upsell Cortex, XSIAM, Prisma Access and Prisma Cloud solutions.

What's driving the weakness; negative sector implications

We believe Palo Alto offers a solid NGS portfolio and the secular growth story has not changed. However, after three years of strong growth, the core business is slowing, and some markets are starting to commoditize. Bundling is both a positive and a negative, with Microsoft leading the pricing action and bringing to front the value of platformization. XDR, for example, is facing strong pricing pressure, yet CrowdStrike is able to offset it via upselling other modules and solutions. Palo Alto Networks is not different, carrying a strong portfolio of solutions, and reporting on 50% NGS ARR growth. Anecdotally, Zscaler is the one company that we flag for its long-term risks, with its offerings largely limited to SASE, an area of growing competition and pricing pressure.

Estimates (Jul) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	2.52	4.44	5.50	5.97	7.18
GAAP EPS	(0.88)	1.28	6.23	1.24	1.44
EPS Change (YoY)	22.9%	76.2%	23.9%	8.5%	20.3%
Consensus EPS (Bloomberg)			5.53	6.52	7.85
DPS	0	0	0	0	0
Valuation (Jul)					
P/E	145.3x	82.5x	66.6x	61.3x	51.0x
GAAP P/E	NM	286.0x	58.8x	295.2x	254.2x
EV / EBITDA*	86.4x	58.9x	47.4x	41.7x	35.1x
Free Cash Flow Yield*	1.6%	2.4%	2.8%	3.1%	3.7%

* For full definitions of *IQmethod*SM measures, see page 6.

21 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	390.00	370.00

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Stock Data

Price	366.09 USD
Price Objective	370.00 USD
Date Established	21-Feb-2024
Investment Opinion	B-2-9
52-Week Range	165.36 USD - 380.84 USD
Mrkt Val (mn) / Shares Out (mn)	109,388 USD / 298.8
Free Float	98.8%
Average Daily Value (mn)	1339.50 USD
BofA Ticker / Exchange	PANW / NYS
Bloomberg / Reuters	PANW US / PANW.OQ
ROE (2024E)	53.4%
Net Dbt to Eqty (Jul-2023A)	49.0%
ESGMeter TM	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

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Timestamp: 21 February 2024 01:00AM EST

iQprofileSM Palo Alto Networks

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	11.4%	15.8%	15.2%	12.8%	12.3%
Return on Equity	190.1%	147.1%	53.4%	32.4%	28.4%
Operating Margin	19.0%	24.1%	26.8%	27.3%	28.9%
Free Cash Flow	1,792	2,631	3,066	3,419	4,089

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	2.5x	1.9x	1.7x	1.7x	1.7x
Asset Replacement Ratio	0.7x	0.5x	0.5x	0.5x	1.7x
Tax Rate	22.0%	22.0%	22.0%	22.0%	22.0%
Net Debt-to-Equity Ratio	NM	49.0%	-16.4%	-55.4%	-79.2%
Interest Cover	NA	NA	NA	NA	NA

Income Statement Data (Jul)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	5,502	6,893	7,975	9,077	10,639
% Change	29.3%	25.3%	15.7%	13.8%	17.2%
Gross Profit	4,049	5,230	6,161	6,951	8,157
% Change	26.5%	29.2%	17.8%	12.8%	17.3%
EBITDA	1,325	1,942	2,416	2,744	3,264
% Change	24.7%	46.5%	24.4%	13.6%	18.9%
Net Interest & Other Income	(14)	186	306	253	275
Net Income (Adjusted)	803	1,440	1,903	2,131	2,611
% Change	30.8%	79.4%	32.1%	12.0%	22.5%

Free Cash Flow Data (Jul)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	803	1,440	1,903	2,131	2,611
Depreciation & Amortization	283	282	283	264	190
Change in Working Capital	521	563	(784)	901	1,383
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	379	492	1,820	247	225
Capital Expenditure	(193)	(146)	(154)	(124)	(319)
Free Cash Flow	1,792	2,631	3,066	3,419	4,089
% Change	29.2%	46.8%	16.5%	11.5%	19.6%
Share / Issue Repurchase	(756)	(14)	77	0	0
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	0	0	0	0	0

Balance Sheet Data (Jul)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	2,119	1,135	2,705	6,123	10,213
Trade Receivables	2,143	2,463	2,955	3,582	4,528
Other Current Assets	2,154	2,450	3,089	3,489	3,889
Property, Plant & Equipment	358	355	285	145	274
Other Non-Current Assets	5,481	8,099	10,407	11,105	11,864
Total Assets	12,254	14,501	19,439	24,444	30,768
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	4,630	5,746	6,287	7,410	8,889
Long-Term Debt	3,677	1,992	1,822	1,822	1,822
Other Non-Current Liabilities	3,737	5,015	5,947	7,451	9,459
Total Liabilities	12,044	12,753	14,055	16,683	20,170
Total Equity	210	1,748	5,384	7,762	10,598
Total Equity & Liabilities	12,254	14,501	19,439	24,444	30,768

* For full definitions of iQmethodSM measures, see page 6.

Company Sector

Data Networking

Company Description

Palo Alto Networks develops and sells network security solutions, ranging from solutions in appliance form factors to software and cloud based solutions.

Investment Rationale

Our Neutral is based on weakness in billings trends and shortening of duration, as customers are demanding greater discounts or shorter deal duration, driven by the weak macroenvironment. This suggests risk of further deterioration to billings, but also a possible negative impact on FCF generation and challenges to hit the LT growth targets. On the positive side, we favor PANW's technological and product leadership which should help to solidify Palo Alto as a cybersecurity leader longer-term.

Stock Data

Average Daily Volume 3,658,937

Quarterly Earnings Estimates

	2023	2024
Q1	0.83A	1.38A
Q2	1.05A	1.47A
Q3	1.10A	1.25E
Q4	1.44A	1.41E

Financial Highlights

Exhibit 1: Actual versus Estimated Results

2Q24 results were above BofA estimates

	Jan-23A	Apr-23A	Jul-23A	Oct-23A	Jan-24A				
					Reported	Prior BofA	Delta	QoQ	YoY
Next-Gen Security ARR	2,332,000	2,574,000	2,955,000	3,227,000	3,490,000	3,411,716	78,284	8.1%	49.7%
y/y	63.0%	60.2%	56.1%	52.9%	49.7%	46.3%			
Deferred Revenue	7,554,000	8,089,600	9,296,400	9,442,800	9,818,400	9,808,236	10,164	4.0%	30.0%
Total Billings	2,029,100	2,256,200	3,160,100	2,024,500	2,347,200	2,335,563	11,637	15.9%	15.7%
y/y	26.2%	25.6%	17.7%	15.8%	15.7%	15.1%			
Product	352,900	388,100	507,400	341,100	390,700	362,503	28,197	14.5%	10.7%
Services	1,302,200	1,332,800	1,445,900	1,537,000	1,584,400	1,607,624	(23,224)	3.1%	21.7%
Total Revenues	1,655,100	1,720,900	1,953,300	1,878,100	1,975,100	1,970,127	4,973	5.2%	19.3%
y/y	25.7%	24.1%	26.0%	20.1%	19.3%	19.0%			
Total Gross Profit (Non-GAAP)	1,249,100	1,310,200	1,509,300	1,465,800	1,540,500	1,507,147	33,353	5.1%	23.3%
Research & Development	270,100	281,400	294,500	285,600	302,000	305,592	(3,592)	5.7%	11.8%
Sales and Marketing	527,700	547,400	574,100	571,200	586,000	611,184	(25,184)	2.6%	11.0%
General and Admin	74,500	74,700	86,700	79,700	88,300	84,482	3,818	10.8%	18.5%
Total Operating Expenses (Non-GAAP)	872,300	903,500	955,300	936,500	976,300	1,001,258	(24,958)	4.2%	11.9%
Operating Income (Non-GAAP)	376,800	406,700	554,000	529,300	564,200	505,889	58,311	6.6%	49.7%
Total Other Income (Non-GAAP)	48,500	54,100	64,500	68,400	83,000	60,000	23,000	21.3%	71.1%
Pretax Income (Non-GAAP)	425,300	460,800	618,500	597,700	647,200	565,889	81,311	8.3%	52.2%
Non-GAAP Net Income Attr. to Common	331,700	359,400	482,500	466,300	504,700	441,586	63,114	8.2%	52.2%
Non-GAAP EPS	\$1.05	\$1.10	\$1.44	\$1.38	\$1.47	\$1.30	\$0.17	6.3%	39.7%
Weighted average diluted shares outstanding	316,400	325,400	335,200	338,200	344,500	340,500	4,000	1.9%	8.9%
Margin analysis:									
Product Gross Margin	72.5%	76.9%	80.1%	78.4%	78.3%	76.5%	180bps	-7bps	575bps
Services Gross Margin	76.3%	75.9%	76.3%	78.0%	77.9%	76.5%	142bps	-5bps	166bps
Total Gross Margin (Non-GAAP)	75.5%	76.1%	77.3%	78.0%	78.0%	76.5%	150bps	-5bps	253bps
Operating Margin (Non-GAAP)	22.8%	23.6%	28.4%	28.2%	28.6%	25.7%	289bps	38bps	580bps
Non-GAAP Net Margin	20.0%	20.9%	24.7%	24.8%	25.6%	22.4%	314bps	72bps	551bps
Non-GAAP Tax Rate	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	5bps	3bps	1bps

Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH

Exhibit 2: Summary of Model Changes

We fine-tune our estimates to be more streamlined with guidance

	Sales			Non-GAAP EPS			Billings			NGS ARR		
	Old	New	Delta	Old	New	Delta	Old	New	Delta	Old	New	Delta
FY24												
Q1	1,878,100	1,878,100	-	\$1.38	\$1.38	(0.00)	2,024,500	2,024,500	-	3,230,000	3,227,000	(3,000)
Q2E	1,970,127	1,975,100	4,973	\$1.30	\$1.47	0.17	2,335,563	2,350,700	15,137	3,411,716	3,490,000	78,284
Q3E	2,037,111	1,965,225	(71,887)	\$1.29	\$1.25	(0.04)	2,616,778	2,325,069	(291,709)	3,629,340	3,629,340	-
Q4E	2,291,750	2,156,834	(134,916)	\$1.54	\$1.41	(0.13)	3,727,358	3,453,237	(274,121)	4,001,070	3,975,066	(26,004)
Total	8,177,088	7,975,258	(201,830)	\$5.50	\$5.50	(0.00)	10,704,200	10,153,506	(550,694)	4,001,070	3,975,066	(26,004)
FY25												
Q1E	2,218,414	2,087,815	(130,599)	\$1.49	\$1.38	(0.11)	2,363,843	2,168,138	(195,706)	4,279,750	4,275,775	(3,975)
Q2E	2,327,116	2,190,118	(136,998)	\$1.54	\$1.42	(0.12)	2,756,801	2,551,789	(205,013)	4,486,407	4,582,025	95,618
Q3E	2,406,238	2,264,582	(141,656)	\$1.56	\$1.45	(0.12)	3,059,646	2,816,323	(243,323)	4,739,918	4,730,534	(9,384)
Q4E	2,692,581	2,534,067	(158,513)	\$1.86	\$1.73	(0.13)	4,333,221	3,984,140	(349,081)	5,181,386	5,144,194	(37,192)
Total	9,644,350	9,076,583	(567,767)	\$6.45	\$5.97	(0.48)	12,513,512	11,520,389	(993,123)	5,181,386	5,144,194	(37,192)
FY26												
Q1E	2,614,496	2,460,579	(153,916)	\$1.81	\$1.67	(0.13)	2,834,886	2,627,601	(207,285)	5,490,919	5,482,912	(8,007)
Q2E	2,732,148	2,571,306	(160,843)	\$1.85	\$1.71	(0.14)	3,222,788	3,007,955	(214,833)	5,706,709	5,829,423	122,714
Q3E	2,822,309	2,656,159	(166,150)	\$1.87	\$1.73	(0.14)	3,620,221	3,367,743	(252,478)	6,005,476	5,991,089	(14,387)
Q4E	3,135,585	2,950,992	(184,593)	\$2.20	\$2.06	(0.15)	5,037,655	4,702,869	(334,786)	6,476,732	6,433,465	(43,267)
Total	11,304,539	10,639,036	(665,503)	\$7.74	\$7.18	(0.56)	14,715,550	13,706,168	(1,009,382)	6,476,732	6,433,465	(43,267)

Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH



Exhibit 3: Income Statement

Updated summary of financials; we reduce our FY24 revenue estimate to \$7,975.3mn

	FY2023				FY2024E				FY2025E				FY2026E								
Fiscal Year Ends in July (in Thousands except EPS)	Q1 Oct-22	Q2 Jan-23	Q3 Apr-23	Q4 Jul-23	Q1 Oct-23	Q2 Jan-24	Q3 Apr-24	Q4 Jul-24	Q1 Oct-24	Q2 Jan-25	Q3 Apr-25	Q4 Jul-25	Q1 Oct-25	Q2 Jan-26	Q3 Apr-26	Q4 Jul-26	FY2022	FY2023	FY2024E	FY2025E	FY2026E
Product	330,000	352,900	388,100	507,400	341,100	390,700	381,254	480,974	331,963	356,989	384,979	499,211	339,560	365,125	393,111	507,571	1,363,100	1,578,400	1,594,028	1,573,142	1,605,368
Services	1,233,400	1,302,200	1,332,800	1,445,900	1,537,000	1,584,400	1,583,971	1,675,860	1,755,853	1,833,129	1,879,603	2,034,856	2,121,020	2,206,180	2,263,047	2,443,422	4,138,400	5,314,300	6,381,231	7,503,441	9,033,668
Total Revenues	1,563,400	1,655,100	1,720,900	1,953,300	1,878,100	1,975,100	1,965,225	2,156,834	2,087,815	2,190,118	2,264,582	2,534,067	2,460,579	2,571,306	2,656,159	2,950,992	5,501,500	6,892,700	7,975,258	9,076,583	10,639,036
YoY Growth	25.3%	25.7%	24.1%	26.0%	20.1%	19.3%	14.2%	10.4%	11.2%	10.9%	15.2%	17.5%	17.9%	17.4%	17.3%	16.5%	29.3%	25.3%	15.7%	13.8%	17.2%
Cost of sales (Non-GAAP)	401,700	406,000	410,700	444,000	412,300	434,600	463,412	503,985	482,853	515,749	535,551	591,436	566,952	604,637	625,281	685,645	1,452,500	1,662,400	1,814,297	2,125,589	2,482,516
Total Gross Profit (Non-GAAP)	1,161,700	1,249,100	1,310,200	1,509,300	1,465,800	1,540,500	1,501,813	1,652,849	1,604,962	1,674,369	1,729,031	1,942,631	1,893,628	1,966,668	2,030,878	2,265,347	4,049,000	5,230,300	6,160,961	6,950,994	8,156,520
Total Gross Margin (Non-GAAP)	74.3%	75.5%	76.1%	77.3%	78.0%	78.0%	76.4%	76.6%	76.9%	76.5%	76.4%	76.7%	77.0%	76.5%	76.5%	76.8%	73.6%	75.9%	77.3%	76.6%	76.7%
Research & Development	251,400	270,100	281,400	294,500	285,600	302,000	323,140	355,454	334,127	350,833	361,358	390,267	378,559	397,487	417,361	450,750	926,300	1,097,400	1,266,194	1,436,585	1,644,156
Sales and Marketing	518,800	527,700	547,400	574,100	571,200	586,000	597,720	649,124	610,176	640,685	666,313	712,955	698,696	726,643	755,709	793,495	1,805,900	2,168,000	2,404,044	2,630,129	2,974,542
General and Admin	69,100	74,500	74,700	86,700	79,700	88,300	90,949	98,225	93,314	98,912	102,869	109,041	106,860	112,203	117,813	127,239	274,000	305,000	357,174	404,136	464,116
Total Operating Expenses (Non-GAAP)	839,300	872,300	903,500	955,300	936,500	976,300	1,011,809	1,102,803	1,037,617	1,090,431	1,130,540	1,212,262	1,184,115	1,236,333	1,290,884	1,371,483	3,006,200	3,570,400	4,027,412	4,470,850	5,082,814
Operating Income (Non-GAAP)	322,400	376,800	406,700	554,000	529,300	564,200	490,004	550,046	567,345	583,939	598,491	730,369	709,513	730,335	739,994	893,864	1,042,800	1,659,900	2,133,550	2,480,144	3,073,706
Operating Margin (Non-GAAP)	20.6%	22.8%	23.6%	28.4%	28.2%	28.6%	24.9%	25.5%	27.2%	26.7%	26.4%	28.8%	28.8%	28.4%	27.9%	30.3%	19.0%	24.1%	26.8%	27.3%	28.9%
Total Other Income (Non-GAAP)	19,200	48,500	54,100	64,500	68,400	83,000	70,000	85,000	60,000	63,000	64,500	65,500	65,300	67,300	70,000	72,500	(13,900)	186,300	306,400	253,000	275,100
Non-GAAP Income Tax Expense / (Benefit)	75,200	93,600	101,400	136,000	131,400	142,500	123,301	139,824	138,128	142,442	145,977	175,234	170,598	175,623	178,344	212,773	226,400	406,200	537,025	601,781	737,338
Non-GAAP Net Income Attributable to Common	266,400	331,700	359,400	482,500	466,300	504,700	436,703	495,222	489,217	504,496	517,014	620,635	604,215	622,012	631,650	753,591	802,500	1,440,000	1,902,924	2,131,362	2,611,468
Non-GAAP EPS	\$0.83	\$1.05	\$1.10	\$1.44	\$1.38	\$1.47	\$1.25	\$1.41	\$1.38	\$1.42	\$1.45	\$1.73	\$1.67	\$1.71	\$1.73	\$2.06	\$2.52	\$4.44	\$5.50	\$5.97	\$7.18
GAAP EPS	\$0.06	\$0.25	\$0.31	\$0.64	\$0.56	\$0.89	\$0.24	\$0.46	\$0.50	(\$0.13)	\$0.24	\$0.63	\$0.60	(\$0.16)	\$0.27	\$0.73	(\$0.88)	\$1.28	\$6.23	\$1.24	\$1.44
Diluted share count	320,600	316,400	325,400	335,200	338,200	344,500	349,000	352,300	353,815	355,796	357,718	359,757	360,944	362,712	364,635	366,421	318,300	324,400	346,000	356,771	363,678
Operating Cash Flow	1,236,700	694,600	432,100	414,100	1,526,000	690,000	494,390	510,305	1,462,808	755,393	611,987	712,753	1,777,047	931,448	841,809	858,337	1,984,700	2,777,500	3,220,695	3,542,941	4,408,641
OCF Margin	79.1%	42.0%	25.1%	21.2%	81.3%	34.9%	25.2%	23.7%	70.1%	34.5%	27.0%	28.1%	72.2%	36.2%	31.7%	29.1%	36.1%	40.3%	40.4%	39.0%	41.4%
Free Cash Flow	1,197,100	656,300	400,900	376,900	1,489,200	654,800	455,085	467,168	1,421,052	720,351	584,812	692,481	1,703,230	854,309	762,124	769,807	1,791,900	2,631,200	3,066,253	3,418,696	4,089,470
FCF Margin	77%	40%	23%	19%	79%	33%	23%	22%	68%	33%	26%	27%	69%	33%	29%	26%	32.6%	38.2%	38.4%	37.7%	38.4%
Cash and cash equivalent	5,898,400	6,167,500	6,668,000	5,437,900	6,882,700	6,990,600	7,445,685	7,912,853	9,333,905	10,054,257	10,639,068	11,331,549	13,034,778	13,889,088	14,651,212	15,421,019	4,686,400	5,437,900	7,912,853	11,331,549	15,421,019
Total debt	3,678,600	3,680,300	3,682,100	1,991,500	1,946,700	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	1,821,800	3,676,800	1,991,500	1,821,800	1,821,800	1,821,800
Net cash	2,219,800	2,487,200	2,985,900	3,446,400	4,936,000	5,168,800	5,623,885	6,091,053	7,512,105	8,232,457	8,817,268	9,509,749	11,212,978	12,067,288	12,829,412	13,599,219	1,009,600	3,446,400	6,091,053	9,509,749	13,599,219
Margin Analysis																					
Total Gross Margin (Non-GAAP)	74.3%	75.5%	76.1%	77.3%	78.0%	78.0%	76.4%	76.6%	76.9%	76.5%	76.4%	76.7%	77.0%	76.5%	76.5%	76.8%	73.6%	75.9%	77.3%	76.6%	76.7%
R&D	16.1%	16.3%	16.4%	15.1%	15.2%	15.3%	16.4%	16.5%	16.0%	16.0%	16.0%	15.4%	15.4%	15.5%	15.7%	15.3%	16.8%	15.9%	15.9%	15.8%	15.5%
S&M	33.2%	31.9%	31.8%	29.4%	30.4%	29.7%	30.4%	30.1%	29.2%	29.3%	29.4%	28.1%	28.4%	28.3%	28.5%	26.9%	32.8%	31.5%	30.1%	29.0%	28.0%
G&A	4.4%	4.5%	4.3%	4.4%	4.2%	4.5%	4.6%	4.6%	4.5%	4.5%	4.5%	4.3%	4.3%	4.4%	4.4%	4.3%	5.0%	4.4%	4.5%	4.5%	4.4%
Total Operating Expenses (Non-GAAP)	53.7%	52.7%	52.5%	48.9%	49.9%	49.4%	51.5%	51.1%	49.7%	49.8%	49.9%	47.8%	48.1%	48.1%	48.6%	46.5%	54.6%	51.8%	50.5%	49.3%	47.8%
Operating Margin (Non-GAAP)	20.6%	22.8%	23.6%	28.4%	28.2%	28.6%	24.9%	25.5%	27.2%	26.7%	26.4%	28.8%	28.8%	28.4%	27.9%	30.3%	19.0%	24.1%	26.8%	27.3%	28.9%
Non-GAAP Tax Rate	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%	22.0%
Net Income (Non-GAAP)	17.0%	20.0%	20.9%	24.7%	24.8%	25.6%	22.2%	23.0%	23.4%	23.0%	22.8%	24.5%	24.6%	24.2%	23.8%	25.5%	14.6%	20.9%	23.9%	23.5%	24.5%
YoY % Growth																					
Product	11.7%	14.6%	10.4%	24.3%	3.4%	10.7%	-1.8%	-5.2%	-2.7%	-8.6%	1.0%	3.8%	2.3%	2.3%	2.1%	1.7%	21.7%	15.8%	1.0%	-1.3%	2.0%
Services	29.6%	29.1%	28.7%	26.6%	24.6%	21.7%	18.8%	15.9%	14.2%	15.7%	18.7%	21.4%	20.8%	20.4%	20.4%	20.1%	32.0%	28.4%	20.1%	17.6%	20.4%
Total Revenues	25.3%	25.7%	24.1%	26.0%	20.1%	19.3%	14.2%	10.4%	11.2%	10.9%	15.2%	17.5%	17.9%	17.4%	17.3%	16.5%	29.3%	25.3%	15.7%	13.8%	17.2%
Total Opex (Non-GAAP)	19.2%	19.1%	19.3%	17.6%	11.6%	11.9%	12.0%	15.4%	10.8%	11.7%	11.7%	9.9%	14.1%	13.4%	14.2%	13.1%	25.3%	18.8%	12.8%	11.0%	13.7%
Operating Income (Non-GAAP)	43.9%	55.3%	60.8%	71.4%	64.2%	49.7%	20.5%	-0.7%	7.2%	3.5%	22.1%	32.8%	25.1%	25.1%	23.6%	22.4%	30.0%	59.2%	28.5%	16.2%	23.9%
EPS (non-GAAP)	52.1%	80.7%	85.0%	80.8%	65.9%	39.7%	13.3%	-2.3%	0.3%	-3.2%	15.5%	22.7%	21.1%	20.9%	19.9%	19.2%	23.2%	76.1%	23.9%	8.6%	20.2%
QoQ % Growth																					
Product	-19.1%	6.9%	10.0%	30.7%	-32.8%	14.5%	-2.4%	26.2%	-31.0%	7.5%	7.8%	29.7%	-32.0%	7.5%	7.7%	29.1%					
Services	8.0%	5.6%	2.3%	8.5%	6.3%	3.1%	0.0%	5.8%	4.8%	4.4%	2.5%	8.3%	4.2%	4.0%	2.6%	8.0%					
Total Revenues	0.8%	5.9%	4.0%	13.5%	-3.8%	5.2%	-0.5%	9.7%	-3.2%	4.9%	3.4%	11.9%	-2.9%	4.5%	3.3%	11.1%					
Total OPEX (Non-GAAP)	3.3%	3.9%	3.6%	5.7%	-2.0%	4.2%	3.6%	9.0%	-5.9%	5.1%	3.7%	7.2%	-2.3%	4.4%	4.4%	6.2%					
Operating Income (Non-GAAP)	-0.2%	16.9%	7.9%	36.2%	-4.5%	6.6%	-13.2%	12.3%	3.1%	2.9%	2.5%	22.0%	-2.9%	2.9%	1.3%	20.8%					
EPS (non-GAAP)	4.4%	26.2%	5.4%	30.3%	-4.2%	6.3%	-14.6%	12.3%	-1.6%	2.5%	1.9%	19.4%	-3.0%	2.4%	1.0%	18.7%					

Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH



Price objective basis & risk

Palo Alto Networks (PANW)

Our price objective of \$370 is based on roughly 12x CY25E EV/Sales, which is above the high-end range of appliance companies, which trade at roughly 6-8x 2025E EV/Sales. The migration to Software and Cloud warrants a higher valuation, in our view, with successful SaaS vendors trading at 12-16x forward revenues.

Downside risks to our PO are increased competition and execution-related challenges as the company transitions to the cloud and SASE models.

Analyst Certification

I, Tal Liani, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Telecom and Data Networking Equipment Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Akamai	AKAM	AKAM US	Madeline Brooks
	Amdocs	DOX	DOX US	Tal Liani
	Arista Networks	ANET	ANET US	Tal Liani
	Cellebrite	CLBT	CLBT US	Tomer Zilberman
	Check Point Software Technologies	CHKP	CHKP US	Tal Liani
	Ciena	CIEN	CIEN US	Tal Liani
	CrowdStrike Holdings Inc.	CRWD	CRWD US	Tal Liani
	CyberArk	CYBR	CYBR US	Tal Liani
	Fastly	FSLY	FSLY US	Madeline Brooks
	Fortinet	FTNT	FTNT US	Tal Liani
	Gen Digital, Inc.	GEN	GEN US	Jonathan Eisenson
	InterDigital, Inc.	IDCC	IDCC US	Tal Liani
	Motorola Solutions	MSI	MSI US	Tomer Zilberman
	Qualcomm	QCOM	QCOM US	Tal Liani
	SentinelOne, Inc.	S	S US	Tal Liani
	Zscaler	ZS	ZS US	Tal Liani
NEUTRAL				
	Cisco Systems	CSCO	CSCO US	Tal Liani
	Palo Alto Networks	PANW	PANW US	Tal Liani
UNDERPERFORM				
	Cloudflare	NET	NET US	Madeline Brooks
	CommScope	COMM	COMM US	Tal Liani
	F5 Inc	FFIV	FFIV US	Tal Liani
	Okta Inc	OKTA	OKTA US	Madeline Brooks
	SecureWorks	SCWX	SCWX US	Tal Liani

iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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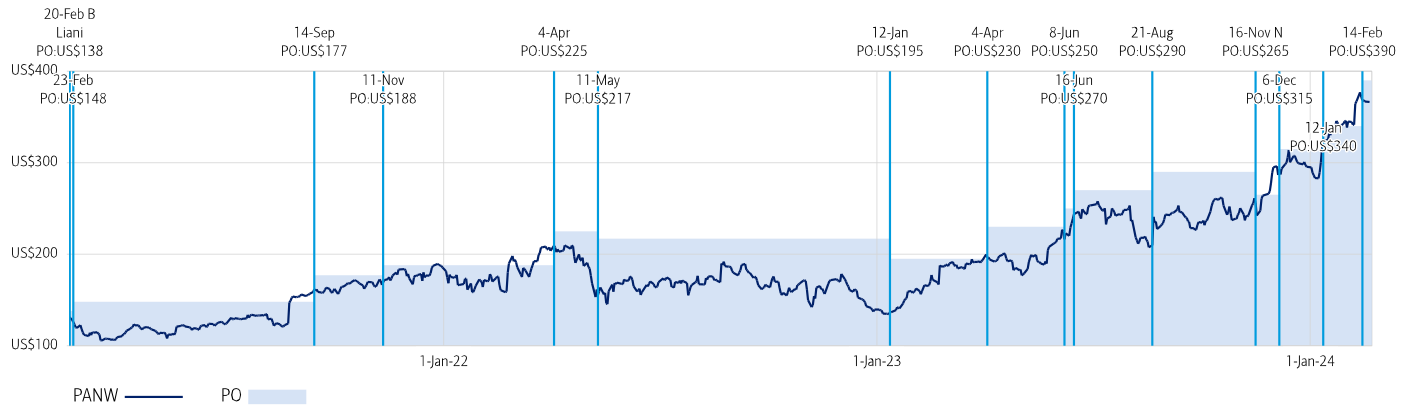
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Disclosures

Important Disclosures

Palo Alto Networks (PANW) Price Chart



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

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Telecommunications Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	57	51.82%	Buy	43	75.44%
Hold	27	24.55%	Hold	17	62.96%
Sell	26	23.64%	Sell	12	46.15%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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