

Equity Research

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Software and Cloud Technology

Salesforce.com, Inc.

Making It Look Easy

Salesforce reported excellent F1Q17 results and bumped up guidance for the third straight quarter. Billings and revenues came in ahead of consensus, with strong results across all geos and clouds. Off-balance sheet deferred grew 26% y/y. Sales Cloud (+14.5% y/y) continues to show nice growth even as it passes a \$3.3B run rate while momentum in digital transformation initiatives is starting to contribute to overall growth (Marketing Cloud +32% y/y ex-Demandware). Salesforce should easily march past \$10B in revenue this year and at this rate the road to \$20B looks pretty clear. CRM should continue to be a core holding.

CRM

\$87.75

12 month target

\$100.00

BUY

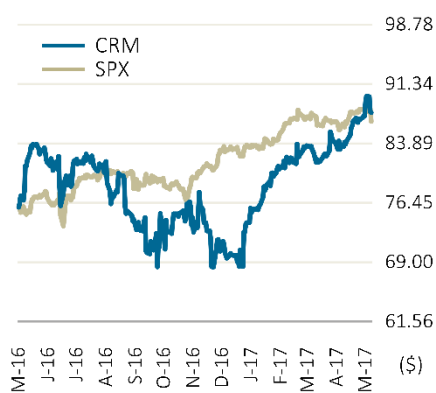
52 week range

\$68.41 - \$89.80

Market Cap (m)

\$63,316

Price Performance



Source: IDC

► **Excellent results.** Revenues of \$2.39B ahead of cons. \$2.35B while FY outlook gets a \$100M boost. Billings (+16% y/y) ahead of cons. (7%) on a tough compare due to increasing (but well understood) seasonality in the business. Management visibility sounds very good, supported by deferred revenue strength with total deferred plus backlog now standing at \$14B. Operating cash flow of \$1.2B was a record and higher than all of F16. Operating margin expansion continues at a balanced rate (125-150 bps this FY), driving nice cash flow growth (+20-21% y/y in F18 re-affirmed).

► **Sum is more than the parts.** A rare case of the sum being more than the parts, Salesforce continues to deliver on its broadening platform strategy. Ongoing strength in its core CRM product augmented by high growth in marketing, platform, and service, driving plenty of upsell opportunities, including the new Einstein AI engine. Along with increasing contribution from recent acquisitions, we are comfortable that the product portfolio can drive low- to mid-20s growth on a consolidated basis, which give us clear line of sight to \$20B. A rare achievement.

► **Valuation:** Numbers change little, aside from shifting some expenses from F3Q to F4Q to reflect Dreamforce conference later in the year. Our 10-year DCF analysis yields a \$100 price target. This implies 7x EV/FY18E Revenues and 36x EV/FY18E FCF. Maintain Buy.

Estimates

	1Q17 A	2Q17 A	3Q17 A	4Q17 A	FY17 A	1Q18 A	2Q18 E	3Q18 E	4Q18 E	FY18 E	FY19 E
Sales	1,917	2,037	2,145	2,294	8,392	2,388	2,514	2,605	2,773	10,279	12,351
Diluted EPS (Adj.)	0.24	0.24	0.25	0.28	1.01	0.28	0.31	0.35	0.34	1.28	1.67
FCF	968	155	14	562	1,698	1,073	336	(10)	676	2,075	2,213
EV/Sales (x)	-	-	-	-	7.37	-	-	-	-	6.02	5.01
P/FCF (x)	-	-	-	-	35.95	-	-	-	-	30.92	29.60

Source: BTIG Estimates and Company Documents (\$ in millions, except per share amount)

Adjusted EPS excludes stock-based comp and amortization and acquisition related costs.

Please Read: Important disclosures and analyst's certification appear in Appendix

Salesforce.com, Inc. Income Statement

Salesforce Income Statement (\$ in millions, except per share)	FY15 A	FY16 A	Apr-16 1Q17 A	Jul-16 2Q17 A	Oct-16 3Q17 A	Jan-17 4Q17 A	FY17 A	Apr-17 1Q18 A	Jul-17 2Q18 E	Oct-17 3Q18 E	Jan-18 4Q18 E	FY18 E	FY19 E
Non-GAAP Income Statement													
Subscription and Support	\$5,013.8	\$6,205.6	\$1,775.5	\$1,886.1	\$1,984.0	\$2,110.7	\$7,756.2	\$2,200.9	\$2,319.9	\$2,400.6	\$2,543.3	\$9,464.7	\$11,357.7
Professional Services and other	359.8	461.6	141.1	150.5	160.8	183.3	635.8	186.7	194.2	204.2	229.2	814.2	993.4
Total net revenues	5,373.6	6,667.2	1,916.6	2,036.6	2,144.8	2,294.0	8,392.0	2,387.6	2,514.1	2,604.8	2,772.5	10,279.0	12,351.1
Subscription and Support	780.5	1,038.6	287.0	311.9	347.9	374.5	1,321.2	387.8	383.6	420.9	451.2	1,643.6	1,983.7
Professional Services and other	364.6	465.6	161.2	164.6	174.2	177.7	677.7	187.6	198.1	208.3	233.8	827.8	1,013.2
Non-GAAP cost of revenues	1,145.2	1,504.2	448.1	476.5	522.0	552.2	1,998.9	575.5	581.7	629.2	685.0	2,471.4	2,997.0
Non-GAAP Gross Profit	4,228.4	5,163.0	1,468.5	1,560.1	1,622.7	1,741.8	6,393.1	1,812.1	1,932.4	1,975.6	2,087.5	7,807.6	9,354.1
Non-GAAP Operating Expenses													
Research and development	671.7	816.9	225.8	252.9	261.1	280.9	1,020.6	312.2	314.3	315.2	318.8	1,260.4	1,452.8
Marketing and Sales	2,406.0	2,873.5	785.0	825.5	876.2	944.8	3,431.5	959.9	1,020.7	1,018.5	1,122.9	4,121.9	4,829.3
General and administrative	576.6	642.6	179.2	218.2	212.9	220.8	831.1	223.2	243.9	240.3	264.1	971.5	1,167.3
Total Non-GAAP Operating Expenses	3,654.3	4,333.0	1,190.0	1,296.5	1,350.2	1,446.5	5,283.2	1,495.2	1,578.8	1,574.0	1,705.8	6,353.9	7,449.4
Non-GAAP Operating Income	574.1	830.0	278.5	263.6	272.6	295.3	1,109.9	316.9	353.5	401.6	381.7	1,453.7	1,904.7
Non-GAAP EBITDA	867.4	1,197.7	373.7	364.2	377.1	401.8	1,516.8	427.8	470.3	522.6	510.4	1,931.1	2,546.9
Other income (expense), net	(37.9)	(44.3)	(20.8)	(1.4)	(9.6)	6.8	(24.9)	(7.3)	(11.4)	(9.6)	8.3	(20.0)	(3.5)
Non-GAAP Earnings Before Taxes	536.2	785.7	257.7	262.2	263.0	302.0	1,085.0	309.6	342.1	392.0	390.0	1,433.8	1,901.1
Provision for Income Taxes	196.3	278.9	90.2	91.8	92.0	105.7	379.7	106.8	118.0	135.3	134.6	494.7	655.9
Tax Rate	36.6%	35.5%	35.0%	35.0%	35.0%	35.0%	35.0%	34.5%	34.5%	34.5%	34.5%	34.5%	34.5%
Minority Interest in consolidated joint venture (J)	(1.7)	-	-	-	-	-	-	-	-	-	-	-	-
Non-GAAP Net Income ⁽¹⁾	\$341.6	\$506.8	\$167.5	\$170.4	\$170.9	\$196.3	\$705.2	\$202.8	\$224.1	\$256.8	\$255.5	\$939.1	\$1,245.2
Non-GAAP Diluted EPS	\$0.53	\$0.75	\$0.24	\$0.24	\$0.25	\$0.28	\$1.01	\$0.28	\$0.31	\$0.35	\$0.34	\$1.28	\$1.67
Avg Diluted Shares Outstanding	650.4	674.4	686.8	696.0	690.5	711.2	696.1	721.6	728.2	734.8	741.4	731.5	746.9

(1) Non-GAAP excludes: amortization, restructuring, impairments, and stock-based comp.

Income Statement Ratios													
Revenue Analysis:													
Subscription and Support	93.3%	93.1%	92.6%	92.6%	92.5%	92.0%	92.4%	92.2%	92.3%	92.2%	91.7%	92.1%	92.0%
Professional Services and other	6.7%	6.9%	7.4%	7.4%	7.5%	8.0%	7.6%	7.8%	7.7%	7.8%	8.3%	7.9%	8.0%
Expense Analysis:													
Cost of Subscription	15.6%	16.7%	16.2%	16.5%	17.5%	17.7%	17.0%	17.6%	16.5%	17.5%	17.7%	17.4%	17.5%
Cost of Services	101.3%	100.9%	114.2%	109.4%	108.3%	96.9%	106.6%	100.5%	102.0%	102.0%	102.0%	101.7%	102.0%
Cost of Revenues	21.3%	22.6%	23.4%	23.4%	24.3%	24.1%	23.8%	24.1%	23.1%	24.2%	24.7%	24.0%	24.3%
Research and Development	12.5%	12.3%	11.8%	12.4%	12.2%	12.2%	12.2%	13.1%	12.5%	12.1%	11.5%	12.3%	11.8%
Marketing and Sales	44.8%	43.1%	41.0%	40.5%	40.9%	41.2%	40.9%	40.2%	40.6%	39.1%	40.5%	40.1%	39.1%
General & Admin.	10.7%	9.6%	9.3%	10.7%	9.9%	9.6%	9.9%	9.3%	9.7%	9.2%	9.5%	9.5%	9.5%
Depreciation	5.5%	5.5%	5.0%	4.9%	4.9%	4.6%	4.8%	4.6%	4.6%	4.6%	4.6%	4.6%	5.2%
Margin Analysis:													
Non-GAAP Subscription Gross Margin	84.4%	83.3%	83.8%	83.5%	82.5%	82.3%	83.0%	82.4%	83.5%	82.5%	82.3%	82.6%	82.5%
Non-GAAP Services Gross Margin	(1.3%)	(0.9%)	(14.2%)	(9.4%)	(8.3%)	3.1%	(6.6%)	(0.5%)	(2.0%)	(2.0%)	(2.0%)	(1.7%)	(2.0%)
Non-GAAP Gross Margin	78.7%	77.4%	76.6%	76.6%	75.7%	75.9%	76.2%	75.9%	76.9%	75.8%	75.3%	76.0%	75.7%
Non-GAAP Operating Margin	10.7%	12.4%	14.5%	12.9%	12.7%	12.9%	13.2%	13.3%	14.1%	15.4%	13.8%	14.1%	15.4%
EBITDA Margin	16.1%	18.0%	19.5%	17.9%	17.6%	17.5%	18.1%	17.9%	18.7%	20.1%	18.4%	18.8%	20.6%
Non-GAAP Tax Rate	36.6%	35.5%	35.0%	35.0%	35.0%	35.0%	35.0%	34.5%	34.5%	34.5%	34.5%	34.5%	34.5%
Non-GAAP Net Margin	6.4%	7.6%	8.7%	8.4%	8.0%	8.6%	8.4%	8.5%	8.9%	9.9%	9.2%	9.1%	10.1%
Q/Q Growth Rates:													
Subscription and Support			5.5%	6.2%	5.2%	6.4%		4.3%	5.4%	3.5%	5.9%		
Professional Services and other			11.3%	6.7%	6.8%	14.0%		1.8%	4.0%	5.2%	12.2%		
Total Revenue			5.9%	6.3%	5.3%	7.0%		4.1%	5.3%	3.6%	6.4%		
Gross Profit			4.4%	6.2%	4.0%	7.3%		4.0%	6.6%	2.2%	5.7%		
Non-GAAP Operating Income			27.3%	(5.4%)	3.4%	8.3%		7.3%	11.5%	13.6%	(5.0%)		
Net Income			29.2%	1.7%	0.3%	14.9%		3.3%	10.5%	14.6%	(0.5%)		
Y/Y Growth Rates:													
Subscription and Support	31.1%	23.8%	26.3%	24.0%	24.3%	25.4%	25.0%	24.0%	23.0%	21.0%	20.5%	22.0%	20.0%
Professional Services and other	46.0%	28.3%	33.3%	32.8%	39.1%	44.7%	37.7%	32.3%	29.0%	27.0%	25.0%	28.1%	22.0%
Total Revenue	32.0%	24.1%	26.8%	24.6%	25.3%	26.8%	25.9%	24.6%	23.4%	21.4%	20.9%	22.5%	20.2%
Gross Profit	29.8%	22.1%	26.1%	23.2%	22.4%	23.9%	23.8%	23.4%	23.9%	21.7%	19.8%	22.1%	19.8%
Research and development	30.1%	21.6%	18.3%	26.2%	25.7%	28.9%	24.9%	38.2%	24.3%	20.7%	13.5%	23.5%	15.3%
Marketing and Sales	28.5%	19.4%	21.4%	17.4%	20.0%	19.0%	19.4%	22.3%	23.7%	16.2%	18.8%	20.1%	17.2%
General and administrative	14.2%	11.5%	19.1%	40.1%	32.1%	25.9%	29.3%	24.6%	11.8%	12.9%	19.6%	16.9%	20.2%
Non-GAAP Operating Expenses	26.3%	18.6%	20.5%	22.4%	22.8%	21.8%	21.9%	25.7%	21.8%	16.6%	17.9%	20.3%	17.2%
Non-GAAP Operating Income	57.8%	44.6%	57.6%	27.0%	20.1%	35.0%	33.7%	13.8%	34.1%	47.4%	29.3%	31.0%	31.0%
Non-GAAP Net Income	54.0%	48.4%	54.6%	32.9%	21.6%	51.4%	39.2%	21.0%	31.5%	50.2%	30.1%	33.2%	32.6%
Non-GAAP EPS	50.2%	43.1%	49.6%	28.4%	19.4%	45.4%	34.8%	15.2%	25.7%	41.2%	24.8%	26.7%	29.9%

Source: BTIG, Company Filings.

BTIG Covered Companies Mentioned in this Report

SALESFORCE.COM, INC. (CRM, Buy, \$100.00 PT; Current Price: \$87.75; Analyst: Joel.Fishbein)

Appendix: Analyst Certification and Other Important Disclosures

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Company Valuation and Risk Disclosures

Salesforce.com, Inc. (CRM, Buy, \$100.00 PT)

Valuation: Our Buy rating and \$100 price target is based on our 10-year DCF model and reflects 7x our EV/FY18E Revenues and 34x EV/FY18E FCF. Our DCF-supported price target assumes a 10-year revenue CAGR of 14%, FCF CAGR of 19%, and a 16x terminal cash flow multiple. This implies a terminal EV/EBITDA multiple of 11x compared to current multiples for Oracle and SAP of 9-10x EBITDA, which we believe is reasonable based on Salesforce's recurring subscription revenue stream.

Risks: Primary risk revolves around valuation, which has little margin for error. The Street fully expects that core CRM growth will be sustained while salesforce.com grows and monetizes its new cloud businesses.

Salesforce.com, Inc. (CRM)



Note: Closing Price and Target Price have been adjusted for corporate actions.

Date	Closing Price (\$)	Target Price (\$)	Analyst	Rating
10-Sep-15	70.05	88	Joel Fishbein	Buy
18-Nov-15	80.64	92	Joel Fishbein	Buy
19-May-16	81.02	100	Joel Fishbein	Buy

Company-Specific Regulatory Disclosures

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