Buy HubSpot

David Gardner | June 11, 2020 | Buy Recommendation

CURRENT PRICE: HUBS $ 221.75 ↑ $ 2.66 (1.2%)

Just like a hit song, it's great when a company has a hook — that catchy slogan or concept that sets it apart from its competitors. This month's rerecommendation, **HubSpot** (NYSE: HUBS), has the potential to be a smash hit. It is, in its own words, the "spiritual leader" of inbound marketing — the philosophy that instead of seeking out customers through cold calls and spam emails, you should create valuable content that brings them to you. That approach has brought in thousands of customers, meteoric sales growth, and fast-rising cash flow for this young company.

We love its philosophy, but we're more excited about what the HubSpot platform has become and where it's going. A company that cut its teeth helping small businesses get off the ground is becoming increasingly sophisticated and powerful, and it offers a great opportunity for long-term investors. HubSpot is already a two-time winner on our scorecard — the original recommendation from 2017 is beating the market by 167 percentage points — but the company is only now entering a new chapter. The third time, we believe, will continue to charm.

Inbound Is Here to Stay

The truth is, HubSpot didn't invent inbound marketing. As much as it is a deliberate strategy to help win over and delight customers, it's simply a reflection of how the world works now. Think about some of your most recent purchases. You might have noticed a problem or need, done some research, narrowed down into several products, looked at some online reviews, and finally made a decision about what and where to buy. That's an inbound process, and it has arisen organically as customers have bypassed salespeople as gatekeepers through online research, blocking ads, filtering spam, streaming past commercials, and so on.

HUBSPOT IN 1 MINUTE

WHAT IT DOES

HubSpot is a marketing automation company serving small and medium-sized businesses.

WHY BUY

- HubSpot's newest product launch — the CMS Hub — is emblematic of its move toward serving larger and more sophisticated customers while maintaining usability.
- The company has grown its client roster even faster than we expected and is taking the right steps to support users during an economic crisis.
- While not yet profitable, the company is producing strong and growing cash flow.

BUYER'S GUIDE

- **Industry:** Software
- **Size:** Mid cap
- **Region:** Global
- **June 8 Price:** $210.94
- **Allocation:** Many Fools choose to fill out their positions incrementally, starting with a small amount — 2% of their portfolio's overall value, for instance — and adding a little at a time.

KEY DATA

HubSpot's tools serve as a survival toolkit for the modern world of marketing — a single platform for managing customers and content, organizing social media and email campaigns, conducting search engine optimization, and more. The company began with a focus on marketing automation, then added in a sales platform (which it significantly expanded in 2017), followed by its Service Hub in 2018 to keep existing customers engaged and satisfied. Just a few weeks ago, it launched its CMS Hub to help customers create, maintain, and improve websites.

But here's the bigger picture: HubSpot has been successful in introducing new products and cross-selling them to customers because it's a single platform built for interoperability and scalability. While the company still officially targets mid-market customers (businesses with 2 to 2,000 employees), it's winning even larger customers and is seeing strong growth in its enterprise-level contracts. Gross margin is steadily improving even as the company brings in thousands of new clients with its freemium model.

- **Headquarters:** Cambridge, Mass.
- **Website:** HubSpot investor relations
- **Market Cap:** $9.3 billion
- **Cash/Debt:** $968.6 million / $610.5 million
- **Revenue (2018/'19/LTM):** $513.0 million / $674.9 million / $722.0 million
- **Earnings (2018/'19/LTM):** ($63.8 million) / ($53.7 million) / ($60.4 million)

Add HUBS to Your Favorites

What's the secret? Founder and CEO Brian Halligan recently borrowed a concept from George Hu, COO at fellow Rule Breaker **Twilio** (NYSE: TWLO), to explain the conundrum of business software:

> *He refers to this phenomenon as the tyranny of "or." You can either have it really easy to use or really powerful. And it's the tyranny — you can't have both. And I think for a number of reasons, we've been able to kind of break that tyranny of "or." Part of it is we didn't acquire a bunch of companies and glue this stuff together. It's all one system. ... The other is ... an outsized bet on user research and design here, and it's a real strength of ours. It's an obsession with Net Promoter Score, and Net Promoter Score's been going through the roof these days. And it all kind of comes together.*

One telling sign that this is working is the company HubSpot keeps. These days, $9 billion HubSpot is most often compared to $157 billion behemoth **Salesforce.com** (NYSE: CRM). Are HubSpot's tools as complete and powerful as Salesforce's? No. But they offer an increasingly broad platform for increasingly larger and more demanding customers while keeping the basic advantage of simplicity. Salesforce is breathtaking in its breadth, but it did grow to a significant extent by "gluing things together." For example, one of HubSpot's marketing automation competitors, Pardot, was swallowed up by ExactTarget, which was in turn acquired by Salesforce. That's a lot different than HubSpot's organic platform building.

Better Than We Thought

When we first recommended HubSpot in 2017, it had about 25,000 subscribers. Tim Beyers wrote then that in five years' time, "I'm looking for marketing subscriptions to roughly double to 50,000" — before acknowledging, "Maybe that sounds crazy." Less than three years later, the company has 78,776 paying subscribers. Admittedly, revenue per customer has fallen from $12,773 at the time of the original recommendation to $9,920 in 2019 as the company has introduced more lower-cost products. But that's exactly what the company should be doing — winning customers that will later purchase more products and move to higher tiers of service.

Get More Info

Talk About HUBS

Talk about how HUBS fits into *RB* here

See why HubSpot scores a 12 on our unique 25-point Risk Rating.

See how you can tell if this investment is going right — or wrong.

Like most businesses, HubSpot is facing some uncertainty due to the global pandemic. That could be a concerning position for a business that has yet to turn a GAAP profit. But the company has had positive — and growing — free cash flow since 2016, has close to $1 billion in cash, and manageable debt. We're looking for it to keep aggressively adding customers, keep adding new Hubs and, over time, to increase its revenue per customer.

Risks and When We'd Sell

When it comes to software-as-a-service (SaaS) companies, we often talk about total subscription dollar retention rate or some similarly named metric that illustrates how much money existing customers are spending on the platform now compared to a year earlier. Ideally, we like to see that figure above 100% — the higher the better. That indicates the company is both retaining customers and selling them more products and services.

HubSpot's total subscription dollar retention rate was 99.9% in 2019. That's hardly a terrible figure, nor is it much out of line with past results (100.7% from 2018 and 100.5% from 2017). In fact, it's a darn sight better than the 82.9% the company reported in the year before its IPO. But it is indicative that this is a business with higher customer churn than some other SaaS companies. That's in part because the company is selling to smaller businesses (not all survive) and because the company faces a lot of competition. While we think HubSpot has the best mid-market platform, most of its functionality can be accomplished with other tools, often at a lower price. And at the higher end, it's possible that some of the company's most successful clients are graduating to Salesforce.

All that suggests that there will continue to be a lot of pressure on the company to invest heavily in winning new customers and to introduce new products. We think it's rising to the challenge with grace and integrity. In response to the COVID-19 pandemic, the company has introduced flexible payment to customers and let some clients downgrade contracts without penalties. In the short term, that means total subscription dollar retention rate has fallen to the low 90% — mostly from downgrades, although some small customers have simply failed. It'll probably get worse before it gets better. While we think this is setting the company up to be stronger than ever as things return to normal, customer acquisition costs may remain stubbornly high and make this business less profitable than we'd like.

The Foolish Bottom Line

At HubSpot's first quarterly conference call as a public company in 2014, Halligan boasted, "We pull in tens and thousands of organic leads a month by drinking our own champagne." In other words, the company itself is one of the best examples of how inbound marketing works. If you start researching how to create an inbound marketing campaign, you'll almost instantly be looking at HubSpot materials. By the time the company reaches out to you, you're probably at least halfway sold. That's a pretty powerful position when you consider that inbound marketing has simply become the way of the world.

HubSpot might look a little expensive against its current sales and cash flow, but this is still a small company being sought out by a tide of businesses that realize spam email and "as seen on TV" no longer work.

Karl Thiel contributed to this report.

DAVID CALLED IT: Do you agree that HubSpot will beat the market over the next 3-5 years? (After voting, buy shares to invest right away or add HUBS to your Favorites for alerts later.)

Yes

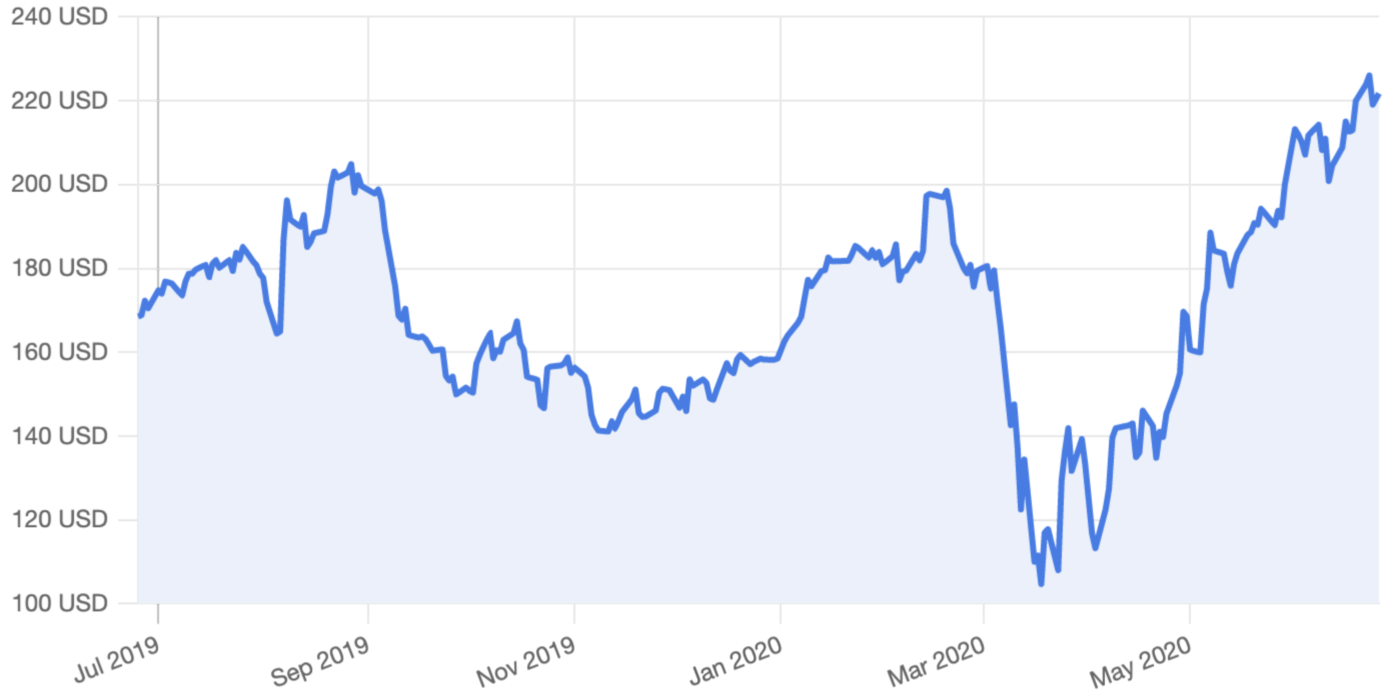
No

Not Sure

Tom Gardner owns shares of Salesforce.com and Twilio. The Motley Fool owns shares of HubSpot, Salesforce.com, and Twilio. The Motley Fool has a disclosure policy.

See the Trends

The Motley Fool thinks buying and holding for at least 3-5 years sets you up for success.



1W 1M 3M 6M YTD 1Y 5Y 10Y MAX

Price Vs S&P

From the Company Page

Last updated June 25, 4:15 p.m.

Current Price	$221.75
Today's Change	$2.66 (1.2%)
Exchange / Symbol	NYSE: HUBS
Market Cap	$10B
Beta	1.58465
Earnings Per Share (Trailing 12 Months)	-$1.41

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Market data provided by FactSet and Web Financial Group.