Valuation of Salesforce Inc. using Discounted Cash Flow (DCF) Analysis

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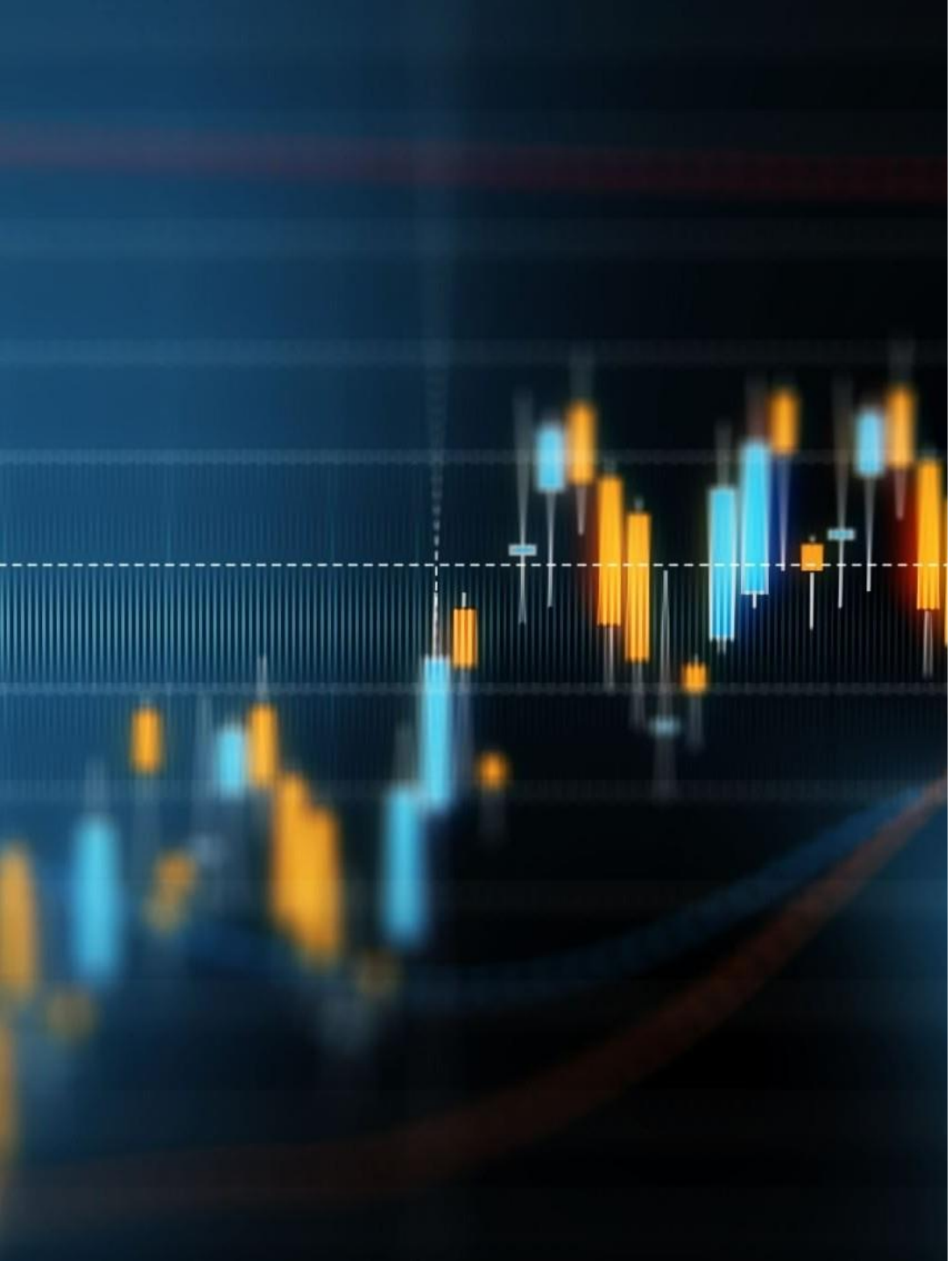
Introduction to Salesforce Inc.

- **Company Overview**: Salesforce Inc. is a global leader in Customer Relationship Management (CRM) software and a prominent player in the cloud computing space.
- **Business Segments**: Core products include Sales Cloud, Service Cloud, and the growing area of artificial intelligence solutions like Salesforce Einstein.
- **Valuation Objective:** To estimate the intrinsic value of Salesforce using DCF analysis based on revenue projections, free cash flow estimates, and terminal growth assumptions.

Gather Financial Data

- **Revenue Data:** Historical sales figures and projections up to 2028.
- **Cost of Goods Sold (COGS):** Historical and projected values.
- **Free Cash Flow (FCF):** Calculated based on sales, capital expenditures, and changes in working capital.
- **Sources of Data:** Salesforce Inc. financial statements (10-Ks). Industry growth data from market reports.



Estimate Revenue Growth Rates

Projected Revenue Growth Rates for Salesforce:

- 2024: $37.6 billion (8% growth)
- 2025: $40.5 billion (7.5% growth)
- 2026: $43.1 billion (6.5% growth)
- 2027: $45.5 billion (5.5% growth)
- 2028: $47.7 billion (5% growth)

Justification: Salesforce’s CRM market dominance and growth in SaaS cloud computing solutions.

.	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenues	21,252	26,492	31,352	34,857	37645.56	40468.98	43099.46	45469.93	47743.43
%GROWTH		25%	18%	11%	8.0%	7.5%	6.5%	5.5%	5.0%

1. How did you determine the revenue growth rates for Salesforce? What factors did you prioritize in making your assumptions?

- ***Maturing Market**: As Salesforce grows larger, it's facing a natural deceleration in growth, with less room for exponential increases.*
- ***Tech Industry Trends**: Factored in expected industry-wide growth rates, cloud services adoption, and digital transformation efforts.*
- ***Economic Outlook:** A stable global economy post-2024 with modest GDP growth, especially in major markets.*
- ***Competition:** Increasing competition from Microsoft, Oracle, and other cloud providers.*
- ***Innovation and Acquisitions:** Ongoing investments in new technologies and acquisitions are expected to support steady, albeit slower, growth.*

Determine Terminal Growth Rate

Terminal Growth Rate: 4%

Factors Considered:

- Long-term industry outlook (SaaS and cloud computing growth).
- Salesforce's position as a market leader and innovator.
- Global economic growth forecasts.

Key Considerations:

- **Long-Term Industry Outlook**:

- The technology sector is expected to grow with digital transformation and cloud adoption.

- Projected CAGR for the global cloud computing market: 20% over the next five years.

- **Economic Factors:**

- GDP Growth: Projected global GDP growth of ~3%annually.

- Inflation: Expected 2-3% inflation rates in developed markets.

- **Salesforce's Position:**

- Competitive advantages: strong brand, extensive ecosystem, continuous innovation.

- Historical revenue growth: 20%+ in recent years, though moderating as the market matures.

Terminal Growth Rate Assumption

1. **Assumed Terminal Growth Rate: 4% is chosen based on analysis**.

Justification:

- Aligns with long-term GDP growth expectations.

- Reflects sustainable growth potential in a mature technology market.

2. Comparison to Industry and Global Economy:

Global Economy:

- Long-term growth expectations of 3% Technology Industry

- Generally projected growth of 5-6%, driven by innovations and market demand.

3. Conclusion:

- A 4% terminal growth rate for Salesforce balances confidence in its growth while remaining cautious given the market's maturity.

Calculate the Discount Rate (WACC)

- Components of WACC:
- Cost of Equity (Re): Derived from the Capital Asset Pricing Model (CAPM).

  Risk-free rate: 0.037

  Beta: 1.3

  Market risk premium: 0.046

  Cost of Debt (Rd): Based on Salesforce’s average interest expense and debt levels.

Interest ($254) *(1 – 16%)
$8427(Total debt)

0.037(Rf)+[1.3(β)*0.046(risk premium)]

[(3%* 0.0253) +(97% * 0.0968)]

Proportion of Debt to total capital structure	3%
proportion of Equity to total capital structure	97%
Tax rate	16%
COST OF DEBT	0.0253
Risk-free Rate	0.037
Market Risk Premium	0.046
Levered Beta	1.3
Cost of Equity	0.0968
WAAC	9.44%

Perform DCF Analysis:

STEP-1. Forecast Free Cash Flows (FCF) for the next five years.

Salesforce

Discounted Cash Flow Analysis

($ in millions)	2020	2021	2022	2023	2024	2025	2026	2027	2028
Sales	**21,252**	**26,492**	**31,352**	**34,857**	**37646**	**40469**	**43099**	**45470**	**47743**
% growth		**25%**	**18%**	**11%**	**8.0%**	**7.5%**	**6.5%**	**5.5%**	**5.0%**
Cost of Goods Sold	**(5,438)**	**(7,026)**	**(8,360)**	**(8,541)**	**-9411**	**-10117**	**-10775**	**-11367**	**-11936**
Gross Profit	**15,814**	**19,466**	**22,992**	**26,316**	**28,234**	**30,352**	**32,325**	**34,102**	**35,808**
% margin	74.41%	73.48%	73.34%	75.50%	75%	75%	75%	75%	75%
Selling, General & Administrative	(12,513.00)	(15,620.00)	(17,348.00)	(16,358.00)	(17,693.41)	(19,020.42)	(20,256.75)	(21,370.87)	(22,439.41)
EBITDA	3,301	3,846	5,644	9,958	10,541	11,331	12,068	12,732	13,368
% margin	15.53%	14.52%	18.00%	28.57%	28%	28%	28%	28%	28%
Depreciation & Amortization	2846	3298	3786	3959	4,141	4,452	4,741	5,002	5,252
EBIT	455	548	1,858	5,999	6,400	6,880	7,327	7,730	8,116
% margin	2.14%	2.07%	5.93%	17.21%	17%	17%	17%	17%	17%
Taxes	1511	88	452	814	868	934	994	1049	1101
EBIAT	1,966	460	1,406	5,185	5,531	5,946	6,333	6,681	7,015
Plus: Depreciation & Amortization	2846	3298	3786	3959	4141.0116	4451.59	4740.94	5001.69	5251.78
Less: Capital Expenditures	(710.00)	(717.00)	(798.00)	(736.00)	(794.88)	(854.50)	(910.04)	(960.09)	(1,008.09)
Less: **Inc./(Dec.) in Net Working Capital	-	3,099.00	558.00	(1,939.00)	(195.44)	(197.88)	(184.36)	(166.14)	(159.34)
Unlevered Free Cash Flow					8,682	9,345	9,979	10,556	11,099
WACC	**9.44%**								
Discount Period					0.5	1.5	2.5	3.5	4.5
Discount Factor					0.955893196	0.873430012	0.798080778	0.729231787	0.666322275
Present Value of Free Cash Flow					8299.12	8162.58	7964.26	7698.13	7395.79

	2020	2021	2022	2023	2024	2025	2026	2027	2028
NWC	4161	1062	504	2443	2638.44	2836.323	3020.683995	3186.821615	3346.162695
%sales	19.58%	4.01%	1.61%	7.01%	7.01%	7.01%	7.01%	7.01%	7.01%
**(INCREASE)/decrease in Net working capital		3099	558	(1,939.00)	(195.44)	(197.88)	(184.36)	(166.14)	(159.34)

STEP-2 : Calculate the Terminal Value using the Gordon Growth Model .

Calculation of Terminal Value	
FCF (2028)	11099.42
WACC	9.44%
g	4.0%
terminal value	212143.89

1. **Terminal Value Formula**: The terminal value is calculated using the formula:

$$\text{Terminal Value} = \frac{\text{FCF}_{2028} \times (1 + g)}{(\text{WACC} - g)}$$

2. **Assumptions Used**: For the calculation, the Free Cash Flow (FCF) in 2028 is $11,099.42 million, the WACC is 9.44%, and the perpetual growth rate (g) is 4.0%.

3. **Result**: This leads to a terminal value of approximately $212.14 billion, reflecting the estimated value of Salesforce's cash flows beyond the explicit forecast period.

STEP-3 : Discount the projected FCFs and Terminal Value back to present value.

					2024	2025	2026	2027	2028
Unlevered Free Cash Flow					8,682	9,345	9,979	10,556	11,099
WACC	9.44%								
Discount Period					0.5	1.5	2.5	3.5	4.5
Discount Factor					0.9558932	0.87343001	0.79808078	0.72923179	0.66632227
Present Value of Free Cash Flow					8299.12	8162.58	7964.26	7698.13	7395.79

Unlevered FCF * Discount Factor

The discount factor is calculated using the formula:

$$\text{Discount Factor} = \frac{1}{(1 + \text{WACC})^n}$$

Where:

- **WACC** is the Weighted Average Cost of Capital (9.44% or 0.0944).
- **n** is the discount period in years.

Terminal Value back to present value.

Discount Factor Calculation:

$$\text{Discount Factor} = \frac{1}{(1+\text{WACC})^n}$$

$$\text{Discount Factor} = \frac{1}{(1+0.0944)^5} \approx 0.6449 \quad (\text{rounded to } 0.64)$$

Present Value Formula:

$$\text{PV of Terminal Value} = \text{Terminal Value} \times \text{Discount Factor}$$

PV of Terminal Value	
terminal value	212143.89
WACC	9.44%
n	5
Discount	0.64
PV of terminal value	135,121

Step 4 : Determine the enterprise value.

Cumulative Present Value of FCF	39519.88
PV of terminal value	135121.43
Enterprise Value	174641.31

Cumulative Present Value of Free Cash Flows (FCF): The total present value of projected free cash flows from 2024 to 2028 is approximately **$39519.88 million**. This value represents the sum of the discounted UFCF for each year, reflecting the operational cash generation potential of the company during the explicit forecast period.

Present Value of Terminal Value: The present value of the terminal value, calculated to be around **$135,12.43 million**, represents the estimated value of the company's cash flows beyond 2028. This amount is discounted back to the present using the WACC, capturing the long-term value of the business.

Enterprise Value Calculation: The Enterprise Value (EV) is derived by adding the cumulative present value of the FCF and the PV of the terminal value:

What did your DCF analysis reveal about Salesforce's intrinsic value? How does this compare to its current market price?

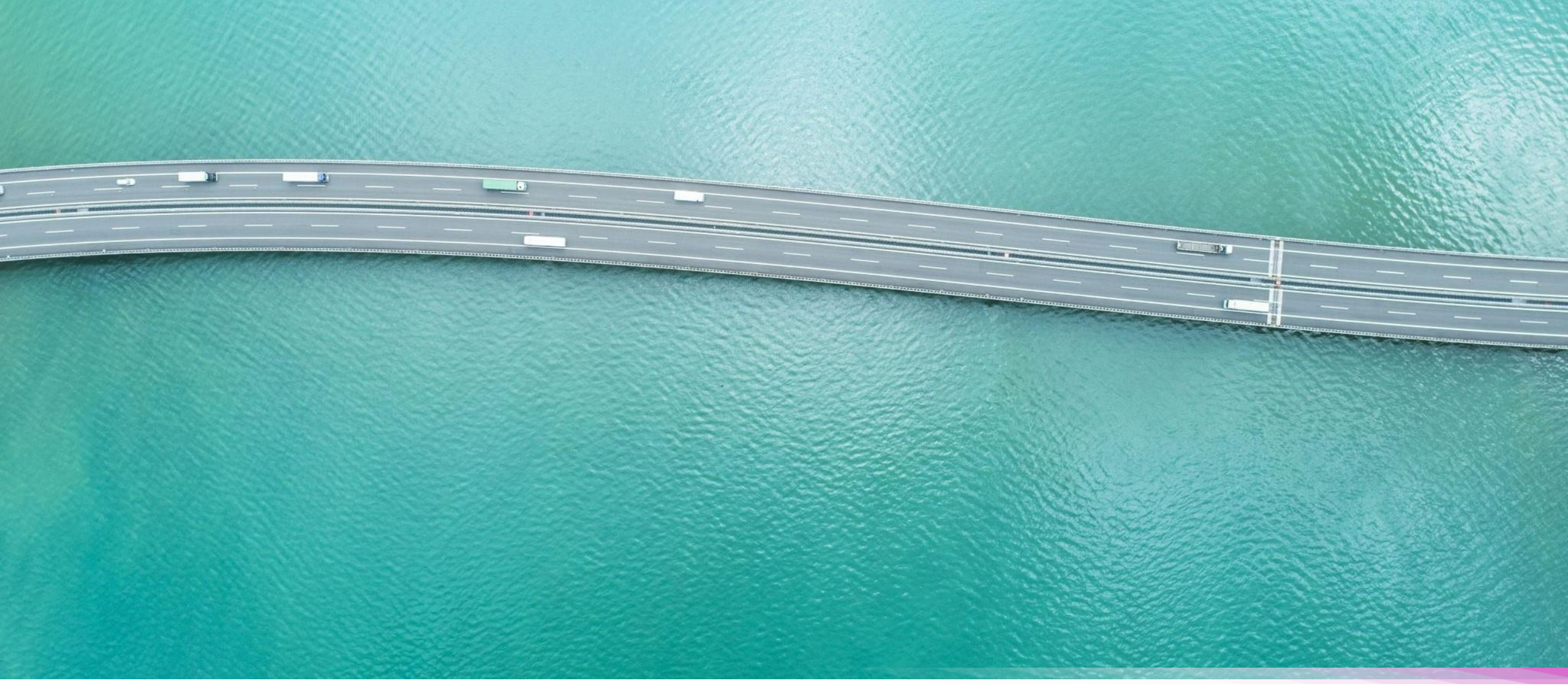
- **Calculation of Intrinsic value**

	Enterprise Value	174641
	Net Debt = Debt - cash	-45
[A]	EV - Net Debt	174686
[B]	Outstanding Share	870
	Terminal Value [A] / [B]	201

Market Price Comparison:

Current Market Price: $240

Conclusion: The DCF analysis reveals an intrinsic value of $201 per share for Salesforce. This is significantly lower than the current market price of $240, suggesting that the stock may be overvalued based on the analysis.



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