

F5 Networks, Inc.(FFIV)

\$116.76 (As of 04/07/20)

Price Target (6-12 Months): **\$123.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 02/27/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:F

Value: D

Growth: D

Momentum: D

Summary

F5 Networks is gaining traction from strong software growth, backed by a solid uptick in public cloud and security offerings. The company is benefiting from growing demand for consistent application security across multi-cloud environments, which is aiding revenue growth. Acceleration in ELA and Virtual Edition subscription software deals is a positive. The BIG-IP Cloud Edition is also expected to be a key growth driver. The company is incorporating more automation and orchestration on its platforms to enable quicker application provisioning. However, although the recent buyout of NGINX improves the company's position within the DevOps ecosystem and helps boost its long-term revenues, the near-term pressure on the margins and earnings is a concern. Shares of the company have underperformed the industry in the past year.

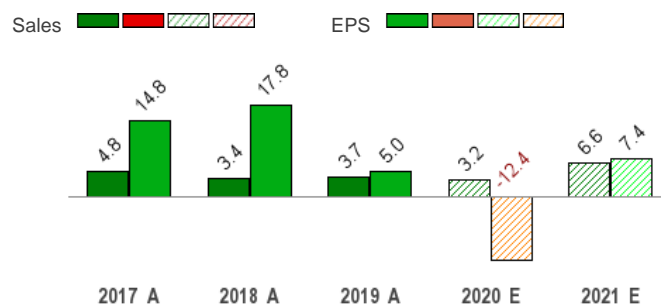
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$168.94 - \$79.78
20 Day Average Volume (sh)	1,040,992
Market Cap	\$7.1 B
YTD Price Change	-16.4%
Beta	0.89
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Internet - Software
Zacks Industry Rank	Top 34% (85 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.9%
Last Sales Surprise	0.6%
EPS F1 Est- 4 week change	-8.5%
Expected Report Date	04/27/2020
Earnings ESP	-4.4%
P/E TTM	11.4
P/E F1	12.9
PEG F1	1.4
P/S TTM	3.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	592 E	610 E	627 E	653 E	2,466 E
2020	569 A	573 E	569 E	601 E	2,314 E
2019	544 A	545 A	563 A	590 A	2,242 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.22 E	\$2.26 E	\$2.41 E	\$2.66 E	\$9.74 E
2020	\$2.55 A	\$2.08 E	\$1.99 E	\$2.32 E	\$9.07 E
2019	\$2.70 A	\$2.57 A	\$2.52 A	\$2.59 A	\$10.36 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/07/2020. The reports text is as of 04/08/2020.

Overview

Seattle, WA-based F5 Networks Inc, founded in 1996, provides products and services to manage Internet traffic worldwide. Its application, delivery and networking products improve performance, availability and security of applications running on networks that use the Internet Protocol (IP). The company offers BIG-IP products to manage the IP traffic between network servers, clients and other devices. The company's FirePass systems provide SSL VPN access to remote IP network users and any applications connected to those networks from any standard web browser on any device.

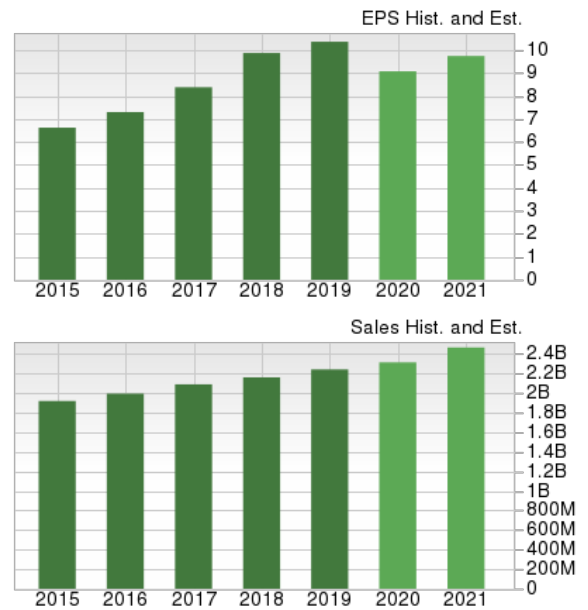
F5 Networks also offers TrafficShield, a web application firewall that provides an application-layer protection against generalized and targeted attacks. The company's WANJet devices helps to combine wide area network optimization and traffic shaping in a single device to accelerate file transfers, email, data replication and other applications over the IP networks. WebAccelerator speeds up web transactions, enhances web application performance from any location, speeds up interactive performance and improves download time. F5 Networks serves a wide variety of enterprises and service providers among Fortune 1000 and Business Week Global 1000 companies, which includes telecommunications, financial services, technology, manufacturing and transportation enterprise customers as well as the government.

In fiscal 2019, the company reported revenues of \$2.24 billion, which increased 4% from the fiscal 2018-level.

In fiscal 2019, Product revenues made up 44% of total revenues (\$986 million) and Services revenues accounted for the remaining 56% of total revenues (\$1.26 billion).

The company's distributors Ingram Micro, Tech Data and Westcon accounted for 18.2%, 10.2% and 10%, respectively, of fiscal 2019 total revenues.

F5 Networks has three geographic segments. In fiscal 2019, the Americas generated 56% of revenues; EMEA, 25% and Asia-Pacific, 19%.



Reasons To Buy:

- ▲ F5 Networks is uniquely positioned to benefit from the growth prospects of the application networking market as enterprises cope with rapidly increasing capacity and security demands of next-generation applications and architectures. The company enjoys a strong market position in the Layer 4-7 content switching market. While its competitors are outlining application networking strategies, we believe that F5 Networks will likely maintain and grow its market share due to its lucrative position in the data center space while maintaining proximity with data applications. We believe that F5 Networks will get wide coverage for its products with its new release. Management is also positive regarding F5 Networks' increasing push into the security market as it expects this to help increase its addressable market and revenue growth prospects. Moreover, a new product cycle and better execution will increase revenues and can strengthen its market leadership in the future.
- ▲ F5 Networks holds a major position in the application delivery controller (ADC) market as its products are important components for data center consolidation, virtualization and cloud services. Also, Cisco's decision to shift its focus from the core ADC market has helped F5 capture considerable market share. F5 Networks is the leading developer and provider of software defined application services (SDAS) to ensure that applications delivered over the Internet Protocol (IP) networks are secure, fast and available to any user anywhere, anytime on any device.
- ▲ F5 Networks has resorted to acquisitions to boost its network security capabilities and tap the solid growth prospects in the market. The buyouts have helped the company enhance security capabilities, increasing the market share. Currently, though the security solutions available in the market have elevated the security level, the administrative expenses have also risen exponentially. This has led to a need for an integrated security solution platform that provides constant detection, prevention and remediation of security threats without elevating administrative costs. The acquisitions have enabled F5 Networks to provide its customers with secured access to data and applications, which in turn, will create a protected business environment. As the Internet security market is evolving rapidly, we believe, these deals are an important strategic move by the company.
- ▲ F5 Networks has entered into a number of partnerships or strategic alliances, striking deals with companies like Microsoft, Oracle, VMware, Cisco Systems, and HP to provide integrated application services for their Software Defined Networking (SDN) offerings. Further, the company also partnered with Amazon AWS, Microsoft Azure, VMware vCloud Air, Cisco ACI and many others to provide cloud-based application services and solutions. The company had also entered into a partnership with FireEye, a company which provides security platforms to protect against cyber-attacks to corporations and government agencies. These alliances have increased access to new technology, helped innovative product development, beef up F5 networks' cyber security suite, facilitated joint sales and marketing programs and improve its competitive dynamics.

F5 benefits from an ongoing transition toward multi-cloud environments and rising demand for application security.

Reasons To Sell:

- ▼ F5 Networks has a competitive edge over ARX, BIG-IP and VIPRION. However, Cisco Systems represents the greatest competitive threat to F5 Networks, given the dominance of the former in the overall networking market. Cisco has tremendous engineering and marketing resources at its disposal. Although F5's technology has been able to hold its leading position for many years, Cisco could potentially become more competitive if it invests more aggressively in the technology. In addition, Citrix Inc., Juniper Networks, Checkpoint Systems, Barracuda Networks also have a strong technology platform that could pose a more significant competitive threat on improved execution.
- ▼ F5 Networks continues to acquire a large number of companies. While this improves revenue opportunities, business mix and profitability, it also adds to integration risks. Moreover, frequent acquisitions are a distraction for management, which could impact organic growth, going forward.
- ▼ A substantial portion of the company's sales is derived from outside the U.S. During fiscal 2019, 44.5% of total revenue was garnered in currencies other than the U.S. dollar. This exposes the company to exchange rate fluctuations and counterparty default risk. Thus, an economic condition, which impacts foreign currency exchange rates, does result in transaction exposure, which leads to profit fluctuation. Moreover, execution challenges in Europe as a result of the macro economic uncertainty in the region (particularly UK and Germany), are an overhang on the company.
- ▼ Although ongoing transition toward subscription is likely to boost growth in the long run, we remain apprehensive in the near term as the transition continues to weigh on the results. Customers' adherence to a cloud-first mentality is a downtrend for hardware investment and use cases as this inclination is prolonging deal timings. Notably, declining systems revenue growth is putting pressure on the company, which is evident from the last quarterly results.

Declining systems revenues, a volatile spending atmosphere and competition from peers remain key concerns for the company.

Last Earnings Report

F5 Networks Reports Q1 Results

F5 Networks reported first-quarter fiscal 2020 Non-GAAP earnings per share of \$2.55, beating the Zacks Consensus Estimate of \$2.43 but decreasing 5.6% year over year.

Revenues rose 5% year over year to \$569.3 million and also surpassed the Zacks Consensus Estimate of \$566 million, driven by solid software growth.

Robust customer demand for security use cases including WAF and SSLO as well as ongoing ELA traction fueled growth in Software.

Quarter Ending **12/2019**

Report Date	Jan 27, 2020
Sales Surprise	0.56%
EPS Surprise	4.94%
Quarterly EPS	2.55
Annual EPS (TTM)	10.23

Quarterly Details

Products revenues (41% of total revenues) during the quarter totaled \$265 million, up 0.3% year over year. Lumpiness in some large deals was an overhang on product revenues. Realignment of the North American sales organization induced to a pause in short-term momentum.

Software soared 50% year over year and represented 28% of product revenues. This upside can be attributed to the growing adoption of the Enterprise License Agreement (ELA) and annual subscriptions among customers.

Systems revenues of \$170 million, representing 72% of product revenues, declined 11% on a year-over-year basis due to continued transition of customers to software-based solutions.

Services revenues (59%) increased 8% to \$335 million. Improvements to the tools and processes that the company's team uses to identify and secure renewals are among the key catalysts. Further, healthy services attached in renewal rates to software sold as perpetual or as subscriptions including NGINX-related sales, are tailwinds. Moreover, increase in consulting services demand associated with the rising software sales is an upside.

Region wise, on a year-over-year basis, revenues from the Americas reflecting 53% of the total count grew 3%. APAC revenues rose 8% and represented 20% of the total top line. EMEA climbed 5% and accounted for 20% of total revenues.

Going by the verticals, Enterprise, Service providers and Government (including 7% from the U.S. Federal) depicted 65%, 16% and 19% of the total product bookings, respectively.

The company's distributor Ingram Micro translated to 16% of the company's revenues. Westcon accounted for 11% and Arrow contributed 10% to the total revenue base.

Non-GAAP gross margin was 81% and non-GAAP operating margin was 33.8%.

Balance Sheet & Cash Flow

F5 Networks exited the quarter with cash, cash equivalents and short-term investments of approximately \$1.16 billion compared with \$972.3 million in the prior quarter.

Long-term liabilities were \$795.4 million compared with \$523.3 million in the previous quarter.

The company reported cash flow of \$144 million from operations compared with \$206 million in the sequential quarter.

Outlook

For second-quarter fiscal 2020, F5 Networks expects revenues in the range of \$580-\$590 million.

The company anticipates non-GAAP earnings per share in the band of \$2.14-\$2.16.

The company expects to incur operating expenses of \$325-\$337 million, implying the addition of Shape.

Management remains optimistic that surging demand for the multi-cloud application services will be a key driver. Moreover, strong demand for software solutions is a tailwind. Rising traction from subscription and ELA offerings is a tailwind.

In the fiscal second quarter, the company anticipates software growth to reaccelerate the above 50% uptrend witnessed in the earlier quarter even before any contribution recorded from Shape.

Moreover, F5 Networks and NGINX's first combined solution, Controller 3.0, is expected to increase the total addressable market and deal sizes by spending more use cases across DevOps and Super-NetOps customer profiles.

For 2020, the company projects 60-70% software growth including benefits drawn from Shape Security.

Recent News

On Feb 4, 2020, F5 announced a customer-focused approach to Application Protection, equipped with new offerings and the recent buyout of Shape Security. The portfolio will safeguard all applications without affecting end-user experience or decelerating time-to-market.

On Jan 28, 2020, F5 launched a cloud-native application delivery solution, NGINX Controller 3.0, to help organizations increase business agility, mitigate risk, and enhance their customers' digital experiences.

On Jan 25, 2020, F5 Networks completed the acquisition of Shape Security which will add protection from automated attacks, botnets, and targeted fraud to F5's portfolio of application services.

On Dec 19, 2019, F5 Networks announced a definitive agreement to acquire Shape Security for approximately \$1 billion.

Valuation

Shares of F5 have lost 16.4% in the year-to-date (YTD) period and 29.5% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector have plunged 10.1% and 11.6%, respectively, YTD. Over the past year, the Zacks sub-industry and the sector declined 16.3% and 1.6%, respectively.

The S&P 500 Index has fallen 17.2% in the past six months and 7.6% in the past year.

The stock is currently trading at 2.87X forward 12-month sales, which compares to 5.23X for the Zacks sub-industry, 3.12X for the Zacks sector and 2.92X for the S&P 500 index.

Over the past five years, the stock has traded as high as 5.44X and as low as 2.24X, with a 5-year median of 3.89X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$123 price target reflects 3.01X trailing 12-month sales.

The table below shows summary valuation data for FFIV

Valuation Multiples - FFIV					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	2.87	5.23	3.12	2.92
	5-Year High	5.44	15.62	3.58	3.44
	5-Year Low	2.24	3.07	2.32	2.54
	5-Year Median	3.89	5.26	3.09	3.00
P/B TTM	Current	3.68	5.72	4.19	3.54
	5-Year High	9.58	8.23	5.37	4.55
	5-Year Low	2.85	2.30	3.15	2.84
	5-Year Median	6.68	5.18	4.27	3.63
EV/Sales TTM	Current	2.77	5.84	3.56	2.65
	5-Year High	5.17	11.57	4.44	3.46
	5-Year Low	2.07	3.05	2.57	2.16
	5-Year Median	3.64	6.01	3.55	2.83

As of 04/07/2020

Industry Analysis Zacks Industry Rank: Top 34% (85 out of 253)



Top Peers

j2 Global, Inc. (JCOM)	Neutral
LINE Corporation (LN)	Neutral
Nice Ltd. (NICE)	Neutral
Snap Inc. (SNAP)	Neutral
Sogou Inc. Sponsored ADR (SOGO)	Neutral
Splunk Inc. (SPLK)	Neutral
Twitter, Inc. (TWTR)	Neutral
Workday, Inc. (WDAY)	Neutral

Industry Comparison Industry: Internet - Software				Industry Peers		
	FFIV Neutral	X Industry	S&P 500	LN Neutral	SPLK Neutral	WDAY Neutral
VGM Score	F	-	-	D	F	B
Market Cap	7.10 B	359.11 M	18.38 B	11.69 B	19.07 B	30.58 B
# of Analysts	10	5	13	1	16	35
Dividend Yield	0.00%	0.00%	2.31%	0.00%	0.00%	0.00%
Value Score	D	-	-	F	F	F
Cash/Price	0.18	0.16	0.06	0.19	0.11	0.07
EV/EBITDA	10.30	-0.16	11.23	-45.41	2,670.04	-486.10
PEG Ratio	1.46	2.35	1.91	NA	41.49	2.40
Price/Book (P/B)	3.68	4.17	2.45	7.28	9.38	12.30
Price/Cash Flow (P/CF)	12.40	20.84	9.63	NA	678.88	293.09
P/E (F1)	13.15	37.17	15.92	NA	1,209.76	62.67
Price/Sales (P/S)	3.13	3.26	1.94	5.67	8.08	8.43
Earnings Yield	7.77%	0.84%	6.15%	-3.40%	0.08%	1.59%
Debt/Equity	0.18	0.13	0.70	1.08	0.98	0.51
Cash Flow (\$/share)	9.42	-0.01	7.01	-0.94	0.18	0.45
Growth Score	D	-	-	C	F	A
Hist. EPS Growth (3-5 yrs)	14.40%	18.55%	10.92%	NA	NA	NA
Proj. EPS Growth (F1/F0)	-12.41%	4.00%	-0.12%	9.34%	-94.71%	11.87%
Curr. Cash Flow Growth	2.02%	3.20%	5.93%	-452.52%	-139.74%	10.10%
Hist. Cash Flow Growth (3-5 yrs)	9.12%	18.18%	8.55%	NA	16.42%	23.82%
Current Ratio	1.51	1.46	1.24	1.83	2.15	1.04
Debt/Capital	15.07%	19.47%	42.36%	51.84%	49.38%	33.62%
Net Margin	17.43%	-16.16%	11.64%	-16.97%	-14.27%	-13.25%
Return on Equity	28.40%	-13.06%	16.74%	-21.37%	-10.80%	-12.92%
Sales/Assets	0.68	0.62	0.54	0.42	0.49	0.59
Proj. Sales Growth (F1/F0)	3.21%	9.73%	0.85%	14.04%	8.43%	19.07%
Momentum Score	D	-	-	A	B	B
Daily Price Chg	3.61%	0.00%	0.69%	1.10%	1.54%	1.14%
1 Week Price Chg	-3.16%	-5.57%	-4.40%	0.68%	-18.13%	-14.78%
4 Week Price Chg	-0.95%	-11.08%	-10.67%	-3.56%	-9.12%	-12.32%
12 Week Price Chg	-14.21%	-25.00%	-23.70%	-0.53%	-23.45%	-26.77%
52 Week Price Chg	-29.52%	-28.52%	-15.92%	40.65%	-7.30%	-30.92%
20 Day Average Volume	1,040,992	422,068	4,068,329	33,820	2,640,055	3,706,867
(F1) EPS Est 1 week change	-2.25%	0.00%	0.00%	0.00%	-1.24%	0.00%
(F1) EPS Est 4 week change	-8.52%	-1.50%	-5.24%	0.00%	-1.57%	9.10%
(F1) EPS Est 12 week change	-19.74%	-13.33%	-6.86%	1.20%	-231.69%	11.03%
(Q1) EPS Est Mthly Chg	-24.88%	-0.60%	-8.25%	NA	0.00%	0.79%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	D
Momentum Score	D
VGM Score	F

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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