

ServiceNow Inc. (NOW)

\$341.62 (As of 01/30/20)

Price Target (6-12 Months): **\$359.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/21/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: F

Growth: A

Momentum: C

Summary

ServiceNow reported stellar fourth-quarter results. The company is benefiting from growing adoption of wide range of application-based products by public and big private companies. Robust pipeline and improvement in bookings hold promise. As businesses, government agencies, among others, "cloudify" their infrastructure, ServiceNow platform is well poised to gain adoption. Additionally, the company continues to witness traction from Fortune 500 companies. Further, the company's expanding global presence, strong partnerships and strategic buyouts are expected to aid financial performance. Notably, shares of the company have outperformed the industry in the past year. However, increasing expenses on product development and to expand international presence are likely to limit margin expansion in the near term.

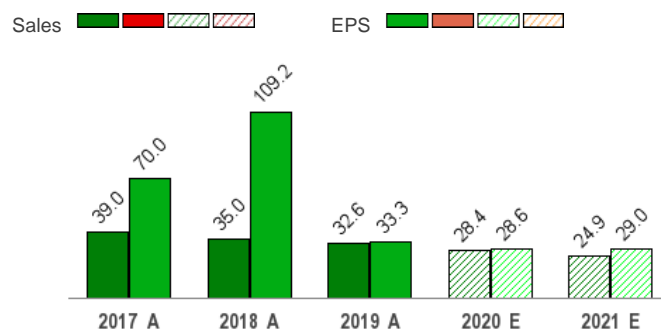
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$343.89 - \$209.99
20 Day Average Volume (sh)	1,796,955
Market Cap	\$64.1 B
YTD Price Change	21.0%
Beta	1.33
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Computers - IT Services
Zacks Industry Rank	Top 44% (113 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	9.1%
Last Sales Surprise	1.0%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	04/22/2020
Earnings ESP	7.2%
P/E TTM	102.6
P/E F1	80.0
PEG F1	2.9
P/S TTM	18.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,280 E	1,348 E	1,427 E	1,528 E	5,550 E
2020	1,028 E	1,075 E	1,134 E	1,211 E	4,442 E
2019	789 A	834 A	886 A	952 A	3,460 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.15 E	\$1.17 E	\$1.52 E	\$1.53 E	\$5.51 E
2020	\$0.91 E	\$0.93 E	\$1.20 E	\$1.19 E	\$4.27 E
2019	\$0.67 A	\$0.71 A	\$0.99 A	\$0.96 A	\$3.32 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 01/30/2020. The reports text is as of 01/31/2020.

Overview

Santa Clara, CA-based ServiceNow Inc. provides cloud computing services that automate digital workflows to accelerate enterprise IT operations. The company's Now Platform enables enterprises to enhance productivity by streamlining system processes.

By utilizing ServiceNow's product portfolio, customers can design any workflow application to reduce the manual time taken by complex processes, and consequently optimize total cost of ownership or TCO.

The company's solutions address the needs of many departments within an enterprise, including IT, human resources (HR), facilities, field service, marketing, customer service, security, legal and finance.

Now platform is the foundation of the company's cloud-based services.

The company has three product suites for IT management and operations. These are IT Service Management (ITSM), IT Operations Management (ITOM) and IT Business Management (ITBM) solutions.

Non-IT products include Customer Service, HR and Security Operations.

ServiceNow's end-markets are quite varied, which includes financial services, consumer products, IT services, health care, government, education and technology.

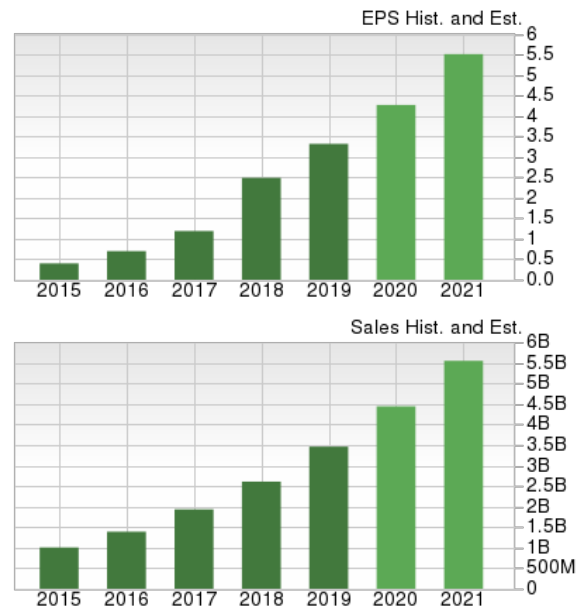
In 2019, total revenues surged almost 33% from 2018 to \$3.460 billion.

ServiceNow derives revenues from two sources – subscriptions (94% of 2019 revenues) and professional services and other (6% of 2019 revenues).

North America, Europe, the Middle East and Africa (EMEA), and Asia Pacific & Other contributed approximately 65%, 26% and 9% of revenues, respectively in fourth-quarter 2019.

The company operates data centers in Australia, Brazil, Canada, Hong Kong, Netherlands, Singapore, Switzerland, UK and the U.S.

ServiceNow has approximately 6,200 enterprise customers, including more than 44% of the world's 2,000 largest companies, as outlined by an annual ranking by the Forbes magazine. The figure also represents more than 80% of the Fortune 500 companies, as defined by an annual ranking by the Fortune magazine.



Reasons To Buy:

- ▲ ServiceNow is a dominant name in the IT service market (ITSM). The company continues to win market share by replacing legacy on-premise systems with cloud-based processes. G2K customers contribute approximately 50% of the top-line and the company expects the mix to remain steady in the long haul. The growing penetration at Fortune 500 clientele (80%) has been driving ServiceNow's top-line growth. Further, it is focusing primarily on public and big private entities, rapidly, which will further drive top-line growth in the long run.
- ▲ ServiceNow is rapidly expanding into non-ITSM markets like human resource and security solutions by launching new products and services. Shorter-sales cycle of these new products (particularly security solutions) as compared with the traditional ITSM business is driving top-line growth. The company is also focused on strengthening sales team across the different non-ITSM markets, which will expand customer base going ahead.
- ▲ ServiceNow has a diversified customer base, which is evident from the fact that none of the customers exceeded 10% of revenues in the last couple of years. Notably, the number of customers with annualized contract value (ACV) greater than \$1 million has also increased from 157 at the end of 2014 to 892 at the end of 2019. Given the company's expanding product portfolio (including emerging products), increasing multi-product customer base and strong renewal rate (almost 98%), we expect the company to achieve this target much earlier. ACV is also expected to improve from \$1 million in 2016 to \$2 million by 2020, which will help the company in achieving the top-line target of \$10 billion.
- ▲ Acquisitions have played an important part in ServiceNow's growth trajectory over the years. The acquisitions of Neebula Systems (2014), BrightPoint Security and ITapp (both in 2016) has aided the company to expand product portfolio, particularly security and ITOM solutions. Also in 2017, the company had acquired Qlue, a developer of virtual messaging agents. The buyout is expected to enhance its customer experience. The acquisitions of Telepathy and SkyGiraffe (both concluded in 2017) are expected to enhance the company's enterprise mobile experience. The acquisitions of DxContinuum (2017), Parlo (2018), FriendlyData (2018), Appsee (2019), Loom Systems (2020) and Passage AI (2020) are expected to boost its predictive modelling capabilities, consequently expanding ServiceNow's intelligent automation product portfolio going ahead.

Dominant position in the ITSM, ITOM markets, growing fortune 500 customer base, rapid growth in non-ITSM markets like HR, Security and product enhancements via strategic acquisitions are key catalysts.

Reasons To Sell:

- ▼ Stiff competition in non-ITSM product segments, modest growth in professional business, continuing losses, muted free cash flow growth and stretched valuation are key negatives.
- ▼ ServiceNow faces stiff competition in the non-ITSM markets from the likes of Oracle and salesforce.com, which are well-established players. Although the company has an edge in the security response market, the customer service and HR solutions faces significant competition from these players. As non-ITSM markets become a larger contributor to the company's total revenue, increasing competition can weigh on growth. Moreover, cut-throat competition can hurt pricing power as well as lengthen the sales cycle, which will negatively impact top-line.
- ▼ ServiceNow has been incurring losses over the last five years and has an accumulated deficit of \$950.97 million as of Sep 30, 2019. The company anticipates reporting loss in the near term due to increased costs such as non-cash charges associated with equity awards, business combinations and other expenses. Despite the improving top line, mounting losses doesn't bode well for investor confidence.
- ▼ ServiceNow generates a significant portion (35% in fourth-quarter 2019) of revenues from the International market. Adverse foreign currency exchange rates are likely to impede revenue growth in the near term owing to the strengthening of the U.S. dollar compared with the Euro and other foreign currencies, which is a significant concern.
- ▼ Moreover, the company is trading at a premium in terms of Price/Book (P/B). ServiceNow currently has a trailing 12-month P/B ratio of 44.81, which compares unfavorably to some extent with what the industry saw last year. Hence, the valuation looks slightly stretched from a P/B perspective.

Stiff competition in non-ITSM product segments, modest growth in professional business, continuing losses, muted free cash flow growth and stretched valuation are key negatives.

Last Earnings Report

Service Now's Q4 Earnings Beat, Revenues Rise Y/Y

Service Now reported fourth-quarter 2019 adjusted earnings of 96 cents per share, which beat the Zacks Consensus Estimate by 9.1% and increased 24.7% year over year.

Revenues of \$951.8 million beat the consensus mark by 1% and increased 33.1% year over year.

Moreover, non-GAAP revenues (excluding impact of foreign exchange) of \$960.4 million surged 34% from the year-ago quarter.

Quarter Ending **12/2019**

Report Date	Jan 29, 2020
Sales Surprise	1.00%
EPS Surprise	9.09%
Quarterly EPS	0.96
Annual EPS (TTM)	3.33

Quarter Details

Non-GAAP Subscription revenues (adjusted for constant currency) advanced 36% from the year-ago quarter to \$907 million.

Non-GAAP Professional services and other revenues improved 8% (adjusted for constant currency) from the year-ago quarter to \$53.3 million.

Total billings improved 35% on a year-over-year basis (adjusted for constant currency and constant billings duration) to \$1.365 billion.

Non-GAAP adjusted subscription billings of \$1.303 billion surged 37% year over year. Professional services and other billings increased 1% to \$61.4 million.

ServiceNow maintained consistent renewal rate of 97% during the reported quarter.

Additionally, the company completed 76 transactions that generated net new annualized contract value (ACV) exceeding \$1 million. Further, the company's total number of customers contributing more than \$1 million to business reached 892 in the fourth quarter. The figure surged 32% on a year-over-year basis.

The ongoing digital transformation of organizations, including big private and public companies, and different levels of government agencies, drove the company's growth during the quarter. ServiceNow's expanding global footprint was also a positive.

Product-Wise Break-Up of Top 20 New Wins

Out of top 20 new customer additions to the company's customer base in the fourth quarter, 19 included adoption of three or more products.

Considering the IT domain, IT Service Management (ITSM), IT Operations Management (ITOM), IT Asset Management (ITAM) and IT Business Management (ITBM) product lines witnessed adoption by 17, 15, five and 17 customers out of these 20 wins, respectively.

Further, the emerging products (EP) segment is comprised of Customer Service Management (CSM), HR Service Delivery (HR), Security Operations and Intelligent Apps (IA) product lines. In the reported quarter, out of the top 20 new deals, CSM, HR, Security and IA were part of six, eight, seven and 14 deals, respectively.

Meanwhile, Platform Add-ons and other services, comprising Performance Analytics, Cloud Options, among others, were leveraged by 18 customers out of the 20 wins.

Notably, IT, EP and Platform Add-ons contributed 57%, 30% and 13%, respectively to net new ACV.

Operating Details

In the fourth quarter, non-GAAP gross margin was 82%, up 200 basis points (bps) on a year-over-year basis.

The company's non-GAAP operating margin was 22%, expanding 100 bps on a year-over-year basis.

Balance Sheet & Cash Flow

As of Dec 31, 2019, ServiceNow had cash and cash equivalents and short-term investments of \$1.691 billion compared with \$1.471 billion as of Sep 30, 2019.

During the reported quarter, cash from operations came in at \$421.2 million compared with the prior-quarter figure of \$210 million. The company also generated free cash flow of \$342.2 million compared with \$121 million reported in the prior quarter.

Further, non-GAAP free cash flow margin was 36%, up 200 basis points on a year-over-year basis.

First-Quarter Guidance

For first-quarter 2020, non-GAAP adjusted subscription revenues are anticipated between \$978 million and \$983 million, indicating growth of 32%-33% from the year-ago quarter.

Non-GAAP adjusted subscription billings are projected within the range of \$1.042-\$1.047 billion, suggesting an improvement of 29% from the year-ago reported figure.

Further, non-GAAP operating margin is anticipated to be 22%.

2020 Guidance

For full-year 2020, non-GAAP adjusted subscription revenues are anticipated between \$4.21 billion and \$4.23 billion, indicating growth of 29%-30% from the year-ago quarter.

Non-GAAP adjusted subscription billings are projected within the range of \$4.807-\$4.827 billion, suggesting an improvement of 27% from the year-ago reported figure.

Further, non-GAAP operating margin is anticipated to be 22%.

Recent News

On Jan 28, 2020, ServiceNow inked a deal to acquire Passage AI, with an aim to improve its deep-learning AI capabilities.

On Jan 27, 2020, ServiceNow introduced a industry solutions strategy to deliver workflows that will aid customers in specific industries to facilitate their digital transformation process and create value at scale.

On Jan 22, 2020, ServiceNow inked a deal to acquire Loom Systems, with an aim to improve its AIOps capabilities.

On Nov 19, 2019, it was reported that ServiceNow will replace Celgene to join S&P 500 on Nov 21.

On Nov 18, 2019, ServiceNow announced appointment of Gina Mastantuono as Chief Financial Officer, effective Jan 13, 2020.

On Oct 22, 2019, ServiceNow declared that Bill McDermott is set to join ServiceNow as CEO, president and a member of the board of directors, by end of 2019.

On Sep 24, 2019, ServiceNow introduced two latest certified ServiceNow applications, namely BitSight for Security Incident Response and BitSight for Vendor Risk Management. The latest applications offer robust automation of digital workflows, enabling customers to identify cyber risks and assess security performance.

On Sep 18, 2019, ServiceNow's GovCommunityCloud achieved FedRAMP High Impact Provisional Authority to Operate (P-ATO). The certification will aid federal agencies in adopting cloud-based solutions in a secure manner.

Valuation

ServiceNow shares are up 24.7% in the past six-month period and 54.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and Zacks Computer & Technology sector are up 3.2% and 15.6%, respectively, in the past six-month period. Over the past year, the Zacks sub-industry and sector are up 18.8% and 28.5%, respectively.

The S&P 500 index is up 11.7% in the past six-month period and 20.4% in the past year.

The stock is currently trading at 14.22X forward 12-month sales, which compares to 5.30X for the Zacks sub-industry, 3.67X for the Zacks sector and 3.49X for the S&P 500 index

Over the past five years, the stock has traded as high as 15.81X and as low as 5.38X, with a 5-year median of 9.86X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$359 price target reflects 14.94X forward 12-month sales.

The table below shows summary valuation data for NOW

Valuation Multiples - NOW					
		Stock	Sub-Industry	Sector	S&P 500
P/S F 12M	Current	14.22	5.30	3.67	3.49
	5-Year High	15.81	10.29	3.67	3.49
	5-Year Low	5.38	4.34	2.30	2.54
	5-Year Median	9.86	7.43	3.01	3.00
P/B TTM	Current	44.81	16.70	5.56	4.49
	5-Year High	44.95	31.78	5.63	4.55
	5-Year Low	13.22	7.05	3.13	2.85
	5-Year Median	36.26	9.84	4.22	3.62
EV/Sales TTM	Current	18.13	5.34	4.36	3.29
	5-Year High	18.62	8.12	4.36	3.30
	5-Year Low	6.66	4.16	2.56	2.16
	5-Year Median	12.61	5.93	3.46	2.80

As of 01/31/2020

Industry Analysis Zacks Industry Rank: Top 44% (113 out of 255)



Top Peers

Fair Isaac Corporation (FICO)	Outperform
Inovalon Holdings, Inc. (INOV)	Outperform
ASGN Incorporated (ASGN)	Neutral
CDW Corporation (CDW)	Neutral
Amdocs Limited (DOX)	Neutral
DXC Technology Company. (DXC)	Neutral
EPAM Systems, Inc. (EPAM)	Neutral
Infosys Limited (INFY)	Neutral

Industry Comparison Industry: Computers - It Services				Industry Peers		
	NOW Neutral	X Industry	S&P 500	CDW Neutral	DOX Neutral	EPAM Neutral
VGM Score	C	-	-	A	B	C
Market Cap	64.05 B	3.43 B	23.91 B	19.23 B	9.92 B	12.75 B
# of Analysts	13	4	13	7	5	9
Dividend Yield	0.00%	0.00%	1.77%	1.14%	1.55%	0.00%
Value Score	F	-	-	B	C	D
Cash/Price	0.03	0.06	0.04	0.01	0.05	0.07
EV/EBITDA	177.13	12.18	14.07	17.85	12.18	42.17
PEG Ratio	2.86	1.99	2.00	1.56	1.92	1.79
Price/Book (P/B)	30.10	5.47	3.27	20.56	2.80	8.53
Price/Cash Flow (P/CF)	111.10	14.38	13.48	19.15	12.91	48.55
P/E (F1)	80.00	20.44	18.76	20.44	16.29	35.77
Price/Sales (P/S)	18.51	1.54	2.61	1.09	2.43	5.89
Earnings Yield	1.25%	2.81%	5.32%	4.89%	6.14%	2.79%
Debt/Equity	0.51	0.23	0.72	3.57	0.00	0.12
Cash Flow (\$/share)	3.07	1.39	6.88	6.99	5.70	4.78
Growth Score	A	-	-	A	B	B
Hist. EPS Growth (3-5 yrs)	NA%	16.94%	10.68%	21.73%	6.12%	26.81%
Proj. EPS Growth (F1/F0)	28.61%	9.62%	7.73%	9.01%	4.83%	20.91%
Curr. Cash Flow Growth	49.82%	14.90%	12.29%	19.83%	2.45%	38.99%
Hist. Cash Flow Growth (3-5 yrs)	114.97%	18.94%	8.78%	14.79%	3.85%	26.61%
Current Ratio	1.03	1.32	1.23	1.33	1.39	4.38
Debt/Capital	33.63%	33.63%	43.16%	78.13%	0.00%	10.71%
Net Margin	18.11%	2.62%	11.59%	4.04%	11.73%	11.38%
Return on Equity	7.60%	11.38%	17.38%	91.07%	15.98%	18.44%
Sales/Assets	0.70	0.81	0.54	2.31	0.78	1.17
Proj. Sales Growth (F1/F0)	28.35%	8.61%	4.05%	5.65%	3.15%	23.04%
Momentum Score	C	-	-	B	B	D
Daily Price Chg	9.17%	0.13%	-0.21%	-0.76%	0.20%	-0.65%
1 Week Price Chg	-1.00%	-1.00%	-1.09%	0.78%	-0.32%	-2.09%
4 Week Price Chg	17.30%	0.00%	-0.01%	-6.99%	1.56%	7.22%
12 Week Price Chg	41.82%	9.57%	4.14%	0.68%	10.65%	21.88%
52 Week Price Chg	55.27%	6.00%	17.24%	60.72%	31.67%	63.92%
20 Day Average Volume	1,796,955	233,468	1,824,613	1,006,513	745,285	237,600
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.36%	0.00%	0.37%
(F1) EPS Est 12 week change	0.00%	-0.54%	-0.11%	0.36%	-0.70%	2.30%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.19%	0.00%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	F
Growth Score	A
Momentum Score	B
VGM Score	C

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.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.