

Oracle Corp. (ORCL)

\$55.44 (As of 02/13/20)

Price Target (6-12 Months): **\$60.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/18/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:C

Value: B

Growth: D

Momentum: D

Summary

Oracle is benefiting from strong adoption of cloud-based solutions, comprising NetSuite ERP, Fusion ERP and Fusion HCM among others. In fact, momentum witnessed in cloud services is a key upside. Going ahead, the company is expected to reap benefits from rising adoption of SaaS. Moreover, strong demand for the latest autonomous database supported by ML is likely to drive the top line. It will also provide a competitive edge against Amazon Web Services (AWS) in the Database-as-a-Service market. However, stiff competition in the cloud market from dominant players is anticipated to put pressure on profitability. Further, lower hardware volumes are expected to hurt the top line. Additionally, integration risks from buyouts remain a concern. Notably, shares of Oracle have underperformed the industry in the past year.

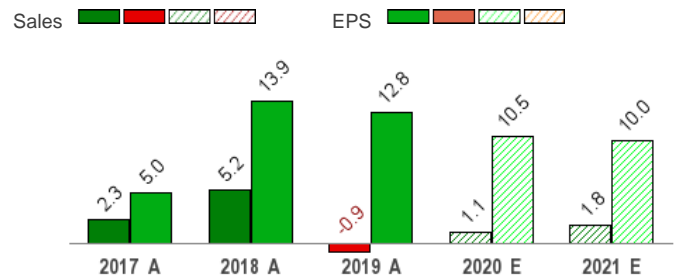
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$60.50 - \$49.89
20 Day Average Volume (sh)	7,763,022
Market Cap	\$177.4 B
YTD Price Change	4.4%
Beta	1.11
Dividend / Div Yld	\$0.96 / 1.7%
Industry	Computer - Software
Zacks Industry Rank	Top 22% (55 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	2.3%
Last Sales Surprise	-0.2%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	03/12/2020
Earnings ESP	0.0%
P/E TTM	14.8
P/E F1	14.3
PEG F1	1.5
P/S TTM	4.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	9,399 E	9,798 E	9,918 E	11,435 E	40,662 E
2020	9,220 A	9,615 A	9,765 E	11,349 E	39,949 E
2019	9,201 A	9,567 A	9,618 A	11,139 A	39,526 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.91 E	\$0.98 E	\$1.04 E	\$1.32 E	\$4.28 E
2020	\$0.81 A	\$0.90 A	\$0.96 E	\$1.23 E	\$3.89 E
2019	\$0.71 A	\$0.80 A	\$0.87 A	\$1.16 A	\$3.52 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 02/13/2020. The reports text is as of 02/14/2020.

Overview

Redwood City, CA-based Oracle Corporation was founded in 1977 and incorporated later in 2005. Oracle is one of the largest enterprise-grade database, middleware and application software providers. With the acquisition of Sun Microsystems in Jan 2010, Oracle began selling hardware products and services, primarily comprising computer server and storage products. Oracle's software and hardware products and services include Oracle Database, Oracle Fusion Middleware, Java and Oracle Engineered Systems. Oracle Engineered Systems include Exadata Database Machine, Exalogic Elastic Cloud, Exalytics In-Memory Machine, SPARC SuperCluster, Virtual Compute Alliance, Oracle Database Appliance, Oracle Big Data Appliance and ZFS Storage.

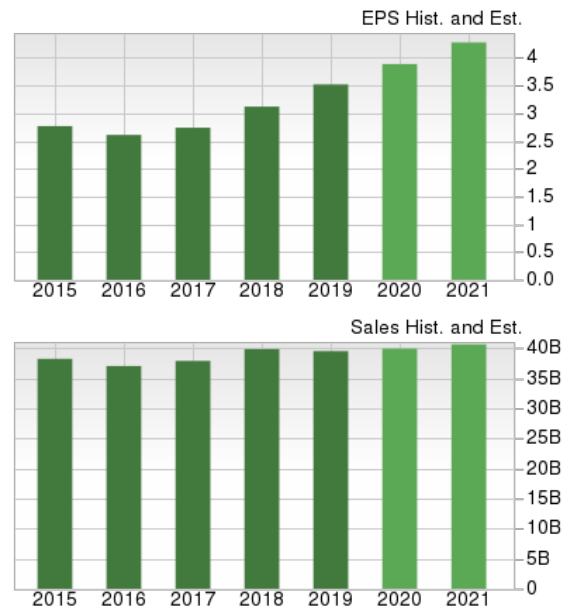
The company market and sell offerings worldwide to businesses of many sizes, government agencies, educational institutions and resellers with a global sales force to offer solutions that best meet customer requirements.

Oracle has expanded its cloud computing operations over the last couple of years. The company offers cloud solutions and services that can be used to build and manage various cloud deployment models. Built upon open industry standards such as SQL, Java and HTML5, Oracle Cloud provides access to application services, platform services and infrastructure services for a subscription. Through its Oracle Enterprise Manager offering, the company manages cloud environments.

Oracle reported revenues of \$39.5 billion in fiscal 2019. The company changed its reporting format in the fourth-quarter. The company has adopted a new Accounting Standards Codification ("ASC") 606 using full retrospective method. It now reports its new software licenses under its new Cloud license and on-premise license segment. Further, the company merged its Cloud SaaS, Cloud PaaS and IaaS along with its software license updates and product support into Cloud services and license support.

Total cloud services and license support revenues increased 2% to \$26.71 billion in fiscal 2019. Further, total cloud license and on-premise license increased 1% to \$5.86 billion year over year in fiscal 2019.

Oracle faces significant competition in most of its operational markets (database, applications, storage, cloud computing) from the likes of Dell-EMC, IBM, Hewlett-Packard, Microsoft, SAP, Salesforce.com, Workday and Teradata.



Reasons To Buy:

- ▲ Oracle is gaining ground in its **cloud business**. Both its software-as-a-service (SaaS) and platform-as-a-service (PaaS) products should grow very strongly over the next few years as enterprises increasingly transition to the cloud. Bookings are also picking up. According to latest IDC market report, SaaS will remain the dominant cloud computing type, representing more than half of all public cloud spending through 2023. In fact, according to Gartner, SaaS is expected to grow nearly \$116 billion in 2020. Overall, we believe that Oracle's new cloud-based offerings hold promise. Moreover, the cloud services offering has opened up a new source of recurring revenues (subscriptions), which is expected to improve visibility. Oracle is expected to benefit from the ongoing in-premise to cloud transitions leveraging its new technological developments. Additionally, the company is witnessing strong growth in Cloud HCM, which is being purchased as a part of an ERP cloud application suite. Also, the migration of several midsized SAP customers to Fusion ERP is an upside.
- ▲ Oracle enjoys a dominant position in the **enterprise software and database management system (DBMS)** software market. Markedly, the company's enormous strength in cloud technology has been a key force behind growth in database business. Among infrastructure, DBMS is expected to record strong growth driven by Big Data and digitalization initiatives. We believe that Oracle's leading position in the DBMS software market will make it the primary beneficiary of this increased spending. We expect the 12c multi-tenant, In-Memory database system to help the company win new customers and drive sales in the long run. Moreover, the company's low-cost engineered systems (Oracle Virtual Compute Appliance) are also expected to attract price-sensitive customers in the long run. The latest autonomous database supported by machine learning is also expected to boost competitive position against the likes of AWS. The next-generation autonomous database launched by Oracle, supported by ML, is also gaining traction. During the second quarter of fiscal 2020, Oracle added around 2,000 new Autonomous Database cloud customers. New product introductions are likely to boost growth in this category. Markedly, autonomous database in Gen2 Infrastructure is witnessing rapid adoption.
- ▲ Oracle remains very active on the **acquisition** front and chooses companies that can be easily integrated within its existing or new product lines. From time to time, the company also acquires organizations with competing technologies with the intention of killing rival products. The NetSuite acquisition helped the company to fast penetrate the ERP and small & medium companies' segment. Acquisitions like Maxymiser and CloudMonkey helped Oracle in developing cloud-based software and testing tools & platforms for mobile apps. To-date, it's most important acquisition remains that of Sun, which helped it to enter the hardware market. In the last 10 years, management has spent more than \$50 billion to acquire 100 companies. Over the last three years, the company has aggressively pursued acquisitions that will boost its presence in the cloud computing and database markets. We believe that Oracle will continue to pursue strategic acquisitions to improve its market share and top line in the long haul. Apart from these, Oracle also boasts partnerships with Accenture and Microsoft for better harnessing cloud capabilities and expanding its clientele.
- ▲ Oracle's **strong cash balance** enables it to pursue share repurchases and make consistent dividend payments. Oracle repurchased shares worth approximately \$5 billion during the second-quarter fiscal 2020, and paid out dividends worth nearly \$1.562 billion during the first half of the fiscal. Over the last 12 months, the company repurchased 500 million shares worth \$26 billion. Due to strong and relatively stable cash flow, the aggressive share repurchase activity and dividend payout appear sustainable and make the stock quite attractive, in our view.

Oracle's growing cloud business and the latest autonomous database is expected to boost competitive position in the long haul.

Reasons To Sell:

- ▼ Although engineered systems are expected to drive growth, we believe that lower hardware volumes will continue to hurt Oracle's top-line growth over the next couple of years. Moreover, hardware is significantly a **lower-margin business** that will keep margins under pressure, going forward. Moreover, despite Oracle's growing cloud business, we believe that the business model transition will hurt revenue growth over the next couple of years. The company expects to gain a significant part of its revenues from SaaS compared with legacy on-premise licensing business. However, SaaS revenues will not be recognized upfront as in the case of license business, which will hurt top-line growth in the near term.
- ▼ Acquisitions have played an important part in Oracle's growth trajectory over the years. Being a **late entrant** in the cloud computing space, the company is trying to build its position through aggressive acquisitions. The company is making significant investment in these acquisitions in order to catch up with AWS, Salesforce and IBM. As the SaaS market is getting overcrowded, we believe that all acquisitions may not perform as per company expectations, which will eventually hurt profitability. Moreover, large acquisitions can negatively impact the company's balance sheet in the form of a high level of goodwill and intangible assets.
- ▼ Oracle faces **significant competition** in most of its operational markets (database, applications, storage, cloud computing) from the likes of Dell-EMC, IBM, Hewlett-Packard, Microsoft, SAP, Salesforce.com, Workday and Teradata. The trend toward consolidation is increasing competition for the company in most of these markets. To differentiate products here, large vendors are entering into alliances or partnerships to offer integrated and differentiating solutions. As a result, Oracle continues to face severe pricing pressure and lengthy sales cycles in its core business, which is hurting profitability. Moreover, stiff competition in the cloud is expected to hurt margins and will make revenue growth difficult to come by over the long run.
- ▼ Oracle has been embroiled in various **legal tangles**. In 2016, Oracle faced defeat in two of its most high profile lawsuits. In May 2016, a 10 member jury found no violations of JAVA APIs by Alphabet thus dismissing Oracle's \$9 billion claim. Moreover, a California Court held Oracle liable of paying Hewlett Packard Enterprise \$3 billion in damages for withdrawing support to titanium software. The company is hell bent on re-appealing against these verdicts. In December 2017, the company renewed the legal fight over Android against Alphabet. In the recent filing Oracle challenged the idea of "fair use," and alleged that Google lied when it said Android didn't compete directly with Oracle's ability to license its own products to customers. Moreover, lawsuit expenses pertaining to U.S. Department of Defense's (DoD) Joint Enterprise Defense Infrastructure (JEDI) cloud contract does not bode well for Oracle's business opportunities with DoD. This is likely to weigh on the company's bottom line and might impact the stock performance. We believe such high legal risks, if materialized, might wreak havoc on the company's financials.

Stiff competition, lawsuits and currency volatility are likely to impact Oracle as it transitions from licensing to cloud.

Last Earnings Report

Oracle's Q2 Earnings Beat Estimates, Revenues Miss

Oracle reported second-quarter fiscal 2020 non-GAAP earnings of 90 cents per share, which beat the Zacks Consensus Estimate by 2.3%. However, non-GAAP revenues of \$9.615 billion missed the Zacks Consensus Estimate by 0.2%.

Nonetheless, the bottom line increased 12% from the year-ago quarter's reported figure (up 13% in constant currency). The top line also inched up 1% (in USD and at cc) year over year.

Quarter Ending **11/2019**

Report Date	Dec 12, 2019
Sales Surprise	-0.15%
EPS Surprise	2.27%
Quarterly EPS	0.90
Annual EPS (TTM)	3.74

Top Line in Detail

Oracle reported total revenues (on a GAAP basis) of \$9.614 billion, up 1% (in USD and at cc) year over year.

Revenues by Offerings

Oracle's top line benefited from the ongoing cloud-based momentum. Cloud services and license support revenues (71% of total revenues) in the reported quarter rose 3% year over year (up 4% in cc) to \$6.811 billion.

Meanwhile, cloud license and on-premise license revenues (12% of total revenues) declined 7% year over year (down 7% in cc) to \$1.126 billion.

Hardware revenues (9% of total revenues) were \$871 million, down 2% (down 1% in cc) year over year.

Services revenues (8% of total revenues) inched down 1% to \$806 million (flat at cc).

Revenues by Geography

Revenues from Americas (represented 55.2% of total revenues) dropped 1.2% year over year to \$5.304 billion.

Revenues from Europe/Middle East/Africa (28%) declined 3.1% from the year-ago quarter's figure to \$2.695 billion.

However, revenues from Asia Pacific (16.8%) improved 5% from the year-ago quarter's level to \$1.615 billion.

Break up of Cloud and License Revenues

Oracle reported total cloud and license revenues of \$7.937 billion, which inched up 1% from the year-ago quarter's level.

Applications revenues (contributed 37% to total cloud and license revenues) amounted to \$2.909 billion, up 4% year over year.

Infrastructure related revenues (63%) came in at \$5.028 billion, flat year over year.

Customer Expansion Bodes Well

Management announced that NetSuite ERP and Fusion ERP businesses were up 29% and 37% in fiscal second quarter, respectively. NetSuite ERP and Fusion ERP have customer strength of around 20,000 and 7,000, respectively.

Expanding customer base is enabling the company to maintain leading position in cloud ERP market.

Additionally, the company is witnessing strong growth in Cloud HCM, which is increasingly being purchased as a part of an ERP cloud application suite. Also, the migration of several mid-sized SAP customers to Fusion ERP is an upside.

Further, the next-generation autonomous database launched by Oracle, supported by ML, is gaining traction.

In the reported quarter, Oracle added around 2,000 new Autonomous Database cloud customers. New product introductions are likely to further boost growth in this category. Markedly, autonomous database in Gen2 Infrastructure is witnessing rapid adoption.

The company is undertaking every effort to enhance functionalities of cloud-based applications, which is encouraging adoption. These initiatives are expected to provide the company an edge in the Database-as-a-Service market and reinforce its competitive position against Amazon Web Services.

Operating Details

Non-GAAP operating expenses increased 2% year on year to \$5.573 billion.

Non-GAAP operating income during the reported quarter was \$4.042 billion, down 1% year over year.

Non-GAAP operating margin contracted 100 bps year over year and came in at 42%.

Balance Sheet & Cash Flow

As of Nov 30, 2019, Oracle had cash & cash equivalents, and marketable securities of \$27.4 billion, down from \$35.7 billion sequentially.

Operating cash flow for the 12 months ended Nov 30, 2019 was \$13.8 billion while free cash flow was \$12.2 billion.

Share Repurchases & Dividends

Oracle repurchased shares worth approximately \$5 billion during the fiscal second quarter, and paid out dividends worth approximately \$1.562 billion during the first half of the fiscal.

The company declared a quarterly dividend of 24 cents per share, payable on Jan 23, 2019, to shareholders as on Jan 9, 2019.

Q3 Guidance

For fiscal third quarter, Oracle expects non-GAAP revenues to rise in the range of 1-3%, both at USD and cc. The guidance assumed currency headwind of 1%.

Oracle expects non-GAAP earnings per share in the range of 96-98 cents in cc (and 95-97 cents excluding currency impact).

Recent News

On **Feb 12, 2020**, Oracle rolled out Oracle Cloud Data Science Platform, to aid enterprises to devise, train, manage and deploy machine learning models, to boost data science projects.

On **Jan 15, 2019**, Oracle announced enhancements to its Oracle Enterprise Manager platform for enabling customers to easily shift Oracle Databases to the cloud, as well as simplify management of hybrid cloud environments.

On **Jan 9, 2020**, Oracle Cloud Applications was chosen by Blue Nile — a leading online diamond jeweler. By utilizing Oracle's cloud solutions, Blue Nile is able to streamline financial operations, alongside boosting customer's shopping experience.

On **Dec 27, 2019**, Oracle announced that its Cloud Applications are now live in the Gen 2 cloud region in Mumbai. As a result, the company's Cloud Application can be leveraged by existing and new customers. The move reflects continued momentum for Oracle's cloud business in India.

On **Nov 14, 2019**, Oracle announced that the U.S. Department of Defense (DoD) and Defense Information Systems Agency (DISA) have granted Oracle Cloud Applications with Impact Level 4 (IL4) Provisional Authorization. Moreover post receiving IL4 authorization, Oracle Human Capital Management (HCM) Cloud has been selected by the DoD.

On **Nov 12, 2019**, Oracle announced that New York Burger has selected Oracle MICROS Symphony Point of Sale (POS) System to reduce customer wait-time in its five restaurants.

Valuation

Oracle shares are up 6.1% in the past six-month period and 8.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are up 29.1% and 26.6% in the past six-month period, respectively. Over the past year, the Zacks sub-industry and the sector are up 47.4% and 31.2%, respectively.

The S&P 500 index is up 20.1% in the past six-month period and 23.4% in the past year.

The stock is currently trading at 13.29X forward 12-month earnings, which compares to 30.54X for the Zacks sub-industry, 23.2X for the Zacks sector and 19.37X for the S&P 500 index.

Over the past five years, the stock has traded as high as 19.31X and as low as 13.11X, with a 5-year median of 15.56X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$60 price target reflects 14.42X forward 12-month earnings.

The table below shows summary valuation data for ORCL

Valuation Multiples - ORCL					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	13.29	30.54	23.20	19.37
	5-Year High	19.31	30.54	23.20	19.37
	5-Year Low	13.11	18.59	16.87	15.18
	5-Year Median	15.56	24.45	19.32	17.47
P/S F12M	Current	4.39	7.66	3.79	3.57
	5-Year High	5.72	7.66	3.79	3.57
	5-Year Low	3.76	3.88	2.3	2.54
	5-Year Median	4.64	5.30	3.02	3
EV/Sales TTM	Current	5.07	8.19	4.50	3.11
	5-Year High	5.43	8.19	4.50	3.27
	5-Year Low	3.47	3.19	2.56	2.15
	5-Year Median	4.56	5.27	3.47	2.77

As of 02/13/2020

Industry Analysis Zacks Industry Rank: Top 22% (55 out of 255)



Top Peers

Microsoft Corporation (MSFT)	Outperform
SAP SE (SAP)	Outperform
Adobe Systems Incorporated (ADBE)	Neutral
salesforce.com, inc. (CRM)	Neutral
International Business Machines Corporation (IBM)	Neutral
Intel Corporation (INTC)	Neutral
VMware, Inc. (VMW)	Neutral
Hewlett Packard Enterprise Company (HPE)	Underperform

Industry Comparison Industry: Computer - Software				Industry Peers		
	ORCL Neutral	X Industry	S&P 500	ADBE Neutral	IBM Neutral	MSFT Outperform
VGM Score	C	-	-	C	B	C
Market Cap	177.42 B	2.05 B	24.56 B	180.72 B	136.66 B	1,397.31 B
# of Analysts	13	4	13	13	8	14
Dividend Yield	1.74%	0.00%	1.78%	0.00%	4.20%	1.11%
Value Score	B	-	-	D	B	D
Cash/Price	0.16	0.10	0.04	0.02	0.08	0.10
EV/EBITDA	11.62	23.77	14.00	43.32	11.32	22.97
PEG Ratio	1.45	2.42	2.10	2.35	2.11	2.46
Price/Book (P/B)	10.96	5.79	3.31	17.23	7.55	12.69
Price/Cash Flow (P/CF)	12.54	27.97	13.68	45.77	8.18	28.92
P/E (F1)	14.25	33.91	19.23	38.25	11.55	32.58
Price/Sales (P/S)	4.48	4.93	2.69	16.18	1.77	10.41
Earnings Yield	7.03%	2.79%	5.20%	2.61%	8.66%	3.07%
Debt/Equity	3.13	0.18	0.71	0.09	3.40	0.64
Cash Flow (\$/share)	4.41	1.01	6.92	8.19	18.86	6.35
Growth Score	D	-	-	A	D	C
Hist. EPS Growth (3-5 yrs)	6.17%	10.54%	10.85%	52.77%	-3.50%	17.68%
Proj. EPS Growth (F1/F0)	10.47%	13.10%	7.17%	24.51%	4.30%	18.72%
Curr. Cash Flow Growth	-0.35%	7.45%	8.56%	27.62%	-1.93%	19.70%
Hist. Cash Flow Growth (3-5 yrs)	-1.03%	7.84%	8.36%	41.64%	-5.41%	11.99%
Current Ratio	2.37	1.49	1.23	0.79	1.09	2.80
Debt/Capital	75.79%	18.94%	42.91%	8.59%	77.29%	39.05%
Net Margin	27.62%	6.51%	11.81%	26.42%	12.23%	33.02%
Return on Equity	56.86%	12.71%	16.86%	31.47%	65.38%	40.41%
Sales/Assets	0.37	0.64	0.54	0.56	0.53	0.48
Proj. Sales Growth (F1/F0)	1.07%	7.63%	3.85%	17.68%	1.89%	13.11%
Momentum Score	D	-	-	F	D	A
Daily Price Chg	-0.75%	0.00%	0.00%	0.15%	-0.64%	-0.54%
1 Week Price Chg	4.33%	0.00%	2.47%	4.26%	6.73%	8.02%
4 Week Price Chg	-0.22%	1.48%	0.56%	8.53%	11.84%	10.56%
12 Week Price Chg	-1.64%	8.08%	6.96%	25.45%	15.29%	22.90%
52 Week Price Chg	7.44%	24.87%	16.68%	44.09%	13.06%	71.85%
20 Day Average Volume	7,763,022	66,338	2,020,569	2,159,417	6,817,420	32,541,760
(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%	-0.05%	0.00%	1.15%	5.25%
(F1) EPS Est 12 week change	0.49%	-1.18%	-0.17%	-0.51%	1.34%	5.49%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	-0.24%	0.00%	-8.66%	7.07%

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	B
Growth Score	D
Momentum Score	D
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.

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