

Pure Storage Inc.(PSTG)

\$14.00 (As of 05/13/20)

Price Target (6-12 Months): **\$15.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/19/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: F

Growth: A

Momentum: D

Summary

Pure Storage is banking on robust adoption of cloud storage solutions, including Cloud Block Store, ObjectEngine Cloud, and CloudSnap. Moreover, the company continues to enhance all-flash portfolio including AIRI, FlashArray, FlashBlade and FlashStack offerings with new low-latency and high-bandwidth support capabilities, which is a positive. Furthermore, the company is well poised to benefit from incremental adoption of latest subscription-based Evergreen, Modern Data Experience and Pure as-a-Service solutions. Nevertheless, tough business environment due to coronavirus crisis led lockdowns, remains a concern. Further, growing expenses on product development amid stiff competition NetApp and Dell is a headwind. Notably, shares have underperformed the industry in the past year.

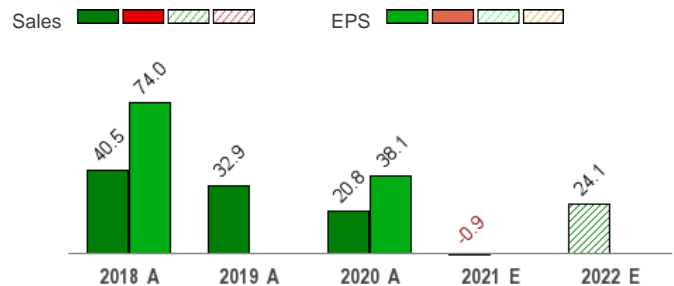
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$21.16 - \$7.93
20 Day Average Volume (sh)	3,093,808
Market Cap	\$3.7 B
YTD Price Change	-18.2%
Beta	1.59
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Computer- Storage Devices
Zacks Industry Rank	Bottom 48% (131 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.6%
Last Sales Surprise	0.6%
EPS F1 Est- 4 week change	-2.7%
Expected Report Date	05/28/2020
Earnings ESP	14.9%
P/E TTM	53.9
P/E F1	NA
PEG F1	NA
P/S TTM	2.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	411 E	474 E	519 E	577 E	2,020 E
2021	342 E	380 E	438 E	519 E	1,628 E
2020	327 A	396 A	428 A	492 A	1,643 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	-\$0.10 E	\$0.03 E	\$0.12 E	\$0.23 E	\$0.17 E
2021	-\$0.16 E	-\$0.11 E	\$0.01 E	\$0.17 E	-\$0.11 E
2020	-\$0.11 A	\$0.01 A	\$0.13 A	\$0.23 A	\$0.29 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 05/13/2020. The reports text is as of 05/14/2020.

Overview

Founded in 2009 and headquartered in Mountain View, CA, Pure Storage Inc. (PSTG) provides software-defined all-flash solutions that are uniquely fast and cloud-capable for customers. The company is the pioneer of Evergreen Storage business model of hardware and software innovation, support and maintenance, which eliminate the 3–5 year forklift refresh cycle of legacy storage systems.

Pure Storage's primary offerings are FlashArray and FlashBlade products, which include Purity Operating Environment (Purity OE) software, Pure1 cloud-based software, and FlashStack, the company's joint converged infrastructure solution with Cisco.

Notably, in 2018, the company had launched Cloud Data Services, a suite of new cloud offerings that aids customers to invest in single storage architecture. This data platform helps customers scale their businesses through real-time and accurate analytics, hereby increasing operational efficiency and enhancing user experience.

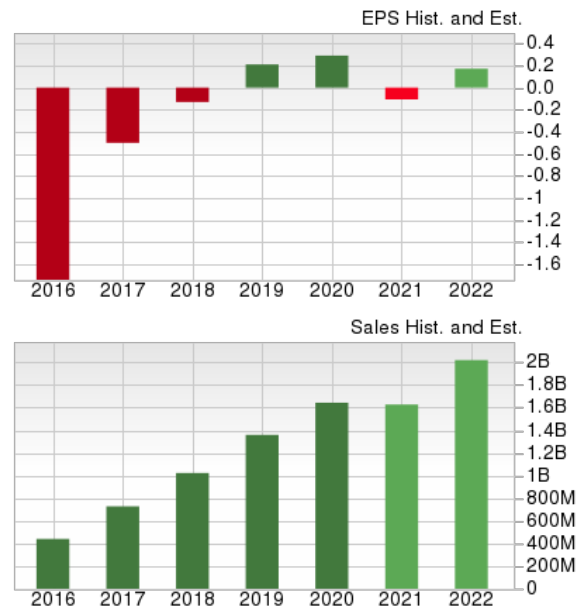
The company's platforms are designed to maximize the performance of flash, by taking advantage of native high bandwidth and low latency PCIe/NVMe networking.

Pure Storage became a public company in Oct 2015. The company's customer base comprised around 7,500 organizations, including more than 40% of the Fortune 500. The company's customers includes enterprise and commercial organizations, cloud, Global Systems Integrators, consumer web, education, energy, financial services, governments, healthcare, manufacturing, media, retail and telecommunications.

The company reported revenues of \$1.643 billion in fiscal 2020.

Product revenues amounted to 75.4% of the total revenues, while Support contributed the rest of 24.6%.

Pure Storage faces significant competition from the likes of Hitachi, NetApp, Dell EMC, HP Enterprise, Lenovo and IBM.



Reasons To Buy:

- ▲ Adoption of flash storage is increasing rapidly, particularly at enterprises, due to inherent advantages of speed (i.e. responsiveness), portability, efficiency and reliability over legacy storage systems. Moreover, ongoing data explosion has become a major driver for flash storage systems. Market research firm IDC forecasts that by 2025, the global datasphere will grow to 175 zettabytes (that is a trillion gigabytes) compared with 33 zettabytes (ZB) generated in 2018. More importantly, almost 49% of this will be stored in the public cloud infrastructure. Due to the high performance and low latency features of flash-storage, it is the ideal storage technology to harness this data explosion. We believe that being a pure-play flash storage provider Pure Storage is well-positioned to benefit from this trend. Shared storage (including NAS/SAN/Object/ Backup appliance) has a total addressable market (TAM) of almost \$26 billion, which presents growth opportunities. The company's expanding product portfolio that includes platforms like NVMe, Purity FlashBlade, 75 blades up to 8 PB of storage, Object Storage, and Active Cluster, Cloud solutions that run on AWS holds promise.
- ▲ All-Flash Arrays (AFA) is gradually becoming the preferred storage choice of data-center operators as they have become more cost-effective as compared with traditional data storage systems. Moreover, usage of flash arrays lowers power consumption that reduces data center operating expenses (low electricity bill) over the long term. AFAs also require less space and they usually have a simpler user interface which makes management of the systems easy. These features are driving top-line growth. Gartner placed the company in the leader's quadrant in its latest Magic Quadrant for Primary Storage. We note that Pure Storage is regarded as a pioneer of the all-flash array category and the solid growth projections bodes well for long-term growth.
- ▲ The company is fast gaining traction in the flash storage market, which is evident from its accelerating customer base. Customer growth have been exemplary – count surging from 300 in first-quarter fiscal 2015 to 4,800 in first-quarter fiscal 2019 – a CAGR of 100%. During the fourth quarter of fiscal 2020, Pure Storage added more than 500 customers, bringing the total count to more than 7,500 organizations. Increasing spending from top 25 customers is a major growth driver. Improving penetration into Global 2000 and Fortune 500 is also worth watching. We believe that customer base will continue to expand driven by the impressive product portfolio, innovative pipeline, strong partner base and growth potential from an almost untapped sales force (almost 60% has < 15 months tenure). Moreover, robust demand for FlashArray and FlashBlade products is projected to boost the top line.
- ▲ Pure Storage is targeting the 500 leading cloud providers to boost top-line growth. Moreover, increasing demand for flash storage (due to improving affordability) in the small and medium business (SMB) segment presents significant growth opportunity. The company also sees strong growth prospects in the data-driven markets of artificial intelligence (AI), machine learning, Internet of Things (IoT), Real-time Analytics, Log Analytics and Simulation. The company cited IDC data, which predicts that the cloud storage market will hit \$6 billion in fiscal 2020, witnessing a CAGR of 32%. The company's FlashBlade product has been gaining traction in the AI market. Additionally, the Pure1 META platform – which enables customers to forecast performance requirements to more accurately and timely provision of resources – has significant growth prospect over the long term.
- ▲ The company has a rich partner ecosystem, which is a growth driver. Its partnership with Cisco for FlashStack is worth mentioning. We believe that the hyper-converged solution will continue to gain traction among enterprises going forward. We believe that the expanding partner base, including NVIDIA will further drive customer base.
- ▲ The company has a strong balance sheet with no long-term debt. This is expected to help it in capitalizing on investment opportunities and pursuing strategic business expansion initiatives, further improving growth prospects. Pure Storage exited the quarter ended Feb 2, 2020 with cash, cash equivalents and marketable securities of \$1.299 billion, up from \$1.24 billion as of Oct 31, 2019. Cash flow from operations during the reported quarter was \$69.9 million compared with \$64.3 million in the fiscal third quarter. Free cash flow came in at \$56.2 million compared with \$45.6 million in the prior quarter.
- ▲ Pure Storage has a strong balance sheet with ample liquidity position and no debt obligations. Cash, short-term investments and marketable securities were \$1.299 billion as of Feb 2, 2020, compared with \$1.24 billion as of Oct 31, 2019. Moreover, the company generated \$69.9 million of cash flows from operations in the fiscal fourth quarter compared with \$64.3 million in the previous quarter. Free cash flow came in at \$56.2 million in the fiscal fourth quarter compared with \$45.6 million in the prior quarter. It is to be noted that the company has been able to regularly increase its cash and marketable securities, as well as its cash from operations since 2014. The increasing liquidity and cash flow trend reflect that the company is making investments in the right direction. Moreover, since it carries no long-term debt, the cash is available for pursuing strategic acquisitions, investment in growth initiatives and distribution to shareholders.

Growing adoption of flash storage, advantages of AFA in data centers, impressive product portfolio, strong partner base and growth prospect in emerging data-driven markets are key positives.

Reasons To Sell:

- ▼ Pure Storage faces intensifying competition in the flash-based storage market. The competition has resulted in a decline in the average selling price (ASP). Any decline in ASP is likely to impact the results if shipments do not improve considerably.
- ▼ Moreover, lack of big-shot international customers is a headwind for the company. We note that revenues from customers outside the U.S. were 28% in fiscal 2019. The company doesn't have significant presence in the Asia-Pacific market, which has strong demand for flash-based storage systems. This is a headwind in our view.
- ▼ Further, Pure Storage has been incurring operating losses since inception and has an accumulated deficit of \$1.283 billion as of Feb 2, 2020. The company does not expect to generate profit sooner amid continuing investments on research & development and sales & marketing. Despite the increasing top line, mounting losses doesn't augur well for investor confidence in our view.
- ▼ The company is trading at premium in terms of Price/Book (P/B). Pure Storage currently has a trailing 12-month P/B ratio of 4.5, which compares unfavorably with some extent with what the industry witnessed over the last year. Hence, valuation looks slightly stretched from P/B perspective.

Intensifying competition, lack of international customers and mounting losses are major concerns.

Last Earnings Report

Pure Storage Q4 Earnings & Revenues Top Estimates

Pure Storage Inc. reported non-GAAP earnings of 23 cents per share in fourth-quarter fiscal 2020, beating the Zacks Consensus Estimate by 4.6%. Moreover, the bottom line improved 64.3% on a year-over-year basis.

Total revenues rose 17% from the year-ago quarter's level to \$492 million. Moreover, the top line surpassed the Zacks Consensus Estimate of \$489.2 million. Notably, the figure came within management's guidance of \$484-\$496 million.

Year-over-year increase in revenues can be attributed to strong FlashBlade implementation and new deal wins from three major international banks. Moreover, growth was driven by robust adoption of subscription offerings, including Pure as-a-Service, Cloud Block Store, and Evergreen.

Segmental Details

In the fiscal fourth quarter, Product revenues (contributed 76.5% to total revenues) of \$376.5 million increased 10.7% on a year-over-year basis, primarily on the back of existing customers and continued expansion of the customer base.

During the reported quarter, Pure Storage added more than 500 customers, bringing the total count to more than 7,500 organizations.

Robust adoption of strong product portfolio, including the likes of FlashArray, FlashStack and FlashBlade business segments, is a key catalyst.

Subscription revenues (23.5%) of \$115.5 million surged 40.7% on a year-over-year basis, driven by the company's ongoing support contracts and robust adoption of Pure as-a-Service, Cloud Block Store, and Evergreen subscription services.

Margin Highlights

Non-GAAP gross margin expanded 350 basis points (bps) from the year-ago quarter's level to 72.1%. Management had anticipated non-GAAP gross margin in the range of 67.5-70.5%. Better-than-expected gross margin was primarily driven by product differentiation, and margin expansion of Product and Subscription services.

Non-GAAP Product gross margin expanded 550 bps from the year-ago quarter's level to 73.3%.

Non-GAAP Subscription gross margin was 68.1%, which expanded 130 bps on a year-over-year basis.

Total operating expenses climbed 14.1% year over year to \$348.9 million. As a percentage of total revenues, the figure came in at 70.9%, which contracted 150 bps on a year-over-year basis.

Pure Storage reported a non-GAAP operating margin of 12.4%, which expanded 500 bps on a year-over-year basis.

Balance Sheet & Cash Flow

Pure Storage exited the quarter ended Feb 2, 2020 with cash, cash equivalents and marketable securities of \$1.299 billion, up from \$1.24 billion as of Oct 31, 2019.

Cash flow from operations during the reported quarter was \$69.9 million compared with \$64.3 million in the fiscal third quarter.

Free cash flow came in at \$56.2 million compared with \$45.6 million in the prior quarter.

Guidance

Pure Storage expects revenues of approximately \$365 million in first-quarter fiscal 2021. Pure Storage anticipates non-GAAP gross margin of approximately 69.5%. Non-GAAP operating profit is anticipated at approximately \$60 million.

Moreover, for fiscal 2021, the company expects revenues of approximately \$1.9 billion. The company expects non-GAAP gross margin of approximately 69.5%. Non-GAAP operating loss is anticipated at \$40 million.

Quarter Ending **01/2020**

Report Date	Feb 27, 2020
Sales Surprise	0.58%
EPS Surprise	4.55%
Quarterly EPS	0.23
Annual EPS (TTM)	0.26

Recent News

On May 4, Pure Storage launched the Purity FB 3.0 update for its storage solution software – Flashblade. The update will enable real time performance to speed up modern application workflows.

On Mar 31, Pure Storage expanded its partnership with SAP to drive better business outcomes for customers through joint technical support and deeper technology integrations between the two companies.

On Feb 27, Pure Storage rolled out third-generation all-NVMe FlashArray//X to aid customers with higher performance capabilities and enable faster time-to-market.

On Feb 18, Pure Storage announced that the company has joined Google Cloud's Anthos Ready Storage Initiative, expanding partnership with Google Cloud.

Valuation

Pure Storage shares are down 21.2% in the year-to-date period and 34.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are down 29.8% and 2.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 23.1% while the sector is up 10.5%.

The S&P 500 index is down 12.5% in the year-to-date period and 1.4% in the past year.

The stock is currently trading at 2.11X forward 12-month sales, which compares to 0.87X for the Zacks sub-industry, 3.49X for the Zacks sector and 3.18X for the S&P 500 index.

Over the past three years, the stock has traded as high as 4.41X and as low as 1.21X, with a 3-year median of 2.64X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$15 price target reflects 2.26X forward 12-month sales.

The table below shows summary valuation data for PSTG

Valuation Multiples - PSTG					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	2.11	0.87	3.49	3.18
	3-Year High	4.41	1.41	3.59	3.44
	3-Year Low	1.21	0.87	2.62	2.76
	3-Year Median	2.64	1.17	3.21	3.16
P/B TTM	Current	4.5	2.41	4.62	3.7
	3-Year High	10.27	3.94	5.38	4.55
	3-Year Low	2.79	2.11	3.58	3.02
	3-Year Median	6.58	3.03	4.57	3.91
EV/Sales TTM	Current	1.83	1.15	3.81	2.69
	3-Year High	5.03	1.71	4.43	3.45
	3-Year Low	0.96	0.99	3.05	2.23
	3-Year Median	2.95	1.42	3.79	2.99

As of 05/13/2020

Industry Analysis Zacks Industry Rank: Bottom 48% (131 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Nutanix Inc (NTNX)	Outperform	1
International Business Machines Corporation (IBM)	Neutral	3
Micron Technology Inc (MU)	Neutral	4
NetApp Inc (NTAP)	Neutral	3
Seagate Technology PLC (STX)	Neutral	3
Teradata Corporation (TDC)	Neutral	3
Western Digital Corporation (WDC)	Neutral	4
Hewlett Packard Enterprise Company (HPE)	Underperform	4

Industry Comparison Industry: Computer- Storage Devices				Industry Peers		
	PSTG	X Industry	S&P 500	HPE	IBM	NTAP
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	4	3	3
VGM Score	C	-	-	C	B	A
Market Cap	3.74 B	1.21 B	18.76 B	11.70 B	102.76 B	9.17 B
# of Analysts	9	7	14	6	6	9
Dividend Yield	0.00%	0.00%	2.23%	5.29%	5.63%	4.63%
Value Score	F	-	-	B	B	A
Cash/Price	0.31	0.30	0.06	0.24	0.11	0.30
EV/EBITDA	-38.69	4.99	11.39	4.19	8.16	4.99
PEG Ratio	NA	1.53	2.54	1.58	3.01	0.92
Price/Book (P/B)	4.45	4.45	2.56	0.68	5.11	32.52
Price/Cash Flow (P/CF)	NA	9.29	10.04	2.39	5.86	8.26
P/E (F1)	NA	10.99	18.48	6.13	10.25	10.99
Price/Sales (P/S)	2.27	1.16	1.91	0.41	1.34	1.64
Earnings Yield	-0.79%	6.31%	5.09%	16.30%	9.76%	9.09%
Debt/Equity	0.69	0.20	0.75	0.54	2.62	4.06
Cash Flow (\$/share)	-0.17	0.07	7.01	3.79	19.75	5.02
Growth Score	A	-	-	F	D	B
Hist. EPS Growth (3-5 yrs)	NA%	-6.87%	10.82%	-3.49%	-3.16%	26.08%
Proj. EPS Growth (F1/F0)	-136.78%	-1.54%	-10.51%	-16.29%	-11.89%	-4.66%
Curr. Cash Flow Growth	-37.62%	-28.62%	5.83%	-2.58%	2.09%	21.12%
Hist. Cash Flow Growth (3-5 yrs)	11.70%	6.16%	8.52%	-3.09%	-3.76%	2.57%
Current Ratio	3.08	1.49	1.27	0.79	0.96	1.20
Debt/Capital	40.71%	40.71%	44.25%	35.19%	72.36%	80.25%
Net Margin	-12.23%	-2.58%	10.59%	4.22%	11.78%	18.19%
Return on Equity	-20.80%	1.66%	16.36%	13.68%	57.55%	123.49%
Sales/Assets	0.75	0.90	0.54	0.55	0.50	0.71
Proj. Sales Growth (F1/F0)	1.91%	0.00%	-2.55%	-9.51%	-5.40%	-4.04%
Momentum Score	D	-	-	B	B	C
Daily Price Chg	-3.71%	-3.65%	-2.85%	-4.22%	-3.77%	-3.65%
1 Week Price Chg	16.01%	4.90%	3.23%	8.12%	0.92%	8.24%
4 Week Price Chg	14.66%	1.27%	-0.28%	-4.62%	-2.49%	2.55%
12 Week Price Chg	-25.13%	-15.49%	-23.80%	-37.25%	-23.29%	-22.08%
52 Week Price Chg	-32.43%	-9.71%	-13.31%	-37.03%	-13.89%	-38.84%
20 Day Average Volume	3,093,808	249,233	2,552,088	8,320,359	5,741,735	2,097,459
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-2.66%	-3.52%	-6.15%	0.00%	-10.60%	-4.37%
(F1) EPS Est 12 week change	-109.78%	-12.34%	-16.21%	-20.16%	-15.53%	-19.96%
(Q1) EPS Est Mthly Chg	-2.59%	-1.30%	-12.28%	0.00%	-26.64%	-6.73%

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	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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