

Splunk Inc. (SPLK)

\$190.40 (As of 08/12/20)

Price Target (6-12 Months): **\$200.00**

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:D

Value: F

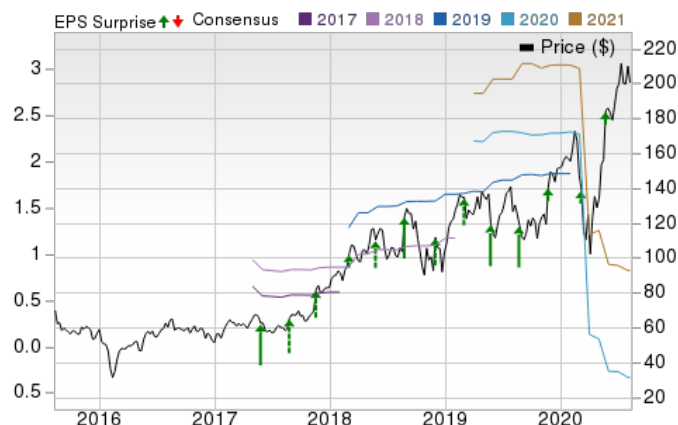
Growth: C

Momentum: B

Summary

Splunk is expected to benefit from software revenue growth and new customer wins. Also, solid demand for cloud-based solutions is anticipated to drive subscription revenues. Management expects cloud contribution to grow significantly over the next few years. Moreover, strategic acquisitions and an expanding partner base are key catalysts. Further, the successful transition to a renewable model from perpetual license model is expected to drive the top line in the long haul. However, this transition hurt Splunk's cash flow generation ability, which does not bode well for investors. Moreover, slowing maintenance & services revenues amid intensifying competition remains a headwind. Notably, shares have underperformed the industry on a year-to-date basis.

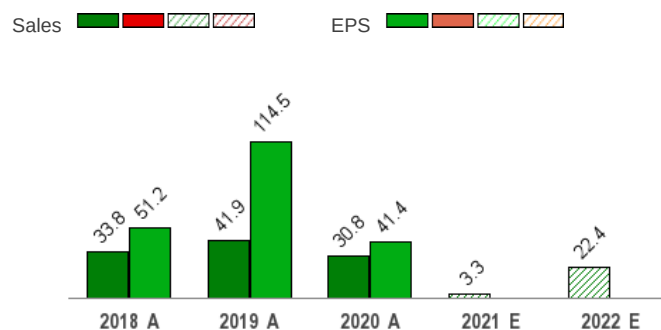
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$217.36 - \$93.92
20 Day Average Volume (sh)	1,183,948
Market Cap	\$30.2 B
YTD Price Change	27.1%
Beta	1.61
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Internet - Software
Zacks Industry Rank	Top 45% (114 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.8%
Last Sales Surprise	-2.3%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	08/26/2020
Earnings ESP	0.0%
P/E TTM	148.8
P/E F1	NA
PEG F1	NA
P/S TTM	12.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	537 E	647 E	791 E	1,001 E	2,984 E
2021	434 A	521 E	645 E	831 E	2,437 E
2020	425 A	517 A	626 A	791 A	2,359 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	-\$0.43 E	-\$0.08 E	\$0.32 E	\$0.92 E	\$0.82 E
2021	-\$0.56 A	-\$0.32 E	\$0.01 E	\$0.49 E	-\$0.34 E
2020	\$0.02 A	\$0.30 A	\$0.58 A	\$0.96 A	\$1.88 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 08/12/2020. The reports text is as of 08/13/2020.

Overview

San Francisco, CA-based Splunk provides software solutions that enable enterprises to gain real-time operational intelligence by harnessing the value of their data. The company's offerings enable users to investigate, monitor, analyze and act on machine data and big data, irrespective of format or source, and helps in operational decision making.

The company's flagship offering, Splunk Enterprise, is primarily a machine data platform. It can collect and index petabytes of machine data on a daily basis. Splunk Enterprise also enables users to interactively explore, analyze and visualize data stored in sources such as Hadoop and Amazon S3.

Splunk Cloud delivers the benefits of Splunk Enterprise deployed and managed reliably and scalably as a service. Splunk Light provides log search and analysis, which are designed, priced and packaged for small IT environments.

The company's premium solutions include Splunk Enterprise Security (ES), Splunk IT Service Intelligence (ITSI) and Splunk User Behavior Analytics (UBA). These solutions address emerging security threats and information and event management (SIEM), monitor health and key performance indicators of critical IT, and detect cyber-attacks and insider threats in business operations, respectively.

Splunk complements the aforementioned services with few add-ons, including Splunk Machine Learning Toolkit (MLTK), Splunk App for AWS, Splunk DB Connect and Cisco Firepower App for Splunk.

Splunk generated revenues of \$2.35 billion in fiscal 2020. License revenues contributed 58.2% to total revenues, while maintenance and services revenues accounted for the rest.

Splunk Enterprise customers pay license fees generally based on their estimated peak daily indexing capacity needs. The company also generates revenues from enterprise adoption agreements (EAAs). Splunk Cloud customers pay an annual subscription fee based on the combination of the volume of data indexed per day and the amount of data stored.

The company faces significant competition from the likes of Oracle, IBM, Intel and Microsoft, among others.



Reasons To Buy:

- ▲ Splunk's software offerings enables users to have deep insight of their data on a real-time basis, thereby making the operational decision-making process faster. The company's software has a broad range of applications, including security analytics, business analytics and IT operations. The valuable insight into machine and big data is allowing users/enterprises to improve service levels, reduce operational costs, mitigate security risks and maintain compliance. Splunk's customer base is expanding rapidly due to these factors. Notably, the company had 19,400 customers in more than 130 countries at the end of fiscal 2020.
- ▲ Splunk's software can be deployed in a wide variety of computing environments, from a single laptop to large globally distributed data centers as well as public, private and hybrid cloud environments. The company's top line is benefiting from high demand for its cloud solutions. Splunk's ES solutions also hold promise. Users leverage ES to centralize security management on a single platform and better handle the big data scale of their security operations center. Splunk also benefits from the ongoing SIEM replacement cycle. Further, the company's integration with Amazon Web Services (AWS) security Hub to help customers accelerate detection, investigation and response to potential threats within their AWS security environment is a key catalyst for the long haul.
- ▲ The company's business transition from perpetual licenses to subscription or renewable model is expected to benefit it in the long run. Splunk has been witnessing an increase in the number of renewable terms contracts, which is a tailwind. The company booked 35 orders greater than \$10 million in 2020 compared with 24 in the prior year. Additionally, cloud ARR was \$442 million in fourth-quarter fiscal 2020. These indicate strong subscription revenue growth for the rest of fiscal 2021.
- ▲ Splunk's aggressive acquisition strategy has played a pivotal part in developing its business over the last couple of years. The SignalFx acquisition makes the company a leader in cloud monitoring and APM for organizations transitioning to cloud. The VictorOps buyout helps it in addressing the needs of DevOps, which is a rapidly growing domain of software engineering. The acquisition of Phantom Cyber aided in the addition of security orchestration, automation and response to Splunk's portfolio. The buyout of Rocana has strengthened the company's machine data platform. Some of the other acquisitions include SignalSense, Drastin and Caspida, among others. These acquisitions are helping the company not only address the needs of IT operations but also DevOps. Splunk is expected to continue pursuing acquisitions in order to expand its portfolio and increase market share over the long term.
- ▲ Moreover, the company's strong partner base is a major top-line growth driver. The Splunk Partner+ Program includes more than 1,700 active partners, of which almost 1,000 partners contribute to sales. In fact, these partners are responsible for expanding Splunk's footprint in EMEA, APAC and the U.S. public sector. Further, partnerships with the likes of Cisco Systems, Deloitte and AWS are expected to boost the company's competitive position in the long haul.

Splunk benefits from a rapidly expanding user base, high demand for cloud solutions, increase in renewable subscription revenues, acquisitions and strong partner base.

Reasons To Sell:

- ▼ Splunk's top line over the last couple of years has been negatively impacted by the ongoing business model transition. Moreover, the transition from perpetual licenses to subscription or renewable-based model has severely hurt the company's cash flow generation ability due to lower upfront payment. Although long-term cash yield is expected to return to the mid-20% level, the company is unsure about the time frame.
- ▼ Moreover, the maintenance & services segment revenues are slowing down due to the ongoing transition to the cloud. Splunk relies on partners to provide maintenance and professional services (since it's a low-margin business), which is another reason behind the declining growth. This trend is expected to continue as the company projects cloud to account for 50% of total revenues over the next few years.
- ▼ Splunk generates a significant portion of revenues (29% in fiscal 2019) from its international operations. Despite its hedging program, the exposure makes the company vulnerable to foreign currency volatility.
- ▼ Splunk also faces significant competition across most of its product lines. Its competitors include the likes of BMC Software, CA Technologies, Micro Focus, IBM, Intel, Microsoft and VMware in the security and systems market. In the business intelligence market, Splunk competes with IBM and Oracle. Moreover, in the big data market it faces intensifying competition from the likes of Elastic.

Splunk's ongoing business model transition hurts its cash flow generation ability. Stiff competition and slowing maintenance & service revenues are concerns.

Last Earnings Report

Splunk's Q1 Earnings Gain on Cloud and Software Revenues

Splunk reported first-quarter fiscal 2021 non-GAAP loss of 56 cents per share, which was narrower than the Zacks Consensus Estimate of a loss of 57 cents. The company had reported non-GAAP earnings of 2 cents per share in the year-ago quarter.

Revenues increased 2.2% year over year to \$434.1 million but missed the Zacks Consensus Estimate by 2.2%. The year-over-year upside was driven by greater utilization of Splunk's products by existing customers and new customer wins.

Quarter Ending **04/2020**

Report Date	May 21, 2020
Sales Surprise	-2.33%
EPS Surprise	1.75%
Quarterly EPS	-0.56
Annual EPS (TTM)	1.28

Quarter in Details

License revenues (34.2% of revenues) were \$148.4 million, down 26.9% year over year.

Meanwhile, Cloud services revenues (25.8% of revenues) increased 80.7% year over year to \$112.2 million on the back of increased utilization of cloud-based services. Maintenance & service revenues (40% of revenues) rose 8.5% to \$173.5 million.

Notably, Cloud represented 44% of total software bookings for first-quarter fiscal 2021.

Remaining performance obligation (RPO) was \$1.72 billion, up 44% year over year. The company expects to recognize \$1 billion (indicating a 23% year-over-year increase) of this RPO as revenues over the next 12 months. RPO bookings declined 3.2% year over year to \$352.8 million.

Splunk ended the period with total annual recurring revenue (ARR) of \$1.77 billion, up 52% year over year, comprising \$480 million from cloud and \$1.29 billion from term license and maintenance contracts.

Splunk added new enterprise customers in the first quarter. Zoom opted for Splunk's Enterprise Security services in the reported quarter. Additionally, Shopify expanded its use of Splunk's offerings by purchasing the newly launched SignalFx Microservices APM platform.

Moreover, Take-Two Interactive expanded the use of Splunk Cloud to increase its visibility into security of its gaming environment.

The company recorded 81 orders worth more than \$1 million in contract value, up 76.1% from 46 in the year-ago period.

Splunk's Data-to-Everything Platform including new products such as Data Fabric Search (DFS), Data Stream Processor (DSP) and Splunk Mission Control, launched in the third quarter, witnessed rapid adoption in the reported quarter.

Operating Details

Non-GAAP gross margin contracted 560 basis points (bps) from the year-ago quarter to 76% due to greater proportion of cloud revenue contribution. Splunk's non-GAAP cloud gross margin expanded 780 basis points (bps) from the year-ago quarter to 15.2%

Non-GAAP operating expenses, as a percentage of revenues, expanded to 101.6% from 83.4% in the year-ago quarter. Research & development (R&D) expanded 850 bps, general and administrative (G&A) expanded 370 bps while sales & marketing (S&M) expenses expanded 600 bps year over year, respectively.

Non-GAAP operating loss was \$111.1 million compared with a loss of \$7.2 million in the year-ago quarter.

Balance Sheet & Cash Flow

As of Apr 30, 2020, cash & cash equivalents, including investments, were \$922.5 million compared with \$778.6 million reported in the previous quarter.

Guidance

For second-quarter fiscal 2021, Splunk expects revenues of \$520 million. Non-GAAP operating margin is likely to be between negative 10% and negative 15%.

The company withdrew its previous guidance for its fiscal 2021 due to coronavirus-related uncertainties.

Recent News

On Jun 3, Splunk announced the pricing of \$1.1 billion principal amount of 1.125% Convertible Senior Notes due 2027 in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended. The size of the offering was increased from the previously-announced \$900 million of aggregate principal amount.

On May 5, Splunk announced a new strategic partnership with Google to help organizations drive actionable insights from their data and enable fast decisions with real-time visibility across the enterprise. Splunk Cloud will soon be available on Google Cloud to help customers unlock the value of their data and provide increased flexibility for harnessing the power of the Splunk Data-to-Everything Platform.

On Mar 31, Splunk announced the next release of SignalFx Microservices APM, the only application performance monitoring (APM) solution that provides customers complete observability into modern, cloud-native environments to produce meaningful business outcomes regardless of scale by combining the NoSample full-fidelity tracing, open standards based instrumentation, and artificial intelligence (AI)-driven directed troubleshooting from SignalFx and Omnitron into a single best-in-class solution.

On Mar 11, Splunk announced the United States Census Bureau is using Splunk's Data-to-Everything Platform to connect data from 35 operations and 52 systems, ranging from cloud-based applications and data warehousing to field-deployed end-point devices.

Valuation

Splunk shares are up 27.1% in the year-to-date period and 51.6% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are up 51.7% and 18% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector is up 42.4% and 36%, respectively.

The S&P 500 index is up 3.3% in the year-to-date period and 17.5% in the past year.

The stock is currently trading at 11.08X forward 12-month sales, which compares to 8.03X for the Zacks sub-industry, 4.07X for the Zacks sector and 3.65X for the S&P 500 index.

Over the past five years, the stock has traded as high as 12.71X and as low as 4.65X, with a 5-year median of 7.74X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$200 price target reflects 11.63X forward 12-month sales.

The table below shows summary valuation data for SPLK

Valuation Multiples - SPLK					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	11.08	8.03	4.07	3.65
	5-Year High	12.71	8.56	4.07	3.65
	5-Year Low	4.65	3.01	2.32	2.53
	5-Year Median	7.74	5.27	3.14	3.05
EV/Sales TTM	Current	12.19	10.09	4.68	3.28
	5-Year High	14.95	10.85	4.68	3.46
	5-Year Low	4.48	3.02	2.58	2.14
	5-Year Median	8.79	5.96	3.65	2.86
P/B TTM	Current	16.71	10.23	6.26	4.64
	5-Year High	19.07	11.04	6.34	4.68
	5-Year Low	4.66	2.28	3.16	2.83
	5-Year Median	11.65	5.29	4.43	3.74

As of 08/12/2020

Industry Analysis Zacks Industry Rank: Top 45% (114 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Check Point Software Technologies Ltd. (CHKP)	Neutral	2
Citrix Systems, Inc. (CTXS)	Neutral	3
FireEye, Inc. (FEYE)	Neutral	2
F5 Networks, Inc. (FFIV)	Neutral	2
Fortinet, Inc. (FTNT)	Neutral	3
Okta, Inc. (OKTA)	Neutral	4
Palo Alto Networks, Inc. (PANW)	Neutral	3
Proofpoint, Inc. (PFPT)	Neutral	2

Industry Comparison Industry: Internet - Software				Industry Peers		
	SPLK	X Industry	S&P 500	FFIV	FTNT	PANW
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	2	3	3
VGM Score	D	-	-	C	A	D
Market Cap	30.25 B	862.59 M	23.75 B	8.46 B	20.50 B	25.91 B
# of Analysts	13	3	14	10	12	14
Dividend Yield	0.00%	0.00%	1.68%	0.00%	0.00%	0.00%
Value Score	F	-	-	B	D	D
Cash/Price	0.06	0.09	0.07	0.13	0.07	0.08
EV/EBITDA	4,240.05	-0.94	13.35	13.26	34.97	58.44
PEG Ratio	NA	4.43	2.98	1.29	3.06	1.92
Price/Book (P/B)	16.71	6.96	3.20	3.90	37.66	34.79
Price/Cash Flow (P/CF)	1,075.18	28.56	12.97	14.69	43.50	51.40
P/E (F1)	NA	84.50	22.17	14.79	42.88	44.69
Price/Sales (P/S)	12.77	4.77	2.54	3.64	8.71	7.94
Earnings Yield	-0.18%	0.26%	4.31%	6.76%	2.33%	2.24%
Debt/Equity	1.16	0.13	0.77	0.33	0.00	2.45
Cash Flow (\$/share)	0.18	-0.00	6.94	9.42	2.91	5.05
Growth Score	C	-	-	D	A	C
Hist. EPS Growth (3-5 yrs)	NA%	16.26%	10.41%	11.44%	122.35%	NA
Proj. EPS Growth (F1/F0)	-117.92%	-1.62%	-6.32%	-9.76%	19.64%	21.32%
Curr. Cash Flow Growth	-139.74%	6.87%	5.22%	2.02%	45.71%	119.25%
Hist. Cash Flow Growth (3-5 yrs)	16.42%	21.83%	8.55%	9.12%	46.74%	69.30%
Current Ratio	2.27	1.54	1.33	1.32	1.37	1.29
Debt/Capital	53.71%	27.68%	44.59%	25.04%	0.00%	70.98%
Net Margin	-20.56%	-17.73%	10.13%	13.95%	17.46%	-7.01%
Return on Equity	-17.40%	-13.96%	14.59%	21.69%	40.58%	-6.50%
Sales/Assets	0.47	0.60	0.51	0.57	0.67	0.48
Proj. Sales Growth (F1/F0)	3.30%	5.59%	-1.40%	4.66%	16.88%	16.98%
Momentum Score	B	-	-	F	A	C
Daily Price Chg	-2.68%	0.24%	0.67%	0.39%	0.09%	1.80%
1 Week Price Chg	-4.50%	0.00%	2.30%	3.44%	-5.28%	2.08%
4 Week Price Chg	-5.07%	1.57%	4.87%	-5.88%	-2.03%	8.03%
12 Week Price Chg	16.61%	13.68%	13.54%	-1.49%	-12.99%	10.81%
52 Week Price Chg	51.59%	14.85%	6.06%	8.35%	56.98%	19.97%
20 Day Average Volume	1,183,948	505,641	2,006,991	1,010,509	1,427,250	721,812
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	8.16%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	1.95%	5.44%	8.16%	0.00%
(F1) EPS Est 12 week change	-14.38%	3.37%	2.72%	5.44%	12.44%	27.18%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.84%	-32.57%	7.69%	NA

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	C
Momentum Score	B
VGM Score	D

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

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