

Splunk Inc. (SPLK)

\$137.70 (As of 06/23/21)

Price Target (6-12 Months): **\$145.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/01/21)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:C

Value: D

Growth: A

Momentum: F

Summary

Splunk incurred a loss in first-quarter fiscal 2022 while revenues increased, attributed to growth in cloud revenues and customer base expansion. Strength in cloud is expected to continue, driven by an expanding partner base and a robust portfolio. 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 will hurt Splunk's cash-flow generation ability. Moreover, slowing maintenance & services revenues is a concern. Management expects sluggish on-premise business to hurt growth in the near term. Moreover, volatile term business is expected to negatively impact growth. Although the demand environment remains strong, continuing COVID-19-related uncertainties are a headwind. Notably, shares have underperformed the industry year to date.

Price, Consensus & Surprise



Data Overview

52-Week High-Low **\$225.89 - \$110.28**

20-Day Average Volume (Shares) **3,058,495**

Market Cap **\$22.6 B**

Year-To-Date Price Change **-19.0%**

Beta **1.24**

Dividend / Dividend Yield **\$0.00 / 0.0%**

Industry **Internet - Software**

Zacks Industry Rank **Bottom 18% (207 out of 252)**

Last EPS Surprise **-26.4%**

Last Sales Surprise **1.9%**

EPS F1 Estimate 4-Week Change **-19.6%**

Expected Report Date **08/25/2021**

Earnings ESP **0.0%**

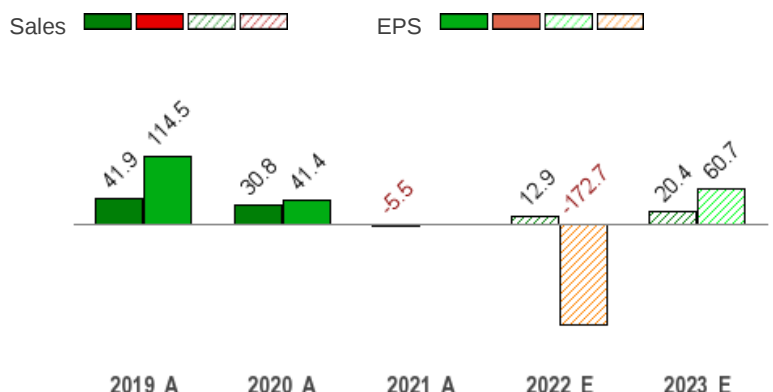
P/E TTM **NA**

P/E F1 **NA**

PEG F1 **NA**

P/S TTM **9.8**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2023	613 E	675 E	745 E	898 E	3,030 E
2022	502 A	562 E	635 E	809 E	2,516 E
2021	434 A	492 A	559 A	745 A	2,229 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2023	-\$0.61 E	-\$0.47 E	-\$0.07 E	\$0.52 E	-\$0.59 E
2022	-\$0.91 A	-\$0.68 E	-\$0.23 E	\$0.34 E	-\$1.50 E
2021	-\$0.56 A	-\$0.33 A	-\$0.07 A	\$0.38 A	-\$0.55 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 06/23/2021. The report's text and the

analyst-provided price target are as of 06/24/2021.

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.

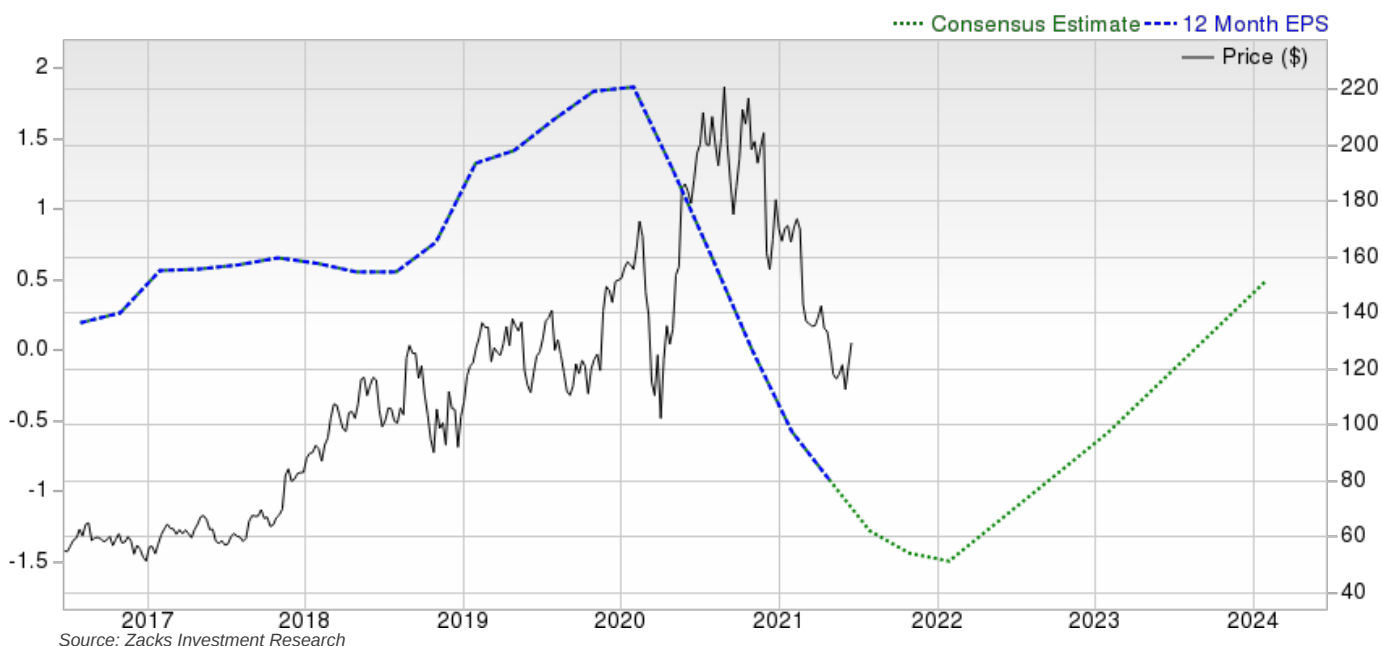
The company's premium solutions include Splunk Enterprise Security (ES), Splunk IT Service Intelligence (ITSI) and Splunk User Behavior Analytics (UBA). These solutions address emerging security threats and information and event management (SIEM), monitor health and key performance indicators of critical 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 \$2.23 billion in fiscal 2021. License and Cloud Services contributed 43.6% and 25% of total revenues, respectively. 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. Additionally, cloud Annual Recurring Revenues (ARR) were \$877 million, up 82.7% in first-quarter fiscal 2022. The company ended fiscal first quarter with 537 customers with ARR greater than \$1 million.
- ▲ 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 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 has a leveraged balance sheet. The company's cash & cash equivalent balance, including investments were \$1.9 billion as of Apr 30, 2021, stable sequentially. However, convertible senior notes balance was much higher at \$2.3 billion as of Apr 30, 2021.

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 Reports Loss in Q1, Revenues Up Y/Y

Splunk reported first-quarter fiscal 2022 non-GAAP loss of 91 cents per share, which missed the Zacks Consensus Estimate by 26.4% and widened from 56 cents in the year-ago quarter.

Revenues increased 15.7% year over year to \$502.1 million and beat the consensus mark by 1.9%.

Quarter in Details

License revenues (28.5% of revenues) were \$143.3 million, down 3.4% year over year. Cloud services revenues (38.6% of revenues) surged 72.9% year over year to \$194 million. Maintenance & service revenues (32.8% of revenues) fell 5% to \$164.8 million.

Notably, Cloud represented 56% of total software bookings in the reported quarter, higher than 51% in the previous quarter and 44% in the year-ago quarter. Splunk has been benefiting from partnerships with Alphabet and Amazon's cloud offerings, namely Google Cloud and AWS.

Splunk ended the quarter with total annual recurring revenues ("ARR") of \$2.47 billion, up 39% year over year. Cloud ARR soared 82.7% year over year to \$877 million.

The company ended fiscal first quarter with 537 customers generating ARR greater than \$1 million, up 46% year over year. Moreover, Splunk had 203 customers with Cloud ARR greater than \$1 million, up 99% year over year.

Notable clients in the reported quarter included Bank of New Zealand, Chipotle, CVS Health, CyberCX (Australia), Deloitte Canada, E-Halsomyndigheten (Sweden), Fastweb (Italy), Florida Department of Economic Opportunity, PRISMA Health, SCI Shared Resources, Sharp Healthcare, UVM Medical, TDC Net and ISTAT (Italy).

Remaining performance obligation ("RPO") was \$2.47 billion, up 7.9% year over year. The company expects to recognize \$1.21 billion (indicating a 21.2% year-over-year increase) of this RPO as revenues over the next 12 months.

Operating Details

Non-GAAP gross margin contracted 440 basis points (bps) from the year-ago quarter to 71.5% due to greater proportion of cloud revenue contribution. Splunk's non-GAAP cloud gross margin expanded 140 bps from the year-ago quarter to 60.3%

Non-GAAP operating expenses, as a percentage of revenues, increased to 106.9% from 101.6% in the year-ago quarter. Research & development and sales & marketing expenses expanded 520 bps and 50 bps year over year, respectively. General and administrative expenses declined 40 bps.

Non-GAAP operating loss was \$177.6 million compared with loss of \$111.1 million in the year-ago quarter.

Balance Sheet & Cash Flow

As of Apr 30, 2021, cash & cash equivalents, including investments, were \$1.86 billion compared with \$1.87 billion as of Jan 31, 2021.

Net cash flow from operating activities was \$70.7 million compared with the year-ago quarter's net cash flow from operating activities of \$46 million and the sequential quarter's net cash used in operating activities of \$23.8 million.

The company's free cash flow was \$69.8 million at the end of the first quarter compared with the year-ago quarter's free cash flow of \$31.3 million and the previous quarter's outflow of \$32.6 million.

Guidance

For second-quarter fiscal 2022, Splunk expects revenues in the range of \$550 million to \$570 million. Non-GAAP operating margin is likely to be -25%.

Moreover, total ARR is expected between \$2.59 billion and \$2.61 billion. Cloud ARR is expected to be between \$950 million and \$960 million.

Quarter Ending 04/2021

Report Date	Jun 02, 2021
Sales Surprise	1.86%
EPS Surprise	-26.39%
Quarterly EPS	-0.91
Annual EPS (TTM)	-0.93

Recent News

On Jun 22, Splunk announced the launch of cloud-based security platform—Splunk Security Cloud. Splunk Security Cloud offers enterprise-grade advanced security analytics, automated security operations and integrated threat intelligence.

On Jun 8, Splunk announced that the company has completed the assessment against the Protected Level under the Australian Information Security Registered Assessors Program (IRAP). The successful completion of IRAP assessment allows the Commonwealth of Australia and commercial customers required or seeking an approval to operate in line with the Australian Government Information Security Manual to use the IRAP security assessment of Splunk Cloud Platform in their independent risk assessment of their Splunk Cloud Platform deployment in Australia (AWS Australia region). With Splunk Cloud Platform, agencies can ingest and use data across their organizations and programs to address a variety of IT and security challenges.

On Feb 8, 2021 Splunk announced a multi-year partnership extension with McLaren Racing whereby Splunk will continue as an official McLaren Technology Partner of the McLaren Formula 1 team and McLaren Group.

Valuation

Splunk shares are down 19% in the year-to-date period and 28.7% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 0.7% while the same in the Zacks Computer & Technology sector are up 17% in the year-to-date period. Over the past year, the Zacks sub-industry and sector is up 35.2% and 48%, respectively.

The S&P 500 index is up 13.7% in the year-to-date period and 39.6% in the past year.

The stock is currently trading at 8.3X forward 12-month sales, which compares to 9.39X for the Zacks sub-industry, 4.95X for the Zacks sector and 4.71X for the S&P 500 index.

Over the past five years, the stock has traded as high as 13.41X and as low as 5.52X, with a 5-year median of 7.94X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$145 price target reflects 8.72X 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	8.3	9.39	4.95	4.71
	5-Year High	13.41	10.48	4.95	4.74
	5-Year Low	5.52	5	2.8	3.21
	5-Year Median	7.94	6.31	3.53	3.72
EV/Sales TTM	Current	9.01	11.25	5.71	4.87
	5-Year High	14.43	14.12	5.79	4.88
	5-Year Low	5.58	3.12	3.09	2.65
	5-Year Median	8.96	6.53	4	3.64
P/B TTM	Current	18.1	12.62	10.16	7.06
	5-Year High	21.48	14.7	10.16	7.08
	5-Year Low	7.47	2.89	4.44	3.84
	5-Year Median	12.65	6.62	5.86	5.02

As of 06/23/2021 Source: Zacks Investment Research

Industry Analysis Zacks Industry Rank: Bottom 18% (207 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Check Point Software Technologies Ltd. (CHKP)	Neutral	3
F5 Networks, Inc. (FFIV)	Neutral	3
Fortinet, Inc. (FTNT)	Neutral	3
Palo Alto Networks, Inc. (PANW)	Neutral	2
VMware, Inc. (VMW)	Neutral	3
Citrix Systems, Inc. (CTXS)	Underperform	5
FireEye, Inc. (FEYE)	Underperform	4
Okta, Inc. (OKTA)	Underperform	4

The positions listed should not be deemed a recommendation to buy, hold or sell.

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)	4	-	-	3	3	2
VGM Score	C	-	-	B	B	F
Market Cap	22.57 B	1.79 B	29.87 B	10.98 B	39.21 B	35.88 B
# of Analysts	12	4	12	9	13	17
Dividend Yield	0.00%	0.00%	1.35%	0.00%	0.00%	0.00%
Value Score	D	-	-	B	D	F
Cash/Price	0.09	0.09	0.06	0.06	0.08	0.08
EV/EBITDA	-51.97	-3.01	17.12	21.74	49.73	83.52
PEG F1	NA	3.48	2.05	1.29	4.50	2.64
P/B	18.10	7.98	4.07	5.66	39.97	35.98
P/CF	NA	47.20	17.35	22.35	63.16	77.81
P/E F1	NA	76.84	20.98	17.98	64.12	61.55
P/S TTM	9.82	8.25	3.36	4.45	14.39	9.00
Earnings Yield	-1.09%	0.14%	4.69%	5.56%	1.56%	1.63%
Debt/Equity	1.87	0.00	0.66	0.18	1.01	3.20
Cash Flow (\$/share)	-2.42	-0.02	6.83	8.24	3.80	4.73
Growth Score	A	-	-	B	A	D
Historical EPS Growth (3-5 Years)	NA%	22.20%	9.59%	5.15%	103.93%	NA
Projected EPS Growth (F1/F0)	-172.42%	-4.86%	21.62%	9.39%	11.76%	22.65%
Current Cash Flow Growth	-1,154.01%	-11.38%	0.99%	-10.95%	23.85%	-6.93%
Historical Cash Flow Growth (3-5 Years)	-13.86%	17.53%	7.28%	3.37%	57.79%	52.55%
Current Ratio	2.16	1.92	1.39	1.01	2.01	1.38
Debt/Capital	65.14%	3.67%	41.51%	15.18%	50.16%	76.19%
Net Margin	-46.72%	-13.29%	11.95%	11.28%	17.96%	-11.00%
Return on Equity	-49.90%	-8.01%	16.48%	18.60%	54.85%	-10.65%
Sales/Assets	0.41	0.52	0.51	0.53	0.67	0.43
Projected Sales Growth (F1/F0)	12.85%	15.12%	9.54%	9.37%	19.75%	23.43%
Momentum Score	F	-	-	C	D	F
Daily Price Change	-1.37%	0.38%	-0.11%	-0.49%	-0.76%	0.82%
1-Week Price Change	6.74%	0.00%	0.43%	-4.79%	2.06%	1.60%
4-Week Price Change	13.33%	6.34%	1.09%	-0.44%	11.29%	0.17%
12-Week Price Change	1.64%	0.42%	6.77%	-11.68%	30.17%	14.39%
52-Week Price Change	-27.76%	39.53%	39.06%	36.47%	78.71%	64.90%
20-Day Average Volume (Shares)	3,058,495	539,723	1,889,295	479,499	794,961	795,692
EPS F1 Estimate 1-Week Change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
EPS F1 Estimate 4-Week Change	-19.56%	0.00%	0.01%	0.00%	0.00%	0.00%
EPS F1 Estimate 12-Week Change	-19.56%	-2.58%	3.54%	1.26%	2.24%	18.42%

Past performance is no guarantee of future results. Please see important disclosures and definitions at the end of this report.

EPS Q1 Estimate Monthly Change	-26.48%	0.00%	0.00%	0.00%	0.00%	0.00%
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Source: Zacks Investment Research

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 maintain a 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	D
Growth Score	A
Momentum Score	F
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

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Additional Disclosure

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Returns quoted represent past performance which is no guarantee of future results. Investment returns and principal value will fluctuate so that when shares are redeemed, they may be worth more or less than their original cost. Current performance may be higher or lower than the performance shown.

Investing involves risk; principal loss is possible. There is no guarantee that companies that can issue dividends will declare, continue to pay or increase dividends.

Glossary of Terms and Definitions

52-Week High-Low: The range of the highest and lowest prices at which a stock has traded during the past year. This range is determined based on the stock's daily closing price which may differ from the intra-day high or low. Many investors use it as a technical indicator to determine a stock's current value and future price movement. The idea here is that if price breaks out from the 52-week range, in either direction, the momentum may continue in the same direction.

20-Day Average Volume (Shares): The average number of shares of a company traded in a day over the last 20 days. It is a direct indication of a security's overall liquidity. The higher the average daily trading volume, the easier it is to enter or exit the stock at a desired price with more buyers and sellers being available.

Daily Price Change: This is the percentage difference between a trading day's closing price and the prior trading day's closing price. This item is updated at 9 p.m. EST each day.

1-Week Price Change: This is the percentage change in a stock's closing price over the last 5 trading days. This change reflects the collective buying and selling sentiment over the 1-week period.

A strong weekly price increase for the stock, especially when accompanied by increased volume, is an indication of it gaining momentum.

4-Week Price Change: This is the percentage change in a stock's closing price over the last 20 trading days or past 4 weeks. This is a medium-term price change metric and an indication of the stock gaining momentum.

12-Week Price Change: This is the percentage change of a stock's closing price over the last 60 trading days or past 12 weeks. Similar to 4-week price change, this is a medium-term price change metric. It shows whether a stock has been enjoying strong investor demand, or if it has been in consolidation, or distress over this period.

52-Week Price Change: This is the percentage change in a stock's closing price over the last 260 trading days or past 52 weeks. This long-term price change metric is a good reference point for investors. Some investors seek stocks with the best percentage price change over the last 52 weeks, expecting the momentum to continue.

Market Cap: The number of outstanding common shares of a company times its latest price per share. This figure represents a company's size, which indicates various characteristics, including price stability and risk, in which investors could be interested.

Year-To-Date Price Change: Change in a stock's daily closing price in the period of time beginning the first day of the current calendar year through to the previous trading day.

of Analysts: Number of EPS estimates used in calculating the current-quarter consensus. These estimates come from the brokerage analysts tracking this stock. However, the number of such analysts tracking this stock may not match the number of estimates, as all brokerage analysts may not come up with an estimate or provide it to us.

Beta: A measure of risk commonly used to compare the volatility of a stock to the overall market. The S&P 500 Index is the base for calculating beta and carries a value of 1. A stock with beta below 1 is less risky than the market as a whole. And a stock with beta above 1 is riskier.

Dividend: The portion of earnings a company is expected to distribute to its common shareholders in the next 12 months for each share they own. Dividends are usually paid quarterly. Dividend payments reflect positively on a company and help maintain investors' trust. Investors typically find dividend-paying stocks appealing because the dividend adds to any market price appreciation to result in higher return on investment (ROI). Moreover, a steady or increasing dividend payment provides investors a cushion in a down market.

Dividend Yield: The ratio of a company's annual dividend to its share price. The annual dividend used in the ratio is calculated based on the most recent dividend paid by the company. Dividend yield is an estimate of the dividend-only return from a stock in the next 12 months. Since dividend itself doesn't change frequently, dividend yield usually changes with a stock's price movement. As a result, often an unusually high dividend yield is a result of weak stock price.

S&P 500 Index: The Standard & Poor's 500 (S&P 500) Index is an unmanaged group of securities considered to be representative of the stock market in general. It is a market-capitalization-weighted index of stocks of the 500 largest U.S. companies. Each stock's weight in the index is

proportionate to its market value.

Industry: One of the 250+ groups that Zacks classifies all stocks into based on the nature of business. These groups are termed as expanded (aka "X") industries and map to their respective (economic) sectors; Zacks has 16 sectors.

Zacks Industry Rank: The Zacks Industry Rank is determined by calculating the average Zacks Rank for all stocks in the industry and then assigning an ordinal rank to it. For example, an industry with an average Zacks Rank of 1.6 is better than an industry with an average Zacks Rank of 2.3. So, the industry with the better average Zacks Rank would get a better Zacks Industry Rank. If an industry has the best average Zacks Rank, it would be considered the top industry (1 out of 250+), which would place it at the top 1% of Zacks-ranked industries. Studies have shown that roughly half of a stock's price movement can be attributed to the industry group it belongs to. In fact, the top 50% of Zacks-ranked industries outperforms the bottom 50% by a factor of more than 2 to 1.

Last EPS Surprise: The percentage deviation of a company's last reported earnings per share from the Zacks Consensus Estimate. Companies with a positive earnings surprise are more likely to surprise again in the future (or miss again if they recently missed).

Last Sales Surprise: The percentage deviation of a company's last reported sales from the Zacks Consensus Estimate.

Expected Report Date: This is an estimated date of a company's next earnings release. The information originated or gathered by Zacks Investment Research from its information providers or publicly available sources is the basis of this estimate.

Earnings ESP: The Zacks Earnings ESP compares the Most Accurate Estimate to the Zacks Consensus Estimate for the yet-to-be reported quarter. The Most Accurate Estimate is the most recent version of the Zacks Consensus EPS Estimate. The idea here is that analysts revising their estimates closer to an earnings release have the latest information, which could potentially be more accurate than what they and others contributing to the consensus had predicted earlier. Thus, a positive or negative Earnings ESP reading theoretically indicates the likely deviation of the actual earnings from the consensus estimate. However, the model's predictive power is significant for positive ESP readings only. A positive Earnings ESP is a strong predictor of an earnings beat, particularly when combined with a Zacks Rank #1 (Strong Buy), #2 (Buy) or #3 (Hold). Our research shows that stocks with this combination produce a positive surprise nearly 70% of the time.

Periods:

TTM: Trailing 12 months. Using TTM figures is an effective way of analyzing the most-recent financial data in an annualized format that helps neutralize the effects of seasonality and other quarter-to-quarter variation.

F1: Current fiscal year. This period is used to analyze the estimates for the ongoing full fiscal year.

F2: Next fiscal year. This period is used to analyze the estimates for the next full fiscal year.

F12M: Forward 12 months. Using F12M figures is an effective way of analyzing the near-term (the following four unreported quarters) estimates in an annualized manner. Instead of typically representing estimates for the full fiscal year, which may not represent the nitty-gritty of each quarter, F12M figures suggest an all-inclusive annualized estimate for the following four quarters. The annualization helps neutralize the potential effects of seasonality and other quarter-to-quarter variations.

P/E Ratio: The price-to-earnings ratio measures a company's current market price per share relative to its earnings per share (EPS). Usually, the trailing-12-month (TTM) EPS, current-fiscal-year (F1) EPS estimate, or forward-12-month (F12M) EPS estimate is used as the denominator. In essence, this ratio shows what the market is willing to pay today for each dollar of EPS. In other words, this ratio gives a sense of what the relative value of the company is at the already reported level of earnings or at a future level of earnings.

It is one of the most widely-used multiples for determining the value of a company and helps comparing its valuation with that of a competitor, the industry group or a benchmark.

PEG Ratio: The price/earnings to growth ratio is a stock's P/E ratio using current fiscal year (F1) EPS estimate divided by its expected EPS growth rate over the coming 3 to 5 years. This ratio essentially determines a stock's value by factoring in the company's expected earnings growth and is thus believed to provide a more complete picture than just the P/E ratio, particularly for faster-growing companies.

P/S Ratio: The price-to-sales ratio is calculated as a company's current price per share divided by trailing 12 months (TTM) sales or revenues per share. This ratio shows what the market is willing to pay today for each dollar of TTM sales per share. The P/S ratio is at times the only valuation metric when the company has yet to become profitable.

Cash/Price Ratio: The cash-to-price ratio or Cash Yield is calculated as cash and marketable securities per share divided by the company's current share price. Like the earnings yield, which shows the anticipated yield (or return) on a stock from earnings for each dollar invested, the cash yield does the same, with cash being the source of return instead of earnings. For example, a cash/price ratio of 0.08 suggests a return of 8% or 8 cents for every \$1 investment.

EV/EBITDA Ratio: The EV/EBITDA ratio, also known as Enterprise Multiple, is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by EBITDA (earnings before interest, taxes, depreciation and amortization). Usually, trailing-12-month (TTM) or forward-12-month (F12M) EBITDA is used as the denominator.

EV/Sales Ratio: The enterprise value-to-sales ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by annual sales. It is an expansion of the P/S valuation, which uses market value instead of enterprise value. The EV/Sales ratio is perceived as more accurate than P/S, in part, because the market capitalization does not take a company's debt into account when valuing it.

EV/CF Ratio: The enterprise value-to-cash flow ratio is calculated as a company's enterprise value (market capitalization + value of total long-

term debt + book value of preferred shares - cash and marketable securities) divided by the trailing-12-month (TTM) operating cash flow. It's a measure of how long it would take to buy the entire business if you were able to use all the company's operating cash flow.

The EV/CF ratio is perceived as more accurate than the P/CF ratio, in part, because the market price does not take a company's debt into account when valuing it.

EV/FCF Ratio: The enterprise value-to-free cash flow metric compares a company's enterprise value to its trailing-12-month (TTM) free cash flow (FCF). This metric is very similar to the EV/CF ratio, but is considered a more exact measure owing to the fact that it uses free cash flow, which subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding growth activities and payments to shareholders.

P/EBITDA Ratio: The P/EBITDA ratio is calculated as a company's per share market value divided by EBITDA (earnings before interest, taxes, depreciation, and amortization). This metric is very similar to the EV/EBITDA ratio, but is considered a little less exact measure as it uses market price, which does not take a company's debt into account. However, since EBITDA is often considered a proxy for cash income, the metric is used as a measure of what the market is willing to pay today for each dollar of the company's cash profitability in the trailing 12 months (TTM) or forward 12 months (F12M).

P/B Ratio: The price-to-book ratio is calculated as a company's current price per share divided by its book value (total assets – liabilities – preferred stocks) per share. In short, the book value is how much a company is worth. In other words, it reflects the total value of a company's assets that its common shareholders would receive if it were to be liquidated. So, the P/B ratio indicates whether you're paying higher or lower than what would remain if the company went bankrupt immediately. Investors typically use this metric to determine how a company's stock price stacks up to its intrinsic value.

P/TB Ratio: The price-to-tangible-book value ratio is calculated as the per share market value of a company divided by the value of its tangible assets (total assets – liabilities – preferred stocks – intangible assets) per share. Tangible book value is the same thing as book value except it excludes the value of intangible assets to get a step closer to the baseline value of the company.

P/CF Ratio: The price-to-cash flow ratio measures a company's per share market price relative to its trailing-12-month (TTM) operating cash flow per share. This metric is used to determine whether a company is undervalued or overvalued relative to another stock, industry or sector. And like the P/E ratio, a lower number is typically considered better from the value perspective.

One of the reasons why P/CF ratio is often preferred over P/E ratio is the fact that operating cash flow adds back non-cash expenses such as depreciation and amortization to net income. This feature helps valuing stocks that have positive cash flow but are not profitable because of large noncash charges.

P/FCF Ratio: The price-to-free cash flow ratio is an extension of P/CF ratio, which uses trailing-12-month (TTM) free cash flow per share instead of operating cash flow per share. This metric is considered a more exact measure than P/CF ratio, as free cash flow subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding activities that generate additional revenues.

Earnings Yield: The earnings yield is calculated as current fiscal year (F1) EPS estimate divided by the company's current share price. The ratio, which is the inverse of the P/E ratio, measures the anticipated yield (or return) from earnings for each dollar invested in a stock today.

For example, earnings yield for a stock, which is trading at \$35 and expected to earn \$3 per share in the current fiscal year (F1), would be 0.0857 ($3/35 = 0.0857$) or 8.57%. In other words, for \$1 invested in the stock today, the yield from earnings is anticipated to be 8.57 cents.

Investors most commonly compare the earnings yield of a stock to that of a broad market index (such as the S&P 500) and prevailing interest rates, such as the current 10-year Treasury yield. Since bonds and stocks compete for investors' dollars, stock investors typically demand a higher yield for the extra risk they assume compared to investors of U.S. Treasury-backed securities that offer virtually risk-free returns. This additional return is referred to as the risk premium.

Debt/Equity Ratio: The debt-to-equity ratio is calculated as a company's total liabilities divided by its shareholder equity. This metric is used to gauge a company's financial leverage. In other words, it is a measure of the degree to which a company is financing its operations through debt versus its own funds. The higher the ratio, the higher the risk for shareholders.

However, this ratio is difficult to compare across industry groups where ideal amounts of debt vary. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-equity ratio should be compared with other companies in the same industry.

Cash Flow (\$/share): Cash flow per share is calculated as operating cash flow (after-tax earnings + depreciation + other non-cash charges) divided by common shares outstanding. It is used by many investors as a measure of a company's financial strength. Since cash flow per share takes into consideration a company's ability to generate cash by adding back non-cash expenses, it is regarded by some as a more accurate measure of a company's financial situation than earnings per share, which could be artificially deflated.

Current Ratio: The current ratio or liquidity ratio is a company's current assets divided by its current liabilities. It measures a company's ability to pay short-term obligations. A current ratio that is in line with the industry average or slightly higher is generally considered acceptable. A current ratio that is lower than the industry average would indicate a higher risk of distress or default. A higher number is usually better. However, a very high current ratio compared to the industry average could be an indication of inefficient use of assets by management.

Debt/Capital Ratio: Debt-to-capital ratio is a company's total debt (interest-bearing debt + both short- and long-term liabilities) divided its total capital (interest-bearing debt + shareholders' equity). It is a measure of a company's financial leverage. All else being equal, the higher the debt-to-capital ratio, the riskier the stock.

However, this ratio can vary widely from industry to industry, the ideal amount of required debt being different. Some businesses are more capital

intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-capital ratio should be compared with the same for its industry.

Net Margin: Net margin is calculated as net income divided by sales. It shows how much of each dollar in sales generated by a company translates into profit. For example, if a company's net margin is 15%, its net income is 15 cents for every \$1 of sales it makes.

A change in margin can reflect either a change in business conditions, or a company's cost controls, or both. If a company's expenses are growing faster than sales, its net margin will decline. However, different net margin rates are considered good for different industries, so it's better to compare net margin rates of companies in the same industry group.

Return on Equity: Return on equity (ROE) is calculated as trailing-12-month net income divided by trailing-12-month average shareholder equity (including reinvested earnings). This metric is considered a measure of how effectively management is using a company's assets to generate profits. For example, if a company's ROE is 10%, it creates 10 cents profits for every \$1 shareholder equity, which is basically the company's assets minus debt. A company's ROE deemed good or bad depends on what's normal for its peers or industry group.

Sales/Assets Ratio: The sales-to-assets ratio or asset utilization ratio or asset turnover ratio is calculated as a company's annual sales divided by average assets (average of assets at the beginning of the year and at the year's end). This metric helps investors understand how effectively a company is using its assets to generate sales. For example, a sales-to-assets ratio of 2.5 indicates that the company generated \$2.50 in sales for every \$1 of assets on its books.

The higher the sales-to-assets ratio, the better the company is performing. However, similar to many other ratios, the asset turnover ratio tends to be higher for companies in certain industries/sectors than in others. So, a company's sales-to-assets ratio should be compared with the same for its industry/sector.

Historical EPS Growth (3-5 Years): This is the average annual (trailing-12-month) EPS growth rate over the last 3-5 years. This metric helps investors see how a company's EPS has grown from a long-term perspective.

Note: There are many factors that can influence short-term numbers — a recession will reduce this number, while a recovery will inflate it. The longterm perspective helps smooth out short-term events.

Projected EPS Growth (F1/F0): This is the estimated EPS growth rate for the current financial year. It is calculated as the consensus estimate for the current fiscal year (F1) divided by the reported EPS for the last completed fiscal year (F0).

Current Cash Flow Growth: It measures the latest year-over-year change in operating cash flow. Cash flow growth tells an investor how quickly a company is generating inflows of cash from operations. A positive change in the cash flow is desired and shows that more 'cash' is coming in than going out.

Historical Cash Flow Growth (3-5 Years): This is the annualized change in cash flow over the last 3-5 years. The change in a longer period helps put the current reading into proper perspective. By looking at the rate, rather than the actual dollar value, the comparison across the industry and peers becomes easier.

Projected Sales Growth (F1/F0): This metric looks at the estimated sales growth for the current year. It is calculated as sales estimate for the current fiscal year (F1) divided by the reported sales for the last completed fiscal year (F0).

Like EPS growth, a higher rate is better for sales growth. A look at a company's projected sales growth instantly tells you what the outlook is for their products and services. However, different sales growth rates are considered good for different industries, so it's better to compare sales growth rates of companies in the same industry group.

EPS F1 Estimate 1-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past week. The change in a company's consensus EPS estimate (or earnings estimate revision) has proven to be strongly correlated with the near-term price movement of its shares. It is an integral part of the Zacks Rank.

If a stock's consensus EPS estimate is \$1.10 now versus \$1.00 a week ago, that will be reflected as a 10% upward revision. If, on the other hand, it went from \$1.00 to 90 cents, that would be a 10% downward revision.

EPS F1 Estimate 4-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past four weeks.

A stock's earnings estimate revision in a 1-week period is important. But it's more meaningful to look at the longer-term revision. And, of course, the 4-week change helps put the 1-week change into proper perspective.

EPS F1 Estimate 12-Week Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past 12 weeks.

This metric essentially shows how the consensus EPS estimate has changed over a period longer than 1 week or 4 weeks.

EPS Q1 Estimate Monthly Change: The percentage change in the Zacks Consensus EPS estimate for the current fiscal quarter over the past four weeks.

While the revision in consensus EPS estimate for the current fiscal year is strongly correlated with the near-term price movement of its shares, the estimate revision for the current fiscal quarter is an important metric as well, especially over the short term, and particularly as a stock approaches its earnings date. If a stock's Q1 EPS estimate decreases ahead of its earnings release, it's usually a negative sign, whereas an increase is a positive sign.