Workday Inc. (WDAY)

$188.15 (As of 01/30/20)

Price Target (6-12 Months): **$201.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 03/11/19) Prior Recommendation: Outperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:C
	Value: F | Growth: A | Momentum: D	

Summary

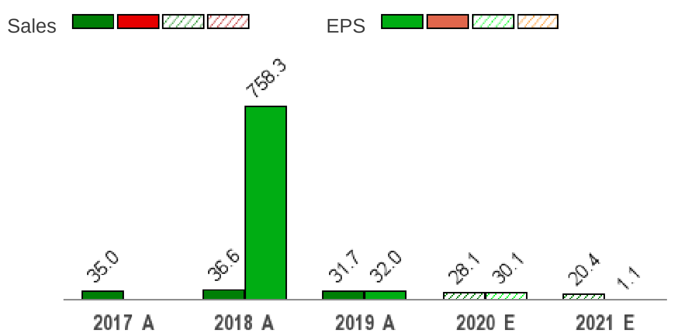
Workday has been benefiting from solid adoption of subscription and professional software solutions. Adaptive Insights buyout is enabling it to help enterprises in making better business decisions and enhance operational expertise. Further, extended capabilities and tools in Workday HCM and Financial Management to enhance customer experience bode well. In fact, the company's HCM suite of applications demonstrates strong growth momentum driven by the transition of organizations to the cloud. Further, the company's foray into the platform-as-a-service market by launching the Workday Data-as-a-Service Platform holds promise. However, stiff competition primarily from Oracle and SAP is likely to limit margin expansion at least in the near term. Increasing investments to achieve long-term growth are likely to weigh on the bottom line.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$226.83 - $151.06**
20 Day Average Volume (sh)	**1,685,276**
Market Cap	**$43.3 B**
YTD Price Change	**14.4%**
Beta	**1.49**
Dividend / Div Yld	**$0.00 / 0.0%**
Industry	**Internet - Software**
Zacks Industry Rank	**Top 41% (104 out of 255)**
Last EPS Surprise	**39.5%**
Last Sales Surprise	**1.9%**
EPS F1 Est- 4 week change	**0.0%**
Expected Report Date	**02/27/2020**
Earnings ESP	**0.0%**
P/E TTM	**104.0**
P/E F1	**106.3**
PEG F1	**3.9**
P/S TTM	**12.6**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	1,005 E	1,067 E	1,119 E	1,159 E	4,351 E
2020	825 A	888 A	938 A	965 E	3,615 E
2019	619 A	672 A	743 A	789 A	2,822 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	$0.40 E	$0.49 E	$0.52 E	$0.57 E	$1.79 E
2020	$0.43 A	$0.44 A	$0.53 A	$0.37 E	$1.77 E
2019	$0.33 A	$0.31 A	$0.31 A	$0.41 A	$1.36 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, except sales and EPS estimates, is as of 01/30/2020. The reports text and the analyst-provided sales and EPS estimates are as of 01/31/2020.

Overview

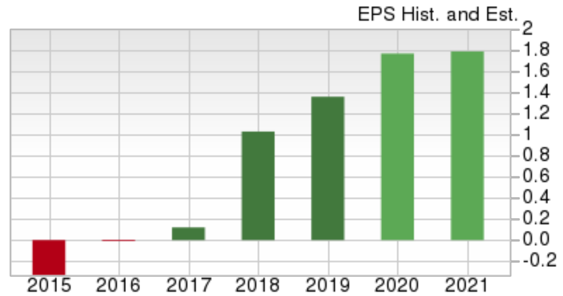
Founded in 2005 and headquartered in Pleasanton, CA, Workday Inc. (WDAY) is a provider of enterprise-level software solutions for financial management and human resource domains. The company's cloud-based platform combines finance and HR in a single system that makes it easier for organizations to provide analytical insights and decision support.

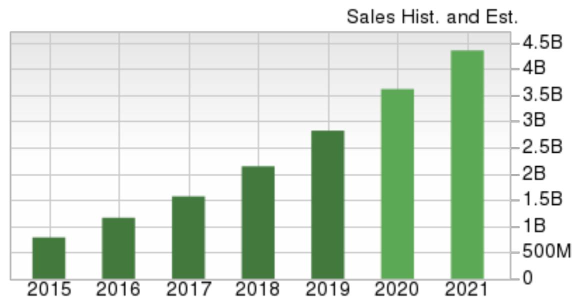
Notably, organizations ranging from medium-sized businesses to Fortune 50 enterprises have opted for Workday solutions. The company also offers open, standards-based web-services application programming interfaces and pre-built packaged integrations and connectors.

In fiscal 2019, the company reported revenues of $2.82 billion, up 31.7% from fiscal 2018 tally. Subscription revenues contributed 84.5% of total revenue, while professional revenues amounted for the rest.

Apart from Financial Management and Human Capital Management (HCM) solutions, the company offers applications related to Payroll, Time Tracking, Recruiting, Learning, Planning, Professional Services Automation and Student.

The company offers Adaptive Insights Business Planning Cloud solutions, Workday Prism Analytics, Workday Data-as-a-Service (DaaS) and Workday Marketplace. Workday Prism Analytics helps in business planning and collaborative approach.





Workday Prism Analytics helps customers to bring Workday data and data from any outside source together in order to make better business decisions. Workday DaaS is a cloud service that provides important data to customers which in turn help in decision-making.

The growing clout of Workday Cloud Platform, Workday Prism Analytics and Workday Marketplace bode well.

The company serves technology, financial services, business services, healthcare and life sciences, manufacturing, and consumer and retail industries, as well as education and government industries.

The company ended the third quarter of fiscal 2020 with more than 42 million users and 3,000 customers, with a focus on medium-sized and large, global organizations.

Workday faces competition from SAP SE, Oracle Corporation, Automated Data Processing, and Ceridian, among others.

Reasons To Buy:

Workday is benefiting from increasing demand for human capital management and financial software solutions, diversified product portfolio, expanding customer base and strong liquidity.

- Workday's revenue growth continues to be driven by high demand for its HCM and financial management solutions. The company's cloud-based business model and expanding product portfolio have been the primary growth drivers. Moreover, growing clout of Workday Prism Analytics and Adaptive Insights business planning cloud offerings holds promise. According to Gartner, the global Software-as-a-Service (SaaS) revenues are expected to touch $143.7 billion in 2022 from $80 billion in 2018, witnessing a CAGR of 15.8%. Based on its expanding product portfolio, we believe that Workday is well positioned to gain from this strong growth prospect going forward.

- Workday's HCM suite of applications demonstrates strong growth momentum driven by the transition of organizations to the cloud. In fact, per research firm MarketsandMarkets, the HCM market size is anticipated to hit $26.5 billion by 2024 from $16.7 billion in 2019, seeing a CAGR of 9.7%. Notably, Gartner's May 2019 "Magic Quadrant for Cloud Core Financial Management Suites for Midsize, Large, and Global Enterprises" report put Workday in the "Leaders" quadrant which reflects the company's growing clout in the cloud market. Workday was recognized as a Leader for the third year in a row. Workday ended third-quarter fiscal 2020 with more than 42 million users and 3,000 customers. The company witnessed rapid deployment of HCM solution in the fiscal third quarter. The company added 11 Global 2000 and six Fortune 500 companies during the fiscal third quarter. We, therefore, see much room for expansion here. Key deal wins include Royal Bank of Canada, Anheuser-Busch InBev, Magna International, and Sutter Health. Moreover, companies like the Dow Chemical Company, Glencore National AG, and Telstra Corporation, went live with Workday's solutions during the fiscal third quarter.

- Workday's diversified product portfolio continues to yield a steady flow of customers. We believe that the company's high customer satisfaction rate bodes well for its long-term business model. In the second-quarter, the company achieved industry-leading 98% customer satisfaction rating, which even surpassed its target of 95%. It plans to achieve similar levels every year. Moreover, Workday is gaining traction in the international market, which is evident from 35% year-over-year increase in revenues to $234 million (25% of total third-quarter fiscal 2020 revenues). Reportedly, Munich Germany-based manufacturing giant, Siemens replaced its current HR system with Workday HCM.

- Workday is a cash-rich company with a strong balance sheet. The company generated approximately $606.7 million cash from operating activities in fiscal 2019, which increased from $11.2 million in 2013. Cash, cash equivalents and marketable securities were $2.10 billion as of Oct 31, 2019 compared with $1.93 billion in the previous quarter. Moreover, the company generated operating cash flow of $258 million in third-quarter fiscal 2020 compared with prior-quarter figure of $100.3 million. Further, Workday has no long-term debt. The strong cash balance can be used for pursuing strategic acquisitions, investment in growth initiatives and distribution to shareholders.

Reasons To Sell:

- Competition in the HCM and financial management software market is increasing, which could lead to pricing pressure and affect Workday's margins. Oracle's strong momentum in the cloud is a headwind for the company. Moreover, we believe that Workday's dominance could be challenged by new entrants. This could make the company take resort to competitive pricing to maintain and capture further market share. This apart, the ongoing trend to invest more in cloud solutions exposes Workday to the risk of losing existing "on-premise customers", which can adversely impact its top-line performance, especially in the near term.

Intensifying competition from the likes Oracle and SAP and increasing marketing spending are major concerns.

- The company's margin continues to be affected by higher operating expense, primarily due to an increase in headcount and marketing spending. As of Jan 31, 2018, Workday had about 10,500 employees (including 500 from Adaptive Insights buyout) compared with about 1,500 employees as of its listing date in October 2012. Notably, non-GAAP sales and marketing expenses in fiscal 2019 increased 27.8% year over year to $738.8 million. We believe Workday's continuous investments in order to achieve long-term growth will hurt its margins in the short haul.

- We note that Workday currently has a trailing 12-month Price/Book (P/B) ratio of 18.66X. This level compares unfavorably with what the industry witnessed in the last year. Hence, valuation looks slightly stretched from a P/B perspective.

Last Earnings Report

Workday Earnings & Revenues Top Estimates in Q3

Quarter Ending	10/2019
Report Date	Dec 03, 2019
Sales Surprise	1.89%
EPS Surprise	39.47%
Quarterly EPS	0.53
Annual EPS (TTM)	1.81

Workday reported third-quarter fiscal 2020 non-GAAP earnings of 53 cents per share, which soared approximately 71% year over year and beat the Zacks Consensus Estimate by 39.5%.

Robust growth can primarily be attributed to an improvement of 26.2% in revenues, which totaled $938.1 million. The figure outpaced the Zacks Consensus Estimate for revenues by 1.9%. The upside was driven by solid growth in subscription and professional services revenues.

Quarter in Detail

Subscription services revenues (85.1% of total revenues) rallied 27.9% year over year to $798.5 million on the back of expanding customer base. The figure surpassed management's guidance of $783-$785 million.

Workday ended the fiscal third quarter with more than 42 million users and 3,000 customers.

Backlogs from Subscription revenues came in at $7.19 billion, up 21.8% year over year, primarily on the back of growth in net new bookings and "add-on business and net retention."

Professional services revenues (14.9% of total revenues) grew 17.5% from the year-ago quarter's tally to $139.6 million and surpassed management's guidance of $135 million.

Revenues outside the United States improved 38% to $234 million and contributed 25% to total revenues.

The company witnessed rapid deployment of HCM solution in the fiscal third quarter. The company added 11 Global 2000 and six Fortune 500 companies in the reported quarter.

Margin Details

Non-GAAP expenses pertaining to Product development, Sales and marketing, and General and administrative climbed 11.8% year over year to $568.6 million.

The company generated non-GAAP operating income of $142.6 million, up 186.9% year over year.

Non-GAAP operating margin expanded 850 bps on a year-over-year basis to 15.2% on higher revenue base and expense control measures. The company had anticipated non-GAAP operating margin of approximately 10.5%. Notably, the company had anticipated expenses pertaining to marketing initiatives and hiring, which have moved into the fiscal fourth quarter.

Balance Sheet & Cash Flow

Cash, cash equivalents and marketable securities were $2.10 billion as of Oct 31, 2019 compared with $1.93 billion in the previous quarter.

Workday generated operating cash flow of $258 million compared with prior-quarter figure of $100.3 million.

Guidance

For fourth-quarter fiscal 2020, Workday expects subscription revenues in the range of $828-$830 million (indicating year-over-year growth of 23%). Professional services revenues are projected at $134 million.

The company raised fiscal 2020 guidance for subscription services revenues. It now expects subscription services revenues in the range of $3.085-$3.087 billion (previously $3.06-$3.07 billion). Professional services revenues are now projected to be around $529 million (previously $520 million).

The company continues to expect non-GAAP operating margin to be approximately 13%, up from the prior guidance of 12.3%. The guidance takes recently announced acquisition of Scout RFP for approximately $540 million in cash into account. The company expects the buyout to close in fourth-quarter fiscal 2020.

For fiscal 2021, management expects subscription services revenue of approximately $3.73 billion, indicating growth of approximately 21% year over year. Scout RFP is anticipated to contribute less than 1% to subscription services revenue growth.

For fiscal 2021, non-GAAP operating margin is anticipated at 14%. Excluding the Scout acquisition, non-GAAP operating margin is envisioned at approximately 15.5%. Over the long-term, Workday is committed to achieve non-GAAP operating margin of more than 25%.

Recent News

On **Dec 9, 2019**, Workday concluded acquisition of Scout RFP. The buyout is anticipated to aid customers in enhancing source-to-pay solution and optimizing spend.

On **Nov 4, 2019**, Workday announced acquisition of Scout RFP for approximately $540 million in cash. The company expects the buyout to close in the fourth quarter of fiscal 2020.

On **Aug 7, 2019**, Workday added Grant Thornton LLP as its Workday Advisory Services Partner. Expanding partner base aids the company to boost adoption of its HCM and Financial Management offerings.

Valuation

Workday shares are down 7.7% in the past six-month period, but up 1.1% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 0.8% while the Zacks Computer & Technology sector are up 16.3% in the past six-month period, respectively. Over the past year, the Zacks sub-industry and the sector are up 14.4% and 30.1%, respectively.

The S&P 500 index is up 12.7% in the past six-month period and 23% in the past year.

The stock is currently trading at 9.95X forward 12-month sales, which compares to 6.55X for the Zacks sub-industry, 3.67X for the Zacks sector and 3.49X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.96X and as low as 6.09X, with a 5-year median of 9.49X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our $201 price target reflects 10.63X forward 12-month sales.

The table below shows summary valuation data for WDAY

Valuation Multiples - WDAY

		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	9.95	6.55	3.67	3.49
	5-Year High	20.96	15.61	3.67	3.49
	5-Year Low	6.09	3.03	2.30	2.54
	5-Year Median	9.49	5.31	3.01	3
P/B TTM	Current	18.66	7.38	5.56	4.49
	5-Year High	24.35	8.17	5.63	4.55
	5-Year Low	8.39	2.28	3.13	2.85
	5-Year Median	15.39	5.16	4.22	3.62
EV/Sales TTM	Current	12.04	7.19	4.36	3.29
	5-Year High	20.06	11.57	4.36	3.3
	5-Year Low	6.54	3.01	2.56	2.16
	5-Year Median	11.11	5.98	3.46	2.8

As of 01/30/2020

Industry Analysis **Zacks Industry Rank:** Top 41% (104 out of 255)

Top Peers

Automatic Data Processing, Inc. **(ADP)**	Neutral
Ceridian HCM Holding Inc. **(CDAY)**	Neutral
salesforce.com, inc. **(CRM)**	Neutral
HubSpot, Inc. **(HUBS)**	Neutral
Microsoft Corporation **(MSFT)**	Neutral
Oracle Corporation **(ORCL)**	Neutral
Anaplan, Inc. **(PLAN)**	Neutral
SAP SE **(SAP)**	Neutral

Industry Comparison Industry: Internet - Software

Industry Peers

	WDAY Neutral	X Industry	S&P 500	ADP Neutral	ORCL Neutral	SAP Neutral
VGM Score	C	-	-	C	B	D
Market Cap	43.27 B	672.17 M	23.91 B	75.72 B	171.00 B	156.33 B
# of Analysts		4	13	11	13	5
Dividend Yield	0.00%	0.00%	1.77%	2.08%	1.80%	0.92%
Value Score	F	-	-	D	B	C
Cash/Price	0.05	0.11	0.04	0.06	0.16	0.04
EV/EBITDA	-449.16	-1.65	14.07	16.14	11.25	18.85
PEG Ratio	3.93	2.69	2.00	2.18	1.41	2.03
Price/Book (P/B)	18.66	5.23	3.27	14.12	10.56	4.53
Price/Cash Flow (P/CF)	440.81	34.14	13.48	20.49	12.09	22.66
P/E (F1)	106.30	59.22	18.76	28.39	13.71	21.15
Price/Sales (P/S)	12.58	4.13	2.61	5.22	4.32	5.07
Earnings Yield	0.95%	0.75%	5.32%	3.52%	7.30%	4.73%
Debt/Equity	0.54	0.12	0.72	0.25	3.13	0.42
Cash Flow ($/share)	0.43	-0.01	6.88	8.54	4.41	5.78
Growth Score	A	-	-	B	D	D
Hist. EPS Growth (3-5 yrs)	NA%	16.72%	10.68%	15.36%	6.17%	4.96%
Proj. EPS Growth (F1/F0)	31.88%	13.64%	7.73%	13.09%	10.47%	8.29%
Curr. Cash Flow Growth	32,349.57%	2.02%	12.29%	15.63%	-0.35%	-1.75%
Hist. Cash Flow Growth (3-5 yrs)	24.78%	14.22%	8.78%	14.63%	-1.03%	1.98%
Current Ratio	1.19	1.53	1.23	1.02	2.37	1.05
Debt/Capital	34.91%	19.84%	43.16%	20.26%	75.79%	29.53%
Net Margin	-13.29%	-14.43%	11.59%	16.97%	27.62%	12.07%
Return on Equity	-11.63%	-12.25%	17.38%	46.96%	56.86%	15.41%
Sales/Assets	0.59	0.66	0.54	0.33	0.37	0.46
Proj. Sales Growth (F1/F0)	28.09%	17.93%	4.05%	5.63%	1.07%	5.90%
Momentum Score	D	-	-	A	B	A
Daily Price Chg	2.47%	0.00%	-0.21%	2.32%	0.21%	-0.52%
1 Week Price Chg	2.77%	0.00%	-1.09%	0.19%	-1.92%	-0.64%
4 Week Price Chg	12.35%	3.15%	-0.01%	2.75%	-1.19%	-4.27%
12 Week Price Chg	17.27%	6.81%	4.14%	7.96%	-4.77%	-3.04%
52 Week Price Chg	3.65%	0.00%	17.24%	25.15%	6.13%	26.64%
20 Day Average Volume	1,685,276	317,770	1,824,613	1,743,013	8,923,589	735,748
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.23%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.23%	0.00%	0.00%
(F1) EPS Est 12 week change	4.27%	0.00%	-0.11%	0.12%	-0.02%	0.00%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	-1.66%	0.00%	0.00%

Zacks Stock Rating System

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

Zacks Recommendation

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

Zacks Rank

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

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	A
Momentum Score	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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