

Palo Alto Networks

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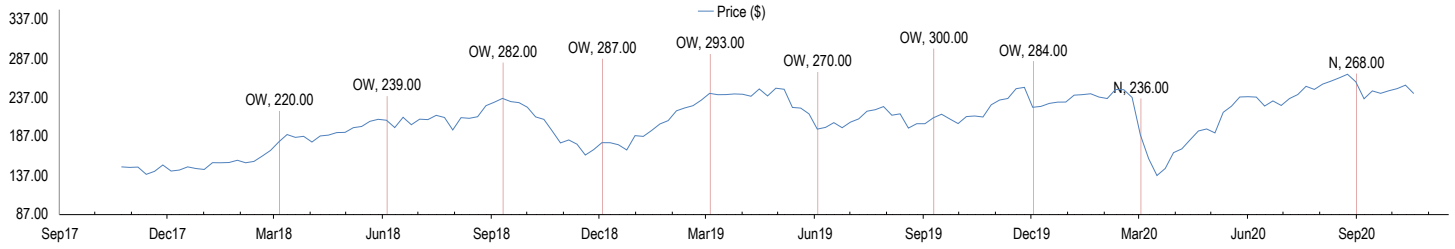
J.P.Morgan

Equity Research
J.P. Morgan Securities LLC

20 October 2020

Recommendation	Price Target	PT End Date	Price	Upside/Downside to PT
Neutral	\$268.00	31-Dec-21	\$239.28	12.00%

Palo Alto Networks, Inc. provides network security solutions. The Company offers firewalls that identify and control applications, scan content to stop threats, prevent data leakage, integrated application, user, and content visibility. Palo Alto Networks serves customers worldwide.



Note: All analysts forecasts are as of last note published on 25-Aug-2020
The Upside/Downside to PT is calculated based on the previous day's closing price which is quoted above.

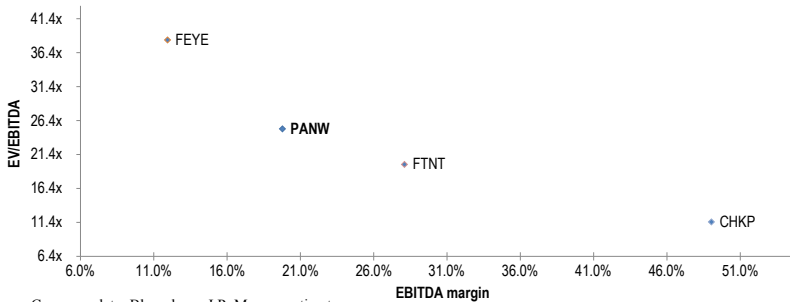
Source: Bloomberg, J.P. Morgan estimates.

Key Financials (\$mn, year end Jul)	FY19	FY20	FY21E	FY22E	FY23E
Revenue	2,900	3,408	4,003	4,693	n/a
EBITDA	738	729	792	984	n/a
EBIT	637	599	699	870	n/a
Pretax Income	692	621	718	915	n/a
Net Profit	539	485	560	714	n/a
Total Assets	6,592	9,065	10,605	12,493	n/a
Shareholder Equity	1,586	1,102	1,662	2,435	n/a
Adjusted Net Debt/(Cash)	n/a	n/a	n/a	n/a	n/a
Capex	(131)	(214)	(214)	(235)	n/a
Free Cash Flow to firm	905	807	968	1,322	n/a
EPS (\$)	5.45	4.88	5.53	6.88	n/a
DPS	n/a	n/a	n/a	n/a	n/a

Key Ratios	FY19	FY20	FY21E	FY22E	FY23E
EBITDA Margin	25.5%	21.4%	19.8%	21.0%	n/a
EBIT Margin	22.0%	17.6%	17.5%	18.5%	n/a
Net Margin	18.6%	14.2%	14.0%	15.2%	n/a
Payout Ratio	n/a	n/a	n/a	n/a	n/a
Net Debt/Equity (excl MI)	n/a	n/a	n/a	n/a	n/a
FCF Yield	3.8%	3.4%	4.0%	5.3%	n/a
P/E	43.9x	49.0x	43.3x	34.8x	n/a
EV/EBITDA	31.0x	28.7x	25.2x	18.9x	n/a
ROE	39.3%	36.1%	40.5%	34.8%	n/a

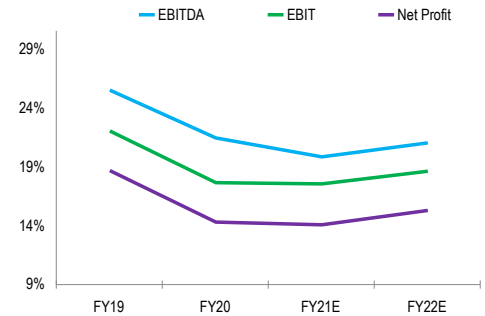
Source: Company data, Bloomberg, J.P. Morgan estimates.

Peer Valuation Chart FY21



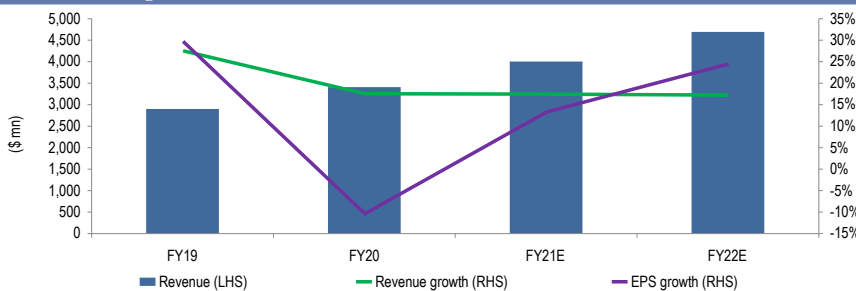
Source: Company data, Bloomberg, J.P. Morgan estimates.

Margin Analysis (PANW)



Source: Company data, J.P. Morgan estimates.

Revenue and EPS growth



Source: Company data, J.P. Morgan estimates.

Company Data

Market Cap (USDmn)	24,883
Shares O/S (mn)	104
Float	97.0%
Dividend Yield	n/a
EPS (\$)	5.53
3M - Avg daily volume (mn)	1.09
52 wk High/Low (\$)	275.03-125.47

JPM EPS Estimate		BBG EPS Estimate	
FY21E	FY22E	FY21E	FY22E
5.53	6.88	5.58	6.83

Source: Company data, Bloomberg, J.P. Morgan estimates.

Peer Valuation Analysis	Ticker	Fiscal Year End	Last Note Published	Rating	Price Target	Mkt Cap (\$mn)	EV/EBITDA		P/BV		P/E		ROE	
							FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Local peers														
FireEye	FEYE	2019/12	29-Jul-20	OW	\$18.00	3,453	38.3x	n/a	5.6x	n/a	53.5x	n/a	10.1%	n/a
Check Point Software	CHKP	2019/12	22-Jul-20	N	\$141.00	18,369	11.5x	n/a	5.5x	n/a	18.4x	n/a	29.3%	n/a
Fortinet, Inc	FTNT	2019/12	07-Aug-20	N	\$140.00	22,394	19.9x	15.8x	15.1x	10.5x	40.1x	34.2x	48.0%	36.5%
Global peers														
Palo Alto Networks	PANW	2020/7	25-Aug-20	N	\$268.00	24,883	25.2x	18.9x	14.6x	10.2x	43.3x	34.8x	40.5%	34.8%
Median							22.6x	17.3x	10.1x	10.3x	41.7x	34.5x	34.9%	35.6%
Mean							23.7x	17.3x	10.2x	10.3x	38.8x	34.5x	32.0%	35.6%
High							38.3x	18.9x	15.1x	10.5x	53.5x	34.8x	48.0%	36.5%
Low							11.5x	15.8x	5.5x	10.5x	18.4x	34.2x	10.1%	36.5%

Source: Company data, J.P. Morgan estimates.

Investment Thesis

Palo Alto Networks is the leading independent network security company targeting one of the largest segments of the cybersecurity industry with one of the best integrated product lines (platforms) on the market. The combination of its market-leading technology, breadth of solutions that tie together network, endpoint, and orchestration/analytics along with go-to-market execution is helping the company gain market share against legacy incumbents like Check Point (CHKP/N) and Cisco (CSCO/N/covered by Samik Chatterjee). PANW has made a series of cloud asset acquisitions and built out a solid cloud portfolio; however, sales execution issues around product revenues in the 1H20 and shift to the cloud are leading to continued product revenue declines. When Next Gen Security is large enough to drive growth acceleration is when we think shares can again sustainably outperform but until then we believe the decline in product will put pressure on billings growth and topline growth and remain Neutral.

Valuation

Maintaining Neutral rating and establishing December 2021 price target of \$268

Our Dec 2021 price target of \$268 (replaces prior Dec 2020 PT of \$236) is based on 18x EV/FCFF multiple applied to our CY22 FCF estimates. The 18x multiple is in line with the topline growth we model through FY22.

Risks to Rating and Price Target

- If the current sales execution issues persist into the coming quarter, revenue could suffer and the stock price could come under pressure; however, if sales execution improves, we could see upside to our stock price expectations.
- Spending in cybersecurity has been a top priority for the past five years; if that spending focus by customers were to fade growth then share performance could suffer.
- Duration is only expected to shorten 10% through FY22. If the macro environment worsens and goes into recession we would expect lower levels of multi-year payments, putting downward pressure on cash flow and our price target.

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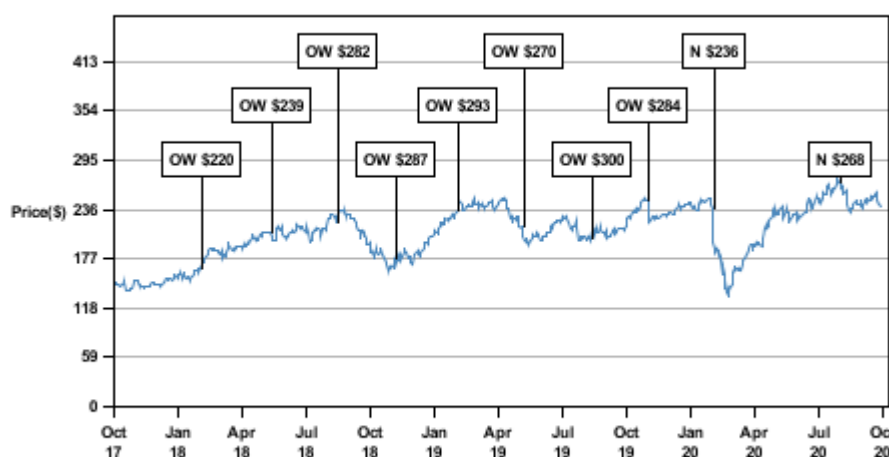
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Palo Alto Networks (PANW, PANW US) Price Chart



Date	Rating	Price (\$)	Price Target (\$)
26-Feb-18	OW	165.54	220
04-Jun-18	OW	209.19	239
07-Sep-18	OW	220.37	282
29-Nov-18	OW	176.54	287
27-Feb-19	OW	235.55	293
30-May-19	OW	215.32	270
05-Sep-19	OW	200.49	300
25-Nov-19	OW	246.87	284
25-Feb-20	N	237.33	236
24-Aug-20	N	269.33	268

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Jul 13, 2015. All share prices are as of market close on the previous business day.

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