SAP SE (SAP)

Updated October 23rd, 2018 by Nick McCullum

Key Metrics

Current Price:	$108	**5 Year CAGR Estimate:**	6.7%	**Volatility Percentile:**	15.0%
Fair Value Price:	$89	**5 Year Growth Estimate:**	9.0%	**Momentum Percentile:**	40.3%
% Fair Value:	121%	**5 Year Valuation Multiple Estimate:**	-3.8%	**Growth Percentile:**	82.4%
Dividend Yield:	1.1%	**5 Year Price Target**	$137	**Valuation Percentile:**	21.9%
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Total Return Percentile:**	35.2%

Overview & Current Events

SAP SE develops, sells, and maintains a variety of enterprise software products that are used by corporations, governments, and educational agencies. The company employs more than 93,800 people and has more than 404,000 customers in more than 180 countries. SAP is headquartered in Germany and reports financial results in Euros. American investors can initiate an ownership stake in SAP through American Depository Receipts that trade on the New York Stock Exchange under the ticker SAP with a market capitalization of US$133 billion.

In mid-October, SAP reported (10/18/18) financial results for the third quarter of fiscal 2018. In the quarter, total revenue increased by 8% (or 10% at constant-currency). The company's robust top-line performance was driven by strength in a number of specific operating segments. More specifically, SAP saw cloud subscription revenue increase by 39% (or 41% on a constant-currency basis) while new cloud bookings were up 36% (or 37% at constant-currency). Further down the income statement, SAP's adjusted operating profit rose by 11% while adjusted earnings-per-share rose 13% from the same period a year ago.

Because of the firm's strong results, SAP raised its guidance for the full year of fiscal 2018. The enterprise software giant now expects adjusted cloud subscriptions and support revenue to be in the range of €5.150 billion to €5.250 billion, which represents 36.5%-39.0% growth from the €3.77 billion reported in fiscal 2017. Adjusted cloud and software revenue is expected to increase by 8%-9% while total revenue is anticipated to rise by 7.5%-8.5%. Lastly, constant-currency operating profit is expected to increase by 9.5%-11.0%. Despite SAP's strong financial performance, the stock has traded down by more than 7% since the publication of its third quarter earnings release, likely due in part to a wider market selloff as well as the company's too-high valuation prior to the earnings release.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$2.25	$2.20	$2.02	$3.27	$3.12	$3.83	$3.54	$3.21	$3.21	$4.03	***$4.45***	***$6.85***
DPS	$0.78	$0.68	$0.60	$0.87	$0.99	$1.11	$1.36	$1.22	$1.30	$1.36	***$1.50***	***$2.30***
Shares	1187.3	1188.8	1187.7	1190.3	1191.5	1193.7	1195.2	1197.5	1198.6	1197.0	***1197.5***	***1200.0***

SAP has managed to generate impressive business growth over the last ten years. More specifically, the last decade saw the enterprise software giant compound its adjusted earnings-per-share at 12.4% per year. Looking ahead, we believe that SAP's growth will likely moderate to the high single-digits. We are forecasting 9% annualized earnings-per-share growth over the next 5 years. SAP is expecting operating profit to grow by approximately 10% in fiscal 2018, and we believe that earnings-per-share are likely to expand by a similar amount, which gives us a 2018 earnings-per-share estimate of $4.45. Applying a 9% growth rate to this figure allows us to calculate a 2023 estimate of $6.85.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	21.2	19.3	23.4	17.7	21.3	20.3	21.4	22.4	25.6	25.7	***24.3***	***20.0***
Avg. Yld.	1.6%	1.6%	1.3%	1.5%	1.5%	1.4%	1.8%	1.7%	1.6%	1.3%	***1.5%***	***1.7%***

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SAP's post-earnings price decline has driven its price-to-earnings ratio down to 24.3, which is much better than the 27.0 earnings multiple it traded at during the time of our last quarterly research report. Our fair value target for SAP is a price-to-earnings ratio of 20. If the company's price-to-earnings ratio contracts to 20 over the next 5 years, this will reduce its total returns by 3.8% per year during this time period.

Investors should note that Germany imposes a 26% dividend withholding tax. This lowers SAP's net yield to 1.1%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

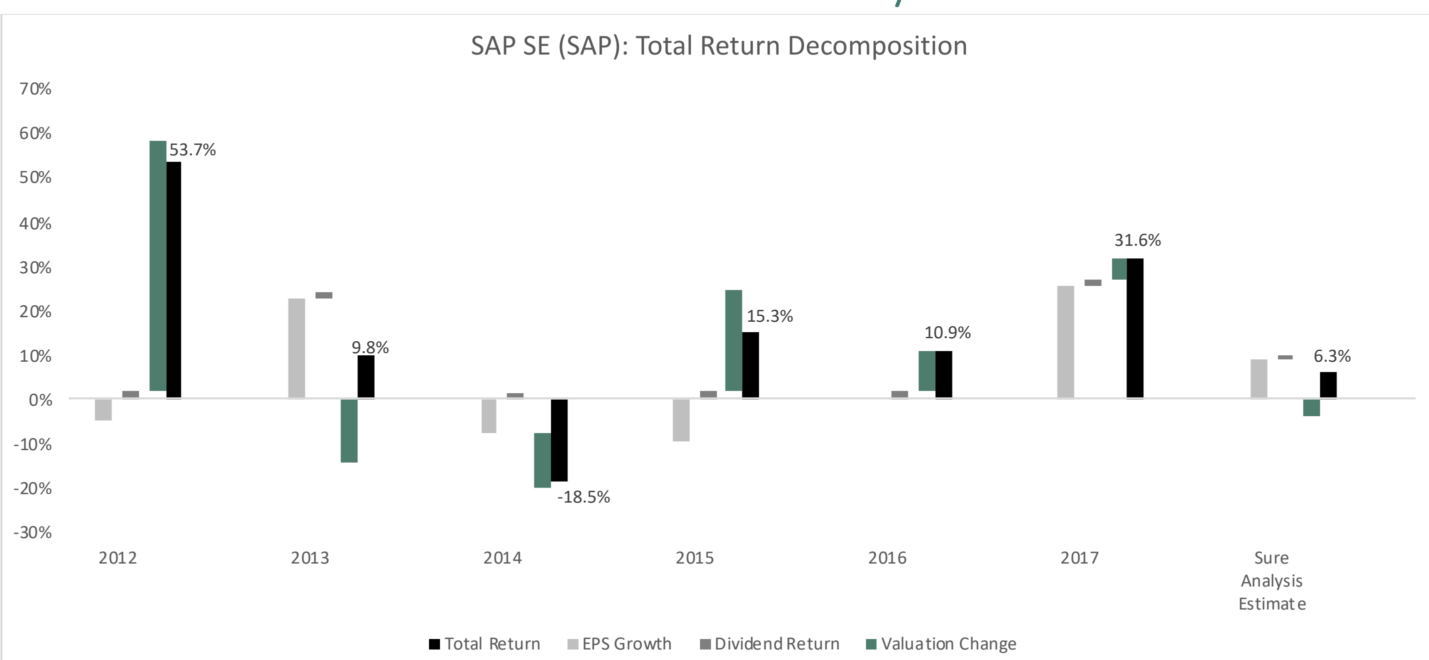
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	57.0%	52.2%	41.0%	45.8%	41.2%	41.8%	35.7%	35.7%	36.6%	36.5%	***36.0%***	***35.0%***
Debt/A	48.4%	36.5%	52.9%	45.3%	46.3%	40.8%	49.3%	43.7%	40.4%	39.9%	***40.0%***	***40.0%***
Int. Cov.	53.9	31.9	36.8	117	55.2	69.3	180.3	847	135.0	N/A	***N/A***	***N/A***
Payout	33.7%	40.5%	38.0%	38.4%	29.0%	31.7%	26.6%	29.7%	30.9%	34.7%	***33.7%***	***33.6%***
Std. Dev.	41.2%	28.5%	24.9%	32.1%	26.6%	15.7%	17.3%	23.8%	18.3%	10.6%	***17.0%***	***17.0%***

Qualitatively, SAP's strongest competitive advantage is its recurring revenue business model. At the end of the most recent reporting period, 68% of the company's revenue was recurring in nature. The company expects this metric to rise to 70%-75% by 2020. Recurring revenue allows the company to optimize customer retention rates and use the resulting cash flows to aggressively invest in compelling growth opportunities (such as its cloud business). Despite these positive qualitative characteristics, SAP earns D ratings for Dividend Safety and Retirement Suitability due largely to its significant historical drawdowns in stock price.

Final Thoughts & Recommendation

As we noted at the time of our last quarterly research report, SAP is a textbook example of a high-quality business trading at poor (meaning too high) valuation. With projected returns in the mid-single-digits, SAP earns a hold recommendation from Sure Dividend at current prices.

Total Return Breakdown by Year



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Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	16989	14882	16521	19845	20857	22332	23352	23074	24417	26569
Gross Profit	11077	9989	11360	13775	14334	15650	16727	16144	17132	18584
Gross Margin	65.2%	67.1%	68.8%	69.4%	68.7%	70.1%	71.6%	70.0%	70.2%	69.9%
SG&A Exp.	4653	3853	4349	5296	6249	6636	7294	7579	8046	9059
D&A Exp.	791	696	708	1009	1110	1263	1343	1430	1403	1441
Operating Profit	4052	3963	4727	5791	5207	5999	6338	5409	5713	5730
Op. Margin	23.9%	26.6%	28.6%	29.2%	25.0%	26.9%	27.1%	23.4%	23.4%	21.6%
Net Profit	2711	2438	2400	4789	3604	4417	4362	3400	4035	4550
Net Margin	16.0%	16.4%	14.5%	24.1%	17.3%	19.8%	18.7%	14.7%	16.5%	17.1%
Free Cash Flow	2670	3891	3430	4643	4218	4338	3673	3331	4014	4270
Income Tax	1139	955	696	1856	1277	1422	1430	1038	1360	1099

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	19424	19125	27718	30086	34790	37409	46896	45252	46808	50984
Cash & Equivalents	1789	2694	4679	6431	3276	3795	4047	3729	3914	4812
Acc. Receivable	4441	3641	4122	4444	5074	5249	5172	5683	6156	6969
Inventories	7	16	16	14						
Goodwill & Int.	8545	8420	14373	13905	21723	22986	31135	29485	28646	29082
Total Liabilities	9403	6983	14652	13627	16099	15249	23142	19783	18902	20343
Accounts Payable	837	912	1226	942	905	884	951	976	1073	1142
Long-Term Debt	3243	9	1462	5126	6579	5894	13480	10053	8330	7561
Total Equity	10018	12122	13043	16449	18680	22149	23711	25438	27884	30603
D/E Ratio	0.32	0.00	0.11	0.31	0.35	0.27	0.57	0.40	0.30	0.25

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	15.7%	12.6%	10.2%	16.6%	11.1%	12.2%	10.3%	7.4%	8.8%	9.3%
Return on Equity	27.8%	22.0%	19.1%	32.5%	20.5%	21.6%	19.0%	13.8%	15.1%	15.6%
ROIC	23.8%	19.2%	18.0%	26.5%	15.4%	16.6%	13.4%	9.3%	11.2%	12.2%
Shares Out.	1187	1188.8	1187.7	1190.3	1191.5	1193.7	1195.2	1197.5	1198.6	1197.0
Revenue/Share	14.26	12.52	13.90	16.68	17.48	18.69	19.51	19.26	20.36	22.18
FCF/Share	2.24	3.27	2.89	3.90	3.54	3.63	3.07	2.78	3.35	3.56

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.