

October, 28, 2017

## Verint Systems Inc.: VRNT

Ryan Rosmarin

**Sector:** Information Technology

**Industry:** Application Software & Cyber Security

**Current Price:** \$42.85

**Target Price:** \$52.75

**Company Description:** Verint Systems Inc. is a global leader in actionable intelligence solutions and cyber security for over 10,000 organizations and governments in more than 180 countries. With the growth of big data across all industries, Verint Systems provides organizations with crucial insights and allows decision makers to anticipate, respond, and efficiently take action with its Customer Engagement and Cyber Intelligence solutions. By combining enterprise-class software with advanced analytics, Verint offers a large variety of customizable services to its customers protected by more than 800 patents worldwide.

### BUY

Current Price:	\$42.85
Target Price:	\$52.75
Market Cap:	2.73B
52 Week Range:	\$33.40-\$44.70
Average Volume:	423,555
D/E Ratio:	0.74
EBITDA Margin:	12.39%
12M Total Return:	18.61%
ROE:	-2.84%
Cost of Equity:	9.2%

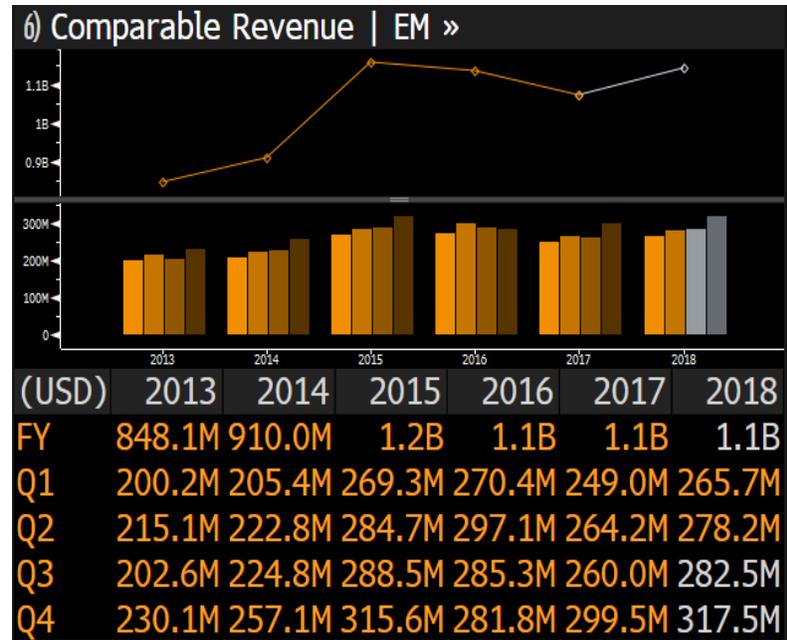
### Catalysts:

- **Short-Term** (within the year): Organic growth opportunity within Cyber Intelligence segment
- **Mid-Term** (1-2 years): Heightened geopolitical risk environment along with forecasted recovery in the cyber security industry
- **Long-Term** (3+years): Continual growth of actionable intelligence use among business & increasing cyber threats worldwide



### Thesis:

Verint Systems Inc. is a worldwide leading force in the expanding actionable intelligence market and will continue to drive organic growth within its Customer Engagement and Cyber Intelligence segments. With over 14,000 professionals working in Research & Development, Verint consistently develops its artificial intelligence platform, allowing organizations to drive efficiencies and cut costs over time. In a risky geopolitical environment, with cyber security threats at an all-time high, Verint can expect revenue growth from a large increase in demand in its cyber intelligence segment. With its Customer Engagement segment, Verint has opportunity for organic growth as industries increasingly shift more towards automating operational activities. Verint’s ability to attract new customers through its innovation and flexibility will create internal value and drive the company’s stock price.



### Business Overview:

Verint Systems Inc. offers its customers an advanced actionable intelligence platform through a four component foundation of data capturing, processing, analysis, and visualization across its Customer Engagement and Cyber Intelligence segments. Verint’s platform allows companies to capture and manage a wide range of structured/unstructured operational, transactional, network, and web data to be used in big data applications. Verint Systems then facilitates the cleansing, fusing, and preparation of the data for analysis where it is classified through a wide range of engines. The analytical process includes correlations, anomaly detection, identity extraction, behavioral analysis, and predictive analytics. This allows for the identification of crucial insights for management during the visualization process and helps them make informed and effective decisions more efficiently. Unlike most of its competitors, Verint provides its network of organizations with deployment flexibility on premise, in the private/public cloud, or in a hybrid fashion. Enterprises are able to integrate Verint solutions on a modular basis as they decide to add pieces of the Verint portfolio to their business over time. Verint’s strategic product flexibility allows for repeat business and the attraction of new customers through its reputation of innovation and domain expertise. The Customer engagement segment offers customer-centric organizations the ability optimize customer interactions, increase loyalty, and maximize revenue opportunities while reducing costs and mitigating risks. The Verint solution allows companies to lever real-time shared intelligence across the enterprise, increasing efficiency and quality as operations become more automated. In the cyber intelligence segment, Verint is a leading provider of security and data mining software to intelligence agencies, national security and law enforcement agencies, and correctional facilities. To enhance its services, Verint also collaborates with various communications networks to intercept potential data threats through calls, emails, texts, social media, etc. Verint earns 51% of its revenues in the Americas, 30% in the EMEA region, and 16% in the APAC region.



## First Half Earnings Performance:

Verint Systems has beaten expectations in the first half this year, earning 48% of their full year revenue outlook, with a forecasted higher demand in the second half due to seasonality. Q1 non-GAAP revenue increased 7% year-over-year to \$266mn, earning \$177mn in Customer Engagement and \$91mn in Cyber Intelligence. On a constant currency basis, Customer Engagement revenue increased 3% and Cyber Intelligence grew 19% year-over-year. Increases in Cyber Intelligence drove a 5% year-over-year improvement in non-GAAP operating margins, as there has been an increased in demand for cyber data mining services. In Q1, Verint delivered \$10mn-plus projects to its customers as well as striking a multimillion-dollar deal with the Latin American government to protect the country against large-scale cyber-attacks. In Q2, Verint delivered \$278mn in total revenue, increasing 4.5% for Q1 and 5.3% year-over-year. Customer Engagement revenue totaled \$184mn increasing 5% from Q1 and at a steady pace of 3% year-over-year. Growth in the Customer Engagement segment was largely due to several \$5mn-plus deals with financial, insurance, telecommunications, and health care services. Cyber Intelligence revenue increased 4% from Q1 to \$95mn, a 12% increase from last year. Verint Systems continues to drive company growth with the increasing demand and improvements in its Cyber Intelligence segment. With the further evolution of security threats worldwide, Verint increased research & development expenditure in the first half and is likely to continue its expansion for the remainder of the year. Verint's latest addition to its Cyber Intelligence platform in Q2 was the release of its new web and social intelligence suites that enhance real time, open source data collections with advance machining and data mining software. The system transforms large volumes of web and social media content into insights, allowing for the identification of suspicious behavioral patterns and the creation of predictive intelligence. Geographically, Q2 led to revenue growth in all regions totaling \$144mn, \$85mn, and \$49mn in the America's, EMEA, and APAC regions respectively. Q2 non-GAAP gross margins were approximately 65% with an operating margin of \$45.6mn, 16.4%. Adjusted EBITDA margins came in at 19.1% of non-GAAP revenue, totaling \$53.2mn. In Q2, Verint earned a net gain of \$3.2mn from foreign exchange and benefited from a \$1.3mn tax reversal of an accrual that was no longer necessary. At the end of the first half, Verint held \$441mn in cash and short-term investments with \$100mn in cash from operations, 45% increase year-over-year. Net debt totaled \$385mn, after Verint acted on an attractive credit market to refinance their term loan, extending its maturity to seven years. Verint Systems expects revenues of \$285mn in Q3 with mid-single digit growth in Customer Engagement and high single digit growth in Cyber Intelligence



## Growth Strategy:

Verint Systems continues to grow through its reputation for innovation and domain expertise, making them a strategic vendor for organizations looking to advance their customer engagement and cyber intelligence. Verint's broad portfolio of software and supporting services continues to enhance operational efficiency, reduce cost, and drive revenues for its customers. Growth in the Customer Engagement segment will be driven by Verint's business approach of flexibility, providing them with a competitive advantage among its competitors. Verint's flexible business model permits organizations to evolve their customer engagement

platform at different paces, allowing them the adaptation to priorities and trends unique to their company. In addition, Verint has cloud-enabled their customer engagement optimization portfolio allowing organizations to deploy Verint solutions in the way that best meets their objectives, whether it is on premise, in a private/public cloud, or in a hybrid fashion. Cloud generated revenue has currently grown 25% year-over-year and continues to gain scale in Verint’s solutions, offering higher profit margins than the traditional on premise application process. Driven by upsell opportunities around analytics and CRM tools, Customer Engagement is expected to grow around 10% over the next two years.



**Cyber Intelligence**

- Leading provider of security and intelligence data mining software
- Used for predictive intelligence, complex investigations, security threat analysis, and to prevent crime and terrorism
- Deployed by governments, critical infrastructure providers and enterprise customers

**Security threats becoming more complex**

**Shortage of qualified intelligence analysts**

**Growth Trends**

**Demand for data mining solutions built with domain expertise**

After double-digit growth in Q1 and Q2, Verint Systems continues to growth its Cyber Intelligence segment, the primary driver of Verint’s stock. Making up 35% of sales, Cyber Intelligence captures, processes, and analyzes big data volumes across communications networks, the internet, and dark web. The reprioritization of Cyber Intelligence with a renewed budget and heightened geopolitical concern will continue to drive organic revenue growth of at least 10% within the segment. The recent 7% depreciation of the US dollar against a trade-weighted basket of currencies will also contribute to revenue growth, as international sales is a large portion of Verint’s revenue. Prior appreciation of the USD created significant headwinds to the purchasing power of Verint’s customers. With the generation of most Cyber Intelligence revenue from Governments, Verint plans to leverage their experience to offer more cyber security and data mining to infrastructure providers and enterprises that fear security breaches. With an expected 15% CAGR in the cyber intelligence market, Verint remains in good position to expand existing customer platform and win multimillion-dollar deals among new ones. In the last year, Verint has signed over \$380mn in large cyber security contracts.

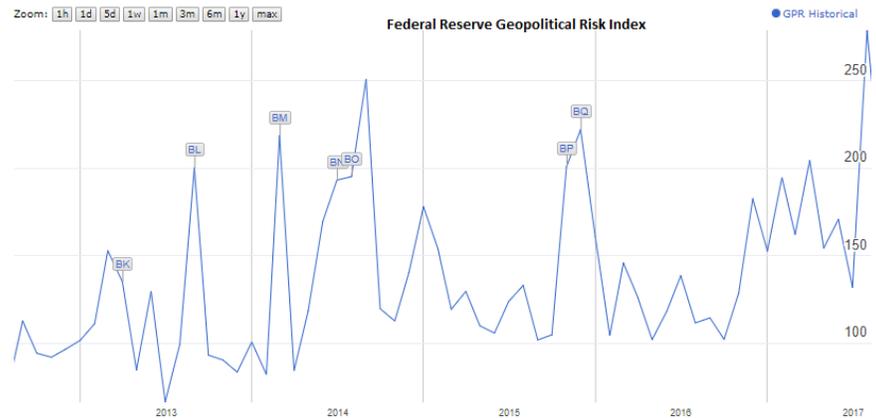
## Industry Analysis:

The overall forecast for the Information Technology sector on the Russell 2000 index continues to look promising as it has outperformed the RTY Index by 6.23% YTD and has beaten it by 45.09% over the last five years. The Russell 2000 IT segment has returned 18.75% YTD as R&D continues to pour into technological innovation, driving growth for the industry as a whole. High levels of product elasticity and substitutes spur competition within the index putting upward pressure on the profit margins of companies who can successfully adapt. More specific to Verint’s operations, the cyber intelligence industry has grown at a CAGR of 20% in 2017 and is forecasted to have a CAGR of 15% over the next two years. As cyber threats and data breaches continue to become more frequent and complex, demand will heavily increase for Verint solutions. Additionally, growth in the cyber intelligence industry has historically been 80% correlated to oil prices and emerging market GDP. Emerging market GDP yoy has increased to 5.2% and is forecasted to stabilize at 5.5%, while WTI crude prices are up around 20% YTD, signaling bullish sentiment in the cyber intelligence industry. Between 2017-2021, global cyber security products and service expenditure is projected

to exceed \$1 trillion cumulatively. This is a potential growth environment for Verint Systems who will continue to be a leading provider in the industry. Another driver of the industry is the economic optimism under the Trump Administration. Markets continue to act bullish despite geopolitical concerns and a projected increasing rate environment. Trump's pro-growth strategy, tax-cuts, and deregulation should have a positive influence on Verint solutions, enabling them easier access to new markets and business expansion.

## Geopolitical Concern:

With sharp increases in the frequency and complexity of cyber-attacks, the demand for cyber intelligence security among world governments continues to grow at an all-time high. This increase in demand is further driven with the high tensions of the current geopolitical environment, which has reached its highest level on the Fed's



GPR Index in the last three years. Historically, there has been three war domains described by NATO: Air, Land, and Sea. In 2016, NATO added Cyber as a fourth dimension of attack between nations in times of international conflict. Increases in geopolitical risk climate lead to complex nation state attacks and heavy expenditure in global government spending on cybersecurity to hedge the risk of hackers breaking into confidential systems and information databases. In today's environment, the Fed's GPR Index has increased to 160 in Q217 compared to 104 at the end of Q416. The heightened risk of attacks from North Korea's nuclear missile program consistently drives volatility in this index as US President Donald Trump continues to combat the threats of Kim Jong Un. The North Korean missile crisis increases tensions among the US and China as well due to China's close relations with Pyongyang. This adds additional threat to two major world economies who are already in distress with current trade relations. Conflict between US and China could potentially bring Russia into the scene as they hold a strategic alliance with China to grow the eastern economy. Growth in demand for cyber intelligence is also driven by increases in acts of terror around the world by ISIS and other radical states. Since the emergence of ISIS in 2011, there has been over 70,000 terrorist attacks worldwide, many of them being against western civilizations and culture. This increase in violence furthers the demand for cyber intelligence among world governments, allowing them to discover acts of terror before they occur. Verint's cyber intelligence technology can track individual persons and groups who pose a threat to national security by scanning for key indicators through their conversations, social media presence, and web browsing. This increase in demand represents significant growth potential for Verint Systems as their stock price is 85% correlated to its growth in its Cyber Intelligence segment. As a leading provider of cyber intelligence in the IT sector, Verint will create value through the organic growth of its CI segment.

## Competitors:

Verint's margins are closer to the median compared to its competitors, leaving significant room for growth as the company becomes more profitable. Although margins are currently low due to the high expenses of operation, Verint continues to improve through sales growth and market expansion. With EBITDA and Operating margins of 16.05% and 5.75% respectively, Verint performs above the median of its competitors, as low margins are common within the industry. Verint's margins are forecasted to increase as the cyber intelligence industry recovers from a slowdown in EBIT over the past two years due in part to reverse operating leverage in the segment when sales were under pressure. After making some adjustments to cost structure in 2017, Verint maintained a high base level of investment in belief that the spending slowdown would only be temporary. Over the next two years, EBIT margins are expected to return to a range of 15-20%, with Verint growing around 25% on a longer-term basis. Margins will increase in Customer Engagement as well as Verint shifts from on premise to cloud based solution integration.

Name	Sales Growth (%)	EBITDA Growth (%)	EBITDA Margin	Operating Income Margin	Net Income Growth (%)
Median	5.32%	9.00%	9.58%	5.75%	9.94%
100) VERINT SYSTEMS INC	1.72%	-8.69%	16.05%	5.75%	-65.37%
101) MICROSOFT CORP	5.43%	12.52%	34.92%	25.16%	12.46%
102) INTL BUSINESS MACHINE...	-2.29%	-9.54%	20.74%	14.98%	-6.60%
103) ORACLE CORP	3.02%	3.87%	41.91%	35.09%	7.41%
104) NICE LTD	24.13%	9.00%	21.34%	11.11%	-33.93%
105) PEGASYSTEMS INC	9.40%	-20.27%	9.58%	6.26%	12.64%
106) SEACHANGE INTERNATIO...	-19.07%	62.97%	-6.36%	-13.36%	38.29%
107) EGAIN CORP	-16.11%	49.18%	-0.64%	-6.13%	-6.93%
108) REALNETWORKS INC	6.30%	50.97%	-13.66%	-17.29%	39.85%

## Conclusion:

Verint Systems Inc. stock price will appreciate 23% over the next 3-6 months as they continue to grow Cyber Intelligence in a favorable environment for information technology. Increased demand in CI due to heightened geopolitical concerns and terror threats will drive revenue and organic growth for Verint, as they are a leading provider in the industry. Verint will grow sales and attract new customers in CE, as firms continue to become more reliant on technology and look to operate with big data applications and cloud software. Verint Systems continues to invest heavily into research & development, leading to a wider range of solutions and increased reputation for innovation and domain expertise. In the current market environment, Verint Systems has strong potential for earnings growth, higher margins, and value creation.

### Verint Systems Inc. (VRNT)

## CENTER FOR GLOBAL FINANCIAL STUDIES

**BULLISH**

Analysis by **RYAN ROSMARIN**  
10/18/2017

**Current Price:** \$42.85  
**Dividend Yield:** 0.0%

**Intrinsic Value:** \$45.99  
**Target Price:** \$52.75

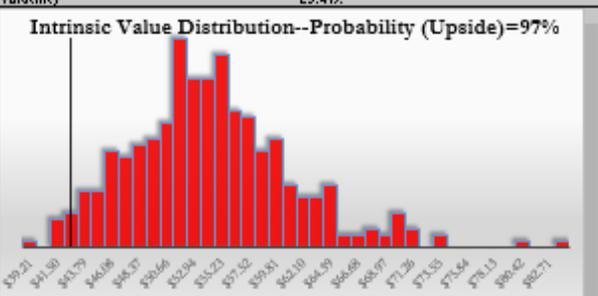
**Target 1 year Return:** 23.11%  
**Probability of Price Increase:**



Description	
Verint Systems Inc. provider actionable intelligence solutions and value-added services worldwide.	
General Information	
Sector	Information Technology
Industry	Software
Last Guidance	November 3, 2015
Next earnings date	December 2, 2017
Estimated Country Risk Premium	6.00%
Effective Tax rate	23%
Effective Operating Tax rate	23%

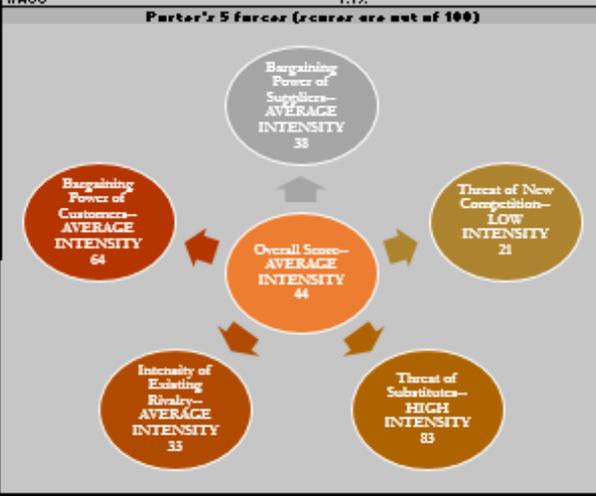
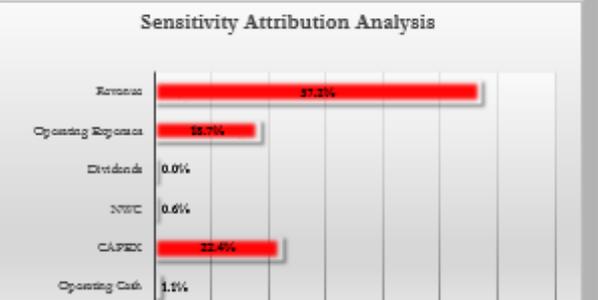
Market Data	
Market Capitalization	\$2,731.03
Daily volume (mil)	0.19
Shares outstanding (mil)	63.73
Diluted shares outstanding (mil)	62.78
% shares held by institutions	84%
% shares held by investment Manager	80%
% shares held by hedge funds	12%
% shares held by insiders	1.13%
Short interest	1.63%
Days to cover short interest	2.35
52-week high	\$44.70
52-week low	\$33.40
Volatility	25.41%

Quarter ending	Part Earning Surprises	EBITDA	Peer
7/31/2016	-1.76%	-54.10%	PTC Inc.
10/31/2016	-7.65%	-64.03%	Pega Systems, Inc.
1/31/2017	-2.05%	-49.50%	Huance Communications, Inc.
4/30/2017	0.38%	-69.75%	Synopsys, Inc.
7/31/2017	1.58%	-59.84%	Zendesk, Inc.
Mean	-1.90%	-59.44%	Salesforce.com, Inc.
Standard error	1.6%	3.6%	RealNetworks, Inc.
			SeaChange International, Inc.



Management	Position	Total compensation (mm)	Total return to shareholders
Badner, Dan	Chairman, CEO & President	4.15% per annum over 6y	4.08% per annum over 6y
Rabinran, Douglas	Chief Financial Officer	-0.68% per annum over 6y	4.08% per annum over 6y
Fante, Peter	Chief Administrative Officer	0.15% per annum over 6y	4.08% per annum over 6y
Marish, Elan	President of Customer Engage	0.59% per annum over 6y	4.08% per annum over 6y
Reden, Alan	Senior Vice President of Car	NM	NM
Sharan, Elad	President of Communications	NM	NM

Profitability	VRNT (LTM)	VRNT (5 year historical)	Peer's Median (LTM)
Return on Capital (GAAP)	3.8%	11.82%	-3.67%
Operating Margin	5%	10.44%	3.45%
Revenue/Capital (GAAP)	0.75	1.13	-1.06
ROE (GAAP)		7.7%	26.1%
Net margin		4.3%	15.6%
Revenue/Book Value (GAAP)	\$ VALUE!	1.77	1.68
Invested Funds	VRNT (LTM)	VRNT (5 year historical)	Peer's Median (LTM)
Cash/Capital	20.5%	19.5%	61.2%
NWC/Capital	-4.3%	-7.5%	-35.8%
Operating Assets/Capital	12.9%	16.0%	14.7%
Goodwill/Capital	70.9%	70.5%	59.9%
Capital Structure	VRNT (LTM)	VRNT (5 year historical)	Peer's Median (LTM)
Total Debt/Market Capitalization	0.42	0.46	0.53
Cost of Existing Debt	4.6%	5.1%	4.8%
CGFS Rating (F=prime, Z=prime, and default Probab	CC	B	B
WACC	7.7%	9.1%	10.0%



Period	Revenue Growth Forecast
Base Year	2%
7/31/2018	6%
7/31/2019	5%
7/31/2020	5%
7/31/2021	5%
7/31/2022	4%
7/31/2023	4%
7/31/2024	4%
7/31/2025	4%
7/31/2026	3%
7/31/2027	3%
Continuing Period	3%

Valuation	NOPAT Margin Forecast	Revenue to Capital Forecast
Base Year	12.1%	0.40
7/31/2018	0.6%	0.40
7/31/2019	3.5%	0.40
7/31/2020	4.5%	0.40
7/31/2021	5.2%	0.39
7/31/2022	5.7%	0.39
7/31/2023	22.2%	0.38
7/31/2024	22.0%	0.35
7/31/2025	21.8%	0.33
7/31/2026	21.6%	0.31
7/31/2027	21.3%	0.29
Continuing Period	21.1%	0.28

Period	Return on Capital Forecast	WACC Forecast	Price per share Forecast
Base Year	4.9%	7.7%	\$45.50
7/31/2018	0.2%	7.7%	\$52.11
7/31/2019	1.4%	8.1%	\$58.82
7/31/2020	1.8%	8.2%	\$65.78
7/31/2021	2.0%	8.3%	\$72.91
7/31/2022	2.2%	8.4%	\$80.21
7/31/2023	8.4%	8.9%	\$87.90
7/31/2024	7.8%	9.1%	\$95.80
7/31/2025	7.2%	9.2%	\$103.91
7/31/2026	6.7%	9.3%	\$112.25
7/31/2027	6.2%	9.5%	\$120.84
Continuing Period	5.9%	9.6%	