
Cornerstone On Demand, Inc.
CSOD - \$44.20 – NasdaqGS
2016 Fourth Quarter update

Recommendation: Sell Short**Reasons For Short Sale Recommendation**

Cornerstone On Demand is a fast growing human capital management software provider that has just become profitable. Except it isn't growing fast anymore and is barely profitable only on a non-GAAP basis. It trades at 130 times 2017 non GAAP EPS estimate of \$0.33 and 57 times 2018 non-GAAP EPS estimate of \$0.75. It earned 11 cents on a non-GAAP basis in 2016. The company is unprofitable on a GAAP basis.

Revenue growth has plunged from 80 percent to 13 percent in the last four years. So, just when the company can eke out a non-GAAP profit, revenue growth has been crushed. This will make it very hard to double even non-GAAP earnings when their top line growth is probably going to be below 10 percent next year.

But at least it generates a lot of cash flow, right? No, **free cash flow declined 44%** in the 2016 fourth quarter from \$49.2 million to \$27.5 million and **declined 15 percent for the 2016 year**, from a whopping \$14.9 million to a paltry \$12.6 million.

But at least they are buying back stock to help earnings per share growth, right? No, fully diluted shares outstanding increased 1.75 million in 2016 to 56.3 million.

“The fourth quarter capped off another strong year with 29% constant currency revenue growth,” said Adam Miller, the Company’s President and CEO. “We believe the tremendous market opportunity in learning and human capital management, combined with our position as the long-standing talent

management leader and our proven ability to innovate, will continue to fuel Cornerstone's long-term growth and **margin expansion.**”-**Gross Margin is flat to declining.**

Fourth Quarter 2016 Results:

- **Revenue** for the fourth quarter of 2016 was \$109.0 million, representing a **13.7% increase** compared to the same period in 2015. Revenue growth on a constant currency basis represented a 20.4% increase compared to the prior year.¹
- **Billings** were \$156.3 million for the fourth quarter of 2016, representing a **10.1% increase** compared to the same period in 2015.¹ Billings growth on a constant currency basis represented a 18.4% increase compared to the prior year.¹
- The Company's **operating loss for the fourth quarter of 2016 was (\$14.5) million**, yielding an **operating loss margin of (13.3)%**, compared to an **operating loss of (\$14.8) million**, yielding an operating loss margin of (15.5)%, for the fourth quarter of 2015. This represents an improvement of 220 basis points year-over-year.
- Non-GAAP operating income for the fourth quarter of 2016 was \$1.6 million, yielding a non-GAAP operating income margin of 1.5%, compared to a non-GAAP operating income of \$0.2 million, yielding a non-GAAP operating income margin of 0.2%, for the fourth quarter of 2015.¹ This represents an improvement of 130 basis points year-over-year.
- The Company's **net loss for the fourth quarter of 2016 was (\$18.6) million, or a (\$0.33) diluted net loss per share**, compared to a **net loss of (\$18.8) million, or a (\$0.35) diluted net loss per share**, for the fourth quarter of 2015.
- **Non-GAAP net loss for the fourth quarter of 2016 was \$(0.1) million, or a \$0.00 non-GAAP diluted net loss per share**, compared to a non-GAAP net loss of (\$1.2) million, or a (\$0.02) non-GAAP diluted net loss per share, for the fourth quarter of 2015.¹

- **Free cash flow for the fourth quarter of 2016 was \$27.5 million compared to free cash flow of \$49.2 million for the fourth quarter of 2015.¹ -A decline of 44 percent!**

Fiscal Year 2016 Results:

- **Revenue** for the full year of 2016 was \$423.1 million, representing a **24.6% increase** compared to the same period in 2015. Revenue growth on a constant currency basis represented a 29.1% increase compared to the prior year.¹
- **Billings** were \$453.3 million for the full year of 2016, representing a **13.2% increase** compared to the same period in 2015.¹ Billings growth on a constant currency basis represented a 20.2% increase compared to the prior year.¹
- The Company's **operating loss for the full year of 2016 was (\$56.3) million**, yielding an operating loss margin of (13.3)%, **compared to an operating loss of (\$68.7) million**, yielding an operating loss margin of (20.2)%, for the full year of 2015. This represents an improvement of 690 basis points year-over-year.
- Non-GAAP operating income for the full year of 2016 was \$7.6 million, yielding a non-GAAP operating income margin of 1.8%, compared to a non-GAAP operating loss of \$(15.1) million, yielding a non-GAAP operating loss margin of (4.4)% for the full year of 2015.¹ This represents an improvement of 620 basis points year-over-year.
- The Company's **net loss for the full year of 2016 was (\$66.8) million, or a \$(1.20) diluted net loss per share, compared to a net loss of (\$85.5) million, or a \$(1.58) diluted net loss per share**, for the full year of 2015.
- **Non-GAAP net income for the full year of 2016 was \$6.4 million, or a \$0.11 non-GAAP diluted net income per share**, compared to a non-GAAP net loss of \$(22.8) million, or a \$(0.42) non-GAAP diluted net loss per share, for the full year of 2015.¹

- **Free cash flow for the full year of 2016 was \$12.6 million compared to free cash flow of \$14.9 million for the full year of 2015.¹**

Financial Outlook:

The following outlook is based on information available as of the date of this press release and is subject to change in the future. **For the first quarter** ending March 31, 2017, the Company provides the following outlook:

- **Revenue** between \$109.0 million and \$111.0 million, representing **year-over-year growth at the mid-point of 10.8%**³, or 15.9%⁴ on a constant currency basis.

For the year ending December 31, 2017, the Company provides the following outlook:

- **Revenue** between \$475.0 million and \$485.0 million, representing **year-over-year growth at the mid-point of 13.4%**⁵, or 16.6%⁶ on a constant currency basis.
- Non-GAAP operating margin of approximately 5.0% to 6.0% of revenue.
- Non-GAAP net income margin of approximately 4.0% to 5.0% of revenue.
- Free cash flow margin of approximately 6.0% to 7.0% of revenue. = **\$31 million**.

Cornerstone OnDemand, Inc.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data)
(unaudited)

	Three Months Ended		Year Ended	
	December 31,		December 31,	
	2016	2015	2016	2015
Revenue	\$ 109,029	\$ 95,862	\$423,124	\$339,651
Cost of revenue ^{1, 2}	34,778	30,063	135,752	109,864
Gross profit	74,251	65,799	287,372	229,787
Operating expenses:				
Sales and marketing ¹	57,405	56,367	225,631	207,026
Research and development ¹	12,050	10,784	46,977	40,991
General and administrative ¹	19,345	13,332	70,956	49,877
Amortization of certain acquired intangible assets	—	150	150	600
Total operating expenses	88,800	80,633	343,714	298,494
Loss from operations	(14,549)	(14,834)	(56,342)	(68,707)
Other income (expense):				
Interest income	520	304	1,702	894
Interest expense	(3,272)	(3,163)	(12,924)	(12,506)
Other, net	(1,004)	(759)	1,934	(4,016)
Other income (expense), net	(3,756)	(3,618)	(9,288)	(15,628)
Loss before income tax provision	(18,305)	(18,452)	(65,630)	(84,335)
Income tax provision	(313)	(391)	(1,207)	(1,181)
Net loss	\$ (18,618)	\$ (18,843)	\$ (66,837)	\$ (85,516)
Net loss per share, basic and diluted	\$ (0.33)	\$ (0.35)	\$ (1.20)	\$ (1.58)
Weighted average common shares outstanding, basic and diluted	56,300	54,551	55,595	54,171

¹ Includes stock-based compensation as follows:

	Three Months Ended		Year Ended	
	December 31,		December 31,	
	2016	2015	2016	2015
Cost of revenue	\$ 1,255	\$ 1,118	\$ 4,732	\$ 3,887
Sales and marketing	6,456	6,735	25,642	23,604
Research and development	1,809	1,835	7,586	6,010
General and administrative	4,429	2,725	16,739	9,580
Total	\$ 13,949	\$ 12,413	\$ 54,699	\$ 43,081

² Cost of revenue includes amortization of intangibles as follows:

	Three Months Ended		Year Ended	
	December 31,		December 31,	
	2016	2015	2016	2015
Cost of revenue	\$ 2,217	\$ 2,492	\$ 9,132	\$ 9,968

A 13.7% increase in revenue led to a 1.2% smaller net loss.

- Page 5 -

All information contained herein is obtained by Badger Consultants, LLC from sources believed by it to be accurate and reliable. However, such information is presented "as is" without warranty of any kind and Badger Consultants, LLC makes no representation or warranty, express or implied, as to the accuracy, timeliness, or completeness of any such information. All expressions of opinion are subject to change without notice. Badger Consultants, LLC hereby discloses that the clients of Badger Consultants, LLC and we the company, officers, employees and relatives, may now have and from time to time have directly or indirectly a "long" or short position in the securities mentioned and may sell or buy such securities at any time.

Cornerstone OnDemand, Inc.

RECONCILIATIONS OF COST OF REVENUE TO NON-GAAP COST OF REVENUE, GROSS PROFIT AND GROSS MARGIN TO NON-GAAP GROSS PROFIT AND NON-GAAP GROSS MARGIN, LOSS FROM OPERATIONS TO NON-GAAP OPERATING INCOME (LOSS) AND OPERATING MARGIN TO NON-GAAP OPERATING INCOME (LOSS)

MARGIN

(in thousands)

(unaudited)

	Three Months Ended December 31,		Year Ended December 31,	
	2016	2015	2016	2015
Reconciliation of cost of revenue, gross profit and gross margin:				
Revenue	\$ 109,029	\$ 95,862	\$ 423,124	\$ 339,651
Cost of revenue	34,778	30,063	135,752	109,864
Gross profit	\$ 74,251	\$ 65,799	\$ 287,372	\$ 229,787
Gross margin	68.1%	68.6%	67.9%	67.7%
Cost of revenue	\$ 34,778	\$ 30,063	\$ 135,752	\$ 109,864
Adjustments to cost of revenue:				
Amortization of intangible assets	(2,217)	(2,492)	(9,132)	(9,968)
Stock-based compensation	(1,255)	(1,118)	(4,732)	(3,887)
Total adjustments to cost of revenue	(3,472)	(3,610)	(13,864)	(13,855)
Non-GAAP costs of revenue	31,306	26,453	121,888	96,009
Non-GAAP gross profit	\$ 77,723	\$ 69,409	\$ 301,236	\$ 243,642
Non-GAAP gross margin	71.3%	72.4%	71.2%	71.7%
Reconciliation of operating income (loss) and operating income (loss) margin:				
Loss from operations	\$ (14,549)	\$ (14,834)	\$ (56,342)	\$ (68,707)
Operating margin	(13.3)%	(15.5)%	(13.3)%	(20.2)%
Adjustments to loss from operations:				
Stock-based compensation	13,949	12,413	54,699	43,081
Amortization of intangible assets	2,217	2,642	9,290	10,568
Total adjustments to loss from operations	16,166	15,055	63,989	53,649
Non-GAAP operating income (loss)	\$ 1,617	\$ 221	\$ 7,647	\$ (15,058)
Non-GAAP operating income (loss) margin	1.5%	0.2%	1.8%	(4.4)%

Gross margin declined, Non-GAAP Gross Margin declined in 4Q16.

Loss from operations barely improved.

Cornerstone OnDemand, Inc.
RECONCILIATIONS OF NET LOSS TO NON-GAAP NET (LOSS) INCOME AND NON-GAAP NET (LOSS) INCOME PER SHARE

(in thousands, except per share amounts)
(unaudited)

	Three Months Ended		Year Ended	
	December 31,		December 31,	
	2016	2015	2016	2015
Net loss	\$ (18,618)	\$ (18,843)	\$ (66,837)	\$ (85,516)
Adjustments to net loss				
Stock-based compensation	13,949	12,413	54,699	43,081
Amortization of intangible assets	2,217	2,642	9,290	10,568
Accretion of debt discount and amortization of debt issuance costs ¹	2,325	2,213	9,130	8,691
Fair value adjustment on strategic investments ²	—	350	150	350
Total adjustments to net loss	18,491	17,618	73,269	62,690
Non-GAAP net (loss) income	<u>\$ (127)</u>	<u>\$ (1,225)</u>	<u>\$ 6,432</u>	<u>\$ (22,826)</u>
Non-GAAP basic net (loss) income per share	\$ —	\$ (0.02)	\$ 0.12	\$ (0.42)
Non-GAAP diluted net (loss) income per share	\$ —	\$ (0.02)	\$ 0.11	\$ (0.42)
Weighted-average common shares outstanding, basic	56,300	54,551	55,595	54,171
Non-GAAP weighted-average common shares outstanding, diluted	56,300	54,551	60,481	54,171

Cornerstone OnDemand, Inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Three Months Ended		Year Ended	
	December 31,	December 31,	December 31,	December 31,
	2016	2015	2016	2015
Cash flows from operating activities:				
Net loss	\$ (18,618)	\$ (18,843)	\$ (66,837)	\$ (85,516)
Adjustments to reconcile net loss to net cash provided by operating activities:				
Depreciation and amortization	8,525	7,615	32,392	27,512
Accretion of debt discount and amortization of debt issuance costs	2,325	2,213	9,130	8,691
Purchased investment premium, net of amortization	21	356	240	262
Net foreign currency loss (gain)	1,139	(85)	(7)	1,584
Stock-based compensation expense	13,949	12,413	54,699	43,081
Deferred income taxes	(736)	(105)	(736)	(105)
Changes in operating assets and liabilities:				
Accounts receivable	(39,148)	(12,314)	(38,092)	(21,837)
Deferred commissions	(4,231)	(8,169)	(2,543)	(10,296)
Prepaid expenses and other assets	184	2,214	(3,623)	(2,575)
Accounts payable	10,876	5,489	5,939	4,444
Accrued expenses	8,938	14,338	3,727	14,724
Deferred revenue	50,869	48,230	43,379	64,774
Other liabilities	(559)	(272)	(2,416)	(947)
Net cash provided by operating activities	33,534	53,080	35,252	43,796
Cash flows from investing activities:				
Purchases of investments	(35,542)	(58,192)	(210,534)	(220,383)
Maturities of investments	21,304	56,945	151,533	138,360
Capital expenditures	(1,883)	(627)	(6,228)	(15,633)
Capitalized software costs	(4,173)	(3,287)	(16,409)	(13,283)
Net cash used in investing activities	(20,294)	(5,161)	(81,638)	(110,939)
Cash flows from financing activities:				
Repayment of debt	—	(57)	—	(352)
Principal payments under capital lease obligations	—	(17)	(33)	(202)
Proceeds from employee stock plans	5,778	2,362	23,548	11,559
Net cash provided by financing activities	5,778	2,288	23,515	11,005
Effect of exchange rate changes on cash and cash equivalents	(1,008)	(443)	(1,520)	(2,728)
Net increase (decrease) in cash and cash equivalents	18,010	49,764	(24,391)	(58,866)
Cash and cash equivalents at beginning of period	65,290	57,927	107,691	166,557
Cash and cash equivalents at end of period	\$ 83,300	\$ 107,691	\$ 83,300	\$ 107,691
Supplemental cash flow information:				
Cash paid for interest	\$ —	\$ 1	\$ 3,796	\$ 1,915
Cash paid for income taxes	497	311	2,334	1,520
Proceeds from employee stock plans received in advance of stock issuance	489	193	489	193
Non-cash investing and financing activities:				
Capitalized assets financed by accounts payable and accrued expenses	\$ 2,080	\$ 705	\$ 2,080	\$ 705
Capitalized stock-based compensation	1,141	814	4,252	2,833

Cornerstone OnDemand, Inc.
RECONCILIATION OF NET CASH PROVIDED BY OPERATING ACTIVITIES TO FREE CASH FLOW AND FREE CASH FLOW MARGIN

(A Non-GAAP Financial Measure)

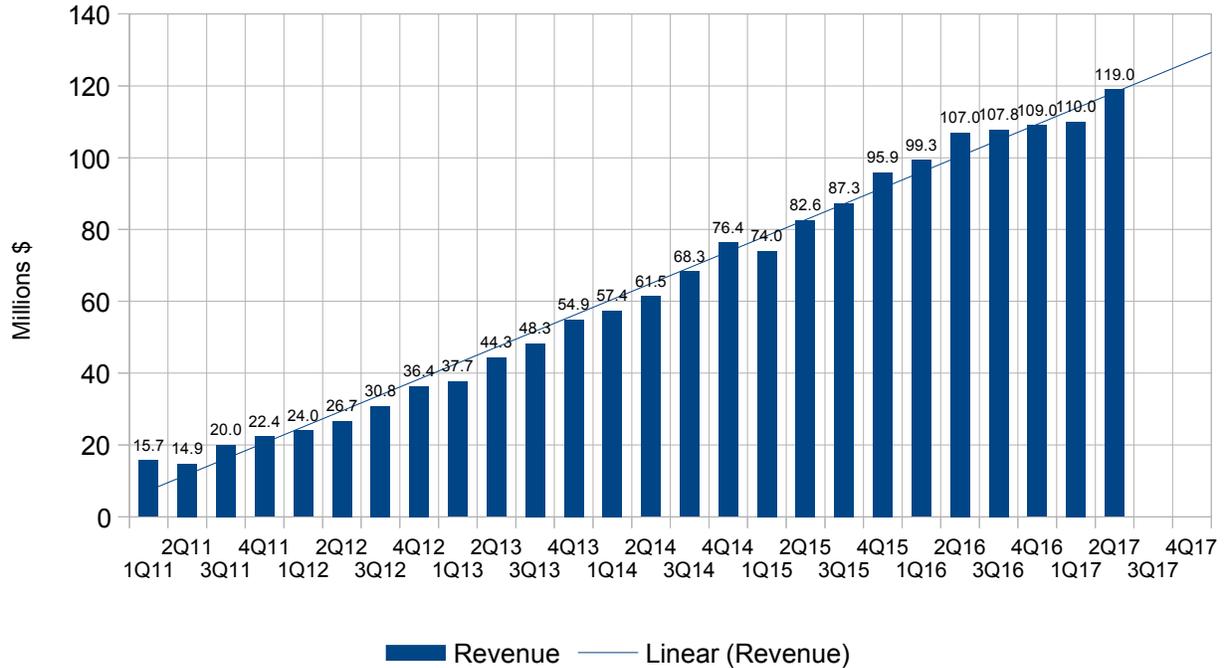
(in thousands)

(unaudited)

	Three Months Ended December 31,		Year Ended December 31,	
	2016	2015	2016	2015
Net cash provided by operating activities	\$ 33,534	\$ 53,080	\$ 35,252	\$ 43,796
Capital expenditures	(1,883)	(627)	(6,228)	(15,633)
Capitalized software costs	(4,173)	(3,287)	(16,409)	(13,283)
Free cash flow	\$ 27,478	\$ 49,166	\$ 12,615	\$ 14,880
Free cash flow margin	25.2%	51.3%	3.0%	4.4%

CSOD Revenue

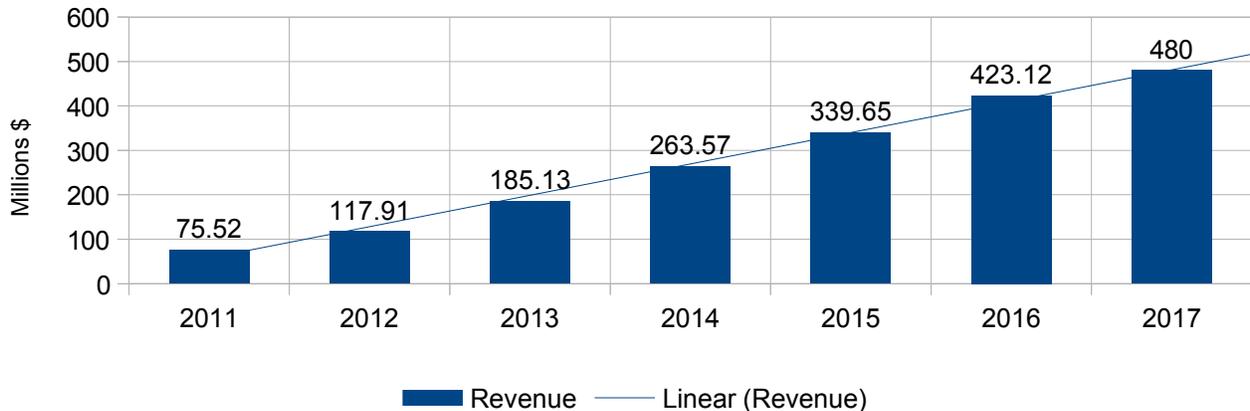
2011 To 2017 est.



Revenue appears to be growing fast. But in reality, it is SLOWING fast.

CSOD Revenue

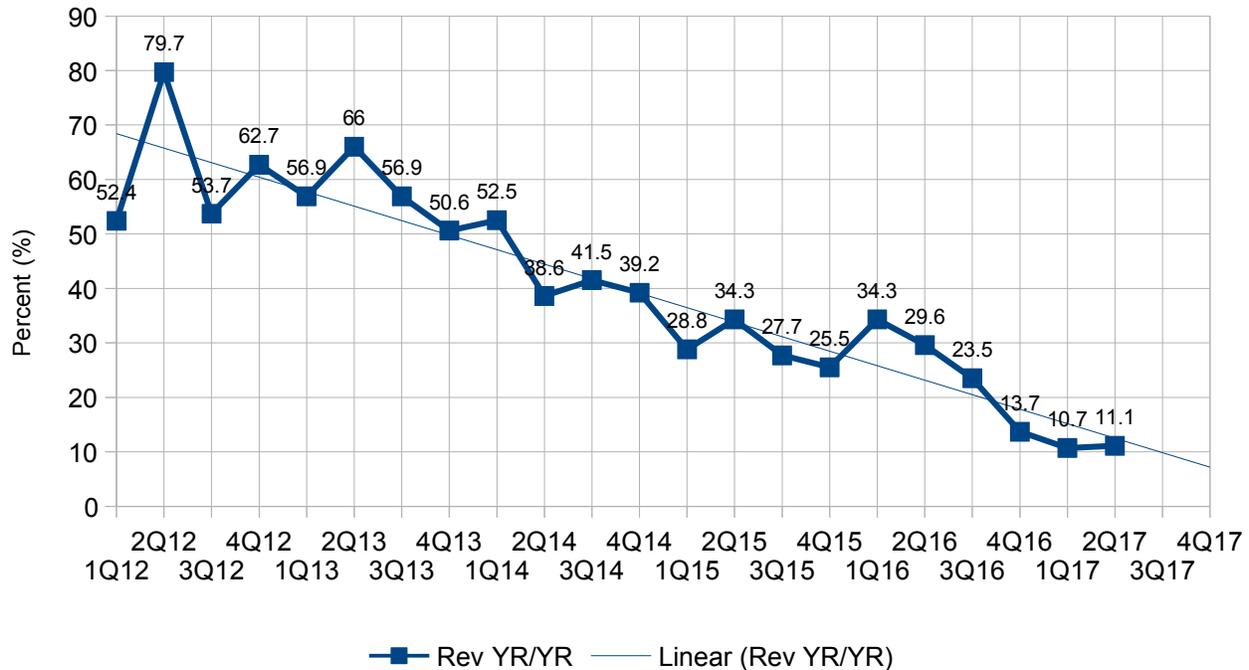
2011 To 2017 est.



The Main Problem

CSOD YR/YR Revenue Growth

2012 To 2017 est.

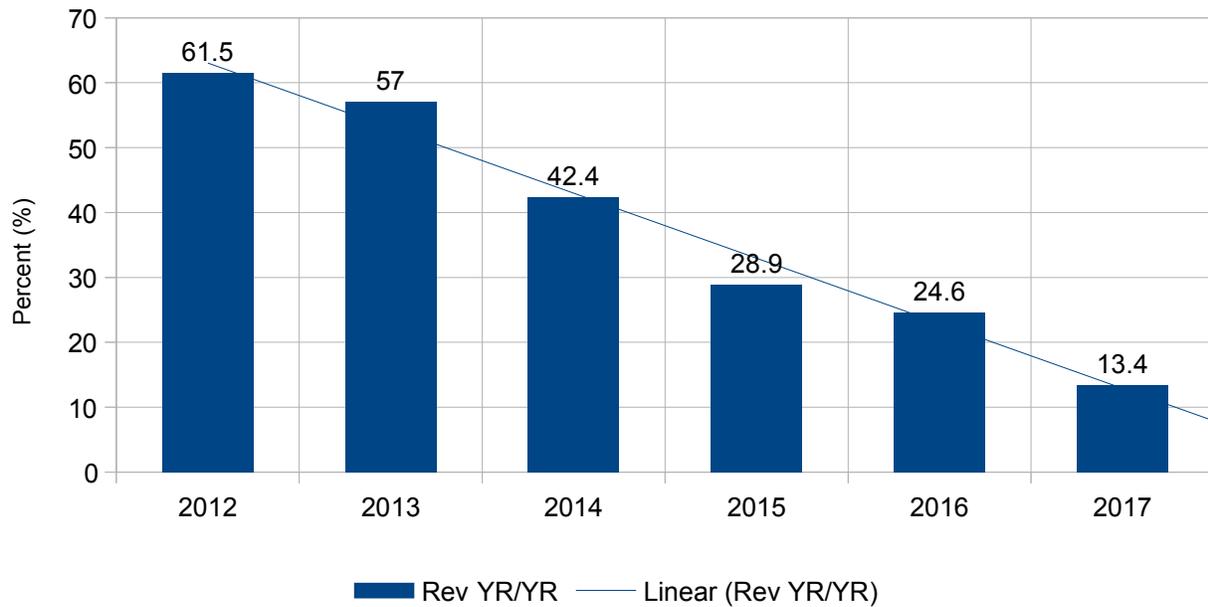


CSOD USED to be a super fast growing company that was unprofitable. In 2012, revenue growth was almost 80 percent. **The 2016 fourth quarter revenue growth of 13.7% year over year was the lowest in the last 20 quarters, or 5 years!** This quarter, 1Q17, will be **lower still at 10.7 percent.** One year ago in the first quarter of 2016, revenue growth was 34.3 percent! **Now, CSOD is a slow growing company that is still unprofitable on a GAAP basis but marginally profitable on a non-GAAP basis.**

Is it smart to pay 130 times non-GAAP earnings for 10 percent revenue growth? This company needs to earn \$1 in non-GAAP earnings per share to justify the current stock price of \$43. That would be 43 times earnings. It will take at least three years, probably four to five, to get there.

CSOD YR/YR Revenue Growth

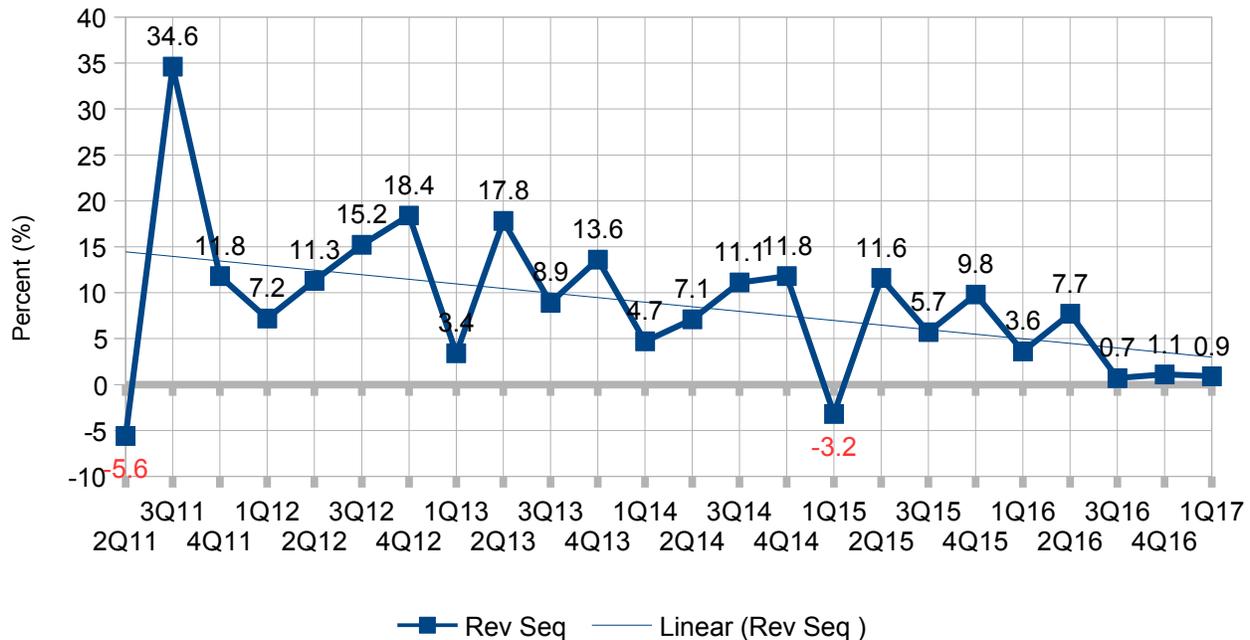
2012 To 2017 est.



2017 revenue growth guided by management will be almost half (45.5%) of the year before. Shouldn't the valuation of the stock be less as well. You pay more for companies growing revenue at 60 percent or 40% or 25%, but you should pay less for companies growing at 13 percent. 130 times non-GAAP earnings seems a tad high.

CSOD Sequential Revenue Growth

2011 To 2017 est.

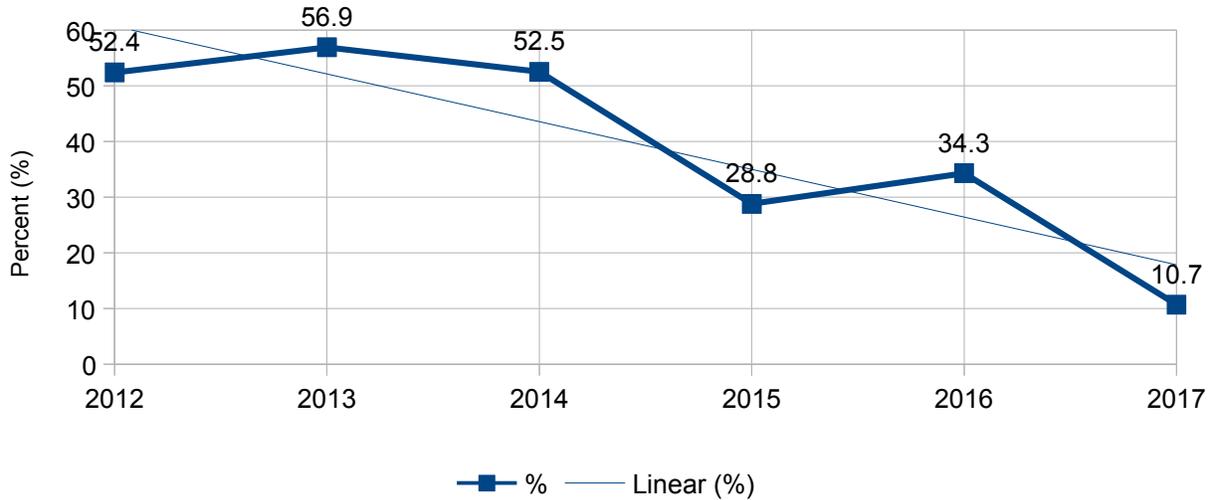


In the 2016 first quarter, sequential revenue growth was 3.6 percent. In the 2017 first quarter, sequential revenue growth should be 0.9 percent, the **lowest in the past two years, and third lowest in the past 20 quarters, five years.**

CSOD is a good company with a good product, but it is just wildly overvalued, with revenue growth declining quickly. It is going to be much harder to double earnings with eight to ten percent revenue growth and three percent growth in shares outstanding every year going forward.

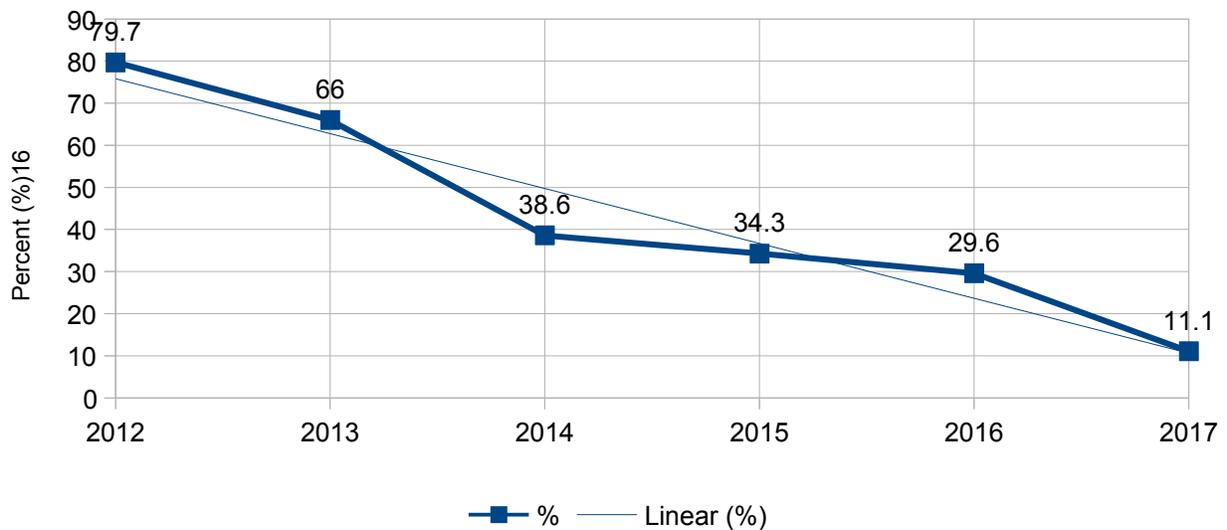
CSOD 1st Quarter Revenue Growth

2012 to 2017 est.



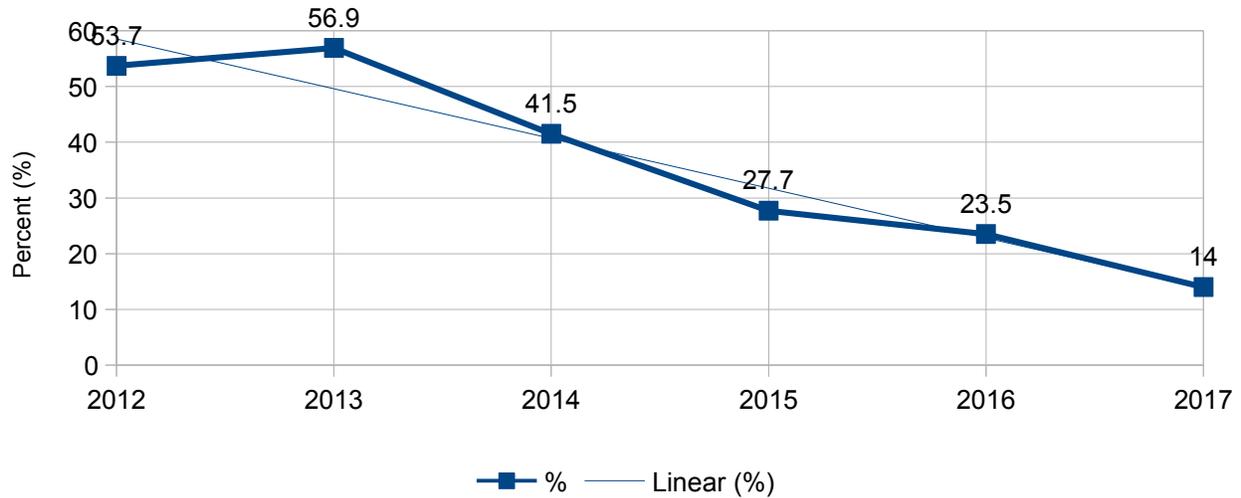
CSOD 2nd Quarter Revenue Growth

2012 To 2017 est.



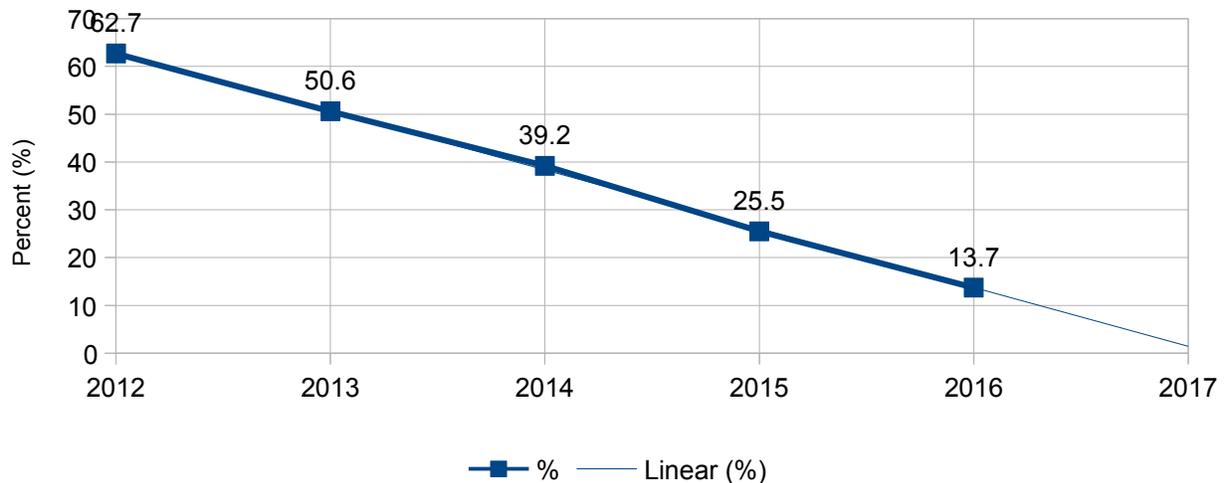
CSOD 3rd Quarter Revenue Growth

2012 To 2017 est.



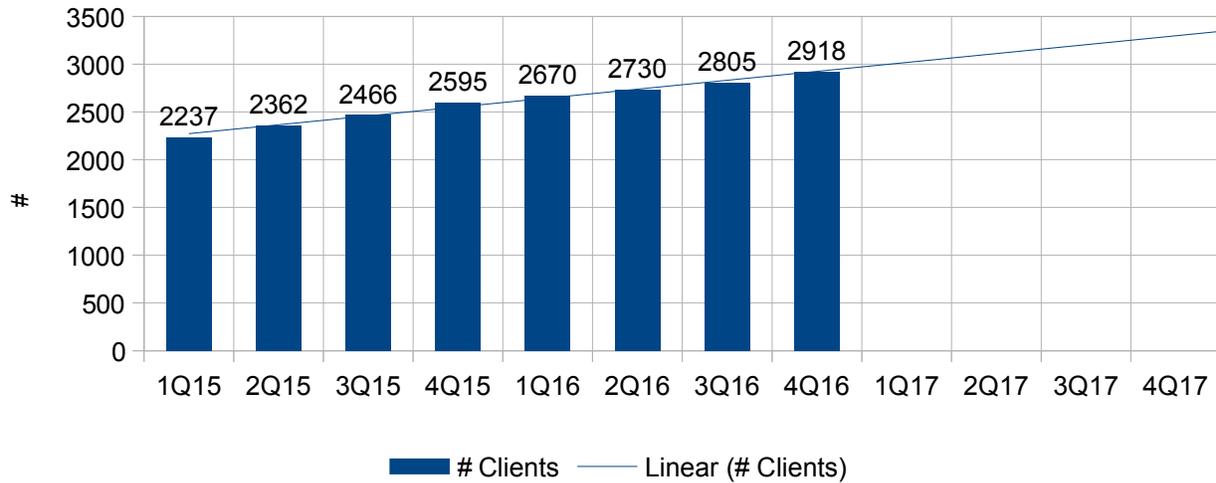
CSOD 4th Quarter Revenue Growth

2012 To 2016



CSOD Number of Clients

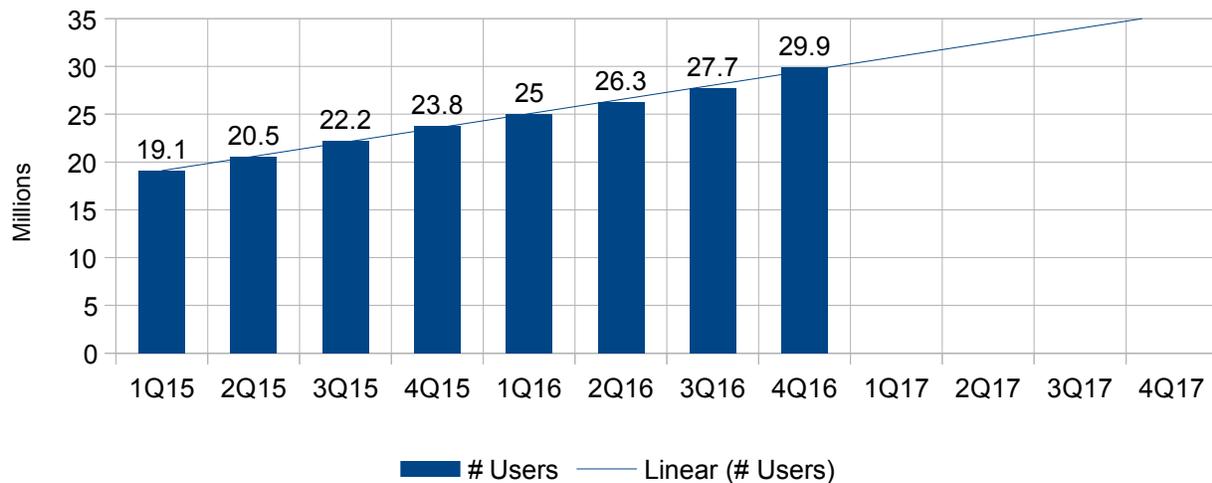
2015 To 2017



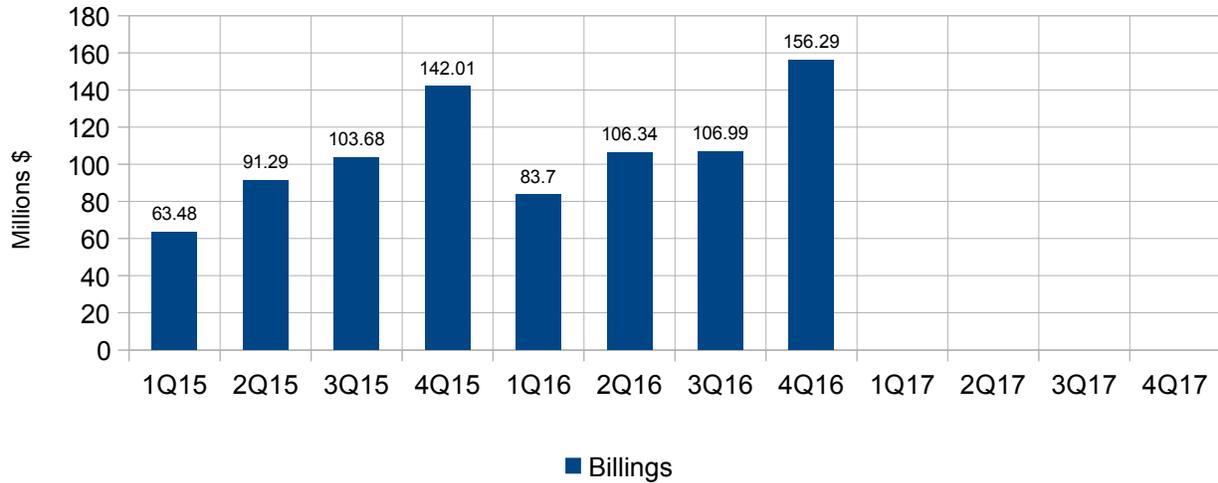
2016 fourth quarter number of clients was only 12 percent higher than 2015's fourth quarter.

CSOD Number of Users

2015 To 2017



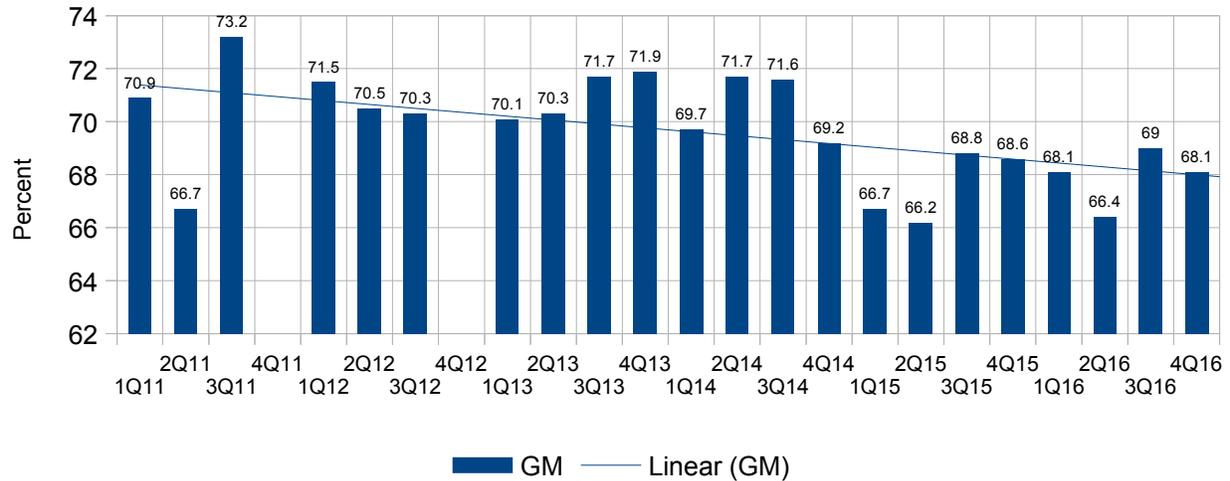
CSOD Billings
 2015 To 2017



Third quarter billings in 2016 were up only 3.2 percent. Fourth quarter 2016 billings were up just 10 percent, less than the 13.7 percent revenue growth.

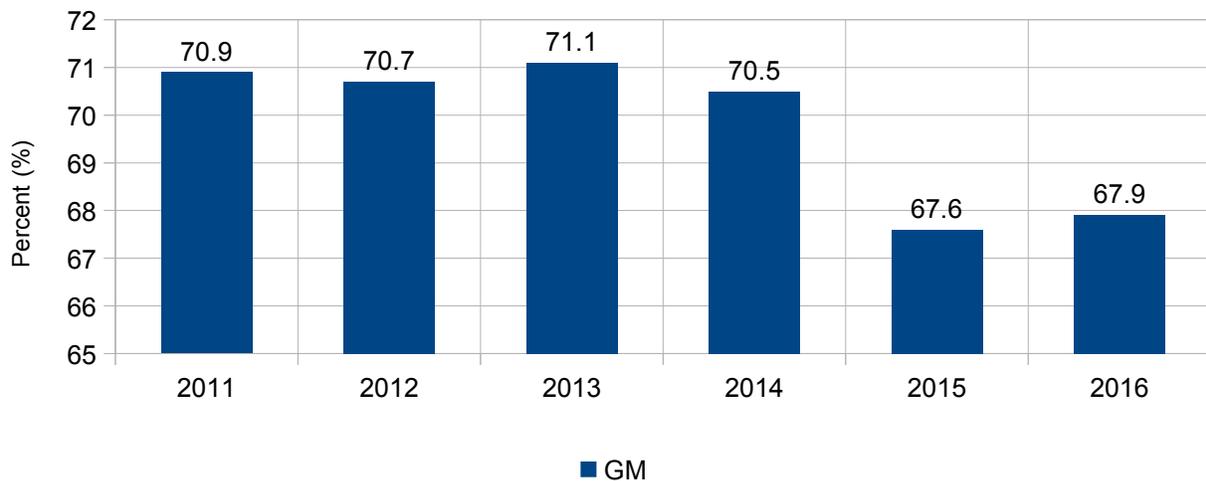
CSOD Gross Margin

2011 To 2015



CSOD Gross Margin

2011 To 2015



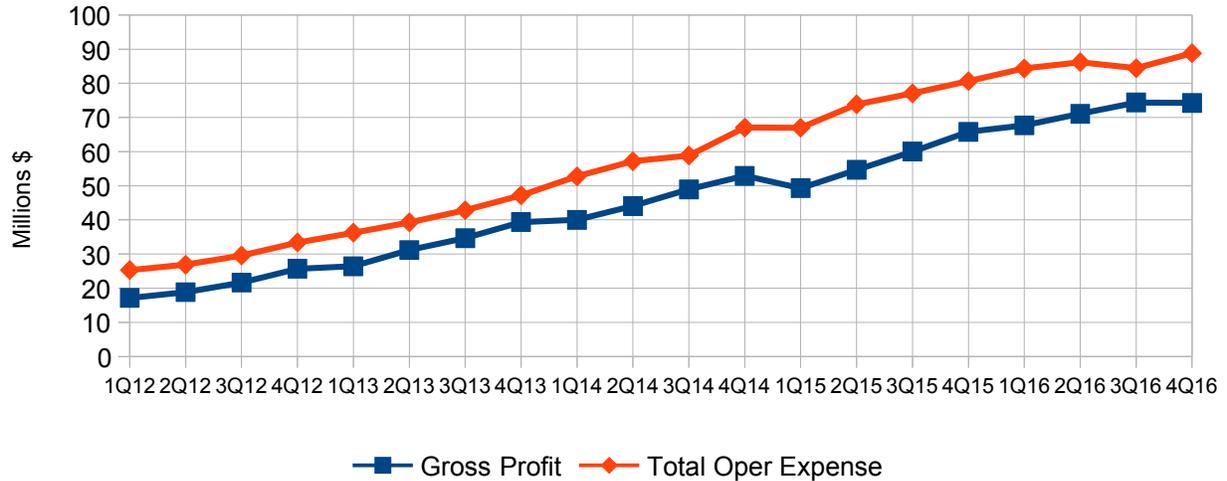
Management is talking about expanded margins?

- Page 18 -

All information contained herein is obtained by Badger Consultants, LLC from sources believed by it to be accurate and reliable. However, such information is presented "as is" without warranty of any kind and Badger Consultants, LLC makes no representation or warranty, express or implied, as to the accuracy, timeliness, or completeness of any such information. All expressions of opinion are subject to change without notice. Badger Consultants, LLC hereby discloses that the clients of Badger Consultants, LLC and we the company, officers, employees and relatives, may now have and from time to time have directly or indirectly a "long" or short position in the securities mentioned and may sell or buy such securities at any time.

CSOD Gross Profit Vs Total Operating Expenses

2012 To 2016



The marginal new customer is not adding to gross margin or gross profit, so there is no great improvement in adding additional customers as the expenses grow just as fast.

CSOD Operating Income

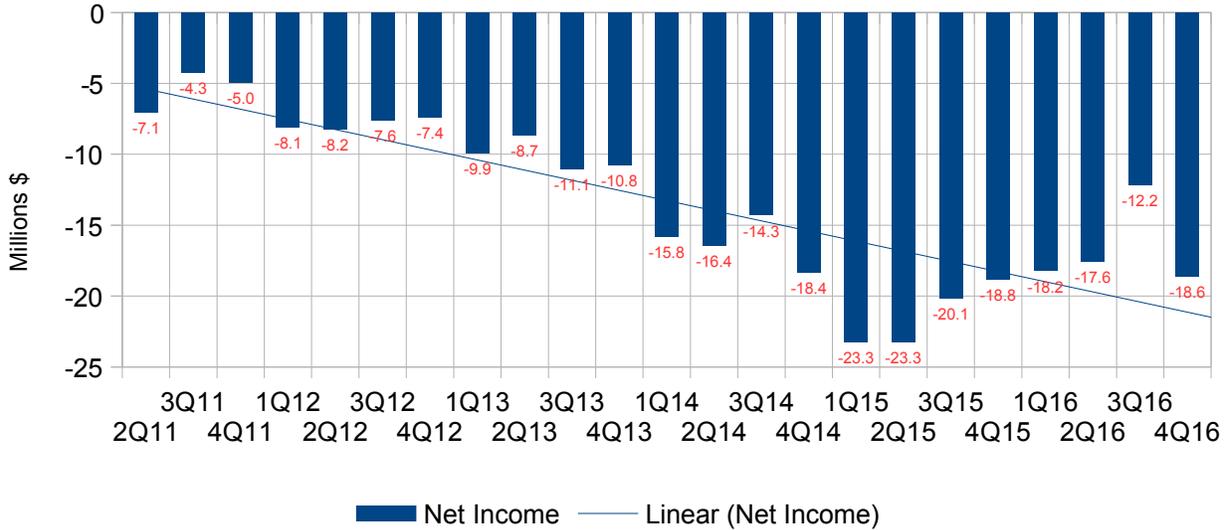
March 2011 To December 2015



Operating income does not improve much even with good revenue growth.

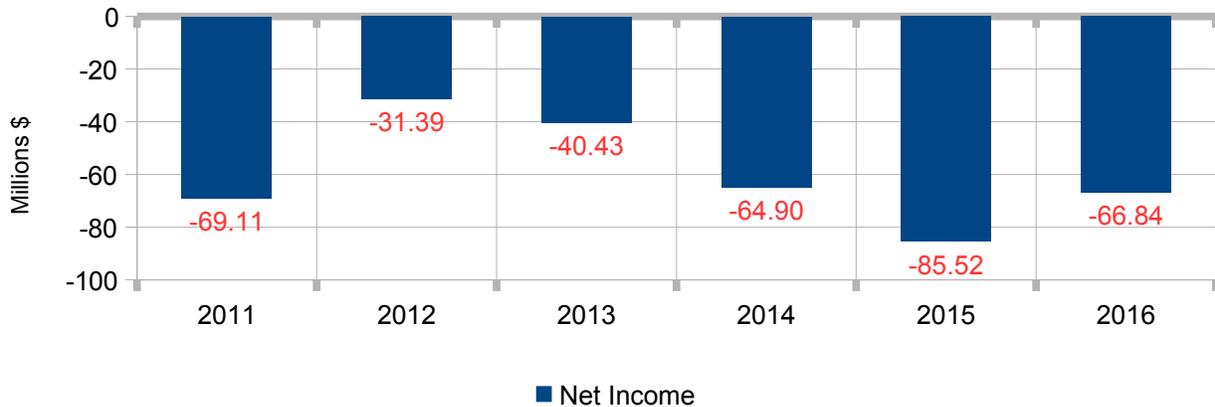
CSOD Net Income

2011 To 2016



CSOD Net Income

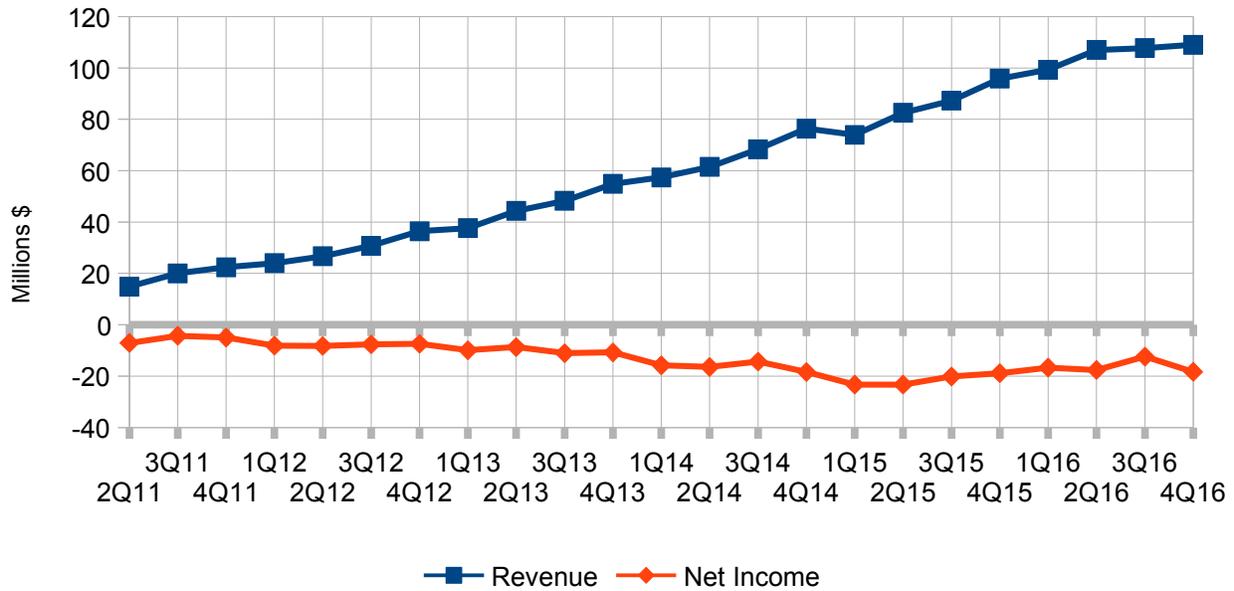
2011 To 2015



Despite having many more clients in 2016 compared to 2011, the net loss is similar.

CSOD Revenue Vs Net Income

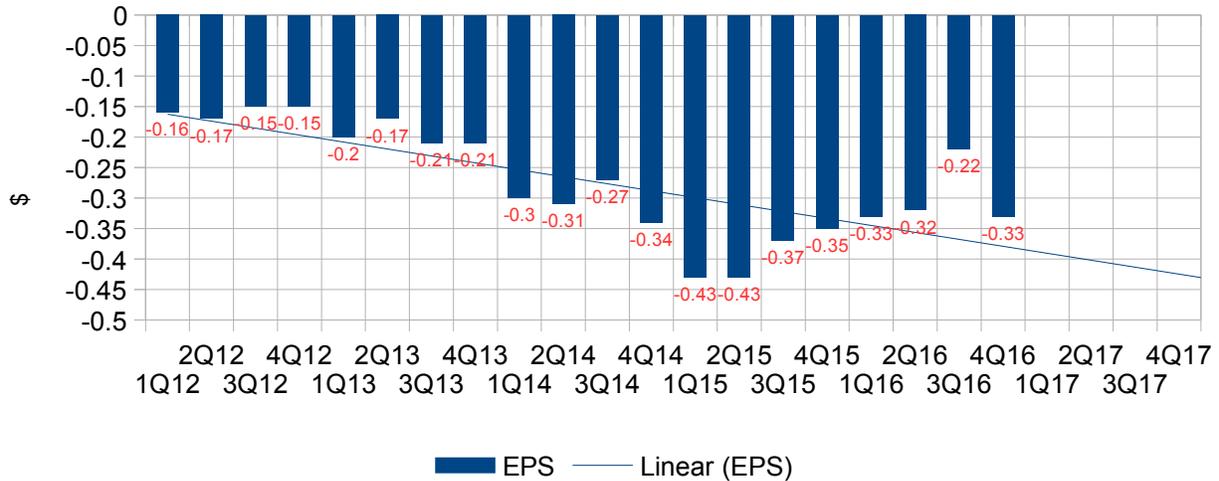
June 2011 To December 2016



Despite revenue being up 82% since 1Q14, net loss is the same. There is no scale to this business.

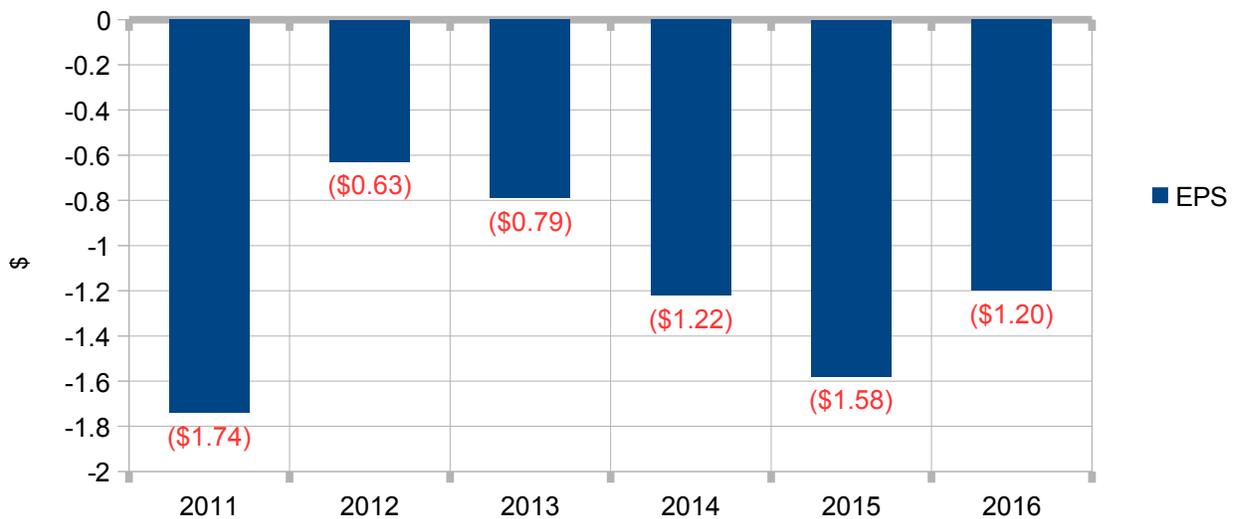
CSOD GAAP Earnings Per Share

2012 To 2017 est.



CSOD GAAP Earnings Per Share

2011 To 2016



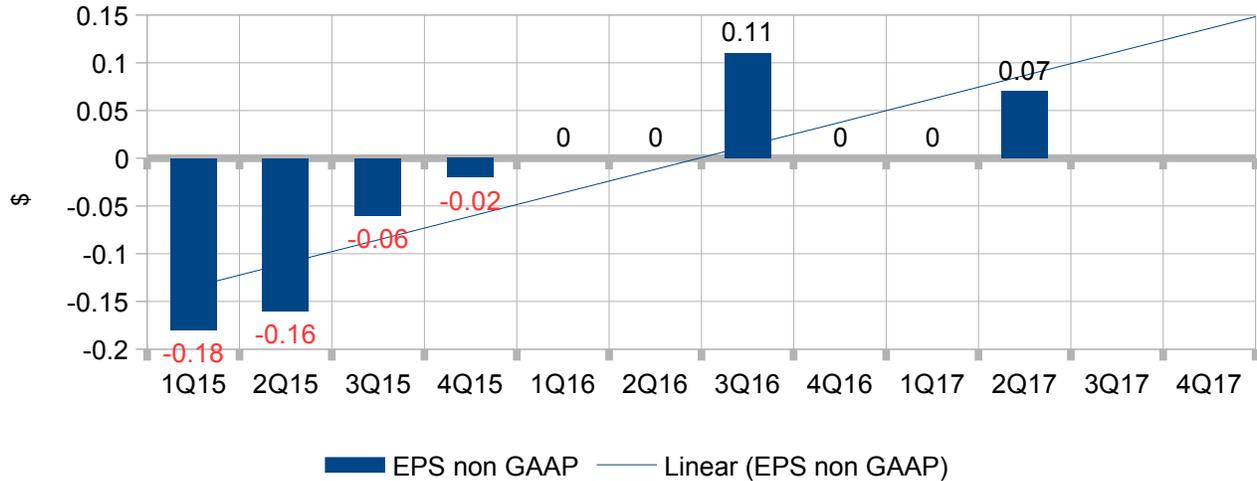
Nobody seems to care about real earnings with this stock.

- Page 22 -

All information contained herein is obtained by Badger Consultants, LLC from sources believed by it to be accurate and reliable. However, such information is presented "as is" without warranty of any kind and Badger Consultants, LLC makes no representation or warranty, express or implied, as to the accuracy, timeliness, or completeness of any such information. All expressions of opinion are subject to change without notice. Badger Consultants, LLC hereby discloses that the clients of Badger Consultants, LLC and we the company, officers, employees and relatives, may now have and from time to time have directly or indirectly a "long" or short position in the securities mentioned and may sell or buy such securities at any time.

CSOD Non-GAAP EPS

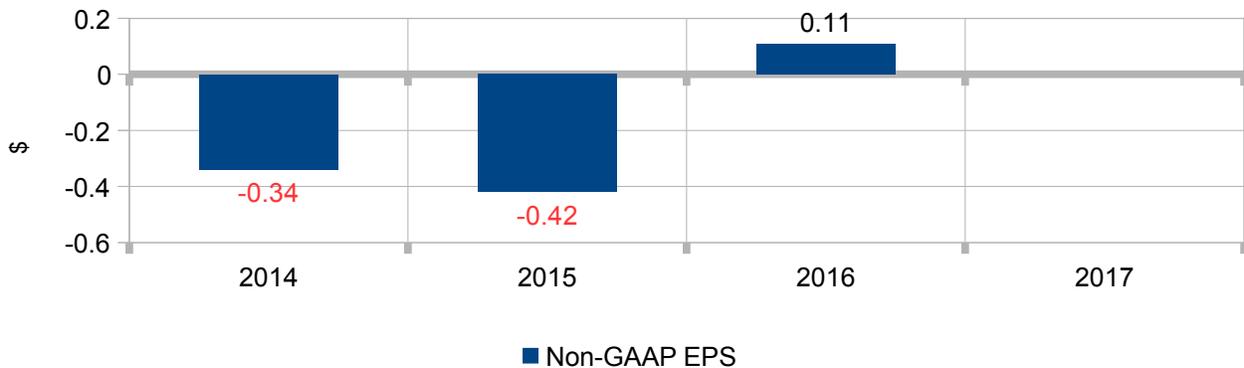
2015 To 2017 est.



This is what everyone is excited about. The non-GAAP losses have turned positive! Ok, but we are talking pennies. If the non-GAAP earnings follow the trend line, which we doubt, CSOD will be earning 15 cents per share per quarter by the fourth quarter of 2017. Already, the **fourth quarter of 2016 and the first and second quarter quarter of 2017 are substantially below the trend line. In the six quarters since 1Q16 to 2Q17, CSOD will have earned a whopping 18 cents of non-GAAP earnings, in a year and a half!**

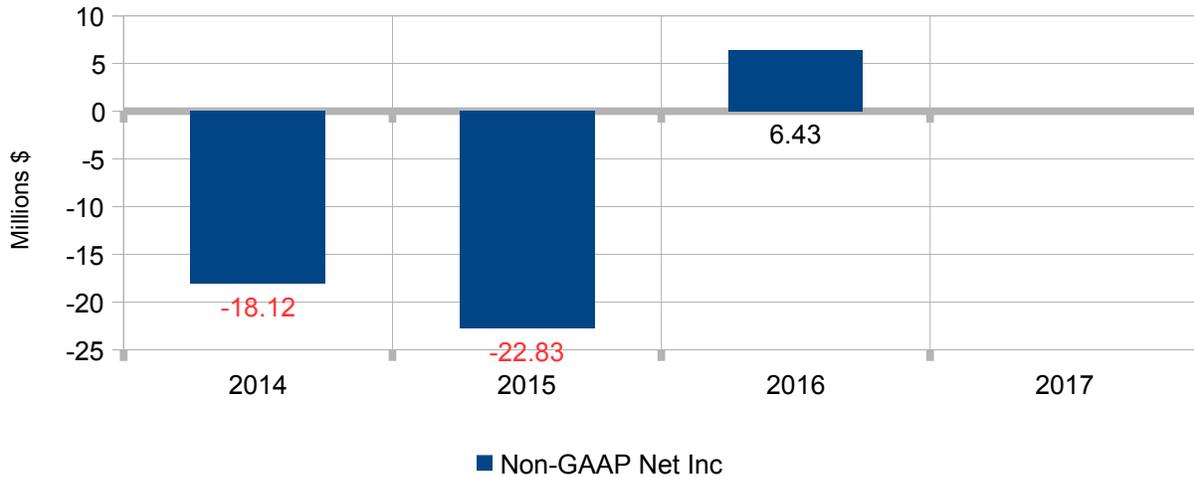
CSOD Non-GAAP EPS

2014 To 2017



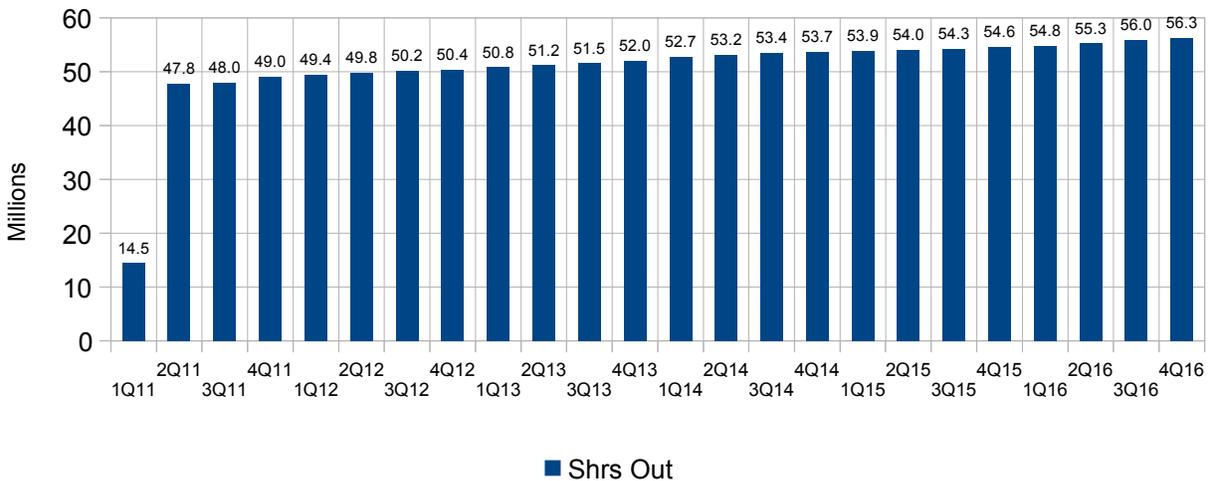
CSOD Non-GAAP Net Income

2014 To 2017



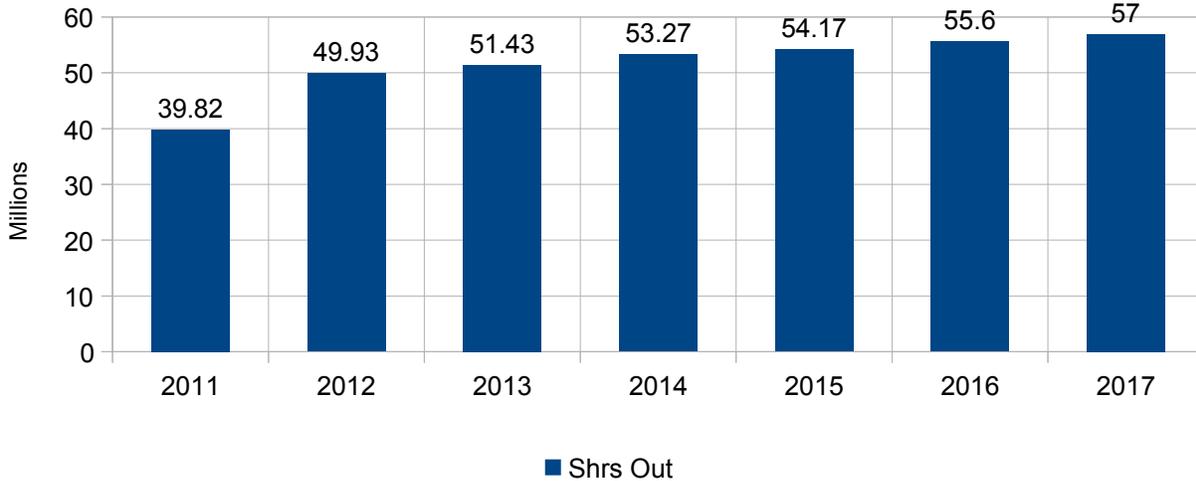
CSOD Shares Outstanding (FD)

March 2011 To March 2016



CSOD Shares Outstanding (FD)

2011 To 2017



Shares outstanding are increasing by about 3 percent a year, which doesn't sound like much, but when revenue growth drops to single digits, its big.

130 times non-GAAP earnings is far too high for a company with rapidly slowing revenue growth that will reach 10 percent soon. We believe that CSOD will eventually trade at 25 times non-GAAP earnings. In three to five years CSOD could earn \$1 in non-GAAP EPS, so the stock should trade at \$25 three to five years from now. In other words, all the good news for the next few years is already factored into today's stock price.

We have a short term price target of \$30-\$34, and a long term price target of \$25-\$30. Sell.