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EDITED TRANSCRIPT

CRM - Q1 2015 Salesforce.com, Inc. Earnings Conference Call

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OVERVIEW:

CRM reported 1Q15 revenue of \$1.23b and non-GAAP EPS of \$0.11. Expects FY15 revenue to be \$5.30-5.34b and non-GAAP EPS to be \$0.49-0.51. Expects 2Q15 revenue to be \$1.285-1.290b and non-GAAP EPS to be \$0.11-0.12.



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PRESENTATION

Operator

Good afternoon. My name is Hannah, and I'll be your conference operator today. At this time, I would like to welcome everyone to the CRM Q1 FY15 earnings conference call.

(Operator Instructions)

I will now turn the call over to John Cummings, Director of Investor Relations. Sir, you may begin your conference.

John Cummings - *Salesforce.com Inc - IR*

Thanks so much, Hannah, and good afternoon, everyone, and thanks for joining us for our FY15 first quarter results conference call. Our first quarter results press release, SEC filings, and a replay of today's call can be found in our website at www.Salesforce.com/investor.

I've also posted the highlights of today's call on Twitter at the handle @Salesforce_IR. With me on the call today are Marc Benioff, Chief Executive Officer, Keith Block, President and Vice Chairman, and Graham Smith, Chief Financial Officer. We'll start the conversation with a few prepared remarks, and then we'll turn the call over for questions.



As a reminder, our commentary today will be in the non-GAAP terms. Reconciliations between our GAAP and non-GAAP results and guidance can be found in our earnings press release issued earlier today. During the call, we may offer additional metrics to provide further insight into our business or results, and this detail may or may not be provided in the future. We may also reference certain unreleased services or features not yet available. We cannot guarantee the timing or availability of these services or features, so we recommend customers listening today to make purchase decisions based on services and features currently available.

The purpose of the call today is to provide you with information regarding our fiscal first quarter results. Some of our comments may contain forward-looking statements which are subject to risks, uncertainties, and assumptions. Should any of these risks, uncertainties materialize, or should our assumptions prove to be incorrect, actual Company results could differ materially from these forward-looking statements. A description of risks, uncertainties, and assumptions, and other factors that could affect our financial results are included in our SEC filings including our most recent report on Form 10-K, particularly under the heading Risk Factors.

With that, let me turn the call over to Marc.

Marc Benioff - *Salesforce.com Inc - CEO*

Okay. Thanks so much, John. I really appreciate it.

I'm absolutely delighted to be with you once again, and celebrating our 15 years of customer success here at Salesforce.com. This quarter was a very important birthday for us. It gave us an opportunity to look back at how we've helped shape this new world of enterprise software, how we've grown to be the world's largest CRM Company, and the world's largest provider of enterprise cloud computing, and as you can see from these results, the fastest growing top 10 software Company in the world today, all in just 15 short years. It's been an exceptional journey, and we're very grateful to all of you who have been with us through this incredible decade and a half.

The new world of enterprise software is the world that's in the cloud. It's a world that's mobile. It's a world that's social, and it's a world that's connected. Our customers are connecting with their customers in entirely new ways. They're consistently turning to Companies like Salesforce to make this customer connection. This has driven this incredible business for us.

Whether they're looking for solutions for sales, for service, for marketing, for engagement, or building custom apps, Salesforce has consistently delivered the world's best customer platform. I'm proud of our employees, our customers, and partners in what they've accomplished over the last 15 years, and I'm looking forward to our very bright future.

We're delighted this quarter to be once again chosen by Fortune Magazine as the world's most admired software Company for the second year in a row, an incredible accomplishment. Earlier this year, Salesforce was recognized by Fortune as the world seventh best place to work, and we were Forbes Magazine's most innovative Company in the world three years in a row.

Through our pioneering 1/1/1 model, we've now delivered more than 700,000 hours of community service, delivered more than \$50 million in grants, and are running more than 20,000 nonprofit organizations on our service for free. Through all of this, through all these accomplishments, nothing is more important to us than the trust and success of our customers. This deep commitment to our customers and their success is why Salesforce delivered these exceptional results especially now in this first quarter.

Revenue grew by 37% from a year ago to more than \$1.2 billion, pretty incredible. Deferred revenue grew by 34% year-over-year to more than \$2.3 billion. Operating cash flow grew by 67% from a year ago to more than \$470 million, and the dollar value of booked business on and off the balance sheet grew by 34% from last year to \$7.1 billion. While we delivered world-class growth, we also grew operating margins sequentially this quarter, which is why we're able to deliver non-GAAP EPS of \$0.11, exceeding our guidance, and we'll deliver 125 to 150 basis points of operating margin improvement this year.

Given our strong financial results and pipeline of new business, we're once again raising our full FY15 guidance by \$40 million to reach \$5.34 billion. With billions of users all over the world now using cloud services, mobile devices, and social networks the technology world has deeply changed. Salesforce continues to lead this change in enterprise software.

Today, I run my business from my phone. I could never have imagined that just a few years ago. I don't need a PC, a laptop, a desktop to connect with my customers, employees, or partners. I just need my phone. That certainly isn't where software was a decade ago.

At Salesforce, we've rebuilt all of our services onto the new Salesforce1 platform, giving our customers the ability to use phones, tablets, PCs, or whatever they choose to manage and share all of their customer information. The Salesforce1 platform has far exceeded our wildest dreams and has accelerated the success of our customers, our ISVs, our developers, our administrators, and their ability to be successful in this new world.

It's why our flagship Sales Cloud and Service Cloud, our ExactTarget Marketing Cloud, and our platform are all leaders in the categories and growing faster than their competition. The Sales Cloud is once again the undisputed leader in Gartner's Magic Quadrant for sales force automation. In fact, we extended our lead this last year, according to Gartner, our market share in sales now larger than the three next competitors combined.

Service Cloud is the clear leader in both vision and execution in Gartner's most recent Magic Quadrant for customer service, and with Desk.com, we're bringing in our world-class customer service solutions to small businesses, as well as to enterprises. The ExactTarget Marketing Cloud doubled its market share according to the recent Gartner report adding more share than any other top 10 marketing vendor. The Salesforce1 platform is the only solution rated by Forrester as a leader in every single platform category and recognized leader in Gartner's first ever Magic Quadrant for enterprise platforms.

Now, I'm delighted to welcome our Vice Chairman and President, Keith Block, to the earnings call, and I'd like to ask Keith to introduce himself but also to give you a review of the quarter's results. We're very fortunate to bring in Keith over a year ago now. He's a member of our Board and runs our distribution organization which represents more than half of all our employees.

Keith?

Keith Block - *Salesforce.com Inc - President and Vice Chairman*

Thanks, Marc.

It's great to be here, and I have to say that Salesforce is an absolutely incredible Company. Over the past year, I've spent a great deal of time speaking with customers and partners all around the world, and the feedback has been overwhelmingly consistent. It's been about great vision. It's been about great products, and it's been about great people.

It's really rare to find a Company whose customers and partners have such a high degree of respect and admiration on a consistent basis, and the great news is our customers and our partners they want more from us. They want us to go deeper with them. They want us to have a more strategic relationship. They want us to help them innovate as they transform their business models. They want us to help them scale their business for the future, and ultimately at the end of the day, they want us to be their trusted advisor on their journey to connect with customers in entirely new ways. This applies to every customer, from the smallest to the largest enterprises in the world.

Now in the quarter, we had some terrific success with companies of all sizes, across all industries, everywhere in the world, and I'd like to just share a few thoughts with you. For example, we entered into a new relationship with Manulife, one of the world's largest insurance and financial services providers. They've selected the Service Cloud to create a single customer engagement platform and delivered personalized service across all of their life insurance, wealth management, and investment products: just a terrific story.

Meiji Yasuda Life Insurance, one of the oldest and largest insurance in Japan: we're thrilled to have that brand as part of our family. They selected Salesforce in the quarter, and this will be the first enterprise-wide cloud implementation in Japan's life insurance industry. We're absolutely excited

about this. They selected our Service Cloud to allow agents to close deals and service customers right from their phones, and they will also be building out their next generation apps on Salesforce1: very, very exciting.

In communications and media, Sky Italia selected Service Cloud, the Salesforce1 platform, Salesforce Communities, all of which for an engine for the company's B2C communication business from call centers to self-service to partner channels. In health care, another great brand brand started sales transformation with our Sales Cloud, and in the quarter, they expanded with ExactTarget Marketing Cloud to leverage the power of social and connect directly with millions of people shopping for insurance.

Many, many, many stories that we can go onto, but again some terrific brands, some terrific stories. I certainly want to congratulate the team for their outstanding accomplishments in Q1, and I also want to thank our customers, and our partners for their continued commitment to our collective success and futures. I do want to say again that I'm absolutely thrilled to be part of this just outstanding organization.

With that, I'll turn the call over to Graham.

Graham Smith - *Salesforce.com Inc - CFO*

Thanks, Keith.

We started fiscal 2015 as you've heard with a really strong first quarter, growing revenue, deferred revenue, and operating cash flow at more than 30% and coming in ahead of our EPS guidance. We are well positioned to deliver another year of industry-leading growth.

Let me take you through the financial highlights of our first quarter starting with the income statement. First quarter revenue was \$1.23 billion. That's an increase of 37%, which did include an FX benefits of approximately \$6 million. Non-GAAP EPS for the first quarter was \$0.11.

On a regional basis revenue in the Americas grew 39% to \$876 million. Revenue in Europe grew 42% in dollars, and 35% in constant currency to \$231 million, and revenue in Asia-Pacific increased 21% in dollars and 26% in constant currency to \$120 million. That's a nice uptick in growth after some of our recent quarters in Asia-Pac.

Dollar attrition continued its slow and steady decline for the 19th consecutive quarter and remains in the high-single digits percentage range. Our non-GAAP gross and operating margins continued to reflect the acquisition of ExactTarget last year. Gross margins were 79.5% in Q1. That's down 70 basis points from Q1 last year, and non-GAAP operating margin was 9.7%, which was down 80 basis points from Q1 last year, but actually up 280 basis points sequentially.

In the first quarter, we added more than 900 people. That's our most significant organic hiring quarter ever, and brings our total headcount at the end of the quarter to just over 14,200. That's up 38% over Q1 last year.

Turning to the balance sheet, we ended the quarter with approximately \$1.5 billion in cash and marketable securities. During the quarter, we paid approximately \$280 million in principle related to conversions of our senior notes that are due in January 2015. This amount was partially offset by an approximately \$30 million deposit we received for the potential sale of four of our eight lots we own in Mission Bay.

Deferred revenue ended the quarter of more than \$2.3 billion, up 34% over last year. Excluding approximately \$13 million of year-over-year FX benefit, deferred revenue increased 33%. On a sequential quarter basis, deferred revenue also had an FX benefit of approximately \$9 million. We expect Q2 deferred revenue to be approximately flat sequentially from Q1.

Approximately 68% of the value of all subscription and support-related invoices, and that includes ExactTarget, were issued with annual terms in Q1, compared with approximately 68% in Q1 last year. Keep in mind however that our billing frequency percentage last year did not include ExactTarget. If you exclude ExactTarget from this quarter's calculation, we saw a year-over-year increase in the proportion of invoices issued with annual terms that is consistent with the FY14 average. It was around 5 percentage points improvement.



Unbilled deferred revenue or revenue that is contracted but not yet invoiced and is off the balance sheet was approximately \$4.8 billion in Q1. That's an increase of 33% over last year.

Turning to cash flow, we had an outstanding start to the year as we talked about for some time. Q4 has historically always been our largest new business quarter, and as a result, has also become our largest renewals quarter. The seasonality of our invoicing has become more pronounced each year because of the compounding effects of the new business seasonality.

In Q4 as our largest invoicing quarter, it follows that Q1 has become our largest collections and operating cash flow quarter, so in the first quarter operating cash flow was \$473 million. That's up 67% over last year. We anticipate our second quarter operating cash flow growth to be lower at approximately 10% year-over-year growth, and continue to expect our full-year operating cash flow to grow in the mid-20s percentage range year-over-year that we talked about on the call in February.

CapEx was \$60 million in the first quarter up 11% year-over-year. CapEx as a percentage of revenue in the first quarter was 5%. That's down from 6% in Q1 last year. We continue to expect our full-year CapEx to be in the range of 5% to 7% of revenue. Free cash flow, which we define as operating cash flow less CapEx was \$413 million in the first quarter. That's up 80% from last year.

Turning to guidance, with our solid results in the first quarter, we're delighted to be raising our full FY15 revenue outlook by \$40 million. That's new range of \$5.3 billion to \$5.34 billion for year-over-year revenue growth of 30% to 31%. We're raising our full-year non-GAAP EPS guidance to reflect the Q1 beat, and now expect it to be in the range of \$0.49 to \$0.51.

As Marc mentioned, we're still committed to increasing our full-year non-GAAP operating margins by 125 to 150 basis points, but clearly that assumes no significant M&A activity during the year. FY15 non-GAAP EPS also assumes that other income expense will continue to be a net expense and assumes a non-GAAP tax rate of 36.5%.

For Q2 we anticipate revenue in the range of \$1.285 billion to \$1.29 billion, representing year-over-year growth of approximately 34% to 35%, and we expect non-GAAP EPS in the range of \$0.11 to \$0.12. As a reminder, all of the underlying assumptions for our GAAP and non-GAAP guidance and a complete GAAP to non-GAAP reconciliation can be found in our earnings press release issued earlier today. To close, Q4 was a great start to the year for Salesforce, really good solid execution across the business, sets us up well to deliver another year of amazing industry-leading growth. With that, we'll open the call up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Jason Maynard.

Jason Maynard - Wells Fargo Securities, LLC - Analyst

Good afternoon, guys. Congratulations on the quarter. I have a question that's probably for Marc, and I would assume maybe for Keith as well. I'd love to get your perspective when you look out over the next 12 months, really two parts here.

One is do you believe your fully penetrated in sales automation and that the majority of the growth or the incremental growth is going to come from upselling to Sales Cloud and Marketing Cloud and platform? Then maybe, Keith, on the distribution side, what do you need to do to turn some of your accounts that maybe are spending a couple million dollars with you today into account that maybe can spend upwards of \$10 million a year with you on a recurring basis? Thanks.

Marc Benioff - *Salesforce.com Inc - CEO*

I think you have to keep all this in perspective. Obviously, our namesake Sales Cloud product is just a huge part of our Company, and it will continue to be a huge part of our Company for the foreseeable future.

We have a lot of other great growth drivers in the Company as well, especially with our Service Cloud and our Marketing Cloud and our platform, and also our new engagement capabilities, and communities capabilities. But the sales product remains to be such a dominant part of the Company's success, that there's no doubt that future growth will also be driven significantly by it.

Keith Block - *Salesforce.com Inc - President and Vice Chairman*

Yes. Jason, nice to hear from you.

A couple things, I think there is still significant opportunity across all of our cloud, certainly with Sales Cloud as our flagship. But as you know, we put in place a multi-pronged strategy to really change the relationship that we have with our customers. Those are customers, whether it's in the SMB space or whether it's in the enterprise space, and it really starts with our focus on industries.

One of the pieces of feedback that I've heard over and over again from the customer base is how important it is to speak the language of industry and to build that trust based relationship and solve business problems surrounding industry. We have obviously launched our industry business unit to help assemble those solutions, were ultimately will give us the opportunity to gain a lot more mind share, and have a more strategic relationship with these customers.

We've also launched the strong initiative around our partners both our SIs and the ISV ecosystem, which is very, very important to our strategy and very important with our customers. We're getting incredible traction across all three of those fronts, as well as focusing on our international expansion. When you really couple the industries and the partners together, it really raises our relevance within these accounts, which will give us the opportunity to continue to drive momentum there.

Graham Smith - *Salesforce.com Inc - CFO*

Jason, this is Graham. One more thing I'd add, I think one of the things we've seen over the last few years is the continual underestimation of the market sizes. I think directionally, clearly we've shown huge increase in share over the last few years and consistent gains in shares.

The other exciting thing has been the trend of constant upward revision of the market sizes. I think that obviously gives us more confidence around continued growth of the Sales Cloud.

Operator

Rick Sherlund.

Rick Sherlund - *Nomura Asset Management - Analyst*

Hi, thanks. Two questions. First, Keith, both for Keith, can you talk about the changes you've made to the sales organization?

Did it have any impact in Q1? Did you do well despite changes? If you could talk about that a little bit?

Also, I think we're all waiting for nine figure deals. Is that realistic? Are there deals of that magnitude in the pipeline we should look forward to over the balance of this year?

Keith Block - *Salesforce.com Inc - President and Vice Chairman*

Hi, Rick. Thanks for the questions. A couple things, this question has come up before.

There were no major reorganizations. We would put a strategy in place about six months ago around our industry growth plans and our partners and international expansion, a focus on continuation around attracting and retaining the best talent in the industry, our most strategic accounts, and specialized sales, and really solving business problems as opposed to just necessarily selling products. Since those things have been in play for a while, it really mitigated any sort of risk around a reorganization that I think most people always are worried about when you start the fiscal year.

These plans were put in place a while ago, and we've continued to see traction. We actually saw traction the second half of the year, and we certainly saw that traction continue, and that momentum continued in Q1.

As far as large deal sizes go, I think the net-net of this thing is that as we continue to execute, and we did a terrific job and I'm very proud of the team and the Company for how we've executed in Q1. It's only natural to assume that our relationships with these customers will become more meaningful and more strategic over time. That will just translate into our continued growth, and we're excited about it.

Operator

Brent Thill.

Brent Thill - *UBS - Analyst*

Thanks. For Marc, maybe if you could talk a little bit about Salesforce1 platform? It seems like there's a lot of really new interesting applications that are being built that require the rest of the platform to be deployed to be helpers, if you will, reinforcing the whole enterprise build-out. Can you give us a sense of what you're seeing from some of the larger commitments on the platform?

Marc Benioff - *Salesforce.com Inc - CEO*

Thanks for that question. We've made a huge investment on the Salesforce1 platform over the last couple of year, and so many customers now have deployed it. As a user myself, I can tell you how it's dramatically changed how I work.

As I mentioned, I work entirely from my phone. More than that I think it's because we've completely re-architected our product on the whole family of APIs and delivered a full range of services. It's really opened up the opportunity for our customers to build applications that we've never really thought they were going to build before.

One of the applications that I saw that got deployed this quarter was with Home Depot, where they rolled out this amazing new how-to application. You go to right on HomeDepot.com, you'll see our platform poking through where it gives them the ability to have deep engagement with all of their customers who are building and crowd sourcing and interacting with Home Depot employees, all in real time. It's really all possible by the platform.

In addition to that, we continue to see really strong support from the ISV community. If you go to the app exchange, you'll see more applications available for Salesforce1 than ever before, and some of them are just incredibly well reviewed. You'll see hundreds or some cases thousands of reviews around these apps, and these are enterprise apps. I don't think there's another app exchange or app store in the industry like that, and so many new and emerging for Salesforce1.



The combination of this just gives us a tremendous competitive advantage with our customers, and I'll tell you why. A lot of our competitors, it's not that they haven't moved to the phone, they haven't moved to the cloud. Here we are, we have a solution that not only runs great as a service, as a cloud service, running billions of transactions every single day. Two, that service is available in whatever device you're using. Three, it runs the way that any other social network would work, like a Facebook or Twitter, but it's your own private company network or with your partners or with your customers.

Then finally, what we're seeing now, where companies can take all of this and build their own apps, that's really exceeded what we thought could happen. We're very excited, and we're feeling great about where Salesforce1 is, and I really think it's given us this huge leg up against the competition.

Operator

Kash Rangan, Merrill Lynch.

Kash Rangan - *BofA Merrill Lynch - Analyst*

Hi. Thank you very much. Marc, that off-balance sheet backlog growth rate is just simply stunning.

I'm curious if you could talk to which particular products of the portfolio are driving that superb strength? Also, with respect to Salesforce1, can you specifically talk about how the industry solution strategy in the sixth verticals are going to be differentiated and facilitated with Salesforce1 in particular? Thank you very much.

Keith Block - *Salesforce.com Inc - President and Vice Chairman*

Kash, nice to see you. Let me talk a little bit about the industry strategy and Salesforce1. I think Marc had touched on this.

We're incredibly excited about the adoption of Salesforce1 and how our ISV community is responding to it. Specific to industry, you may have seen a press release that we issued the other day with Deloitte, and our partnership with Deloitte in financial services around financial services solutions, all build on our platform. There is enormous enthusiasm for Salesforce1. Our ISV community is rallying to the cause, and that obviously is an integral part of our strategy.

The other thing that I think is important to understand here is that as we continue our transformation, one of the things that we're trying to accomplish here is to solve business problems for our customers. Whereas traditionally we would go to market by product, and we will obviously continue to do that, I think the important thing is to listen to our customers and bring a point of view around an industry solution. Again, the example would be what we did, the press release that we did with Deloitte.

When you sell a solution, you bring multiple clouds. It's not necessarily one cloud or two clouds, it's a multi-cloud solution, and that is certainly the momentum that we've enjoyed over Q3 and Q4 and certainly saw that carry over into Q1. That multi-cloud solution approach is really paying off for us, and it looks very, very strong for us in the future.

Operator

Mark Murphy, Piper Jaffray.

Mark Murphy - *Piper Jaffray and Company - Analyst*

Yes, thank you. Congrats on the results, Marc.



Your customers and partners sound very excited about a product called Communities that for some reason, it doesn't seem to be as widely recognized in the investment community. We've been told that it's capable of going wall-to-wall and really touching every employee in an organization. Could you walk us through what is happening under the radar with Communities, and maybe any comments on how strategically significant the offering can be?

Marc Benioff - *Salesforce.com Inc - CEO*

Yes. I'd really be delighted to. We announced this product at Dreamforce, and we now have started rolling it out. I just mentioned it in my comments about Home Depot for example, which is a core part of the platform that they've rolled out which is Communities.

Imagine if you will that I'm using my phone like I do, and I'm using Salesforce1 and I'm going through my social network, and I'm reviewing what's happening with my employees, what's happening on my deals, customer service issues, quotes, and my feed is going by. I'm able to roll between different apps that I'm using.

Maybe I'm issuing an IT trouble ticket request. Maybe I am giving an employee a praise. All of this is happening inside Salesforce1.

Now all of the sudden, right inside the feed, something appears and it says, well, did you know that Frank Blake at Home Depot just commented on the product that you're working on? What has happened is, is that externally on my website, I am running a community of all of my customers. Now, you can go, and you can see this right now, if you go to I think it's Success. Salesforce.com, is our Community site.

If you go to Success. Salesforce.com, you'll see what Communities look like, and you'll see how we've deployed Communities. If there's customers that I'm following, if there's a product I'm following, events I'm following, whatever I'm working on, and now I'm a customer and I come on this site, I'm automatically integrated to the Salesforce employees. Honestly, I don't know a customer who doesn't need this, whether it's partner communities, whether it's for customer service, whether even if it's for employee communities, and we're very excited. This is in the category of engagement.

Today, Salesforce's product tagline is Salesforce, sales, service, market, succeed. You'll really see it evolved to be sales, service, market, and engage. The reason why is because of exactly what you're saying. This has been a tremendous success for us. We continue to see all customers be very excited with this.

This all started with Chatter, if you remember that. That was the brand. We dropped the brand Chatter, in that it's all Salesforce1 now because it's also deeply integrated into our platform. You can't separate our core collaboration capabilities from our sales, service, and marketing, or platform applications and services.

That's where we are right now. It's very exciting. You'll see more at Dreamforce, and you're going to see us really continue to focus and expand this.

I do want to make one key point, which is that this is not some separate app. This is really a core part of our platform, and that we've worked very, very hard to make sure that these are core platform services, and that collaboration is at the very heart of who we are at Salesforce. Okay? I hope that answers your question.

Operator

Heather Bellini, Goldman Sachs.

Heather Bellini - *Goldman Sachs - Analyst*

Great. Thank you. I had two questions, one for Marc, and one for Keith.

I guess, Keith, to start out with you, you mentioned the vertical solutions and the business problems that you're trying to solve as a result of your verticalization. How do we think about how long it takes for you to really hit your stride to serve the customers, and the way that you're thinking about it? Also, back to Rick's question, how do we think about how deal sizes scale as you become that trusted solution provider, if you use your past history as a guide?

Then the question I have for Marc, in regards to Marketing Cloud, a lot of the customers we talk to talk about a big desire to have one integrated dashboard for marketing. So they could open one app instead of opening multiple apps to find out what they're doing, how they're doing with new products, and with new customers. I'm just wondering where you are as a Company in terms of fulfilling that vision.

Keith Block - *Salesforce.com Inc - President and Vice Chairman*

Hi, Heather. I think it's very interesting.

The industry focus for us is obviously very, very important, and we saw after only being organized around industries for I will say six months, we started to see that traction hit in Q4. I think you may remember that I said we pretty much had a run on retail banks in Q4. That was all around our lead referral management solution that was put together by the industry business unit.

That continued into Q1 where to a certain extent we had a run on insurance companies. Again, part of that is because of our ability to speak the language of industry which is all about solving the customer business problem. As we continue to roll those solutions out, I think you'll see us gain mind share again, build those strategic relationships, partner with the SI, partner with our ISVs, and really be more meaningful and take on that trusted advisor role.

It's only natural to assume and to expect that as all those things continue to gain momentum, that there will be more mind share. There will be more wallet share. There will be more market share.

Again very, very pleased with the early returns in Q4 and Q1, but I think that we certainly have significant opportunity in that space. I think that's how you'll see things scale over time.

Operator

Karl Kierstead, Deutsche Bank.

Karl Kierstead - *Deutsche Bank - Analyst*

Hi. Thank you. My question is to Graham.

Graham, that operating cash flow growth, 67%, is pretty stellar. I think I understand the seasonality, but I'm curious if there were any other kickers that made the quarter particularly strong on that front. And if your confidence in your mid-20s operating cash flow growth for the full year has increased as a result of the good Q1 performance? Thank you.

Graham Smith - *Salesforce.com Inc - CFO*

Thanks, Karl. I think it's always great to get a good start to the year, so clearly confidence in mid-20s, I'd say is incrementally higher because of our strong start. Just to reiterate, this compounding effect of just our large fourth quarter has really been going on over a long period of time.

Then I think you layer on top of that clearly we've also been expanding our annual billings. Then we saw some nice margin expansion sequentially from Q4 to Q1. Q4 was still affected by, I'm sure, some cash flows from Dreamforce, those kind of things.

You roll all that up, and we saw a really strong first quarter result. But as I say, I would expect this would be more of our trend in the future, that we'll have this huge receivables number at the end of the fourth quarter, and then a very large collections number in Q1. Yes, we're very happy to get a strong start on the year here.

Operator

Pat Walravens, JMP Group.

Pat Walravens - JMP Securities - Analyst

Great. Thank you. Two questions.

Graham, can you tell us what the contribution was from ExactTarget in the quarter? Then Marc, now that you have over 14,000 employees, it's got to be harder to maintain the same culture you had when you were smaller. How are you going about doing that?

Marc Benioff - Salesforce.com Inc - CEO

I'll take that one first. Also, I didn't answer Heather's question. First, why don't I hit that real quickly?

Heather is absolutely right. Our plan is to build a comprehensive marketing cloud. To do that, we've acquired several different companies including Radian6, Buddy Media, and ExactTarget. And we're integrating those into one integrated application which our customers really would have used to comprehensively manage their marketing. You'll see the evolution of that product at Dreamforce.

What I would say is that to really understand where we're going and how we're maintaining this culture, you have to look at our product. I'm sure that that must sound a little bit strange, but I use Salesforce1 every day. I'm communicating and collaborating with our employees. We have an environment that's filled with transparency, and that transparency has created an environment of trust.

That much communication, or what I call over-communication, is part of what we're doing all the time. We over-communicate. We over-align. We're constantly working on what we call the V2MOM, which is our internal business process service which lets us work on our visions, our values, our methods, obstacles, and measurements. All of that is built into our application.

Then at the core is our philanthropy model. When we first started the Company, we put 1% of our equity, and 1% of our profit, and 1% of all of our employees' time into a 501(c)(3) charity. As I mentioned in the script, that's producing amazing results, like the 700,000 hours of community service, and more than \$50 million in grants, and 20,000 nonprofits.

One thing that's interesting is, in your first day of employment at Salesforce, we show you where your desk is, we show you where the kitchen is, and then you go out and do something for other people. You go to one of our soup kitchens here in San Francisco. You go to one of our homeless shelters. You go to one of our hospitals, and that really sets the tone of our culture. It also provides the referential integrity for our culture, and our culture is different than other technology Companies.

As we've grown our Company, we've been able to maintain that culture by making sure that it's philanthropy first, and that has really set the values that are so important to us. When we look at values like trust, like values, like giving back, like service, and then of course, we have tremendous execution. That's also a key value that we do what we say we're going to do.

We deliver obviously a great quarter this quarter, but this is not our first great quarter. We've had a lot of great quarters. Those things are the things that have really cemented our culture, and that's why it continues to be what it is today. I hope that answers your question.



Graham Smith - *Salesforce.com Inc - CFO*

Just on your second question, we're not intending to provide a breakout of ExactTarget going forward on either the P&L or the balance sheet.

Operator

Steve Ashley, Robert W. Baird.

Steve Ashley - *Robert W. Baird and Company, Inc. - Analyst*

Thank you very much for taking my question. My question is for Keith.

Keith, you mentioned you've been out. You've been talking to customers. What message is it that you wanted to convey to them? What did you want them to take away from your meetings?

Keith Block - *Salesforce.com Inc - President and Vice Chairman*

I think there are several messages that are very important, not the least of which is our corporate messages around the internet of customers and connected customers. And how we sell and service and market, and how we are a Company of system engagement. Those are all very strong messages that certainly resonate with our customers and our partners.

But the other set of conversations that take place are around a dialogue around having a strategic relationship with those customers, and what does that mean? That is all around predictability and transparency, some of the values that Marc talked about earlier. It's about trust, it's about being an advisor. It's about how do those contribute to how our customers unleash the power of social and cloud and mobile and our technologies to change their business models, to transform their businesses, and really unshackle them from old technologies.

If you really think about what's happening in the marketplace, companies have had business processes around selling and servicing and marketing to their customers that have really been hindered/shackled by old technologies. We're providing them with a path forward here and that guidance.

These are messages that truly resonate with the customers. They want these, these conversations. They want this impact that we can bring to the table, and they're excited about our opportunity to partner with them.

Operator

Keith Weiss, Morgan Stanley.

Keith Weiss - *Morgan Stanley - Analyst*

Thank you guys for taking my question, and very nice quarter. Two questions for Graham, one related to headcount, there's definitely big increase in headcount this quarter. Should we think about this in any extent in terms of pull-forward of hiring, of getting a lot of the hiring done up front? What kind of pace should we think about throughout the year?

Question number two, if we look back seasonally, you typically see deferred revenues up 2 to 3 percentage points quarter-on-quarter into Q2. Your guidance of approximately flat, does that hold with the normal seasonality, or should we be thinking about a different seasonality this year versus prior years?



Graham Smith - *Salesforce.com Inc - CFO*

Thanks, Keith. On the headcount question, I think typically we've often had slow starts to our hiring in the year, and then we've built our organic hiring versus people we bring in through acquisitions through the year. We really have tried to focus hard this year on getting off to a fast start and have slightly more linear hiring, and it actually seems to have worked really well. We're just pleased.

I don't view this necessarily as an intentional pull-forward generally, but I think we've got a lot of fantastic news coming out of the Company. Obviously, some of our facilities announcements are super exciting in San Francisco, and I think it's fair to say we're still very much a destination employer, and I think our reputation out there is great. Our hiring in Q1 reflects that profile.

On your second question, I think generally, clearly we've said in the past deferred revenues always got a little bit of, it's a tough number to forecast super accurately. I think there is a general theme that relates to what I talked about earlier around the compounding effect of our fourth quarter, and because Q4 is the large new business quarter, it becomes the large renewals quarter, and it just becomes more and more dominant in terms of its invoicing. As you know, invoicing drives deferred revenues.

I think gradually over time that Q4 spike of deferred revenue and then a more flattish profile through the year is gradually going to change over the year. It's tough to know how quickly, but we haven't changed anything in the methodology, the way we forecast deferred revenue, and clearly as I've said, it's tough to get super accurate on our \$2.3 billion number. But I'd say that overall trend that I described probably will play out over the next few years.

Operator

Brad Zelnick, Macquarie.

Brad Zelnick - *Macquarie Securities - Analyst*

Excellent. Thank you.

Dr. Benioff, congrats on a good quarter, but I really also have to congratulate you on receiving your honorary doctorate degree last week from USC in recognition of your great achievements, particularly your philanthropy, so congratulations.

Marc Benioff - *Salesforce.com Inc - CEO*

Thank you.

Brad Zelnick - *Macquarie Securities - Analyst*

I wanted to ask about the Marketing Cloud, Marc. When you acquired ExactTarget, you said we shouldn't expect any large deals for a while, as you digested the acquisition. But I just wanted to check in and see how do you feel today about the completeness of the Marketing Cloud? What's your appetite to further build it out through acquisitions?

Marc Benioff - *Salesforce.com Inc - CEO*

I think that we have done a fantastic job of building our Marketing Cloud, and it's a very important market. It's something our customers have pushed us to.



You saw it started with Radian6, where we moved in with social listening, with Buddy Media, with social publishing. Then with ExactTarget, which is really a comprehensive application, and that is really going to a whole new level with our journey builder capabilities. If you've seen some of the demonstrations that I've done on the Salesforce1 Tour, you'll notice that ExactTarget Marketing Cloud has just gone leaps and bounds from when we really first started working on it.

Now, as we go forward, there's still gaps in terms of things that we want to fill in. When we'll fill those in, what the right companies are, it's not as easy and as straightforward as it was. We honestly got the best company. I don't think we could have ended up with a better company than ExactTarget.

They have so much product and capability that it's really kept us incredibly satiated. I don't really see that pace like you saw that we were really going through resuming.

That said, we're always looking for great new companies. When we see a great entrepreneur, where we see a great company, or we see a great revenue stream, or we see a great way to cement our position in our market which is all customer-facing applications, we're going to take that.

Operator

Walter Pritchard, Citigroup.

Walter Pritchard - Citigroup - Analyst

Graham, I'm wondering if you could talk a bit about, you've talked for a few years about this matrix with growth and profits as the two coordinates. It feels like you're solidly into the growth part of your matrix here versus high growth or maturity, and in that phase you were talking about 100 to 300 basis points of margin expansion. You've given guidance for the year I think of 125 to 150 basis points margin expansion. You still are absorbing some of the ExactTarget expenses that on board here.

I'm wondering if you could talk to, do you feel like you're really within the high end of that range, if we were to consider ExactTarget? Any commentary as we move throughout the year with most of that dilutions behind us, and then look at next year, how we should think about you on this matrix?

Graham Smith - Salesforce.com Inc - CFO

Thanks, Walter. My recollection of the model, I don't have it in front of me, but basically we've said if we're growing at 30% plus, I think, yes, people could reasonably expect, absent very significant M&A, they could reasonably expect 100 basis points plus of margin improvement in a year. We've committed to a little higher than that this year.

And clearly we will get, it's a little back-end loaded because as you say, really the effects of all the purchase accounting related to ExactTarget fall away after the first half. Then we get the bulk of the deferred revenue write-downs done, and clearly, we're forecasting quite a strong second-half EPS performance here. Overall, our EPS performance this year, we're forecasting as 50% type increase in overall non-GAAP EPS.

I think we feel that model works. I think as long as we're growing that top line more than 30%, I think again, absent major M&A, we feel good about delivering 100 basis points plus a year, and hopefully this year we'll do a little better than that. We'll see.

Operator

Richard Davis, Canaccord.

Richard Davis - *Canaccord Genuity - Analyst*

I realize it's somewhat small, but what do you think about drawing the line on HR? Right now, it's Rypple social performance management, but do you need to get deeper into HR to fully monetize that purchase? I'm just wondering how your thoughts on that component are. Thanks.

Marc Benioff - *Salesforce.com Inc - CEO*

We're not an HR software company. We're the CRM. We're really a customer relationship management software Company, and all of our focus is customer-facing applications, sales, service, marketing, engagement.

Any HR capabilities that we have inside our product really just allow our employees to collaborate and share in the engagement world. Whether it's employee profiles or the performance management that's built into the feed, that's where our focus has been. But we're not really interested in the HR software market. We'll let others worry about that one.

John Cummings - *Salesforce.com Inc - IR*

All right. Hannah, thank you so much for hosting us today. Thanks, everyone on the call for joining us, and we'll look forward to updating you on our second quarter results this summer.

Operator

This does conclude today's conference call. You may now disconnect.

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