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CRM - Q1 2018 Salesforce.Com Inc Earnings Call

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OVERVIEW:

CRM reported 1Q18 revenue of nearly \$2.4b and non-GAAP EPS of \$0.28. Co. expects FY18 revenue to be \$10.25-10.30b and non-GAAP diluted EPS to be \$1.28-1.30.



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PRESENTATION

Operator

Good day. My name is Victoria, and I will be your conference operator. At this time, I would like to welcome everyone to the CRM Q1 FY '18 Earnings Conference Call. (Operator Instructions) I would now like to turn the call over to Mr. John Cummings, the Senior Vice President of Investor Relations. Sir, you may begin.

John Cummings

Thanks so much, Victoria. Good afternoon, everyone, and thanks for joining us for our fiscal first quarter 2018 results conference call. Our first quarter results press release, SEC filings and a replay of today's call can be found on our IR website at www.salesforce.com/investor. With me on the call today is Marc Benioff, Chairman and CEO; Keith Block, Vice Chairman, President and COO; and Mark Hawkins, CFO.

As a reminder, our commentary today will primarily be in non-GAAP terms. Reconciliations between GAAP and non-GAAP results and guidance can be found in our earnings press release. Also, some of our comments today may contain forward-looking statements, which are subject to risks, uncertainties and assumptions. Should any of these materialize or should our assumptions prove to be incorrect, actual company results could differ materially from these forward-looking statements.

A description of these risks, uncertainties and assumptions and other factors that could affect our financial results are included in our SEC filings in our -- including our most recent reports on Form 10-K and 10-Q. With that, let me turn the call over to you, Marc.



Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

All right. Well, hey thanks, John, and welcome, everybody, to the call. We're excited that you're here with us, and I'm personally very excited to be here and to share these amazing first quarter numbers.

So as you can see, the numbers were really outstanding with very strong top and bottom line performance. Revenue for the quarter rose to nearly \$2.4 billion, that's up 25%. And this is the fastest growth of any top 5 enterprise software company, and no company in the history of enterprise software has achieved our scale faster and at this growth rate.

Our non-GAAP earnings per share for the quarter rose to \$0.28, up 17%, and deferred revenue grew to more than \$5.04 billion, up 26%, really excited about that. And the dollar value of booked business on and off the balance sheet is now more than \$14.6 billion. That's up 26% from a year ago and we've added more than \$3 billion since last year.

Operating cash flow for the quarter was \$1.23 billion, up 17%, and we're maintaining our full year operating cash flow guidance of 21% growth at the high end of the range. Based on these strong results, we're raising full year top line revenue guidance by \$100 million to \$10.3 billion this year, the high end of the range, 23% growth for the year.

We're also raising our non-GAAP EPS guidance by \$0.01 to \$1.30 at the high end of the range, which is 29% growth year-over-year. We've consistently delivered excellent top and bottom line growth, driven by our industry-leading CRM product line and strength of our financial and operating model has continued in this quarter.

In fact, our consistent non-GAAP operating margin improvement over the last 3 years has enabled us to triple our free cash flow even as we have doubled our revenue. So that is something that we're very, very proud of at Salesforce that over the last 3 years, we've now tripled our cash flow and doubled our revenue. And we're on track to deliver our fourth consecutive year of non-GAAP operating margin improvement this year, 150 basis points at the high end of our range.

Our strong revenue performance shows the strength of our full product portfolio. In fact, our 4 major clouds are standalone companies, they would represent 4 of the top 10 pure-play cloud software companies in the world. We have strong organic revenue growth across all of our product sales. Cloud revenue is growing at 14%, Service Cloud at 21%, Platform at 32%, Marketing Cloud at 32%, excluding Demandware. And our portfolio has not only gotten stronger as we have continued to strategically invest in our business but as you know, last year, we also acquired a number of amazing companies, and the integrations of these acquisitions has been very successful.

And I just want to thank all of our employees at Salesforce for welcoming these new companies, and I want to also thank these companies who have now become part of Salesforce for their incredible hard work over the past several months integrating it with us.

And a great example of this is, of course, Demandware, which served more than 500 million shoppers and purchased more than \$4 billion in total gross merchandise value in the first quarter, which was up 31% over last year, pretty incredible. And yesterday, I was down in Las Vegas with the entire Salesforce Commerce Cloud team. And I'll tell you, we had over 1,500 people attending our Commerce Cloud conference, and it was amazing to see what's happening right now in this incredible retail industry and how so many retailers are focused on achieving a new level of customer success by going online or creating hybrid solutions between online and stores.

Now this is fuel -- further fueling our B2C CRM product line within our already industry-leading Marketing Cloud. And as retailers are shifting from these brick and mortar to online situations, they're focusing on building more personalized, one-on-one relationships with customers, using artificial intelligence to provide the best capabilities to their customers, delivering world-class customer experiences and not only in the store but even in the mobile environment. And Salesforce is leading all of these transformations.

Our competitive position has never been stronger. Just look at the latest data from the top industry analysts, IDC, shows Salesforce grew its overall market share more than any other CRM vendor. And according to IDC, we are #1 in CRM, we're #1 in sales applications, #1 in customer service applications, #1 in marketing applications in 2016. And you can see that if you go to my Twitter feed, there's a nice chart that we put together using the IDC data.

And Salesforce is gaining share at a much faster rate than our competitors, which you'll also see on that chart. We increased our market share in 2016 by more percentage points than the rest of the top 10 CRM vendors combined. That is, we increased our market share in 2016 by more percentage points than the rest of the top 10 CRM vendors combined, and we are very, very proud of that outstanding market performance in sales, in service and in marketing applications.

Gartner showed similar results. It named Salesforce the #1 in CRM. And based on total software revenue for 2016, for the fifth year in a row in its latest worldwide CRM market share report at Gartner, market share, all software markets, very excited.

So in the same Gartner report, we also saw total software revenue for 2016, Salesforce is again named #1 in application Platform-as-a-Service and for the fourth year in a row as well as the #1 sales provider for the eighth year in a row and the #1 customer service and support provider for the third year in a row. So all these incredible areas that we're focusing on, we're delivering phenomenal results.

With the strength of our market leadership and multiproduct portfolio, in the first quarter, we closed some of the biggest deals in Salesforce's history and Keith will talk more about that. We've also expanded relationships with incredible brands like Visa, very excited to see them go wall to wall with our Salesforce automation technology, with Delta Airlines and 21st Century Fox, very excited about 20,000-seat deployment of Quip, which they are using to replace their Microsoft Office implementation. So very excited to that and congratulations to all of those teams at Salesforce. No one else is closing more strategic CRM deals.

CRM is the fastest-growing enterprise software category today, and by 2021, CRM will be the largest area of spend in enterprise software, according to Gartner. And we are very excited about that. We have a massive opportunity to continue our growth and leadership in CRM and grow the Salesforce economy. Our ecosystem of customers, partners and developers is generating hundreds of billions of dollars in GDP impact and creating millions of new jobs. And in a time an incredible change in the world and incredible areas of workforce development, we are so excited that so many people are coming to Salesforce to find a new employment.

In fact, there's hundreds of thousands of job openings today that are calling for Salesforce skills, and we've seen this incredible situation where Salesforce developers and Salesforce administrator are 2 of the highest-paid jobs today in the United States. It's very exciting time for Salesforce. We expect to grow to nearly 30,000 employees worldwide this fiscal year, something I'm very proud of. And with each and every one of them completely focused on CRM and mostly focused on honestly, our customers and their success. In fact, nothing is more important to Salesforce than our customers' success, which is why we continue to be so successful and no other company has a focus like ours in the CRM market.

Our customer success message is on display this quarter. As you've probably seen, we launched our worldwide advertising campaign featuring some amazing customers and you're going to see some amazing more [ones] but one is -- and this is certainly something that everyone's interested in, the partnership between Salesforce and Amazon Web Services and how Amazon Web Services uses Salesforce to grow. It's been an incredible -- incredibly excited to use Amazon and the success of their cloud to feature the launch of our advertising campaign, and it's backed up with some incredible video testimonials that you can find on YouTube.

Farmers Insurance as well, Intuit, and so many other incredible brands, you're going to see emerging in our advertising campaign as we seek to raise the awareness of Salesforce in the general market to show people how they can connect with their customers in an entirely new way.

And in London today, you probably saw we held a sold-out world tour with more than 10,000 people in attendance and will be in Boston, Paris, Chicago in the next month, having similar world tours. We'll also have our second annual TrailheaDX developer event coming up in June 28 and 29 in San Francisco. And I hope you're going to join me for any of those events or you can join me in Tokyo on July 4 as we continue to deliver our message in the Asian market and to put on display the incredible success of Salesforce in Japan, which has been something that I have really been excited to see, helping our customers to blaze these new trails in CRM.

Okay. Well, that's enough of what's happening. With the numbers, let's hand this over to Keith.



Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

All right. Thanks, Marc. We delivered incredible results in the first quarter across all of our geographies, industries and clouds. As you can see from our numbers, the investments that we have made, and we continue to make an international expansion and industries and our partner ecosystem, continue to pay off.

More importantly, we are deepening our customer relationships. We're engaging with them in more strategic ways, some of which Marc alluded to, and we are acting as a true trusted adviser to their businesses.

We had some of the largest transactions in the company's history this quarter, starting with an iconic technology brand who is standardizing on Salesforce to bring together sales, service and marketing for thousands of employees worldwide. More to come on that next week.

And another large transaction in Q1 was with a major telecommunications company who is using Service Cloud and Marketing Cloud and the Salesforce Platform to transform the shopping experience for its customers. Very, very strategic. Now this company sees Salesforce as the key component to their retail growth strategy, and with this win, now 10 of the top 15 global telecommunications companies rely on Salesforce. Very impressive.

Now while our market-leading core products continue to see great traction and drive success for our customers, we're also seeing momentum with our new additions to the portfolio such as Commerce Cloud and Krux and Quip. Marc gave you an example of 21st Century Fox who's rolling out Quip to 20,000 employees, helping them co-create documents and streamline approval processes and collaborate in real-time.

Looking at our revenue internationally this quarter. We delivered strong results in all of our geographies as we had constant currency revenue growth of 29% in EMEA and 26% in APAC. Expansion outside the U.S. is key to serving our global customers. It's a key part of our strategy and achieving our goal of \$20 billion of revenue. And this starts with investing in our go-to-market resources, our partner ecosystem and our infrastructure.

We made amazing progress on this front in Q1, starting with announcement in March that we are leveraging AWS to deliver Salesforce services to customers in Australia, which I just returned from a couple of days ago.

We also announced the opening of our second data center in Japan in April. And in Europe, we had customer expansions with Banca IFIS, Adecco and Group Atlantic. In Japan, we landed wins with major brands such as SoftBank, Japan Asia Group and Mizuno. And in Australia, we expanded our relationship with AMP, a leading wealth management company. They are turning to Salesforce as many wealth management companies are to reimagine their client advisory relationship for the digital age.

Now turning to industries. We continue our strong showing in Q1 yet again. In fact, as Marc talked about, if you were in Vegas this week, you've seen Salesforce hosting our XChange conference for the retail industry, a great reception there. And at the conference, we announced an expansion of our relationship with iconic fashion brand, Diane von Furstenberg.

We also had a major expansion this quarter with Ralph Lauren. They've been very active in the press, and they have a new vision for growth and customer engagement that is powered by Salesforce Commerce Cloud. They believe that Salesforce will create a best-in-class experience in all of their markets around the world. And with these wins, today 8 of the top 10 U.S. retailers, nearly half of the top 20 global retailers, rely on Salesforce to power their business.

In the public sector, the team recently unveiled Impact Level 4, IL4, provisional authorization for government cloud, enabling even more federal government agencies to benefit from Salesforce. And in the quarter, we expanded our relationship with the United States Army and the United States Air Force.

In state and local government, we drove an amazing win with the state of Florida. They're using Salesforce to implement travel management system that will include authorization requests and approvals and expense reporting. And by streamlining all these processes with Salesforce, the state will be able to better analyze the amount of funding spent on travel and ultimately save tax payer dollars, which is a good thing.



Finally, in financial services, we're thrilled to expand our relationship in Q1 with Northern Trust, a leading provider of wealth and asset management services. And with the addition of Salesforce CPQ and Shield, they're enhancing customer trust and building a 360-degree view of their clients. And today, 9 of the top 10 global wealth management firms rely on Salesforce.

On the partner front, we continue to work with the largest and most strategic SIs and ISVs in the world, reaching new markets, building amazing applications on the AppExchange and ultimately growing our impact with customers, because it is all about customer success.

And in Q1, we expanded our relationship with Accenture. As you know, they're a long-standing and strategic partner for us, and this quarter, they grew their deployment of Sales Cloud to thousands of their consultants worldwide. But it's not just about the SIs. We're also seeing momentum across our thriving ISV ecosystem, and earlier this month, we announced that Quintiles IMS, a leader in life sciences is building new clinical trial applications on the Salesforce Platform.

And just last week, you saw that we launch new AppExchange partner program and a \$100 million platform fund to empower millions of developers and ISVs to create new applications. So it's never been a better time to build on the Salesforce Platform.

At the end of the day, our strategy of international growth and building the world's greatest cloud ecosystem and speaking the language of our customers continues to fuel our results. I'd like to thank our customers and our partners for their trust in us and our employees for strong results for the year, and of course, now over to you, Mark.

Mark J. Hawkins - *Salesforce.com, inc. - CFO and EVP*

Thanks, Keith. I'm really pleased with our first quarter results. We continued strong top line and bottom line growth and our record operating cash flow in the quarter. Revenue grew 25% in both dollars and constant currency, excluding a year-over-year FX headwind of approximately \$11 million.

Sequentially, we benefited from an FX tailwind of approximately \$15 million. Each of our clouds demonstrated strong revenue growth in the quarter as Sales Cloud grew 14%, Service Cloud grew 21%, Platform and Other grew 32% and Marketing Cloud, excluding Demandware, now Commerce Cloud grew 32%. The Commerce Cloud started FY '18 very strong, contributing \$57 million in total revenue and with \$46 million in subscription and support revenue.

Dollar attrition in the first quarter, excluding Marketing Cloud and other acquired businesses, remained below 9%. As you know, our fourth quarter is our largest new business from renewals quarter and Q1 is our largest cash collection quarter. And as a result, we delivered a record operating cash flow in the first quarter of \$1.23 billion, up 17% over last year. This is more operating cash flow than we delivered in all of FY '15.

Deferred revenue ended the quarter at \$5.04 billion, up 26% in dollars and 27% in constant currency, excluding an FX headwind of \$21 million. On a sequential basis, deferred revenue benefited from an FX tailwind of \$41 million. Commerce Cloud contributed \$50 million to deferred revenue in Q1, up from \$49 million in Q4.

Moving on to guidance. With strong results to start our fiscal year, we're very pleased to be raising our full year FY '18 revenue guidance to \$100 million to \$10.25 billion to \$10.3 billion or 22% to 23% growth year-over-year. This guidance includes approximately \$50 million to \$100 million of FX headwind. And we're also raising our FY '18 non-GAAP diluted EPS guidance to \$1.28 to \$1.30.

Please keep in mind that Dreamforce is in Q4 this year versus Q3 last year. And as you update your models for the second half, we anticipate slightly more EPS to come in the third quarter than in the fourth. We continue to expect to deliver 125 to 150 basis points of non-GAAP operating margin improvement in FY '18, our fourth consecutive year of improvement.

We're also maintaining our full year operating cash flow guidance of 20% to 21% year-over-year. For Q2, we're expecting revenue of \$2.51 billion to \$2.52 billion, non-GAAP diluted EPS of \$0.31 to \$0.32 and year-over-year deferred revenue growth of approximately 22%. This deferred revenue guide reflects the increasing seasonality that we've discussed over the last several years.

Before I close, let me give you a quick update on our future adoption of the new revenue standard ASC 606 starting in Q1 of next year. We will adopt this using a full retrospective method, which will result in recasting our results in FY '17 and FY '18. We're on track with the preparations to address the accounting changes.

Regarding commissions, we anticipate capitalizing more selling-related cost, and our amortization of these costs will be over the customer life rather than the contract term. While we expect to increase our disclosures for revenue backlog, deferred revenue and other customer contract information, we have not yet quantified the impact to revenue. However, we do not expect these changes to have any impact on our operating cash flow results upon adoption in FY '19.

All these changes are required under the new standard. We plan to provide you with a thorough review of these changes and the anticipated accounting impact later this year. So to wrap up, our first quarter results position us well for another year of strong financial performance. I'd like to thank all of our employees, customers, partners and our stockholders for their continued support. And with that, we'll open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of Karl Keirstead with Deutsche Bank.

Karl Emil Keirstead - *Deutsche Bank AG, Research Division - Director and Senior Equity Research Analyst*

Question for Mark Hawkins, just on the how front-end loaded the investment spend will be this year. I noticed you and Marc updated the full year operating margin improvement of 125 to 150, but it looks like in Q1, operating margins were down year-over-year and it looks like R&D was up quite a bit. So I'm just curious whether Salesforce is front-end loading your OpEx investments and what would drive the operating margin improvement in the second half.

Mark J. Hawkins - *Salesforce.com, inc. - CFO and EVP*

Sure. Thank you, Karl, and good to speak. Remember last year, Karl, one of the things that we called out is that we had the benefit of a leap year. And while that washes out for the year, what that does is has a material 25 -- \$20 million to \$25 million in revenue impact in Q1 from that standpoint. And so when you -- that's one thing that you would consider. The second thing, Karl, as a reminder, is that we still haven't annualized the full integration costs that we're doing right now for some of the work with our major acquisitions, including Demandware and a few others. And so that obviously has a little bit of a front-end impact. But when you look at those 2, that explains a little bit of the topography as you look quarter by quarter. Of course, for the full year, as we talked about, our operating margin, 125 to 150 is intact. It's consistent with our framework and it's on a higher revenue basis obviously. Therefore, we raised the -- also the EPS for the year. So I think we're in good shape on that but hopefully, that gives you a sense there. Number two is on research and development, Karl. One of the things that we want to call out is we've been having a group of people, as you know, as we've been going into industries, we started industries, trying to talk the language of industries and with a really huge go-to-market focus. And now -- we're now starting to move some of our industry resources into the product development side. And so there's a bit of a reclass of moving some of our resources and shifting those into R&D. So in total, it's just a movement between line items, but we're in good shape overall, and that's what's happening in Q1 in those 2 items.

Operator

Your next question comes from the line of Kash Rangan with Bank of America.



Kasthuri Gopalan Rangan - *BofA Merrill Lynch, Research Division - MD and Head of Software*

Actually a couple of questions. One for you, Marc Benioff. It looks like there's a lot of business coming through on the government side. And I'm also hearing, really over the last several quarters of conference calls, a decided shift in the business towards more B2C-centric industries. Can you talk about the business strategically, Marc, given that we know that according to statistics that the government actually spends the most amount of money on software. It's, by far, the vertical that commands the biggest share of what's spent on software. Can you talk about how the company views this opportunity ahead in the context of the Platform business, which also has a potential to be a multibillion-dollar business? And I guess I'll save the question for Mark Hawkins if you can get through this, that will be fine.

Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

Okay, Kash, it's Keith. So you alluded to the progress that we're making in the government. We have made an incredible amount of progress with our focus on the government business, the public sector business here. We had a big announcement in the quarter of IL4, which obviously is making a difference for us. We've expanded our relationship in the quarter with the U.S. Air Force and the U.S. Army. So we see that as a huge opportunity as the government really focuses on trying to modernize and transform their business and their organization, their technology. So there's a lot of potential there in the quarter. As I mentioned, we had a significant win with the state of Florida. And we did some incredible work in 311 for one of the largest cities. So stay tuned on that. For one of the cities -- largest cities in the country that we all know and love. So again, this industry's strategy is really, really paying off for us, not just in our go-to-market strategy but as Mark Hawkins alluded to in our orientation of our product set. As you know, last year, we released the Financial Services Cloud and the Health Cloud with the acquisition of Krux and Demandware, now Commerce Cloud. We have a widely compelling B2C story. Ralph Lauren is an incredible story and the company that is going through a lot of transformation, and they're leveraging us as the growth platform for B2C. So we just see tremendous opportunity and tremendous upside, and we continue to focus on speaking the language of the customer, leveraging our platform, growing our partner ecosystem and investing our assets in driving solutions for customers in specific industries.

Operator

Your next question comes from the line of Phil Winslow from Wells Fargo.

Philip Alan Winslow - *Wells Fargo Securities, LLC, Research Division - Senior Analyst*

Question for Marc Benioff. Wanted to focus on the Sales Cloud because obviously, a lot of attention has been given to the growth over the past couple of quarters and Service and Marketing. But if you look at the growth in Sales Cloud, that's actually gotten accelerated over the past couple of quarters here. How do you think about Sales Cloud in terms of where we are in the life cycle, pricing, upsell potential, just walk us through just your thoughts on where we are.

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

Well, Sales Cloud has become one of the largest products not just at Salesforce, but in the entire software industry, and it has far exceeded our expectations. And as you can see, as Salesforce, Sales Cloud specifically kind of heads towards that, these kind of incredible revenue levels, I think Sales Cloud has really accelerated because we kind of have a -- had a breakthrough in how we think about Sales Cloud and the ability to grow that revenue stream. And that you saw with our acquisition, for example, of SteelBrick. When we acquired SteelBrick, it also gave us the ability then to extend Sales Cloud with CPQ-type functionality, which just -- was something that we did not have previous to that, previous to the acquisition, and we're able to organically grow the product. And that has been a big revelation for us as we look to all the options and all the things that our Sales Cloud customers need that previously we didn't have. And in addition to that, we continue to close very large new Sales Cloud licenses. I mentioned Visa, for example, which went wall to wall with Sales Cloud this year. But there's been so many other exciting Sales Cloud customers, as you know. And as Keith mentioned, combined with the vertical strategy, it's really opened up all these new opportunities. I think, a great example is financial services where we have the Wealth Cloud, which is built, of course, on the Sales Cloud. And now, 9 out of the 10 largest financial institutions of the world are using Sales Cloud and Wealth Cloud to manage their wealth advisory firms. That's pretty cool and another example



where we're growing Sales Cloud. So we take this very, very seriously that when we look at Sales Cloud and Service Cloud, which are huge products, 2 of the biggest products in the software industry and 2 of our biggest products, we want to continue their strong organic growth. And we have been able to put together a whole portfolio of strategies to do that. And it's working. And I hope that it will continue to work and we're trying to do a lot of cool things this year to make that happen. And I think that we look and talk to Alex or you talk to Keith or I, we're extremely aligned on this breakthrough and we're executing it.

Operator

Your next question comes from the line of Alex Zukin with Piper Jaffray.

Aleksandr J. Zukin - *Piper Jaffray Companies, Research Division - MD and Senior Research Analyst*

Maybe for Marc Benioff or Keith. You guys continue to sign some very large transactions in the quarter. So I guess, as you think about the strategic imperative of growing your wallet share within these Fortune 500 accounts, how should we think about a very large customer that you are for this along with in terms of that percentage of their overall budget or spending on you versus your average? And how does that compare with an Oracle, SAP or Microsoft at this point?

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

It's a very good question. Do you want to handle (inaudible)...

Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

Well, let me -- Alex, it's Keith. Let me take a swing at this. So obviously, we have a very balanced portfolio of business, whether it's our large deals or small deals, whether it's our industries or geographies or segments. We've highlighted a couple of these very large transactions because we're particularly proud of the fact that these are 2 of the largest transactions that we've done in the history of the company. And when you think about the compelling reason why these companies are undertaking these transactions and establishing these relationships, at the end of the day, the CEOs of these companies are very forward-thinking CEOs. And they want to bring their companies into this age of digital transformation, and they have an imperative for growth, and they believe strongly that we are the only technology platform out there that will enable that growth. So that would be point number one. Point number two is that once we've established this relationship and they start to get more and more value as a company, as you know, we continue to innovate. And as we bring new innovations to the table, like Quote-to-Cash or SteelBrick like Marc was talking about, that allows us to go back into those large customers and bring new points of innovation to them. So that huge deal or those large deals really create a platform and an opportunity for us to innovate and continue to attach. That's a big part of our strategy. Obviously, from a percentage of IT spend, if you look at where the market is going, IDC has a study out that says that the largest category of enterprise software by 2020 will be CRM and the fastest growing. And if you look at our results, we're growing at significantly more than that rate of market, so that means we're taking market share, which means we're taking wallet share and that means obviously, we're taking -- which translates to IT budgets. And it translates into the mind share of our CEOs that we're trying to do business with. So we have a compelling offering. We're driving the market. We're taking share from our competition. We've got the mind share with the CEOs of these companies, and that just translates into higher penetration rates from IT budgets.

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

And I think the other point you -- kind of didn't mention that, I think they love to hear about is these top 10 customers just continue to grow. I mean, it's kind of amazing and I think it surprised us, right, to see how big our largest customers are becoming and how committed they are to our technology, especially is our platform. Do you want to illuminate that further?



Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

Yes, I think it's kind of an interesting statistic that we talk at the board level is if you look at the top 10 companies and the barrier to get into what we referred to as the top 10 club. If you look at what that barrier was 4 years ago and then you fast forward to where we are today, particularly at the end of this first quarter, to get into that top 10, you'd have to be spending more than 2.5x what you did before 4 years ago. So we have not only grown these relationships, but we also have new members into this, what we call the top 10 clubs. So again, it's an indication that these companies are adopting our technology and they're transforming our business.

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

And back at that point, you mentioned the kind of -- this kind of pre-growth time, we only really have maybe 1 or 2 products to offer these companies. Now we have a full range of services to help them focus on their customer, sales, service, marketing, community, analytics, apps, platform, commerce and so forth. Is that -- do you think that's one of the reasons that it's growing is the digital transformation of these companies that's doing it? What is it that's happening?

Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

There's no question that there is a laser focus on digital transformation by the CEOs of these organizations. And when you think about the evolution of our company, we have a strategy that we refer to as seeding growth, where we initially penetrate and we drive value, typically, with Sales Cloud. So this reacceleration of Sales Cloud is obviously a great thing. And then once we drive success for those customers, as Marc was talking about, then we're able to say, "Okay, now the walls between sales, service and marketing are coming down." So now we have an opportunity to provide a 360-degree view of the customer with service and with marketing. And take that now one step further, as we've moved from systems of record to systems of engagement to now systems of intelligence. And that's where Einstein, which we're all very excited about and customers are excited about comes into play. So it's an expansion of our capabilities and our opportunity to drive transformation with these customers.

Operator

Your next question comes from the line of Walter Pritchard with Citi.

Walter H Pritchard - *Citigroup Inc, Research Division - MD and U.S. Software Analyst*

Question for Keith. Just first on -- you highlighted Australia rolling out AWS down there. And I'm wondering just generally, is the AWS partnership and you being able to put customer data in more locations, ultimately, long term helping your pipeline internationally or any impact at this point yet?

Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

Well, interestingly enough, I just returned from Australia a couple of days ago. And there is a great deal of excitement about our Australian data center and a great deal of excitement about our partnership with AWS. And this is something that as a company on the -- for the benefit of our customers, it's kind of a big deal strategically for us. And obviously, it's a big deal for our customers. It's something that we're excited about.

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

Yes. And I think at Salesforce, we really strongly believe that the enemy of my enemy is my friend, and I think that makes Amazon Web Services our best friend.



Operator

Your next question comes from the line of Heather Bellini from Goldman Sachs.

Heather Anne Bellini - *Goldman Sachs Group Inc., Research Division - Research Analyst*

This question is actually for Marc Benioff. Marc, I was wondering if you could share with us how you've seen Einstein start to impact deal sizes. And what's the general, I guess, adoption curve look like for machine learning and AI now that you have it embedded into your products?

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

Well, I can just tell you from my personal experience and I think I've mentioned this before, but I think it played out in this quarter once again, which is that we have Einstein now built into all of our capabilities. And like in a lot of our technologies, we've really become the first and most, probably, fastest moving user. And we then have a piece of Einstein now that we've not yet rolled out to our customers called Einstein [Guidance]. So this is a capability that I use with my staff meeting, when I do my forecast and when I do my analysis of the quarter, which happens every Monday at my staff meeting like a lot of CEOs do, it's a very typical process, of course, we have our top 20 or 30 executives around the table. We talk about different regions, different products, different opportunities. And then I ask one other executive their opinion and that executive is Einstein. And I will literally turn to Einstein in the meeting and say, "Okay, Einstein, you've heard all of this. Now what do you think?" And Einstein will give me the over and under on the quarter and show me where we're strong and where we're weak and sometimes will even point out a specific executive, which it's done in the last 3 quarters and said that this executive is somebody who needs specific attention during the quarter. And I can tell you that I do believe that Salesforce's enhanced performance has been greatly attributable to our ability to have Einstein on board and as part of our team. Because that ability to consult with Einstein has made me a better CEO. I have the ability to talk to Einstein and ask Einstein everything from product areas that I should be focusing on, geographies that I should be focusing on, the linearity of bookings during the quarter. Every question that I possibly could have, I'm able to ask Einstein. And I think for a CEO, typically the way it works is, of course, you have various people, mostly politicians and bureaucrats, in your staff meeting who are telling you what they want to tell you to kind of get you to believe what they want you to believe. Einstein comes without bias. So because it's just based on the data, and it's a very exciting next-generation tool. And to have Einstein guidance has transformed me as a CEO. I'm sure that if we are a sales leader in here, they would tell you that it's transforming our individual salespeople's experience as they have the ability to prioritize who to make sales calls onto or who to make phone calls to with our new Einstein dialer or to -- yesterday, I was down in Las Vegas talking to retailers where Einstein is helping shoppers make better shopping decisions because it's able to prioritize based on shopping histories what products that they're seeing. We did a very exciting demonstration with one of our top customers, which is Deckers. They have an incredible brand that I love called UGG shoes. And we demonstrated how one of their consumers is having a mobile experience using Apple Pay and using all these kind of next-generation activities to have a one-on-one shopping experience. And Einstein comes in and says, "You like that shoe. These are the other shoes and other products that we have that we think that you would like and the colors that you would like them. And based on how everybody else has purchased and your purchase history, this is what Einstein recommends to you." And that was very, very powerful for our customers. I mean, so we see it in our analytics product, we see it in our Commerce product, we see it in our Sales Cloud. You're going to -- you see it in our Service product as well, especially with the emergence of bots, where many of our customers want to deflect call using bots, which I think is a great strategy and across the board. So I think that Einstein artificial intelligence, I mean, I guess, I have -- I should probably just point back to we started the quarter in February and many of you saw the demonstration with Coca-Cola were building the smart cooler for them, which has Einstein built into the cooler in a retail store that's paying attention to what products are being taken and removed from the store using Einstein Vision. So you can see into the cooler and actually say, "Oh, they took a Coke, they took a Diet Coke, they took a Sprite. Or oh, there's a competitive product in here. Send somebody to get this out." So Einstein is having, I think, a very dramatic impact. Of course, we're the first major CRM company to roll artificial intelligence so dramatically through all of our products. And I think that it's going to be instrumental. And when you look at AI, there's a couple of things you can think about. One is this is happening a lot faster than anybody expected. The fundamental development of AI whether it's machine learning, machine intelligence or deep learning. The growth of AI, the advancements in AI, and you saw that yesterday in the Google conference as well, it's just the speed of growth is just exceeding everybody's expectations. And two, AI is the next platform. All future applications, all future capabilities for all companies will be built on AI. Much in the same way that we talked about the future with cloud, the future of social and social became the next platform, or mobile became the next platform. Now you can really see how AI is becoming the next platform. And everyone is going to build on AI, and it's going to fundamentally transform all of our customer experiences and Salesforce is going to continue to do -- lead the way with that and also be on point to be able to have that meaningful transformational



conversation with the most important CEOs in the world to help them to do what I'm doing, which is to transform their own business and how they run their businesses using AI. And that's why I'm excited about Salesforce Einstein.

Operator

Your next question comes from the line of Mark Murphy with JPMorgan.

Mark Ronald Murphy - *JP Morgan Chase & Co, Research Division - MD*

Also a question for Marc Benioff. Given the board-level attention that you're receiving, I'm curious what inning you think we're in, in terms of digital transformation. In other words, how many Global 2000 types of firms are seriously considering a digital transformation? And also when you do see a company engage in a use Salesforce as the centerpiece for one of those projects, how does their level of spending with Salesforce change?

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

Well, I think that is really the big question right now here at Salesforce so I appreciate you asking that. And I'll give you an example. I was in Las Vegas yesterday. We had thousands of customers down there. Simultaneously, we had thousands of customers at our London world tour, which is just, in my mind, a major accomplishment for Salesforce for running 2 multi-thousand person events concurrently in 2 different parts of the world. And when I was down in Las Vegas, I was meeting with a very large manufacturer of furniture who has not done a lot of automation. It's a huge company with tens of thousands of employees. And they are both a B2B company, where they are building their furniture, designing their furniture, creating their furniture and they're selling it to partners and they're selling to the resellers, and they're selling it online to different vendors, and their B2C company, they have their own stores and they also do their own online. And they're like, "We are looking for an opportunity to digitally transform our company. And honestly, we have -- we're not the state-of-the-art, and we need a B2B and a B2C transformation. Can you help us?" And I said, "Honestly, I think Salesforce is the only company today who can work with a company like that and be able to come in with a full range of capability, technology, services, relationships, partnerships and say we can transform you whether you're B2B or B2C or both. And it was the first time that a customer actually ever came up to me and said, "I'm B2C and I'm B2B." And it was really very powerful to kind of hear that because I -- it's how we're starting to think a lot at Salesforce, which is, of course, we have this incredible -- we're #1 in B2B. Sales Cloud, Service Cloud, you know the numbers. Marketing Cloud, Pardot, I mean, it's incredible, the Platform, Application Platform as a Service. And now you saw the IDC numbers we're #1 in B2C with the Marketing Cloud, which is incredible. And this is a big, big deal in Commerce Cloud with our digital marketing platform that we introduced yesterday, which is so incredible as well as our -- not just our DFP but also this incredible capability with commerce. And the ability to stitch it together for these customers in a meaningful way to provide deeply interactive experiences and deeply personalized one-to-one experiences and make it all intelligent with Einstein. And with that customer, we're able to sit there for 1 hour and sketch out on a piece of paper everywhere they need to go. And here's the other thing that's so cool is we can say, "We're going to get all this done for you probably in the next 90 days, no more than 180 days." It doesn't take a long time to really build and deliver. And I won't go through this specific example, but we have a major customer right now who just has imploded with SAP Hybris because it's on-premise software product built in the last generation of software. And these retailers, they don't have time to wait and they don't have the ability to take on the risk of this old enterprise on-premise stuff like SAP Hybris. And that's why you see this rapid acceleration of our Commerce Cloud. But that's just a metaphor. They just don't have the ability to take on the risk of any of that old Oracle or SAP on-premise software. So that's why by basically being born cloud, by being born social, born mobile and now being born AI, we can do more for customers today and go faster than ever before. And we have so many examples. And I think that when you look at that IDC chart, the reason why we've really just taken SAP out of their #1 spot in CRM and left them in the dust is because these customers, they need transformation now and we're able to deliver it. And that makes me very proud for the company and makes me really happy when I meet with one like that furniture company yesterday in Vegas to be able to support them so fully.

Operator

Your next question comes from the line of Kirk Materne with Evercore ISI.



Stewart Kirk Materne - *Evercore ISI, Research Division - Senior MD and Fundamental Research Analyst*

Keith, another really nice quarter in Europe for you all. Just 2 quick questions on that region for you. Can you just talk about where you think Europe is versus the U.S. in terms of your mind share with senior executives that are thinking about digital transformation? Do you feel like you have sort of the same sort of brand awareness over there as you do in the U.S.? Or is there still some opportunities on that front? And then second, any concerns at all about the new GDPR regulation that's coming up around data privacy, maybe slowing down decisions on cloud technology as that deadline gets closer?

Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

Kirk, thanks for the question. So let me address the first one then actually, our President and General Counsel is in the room, so we're going to let her talk about the second part. So obviously, we did have another great quarter in EMEA. It's part of our growth strategy around international expansion. And look, at the end of the day, we honestly, we see opportunity everywhere, whether it's in the U.S. or whether it's internationally. And it really is coming back to this notion of CEOs embracing this concept of digital transformation. I spent some time in Europe about a month ago, and I'll give you 2 examples. One is with the CEO of one of the largest consumer banks in the world who is looking at how does he embrace our technology, how does he embrace Einstein to drive digital transformation inside the consumer bank? And it is very real. And financial services, as you know, it's an imperative because there's an incredible amount of disruption that's going on. Another example, I was with our President of EMEA, Miguel Milano, we went -- took a day trip up to Finland to meet with the CEO of Koenig. And this is a company that we would think as they are an elevator company. They are an escalator company, but the way that they view themselves is they're not really a B2B company, they're a B2C company. They move 1 billion people every single day and that's how they view themselves. So they want to go through a digital transformation to drive service because everything in their world is about service. And they're leveraging all of our technology, they're leveraging Sales and Service and Marketing and Einstein to make predictive insights about their customers' behavior and optimizing how they could move to these machines, these escalators and these elevators to optimize the experience for the consumer. So there is a ton of opportunity. I actually think it's limitless. It is bound only by the imagination of what you can do with this technology. And in Europe, I find that the industrial manufacturers are actually quite progressive in their thinking. You find financial services institutions all over the world that are very progressive. AMP in Australia, the wealth manager, many of the financial services institutions that we've talked about here in the United States, the example I just gave you about the consumer bank over in Europe. But in terms of the manufacturing sector, EMEA is very, very progressive in terms of embracing digital transformation. And by the way, we see that at The World Economic Forum every year in Davos. Regarding your second question, I'm going to turn that over to Amy Weaver and she can give us a little bit of an update on that.

Amy E. Weaver - *Salesforce.com, inc. - President of Legal, General Counsel and Secretary*

Great. Thanks for asking about this. So the GDPR, for anyone who does not know, is the new EU General Data Protection Regulation. And that's going to come into effect about 1 year from now in May of 2018. And what this is going to do is this going to replace the current patchwork of national data protection laws in the European Union and at the same time strengthen privacy rights. And at Salesforce, we really welcome the GDPR as an important step forward in streamlining all of these processes. And we're committed to making certain that our customers can continue to use our services while complying with the GDPR. It's something we are looking at very closely, and we will have further update to the market and to all of our customers throughout the year as we get closer to the implementation deadline.

Operator

Your next question comes from the line of Samad Samana with Stephens, Inc.



Samad Saleem Samana - *Stephens Inc., Research Division - Research Analyst*

So we thought at the New York City world tour, the company announced it was lowering the rev share for ISVs back to pre-2015 levels. What's the strategy behind that decision? And maybe related to that, can you give us an idea of what the revenue from ISVs represents as a percentage of total platform revenue? And overall what percentage of new ACV's coming from the partner ecosystem generally versus direct sales?

Keith G. Block - *Salesforce.com, inc. - Vice Chairman, President and COO*

This is Keith. Let me try to address that as best as I can. Look, at the end of the day, we think we have the most compelling platform in the marketplace. I gave the example of Quintiles IMS who's building a mission-critical application. Clinical trial application, it's pretty serious stuff and they're going to be building that on top of our platform. Great example of an ISV. Another example obviously is Accenture. Vlocity, I mean, there's a roster that we've given here. And we want to drive proliferation and usage and adoption in the marketplace, and we want to make sure they're [going to use] price to value, and that's why we made an announcement in New York and also why we made the announcement around our fund, which we're very, very excited about to be able to invest in these ISVs. As far as breakout of ISVs, revenue and ACV and all that stuff, we don't disclose that. Mark Hawkins, I don't know, if you want to...

Mark J. Hawkins - *Salesforce.com, inc. - CFO and EVP*

Yes. In fact, just we concur, we don't, but I totally agree with your points there. I would add, Samad, that this is, as you know, is an exciting offering our Platform app grew 31%. It's another \$1 billion, \$1.5 billion cloud that's growing and rapidly towards \$2 billion. So it's an exciting thing. And I think this change, Keith, is just simply part of amplifying the opportunity for our customers. So that would be the net of it.

Operator

And your last question comes from the line of Raimo Lenschow with Barclays.

Raimo Lenschow - *Barclays PLC, Research Division - Director and Analyst*

A lot of mine have been answered, but the one I wanted to talk to you about is now this year, you're going to hit the \$10 billion in revenue and only very few software companies have achieved that. Now that your eyes are kind of moving on towards the \$20 billion, can you talk a little bit about the changes you need to think about in terms of organization and we need to think about as well because obviously, it's a completely different skill again then and it's something that kind of requires kind of careful planning?

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

Sure. I'm happy to talk to you about that. I think everyone at Salesforce is so excited to see our run rate begin to eclipse \$10 billion in revenue. And of course, the big -- I think the big announcement on this call here, you can see the switches, the book business on and off the balance sheet is just the deferred revenue, which is what Mark, \$14.6 billion. \$14.6 billion...

Mark J. Hawkins - *Salesforce.com, inc. - CFO and EVP*

Yes, \$14.6 billion. You're exactly right. Growing, Marc, 26%.

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

26%. So all of you are going to run your own financial models. You know how our revenue and expense models work. And you can start to model next year now based on that, which is very exciting, I think. Or you can model -- we run our models now for the next 2 or 3 years. Next to that, we

have, of course -- we have a running 5-year long-range plan and a 5-year long-range budget that gets fueled and created by that on- and off-balance sheet deferred revenues, probably one of the most important things to drive that forward. And we -- that gives us the ability to kind of have a true north star of where our company is going and our finance team has done a great job in building these models and giving me the ability and then coupling it with Einstein to actually look to these models, too. And that is part of how we are able to deliver our quarter. Specifically, as we start to look at eclipsing \$10 billion and moving into much higher numbers going forward, of course, it's exciting to have that \$20 billion in sight. And I think that you're going to see the transformation of Salesforce in a few areas and you already saw it with what Keith has -- Keith mentioned, which is started by talking about government. That's a major business opportunity for Salesforce going forward and a major vertical for us. Of course, financial services remains a major opportunity and major capability, health care. These major verticals, that's a major focus for us. Keith has spoken extensively about that transformation. That's really complemented by our strong focus and Keith touched on this with the top 10 enterprise focus as well as our commercial business unit has continued to grow. So those are some of the examples. And then I would have to kind of couple in there the other major growth driver that we've kind of acquired our way into with ExactTarget, with Krux, with Demandware now becoming this incredible Salesforce Marketing Cloud and B2C. So when you look at things like government, financial services, health care, enterprise, commercial, B2C and I could go on and on in other critical areas for the company or by product, we touched on that. I think we have a very strong performance matrix that we are going to manage across all of our geographies, which also remains strong growth drivers, as you can see on the numbers for the quarter with Europe and Asia-Pacific and Latin America as well. So that's how I look at it. I would like Mark to kind of touch on that as well.

Mark J. Hawkins - *Salesforce.com, inc. - CFO and EVP*

Sure, I'd love to add, and Marc, I was going to touch on international that you just covered as well. But I think the thing, Marc, that strikes me and some other really -- rather Raimo, I really appreciate when you teed up that question about going from \$10 billion to \$20 billion because it's talking about doubling the company and how do we think about doing that. Well, one of the things that helps us is we're used to thinking about doing that, we just doubled the company in the last 3 years, and we've been thinking a lot about laying the groundwork to make that happen and that's been a reality. So we obviously extended our planning to do it again. And I think that's one key thing. But the thing that really strikes me when we talk about that is obviously, it starts out with all the innovations and the offerings to make our customers successful to drive our top line, and we're getting that top line growth. You can see the market share progress. But what's hard to do is to get that kind of progress and success with the customer and the market share, Marc, and the operating margin that we talked about and the cash flow we're delivering all of that currently, and we're certainly planning to do that in the long-range plan.

Marc R. Benioff - *Salesforce.com, inc. - Co-Founder, Chairman and CEO*

Yes, and I think that really just touches on our core values in our company, which starts with customer success. And I think is more important than the trust and customer success that we continue to focus on. I think you'll continue to see that be amplified as we head towards \$20 billion. We hire people who are focused on customer success. We have a culture of customer success entrusted. We also hire people who want to build a growing business. These are people who like to work hard and who enjoy growth and who relish that. And that's important to us. And third, I would say innovation. We continue to deliver world-class innovation, both organically. You've seen that with Einstein, with Lightning. And inorganically, we've seen that with Commerce Cloud and Krux and Quip. And this kind of perfect combination of that has created an amazing innovation inside our company. And we hire people who are focused on equality because I think we all realize that we're in a world today where we have to focus on equality, that this is a time when each and every one of us has a personal responsibility to look at the world and ask, "What value are we going to provide back to the world?" And that's why you hear me talk extensively about the importance of K-12 education because I strongly believe education is equality. And you'll hear me talk more about that this weekend. And Saturday, we open our Indianapolis Tower, Salesforce Tower in Indiana where we become the largest tech employer. And that's a place where equality has become a very important and core value of Salesforce.

So anyway, I want to thank all of our employees and customers and partners for an outstanding quarter and being so committed to our company and helping us to achieve these incredible milestones. And we're looking forward not only to the next level, but working together as a Salesforce family going forward to these incredible new heights. So thank you very much, everybody.



Operator

This concludes today's conference call. You may now disconnect. Thank you for your participation and have a good evening.

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