

HOW TO PERFORM AN EXCEPTIONAL INVESTMENT VALUATION?

Part-1

The word “Investment Analysis” conjures upon a myriad of financial tables that one tries to co-relate to spit out a set of numbers. First step of analysis process is to assimilate all the quantifiable data, but if that’s the only thing relevant in your analysis then it will resemble a very basic analysis that will not tell anything special to your reader. One should always remember that Investment analysis is an art and its. Your artistic flavor is what will make your analysis exceptional. In this blog post we will go through a Live CASE STUDY that showcases the importance of factoring a business’ dependencies in the Valuation process.

Factoring dependencies of a business is very critical in the overall valuation of the business. Usually the details of the dependencies are hidden in the foot notes that one might not notice when doing a quick valuation. Let us take the example of Veeva Systems (VEEV). As per its Q3-2014 quarterly report, the company generated \$226 million in sales for the 9 months ending 2014 , compared to \$147 million in sales for 9 months ending 2013. Thus the Growth was 53%. This definitely appears as a phenomenal growth story, but when dig into the foot-notes we can picture the limitations of this growth story.

Following are excerpts from the foot notes of the company’s 10Q report for Q3 2014.

Value-Added Reseller Agreement We have a value-added reseller agreement with salesforce.com, inc. for our use of the Salesforce Platform in combination with our developed technology to deliver our Veeva CRM solution, including hosting infrastructure and data center operations provided by salesforce.com. On March 3, 2014, we extended the term of the Value-Added Reseller Agreement for an additional ten years through September 1, 2025 and amended our minimum order commitments. As of October 31, 2014, we remained obligated to pay fees of at least \$474.8 million prior to September 1, 2025 in connection with this agreement.

If the third-party providers of healthcare reference data and prescription drug sales data do not allow our customers to upload and use such data in our solutions, our business may be negatively impacted. Many of our customers license healthcare provider and healthcare organization data and data regarding the sales of prescription drugs from third parties such as IMS and Cegedim. In order for our customers to upload such data to the Veeva CRM and Veeva Network solutions, such third-party data providers typically must consent to such uploads and often require that we enter into agreements regarding our obligations with respect to such data, which include confidentiality obligations and intellectual property rights with respect to such third-party data. We have experienced delays and difficulties in our negotiations with such third-party data providers in the past and we expect to experience difficulties in the future. If such third-party data providers do not consent to the uploading and use of their data in our solutions, delay consent or fail to offer reasonable conditions for the upload

and use of such data in our solutions, our sales efforts, solution implementations and productive use of our solutions by customers may be harmed, and, in turn, our business may be negatively impacted.

Because key and substantial portions of our Veeva CRM solutions are built on salesforce.com's Salesforce Platform, we are dependent upon our agreement with salesforce.com to provide our Veeva CRM solutions to our customers. Key and substantial portions of our Veeva CRM solution and the commercial applications that complement our Veeva CRM solution are developed on or utilize the Salesforce Platform of salesforce.com, inc., and we rely on our agreement with salesforce.com to continue to use the Salesforce Platform as combined with the proprietary aspects of our Veeva CRM solutions. Our agreement with salesforce.com expires on September 1, 2025. However, salesforce.com has the right to terminate the agreement in certain circumstances, including in the event of a material breach of the agreement by us, or that salesforce.com is subjected to third-party intellectual property infringement claims based on our solutions (except to the extent based on the Salesforce Platform) or our trademarks and we do not remedy such infringement in accordance with the agreement. Also, if we are acquired by specified companies, salesforce.com may terminate the agreement upon notice of not less than 12 months. If salesforce.com terminates our agreement under these circumstances, our customers will be unable to access our Veeva CRM solutions. A termination of the agreement would cause us to incur significant time and expense to acquire rights to, or develop, a replacement customer relationship management platform and we may not be successful in these efforts. Even if we were to successfully acquire or develop a replacement customer relationship management platform, some customers may decide not to adopt the replacement platform and may decide to use a different customer relationship management solution. If we were unsuccessful in acquiring or developing a replacement customer relationship management platform or acquired or developed a replacement customer relationship management platform that our customers do not adopt, our business, operating results and brand may be adversely affected.

Also, if either party elects not to renew the agreement at the end of its September 1, 2025 term or if the agreement is terminated by us as a result of salesforce.com's breach, the agreement provides for a five-year wind-down period in which we would be able to continue providing the Salesforce Platform as combined with the proprietary aspects of our solutions to our existing customers but would be limited with respect to the number of additional subscriptions we could sell to our existing customers. After the wind-down period, we would no longer be able to use the Salesforce Platform.

Our agreement with salesforce.com provides that we can use the Salesforce Platform as combined with our proprietary Veeva CRM application to sell sales automation solutions only to drug makers in the pharmaceutical and biotechnology industries, which does not include the medical devices industry or products for non-drug departments of pharmaceutical and biotechnology companies. Sales of the Salesforce Platform in combination with our Veeva CRM application to additional industries would require the review and approval of salesforce.com. Our inability to freely sell our Veeva CRM solution outside of drug makers in the pharmaceutical and biotechnology industries may adversely impact our growth.

While our agreement with salesforce.com, subject to certain exceptions, provides that salesforce.com will not position, develop, promote, invest in or acquire applications directly competitive to the Veeva CRM solution for sales automation that directly target drug makers in the pharmaceutical and biotechnology industry, or the pharma/biotech industry, our remedy for a breach of this commitment by salesforce.com would be to terminate the agreement, or continue the agreement but be released from our minimum order commitments from the date of salesforce.com's breach forward. While our agreement with salesforce.com also restricts salesforce.com from competing with us with respect to sales opportunities for sales automation solutions for the pharma/biotech industry unless such competition has been pre-approved by salesforce.com's senior management based on certain criteria specified in the agreement, and imposes certain limits on salesforce.com from entering into arrangements similar to ours with other parties with respect to sales automation applications for the pharma/biotech industry, it does not restrict a salesforce.com customer's ability (or the ability of salesforce.com on behalf of a specific salesforce.com customer) to customize or configure the Salesforce Platform. Some current or potential customers of ours may choose to build custom solutions using the Salesforce Platform rather than buying our solutions.

CONCLUSION :From the above footnotes we can see that Veeva System's operations is heavily dependent on Salesforce's infrastructure and is also constrained with certain agreements. In return Veeva does have an advantage of a non-compete agreement that restricts Salesforce from directly competing with it. But in return Veeva has to pay the hefty fees irrespective of the sales it generates. As of Oct-31-2014 it had a liability to pay \$474 million which interestingly is not reflected in the Balance sheet because its considered off-balance sheet liability.