Company Overview

MSFT is an American multinational technology corporation which produces computer software, OS, server/client applications, consumer electronics, personal computers, internet/intranet software, gaming systems & other devices. It’s an extremely stable, bluechip, conglomerate with an aggressive goal of “empowering every person and organization on the planet to achieve more.”

MSFT has a number of income streams generating revenues from different segments & is well positioned to help us reach our portfolio goal for generating alpha against the SPY. The three main segments driving this growth are:

- **More Personal Computing** consists of consumer and enterprise products. Products include:
  - Windows including Windows OEM; Devices including Surface and PC accessories
  - Gaming including Xbox hardware and Xbox content and services
  - Search advertising

- **Intelligent Cloud** consists of public private and hybrid server products and cloud services. Products include:
  - Server products and cloud services including Azure, SQL Server, Windows Server and GitHub
  - Enterprise Services including Premier Support Services and Microsoft Consulting

- **Productivity and Business Processes** consists of products and services representing productivity, communication and information services. Products include:
  - Office Products (Commercial and Consumer) include Office, Exchange, SharePoint, Microsoft Teams, Office 365 Security and Compliance and Skype
  - Linkedin including Talent Solutions, Marketing Solutions, Premium Subscriptions, Sales Solutions, and Learning Solutions
  - Dynamics include Dynamics 365

Investment Thesis

- **Strong growth in intelligent cloud segment**
- **Increased operating efficiency**
- **Low downside risk**
- **Increased organic/inorganic growth**

Microsoft Segment Breakdown

Based on Microsoft’s FY 2021 ended June 30, 2021

- **Revenue**
  - Intelligent Cloud: 36%
  - More Personal Computing: 32%
  - Productivity and Business Processes: 22%

- **Operating Income**
  - Intelligent Cloud: 39%
  - More Personal Computing: 19%
  - Productivity and Business Processes: 37%

Industry Outlook

The Covid-19 pandemic has accelerated growth in mainly two areas: cloud migration & digital transformation. There is a tremendous need to achieve the following objectives; lower IT infrastructure costs & enable easy access to applications from a large number of remote users which drives migration to the cloud through 3 levels of computing.
**Financial Performance**

<table>
<thead>
<tr>
<th>Breakdown</th>
<th>TTM</th>
<th>6/30/2021</th>
<th>6/30/2020</th>
<th>6/30/2019</th>
<th>6/30/2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Revenue</td>
<td>168,088,000</td>
<td>168,088,000</td>
<td>143,015,000</td>
<td>125,843,000</td>
<td>110,360,000</td>
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<tr>
<td>Cost of Revenue</td>
<td>52,232,000</td>
<td>52,232,000</td>
<td>46,078,000</td>
<td>42,910,000</td>
<td>38,353,000</td>
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<tr>
<td>Gross Profit</td>
<td>115,856,000</td>
<td>115,856,000</td>
<td>96,937,000</td>
<td>82,933,000</td>
<td>72,007,000</td>
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<tr>
<td>Operating Expense</td>
<td>45,940,000</td>
<td>45,940,000</td>
<td>43,978,000</td>
<td>39,974,000</td>
<td>36,949,000</td>
</tr>
<tr>
<td>Operating Income</td>
<td>69,916,000</td>
<td>69,916,000</td>
<td>52,959,000</td>
<td>42,959,000</td>
<td>35,058,000</td>
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<tr>
<td>Net Non Operating Interest Inc...</td>
<td>-215,000</td>
<td>-215,000</td>
<td>89,000</td>
<td>76,000</td>
<td>-2,733,000</td>
</tr>
<tr>
<td>Other Income Expense</td>
<td>1,401,000</td>
<td>1,401,000</td>
<td>-12,000</td>
<td>653,000</td>
<td>4,149,000</td>
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<tr>
<td>Pretax Income</td>
<td>71,102,000</td>
<td>71,102,000</td>
<td>53,036,000</td>
<td>43,688,000</td>
<td>36,474,000</td>
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<tr>
<td>Tax Provision</td>
<td>9,831,000</td>
<td>9,831,000</td>
<td>8,755,000</td>
<td>4,448,000</td>
<td>19,903,000</td>
</tr>
<tr>
<td>Net Income Common Stockhold...</td>
<td>61,271,000</td>
<td>61,271,000</td>
<td>44,281,000</td>
<td>39,240,000</td>
<td>16,571,000</td>
</tr>
</tbody>
</table>

**Valuation Assumptions & Key Financials**

We recommend a BUY rate for MSFT based on a target price of $360.87 per share. This target price reflects a 17.43% margin of safety based on its closing price of $309.16 on October 25th, 2021. We calculated WACC as 6.01%, assuming a terminal growth rate of 2% and a 18.01x exit EV/EBITDA.

**ESG Considerations**

MSFT has a low risk rating because it has the highest rankings in energy management, systemic risk management, employee engagement in diversity and inclusion. MSFT is constantly looking to reduce its carbon footprint & donated $1.9B to 243k non profits globally. The MSFT Airband Initiative provides broadband access to 2.1million people (15.1m outside US) & has a Global Skills Initiative goal of 25 million learners by 2021.