

## Analyst Report: Adobe Inc. (ADBE)

Adobe is well-positioned to lead the AI-driven transformation of the creative software industry, but faces intensifying competition and regulatory challenges.

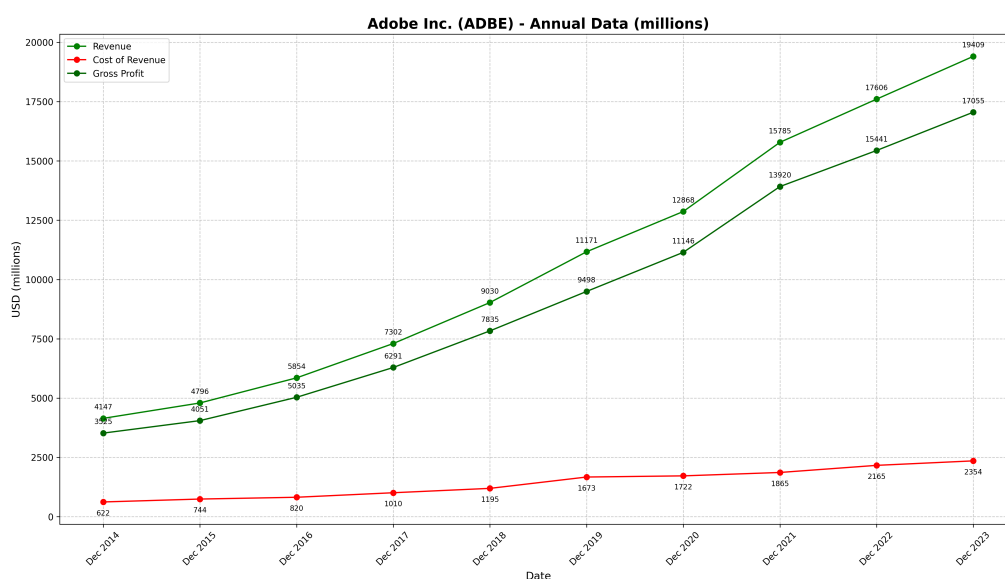
| Forward Valuations       | Bullish             | Bearish             |
|--------------------------|---------------------|---------------------|
| Implied Option Valuation | \$630.00 - \$680.00 | \$460.00 - \$510.00 |
| Sum of the Parts         | \$680.00 - \$730.00 | \$490.00 - \$530.00 |
| Relative Multiples       | \$600.00 - \$650.00 | \$450.00 - \$500.00 |
| Discounted Cash Flow     | \$650.00 - \$700.00 | \$480.00 - \$520.00 |

### SUMMARY DATA (ANNUAL)

|                     |                 |
|---------------------|-----------------|
| <b>52-Week High</b> | <b>\$638.25</b> |
| 52-Week Low         | \$433.97        |
| Shares              | 457             |
| EPS                 | 11.87           |
| Dividend            | 0               |
| Revenue             | 19,409          |
| Cost of Revenue     | 2,354           |
| Gross Profit        | 17,055          |
| EBIT                | 6,912           |

### OUTLOOK

Adobe Inc. is expected to maintain its strong performance over the next two quarters, driven by continued demand for its creative software offerings, particularly its AI-powered tools, and the growth of its Digital Experience segment. However, investors will be closely watching the company's ability to effectively monetize its AI offerings, address the increasing competition from rivals like Canva and CapCut, and navigate the ongoing regulatory scrutiny related to its subscription practices and past statements about competition.



## 1. Business Description

Adobe Inc. is a global technology company with a strong focus on digital media and digital experiences. Their latest 10K filing reveals impressive growth in their subscription-based offerings, Creative Cloud and Document Cloud, which are at the core of their Digital Media segment. These offerings provide individuals and businesses with powerful tools for content creation, editing, and collaboration across various platforms and devices. The company is also actively driving innovation in the Digital Experience market through their Adobe Experience Cloud, which empowers businesses to manage, personalize, and optimize customer experiences.

Adobe's commitment to research and development is evident in their continuous investments in emerging technologies like AI and generative AI. This is particularly noticeable with their Adobe Firefly, a family of creative generative AI models integrated into their products to enhance user creativity. Despite strong competition from established players and emerging startups, Adobe is confident in its ability to compete effectively based on its strong brand, feature-rich products, and extensive partner ecosystem. The company recognizes the increasing importance of AI in shaping the future of digital experiences, and they're actively investing in AI research and development to maintain their leadership position.

Adobe is subject to various risks associated with operating a multinational business, including economic fluctuations, regulatory changes, and geopolitical instability. Data privacy and security are also major concerns, given the sensitive nature of the data their products collect and manage. The company is proactively addressing these risks through investments in robust security measures, compliance efforts, and responsible AI development frameworks. In addition, Adobe acknowledges the competitive pressures in their industry, particularly from companies offering similar products or services, including those incorporating AI. They are also facing scrutiny over their subscription cancellation practices, with an ongoing investigation by the FTC. Adobe is confident in its ability to navigate these challenges and deliver strong future performance.

The company's financial performance in fiscal year 2023 was marked by strong revenue growth, driven by the success of its subscription offerings. Creative Cloud revenue grew by 10% year-over-year, reaching \$11.52 billion, while Document Cloud revenue saw a 13% increase to \$2.70 billion. Digital Experience also performed well, with an 11% revenue growth, reaching \$4.89 billion. Adobe attributes this growth to continued demand for their products in an increasingly digital world, strong customer engagement, and their strategic investments in AI and generative AI.

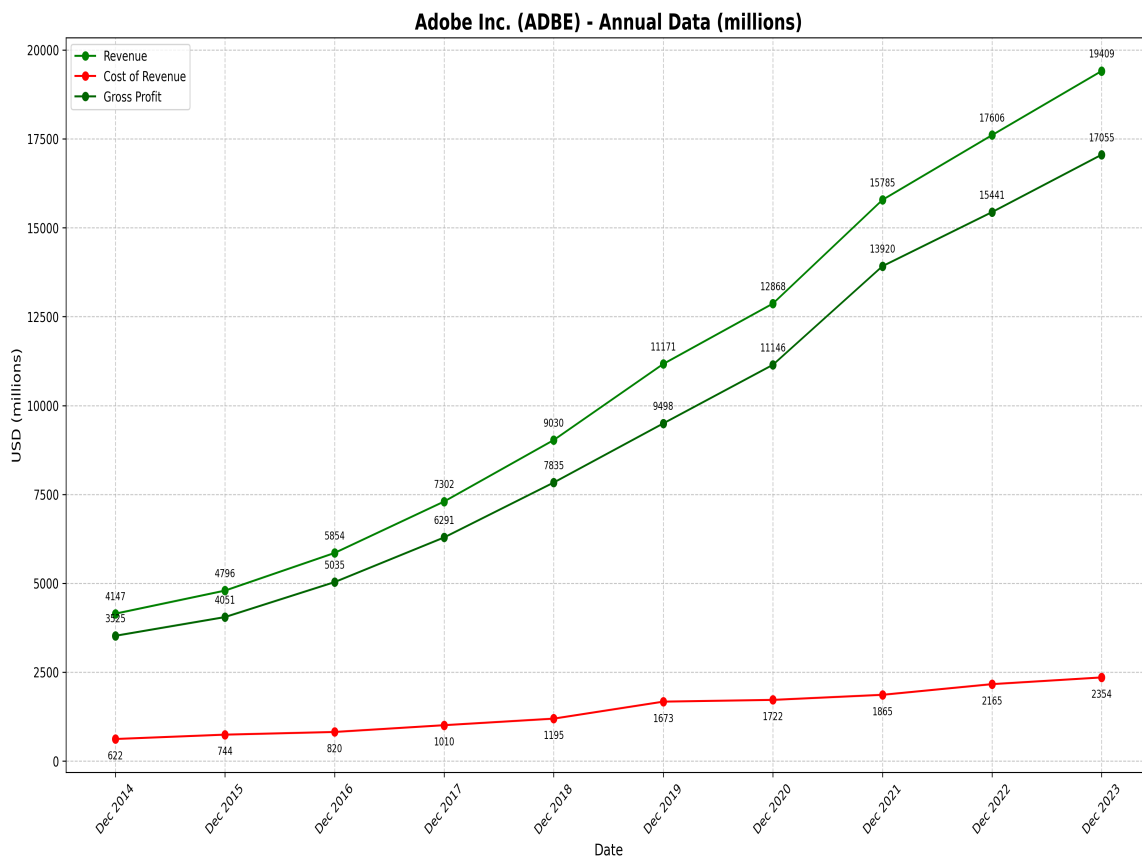
As a result of their strong financial performance, Adobe has a positive outlook for fiscal year 2024. They anticipate continued growth in their ARR, fueled by their expanding customer base and their product innovation efforts. Adobe is also actively pursuing opportunities to further integrate AI into their offerings, which they believe will enhance user experiences and drive future growth. Despite some challenges, Adobe's commitment to innovation, customer engagement, and responsible AI development positions them well for sustained success in the rapidly evolving digital landscape.

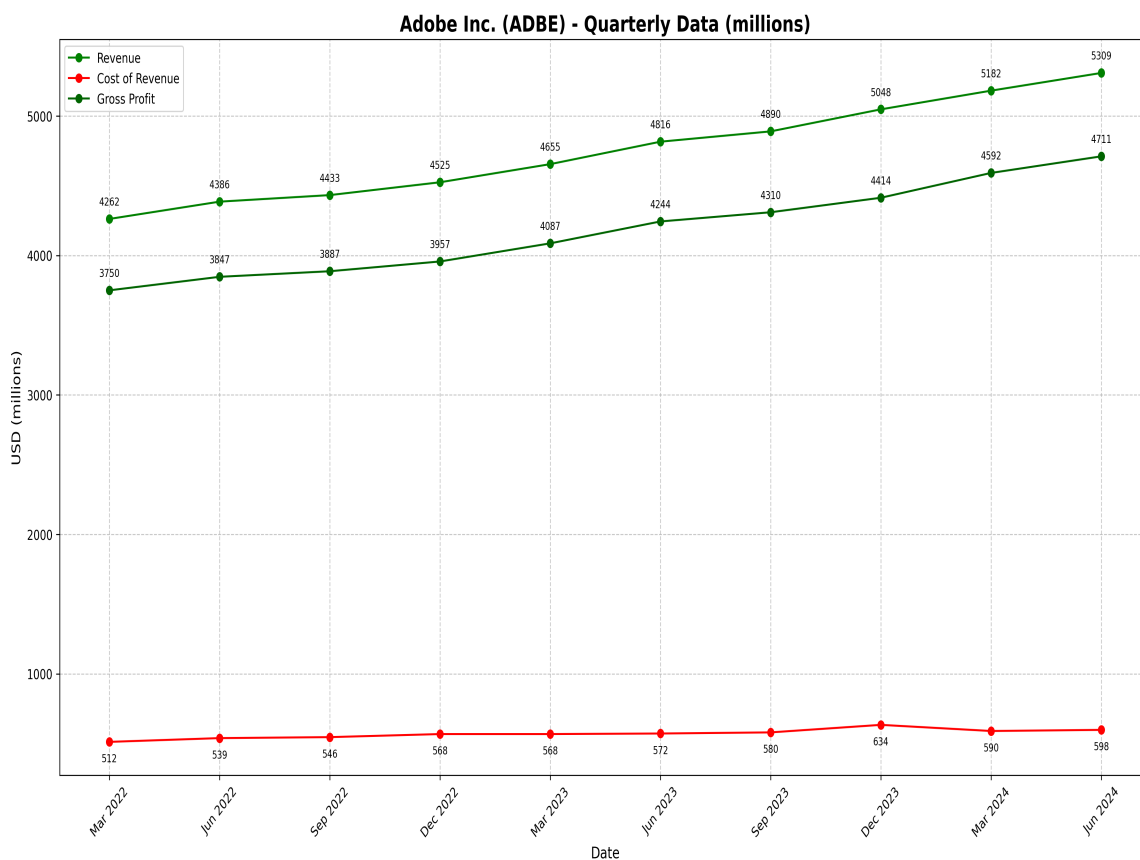
## 2. Financial Analysis

Adobe Inc. has demonstrated remarkable financial strength and a consistent upward trajectory over the past decade. Revenue has more than tripled, driven by the transition to a subscription-based model for its flagship products, Creative Cloud and Document Cloud. This shift has resulted in a more predictable and recurring revenue stream, as evidenced by the steady growth in annual recurring revenue (ARR).

Examining the income statements reveals a consistently high gross profit margin, indicating the strong pricing power of Adobe's products and services. Operating expenses have also increased proportionally with revenue, primarily driven by investments in research and development, sales and marketing, and general and administrative expenses. However, Adobe's operating income has also grown substantially, demonstrating the scalability and efficiency of their operations.

The balance sheets reveal a healthy financial position, with significant cash and short-term investments. Adobe has also utilized stock repurchase programs strategically to enhance shareholder value and minimize dilution. While their total debt has fluctuated over the years, Adobe maintains a manageable debt-to-equity ratio. The cash flow statements showcase strong cash generation from operations. This has enabled Adobe to invest heavily in research and development, make strategic acquisitions, and fund their stock repurchase programs. Adobe's overall financial health reflects its ability to adapt to changing market dynamics, innovate consistently, and maintain its leadership position in the digital media and experience landscape.





## BALANCE SHEET, LAST 10 YEARS

|                 | 2023   | 2022   | 2021   | 2020   | 2019   | 2018      | 2017      | 2016      | 2015      | 2014      |
|-----------------|--------|--------|--------|--------|--------|-----------|-----------|-----------|-----------|-----------|
| Total Assets    | 29,779 | 27,165 | 27,241 | 24,284 | 20,762 | 18,768.68 | 14,535.56 | 12,697.25 | 11,726.47 | 10,785.83 |
| Total Debt      | 4,080  | 4,633  | 4,673  | 4,708  | 4,138  | 4,124.80  | 1,881.42  | 1,892.20  | 1,907.23  | 1,514.32  |
| Shares          | 457    | 470    | 477    | 481    | 486    | 491       | 493.63    | 498.35    | 498.76    | 497.87    |
| EPS             | 11.87  | 10.13  | 10.10  | 10.94  | 6.07   | 5.28      | 3.43      | 2.35      | 1.26      | 0.54      |
| Dividend        | 0      | 0      | 0      | 0      | 0      | 0         | 0         | 0         | 0         | 0         |
| Revenue         | 19,409 | 17,606 | 15,785 | 12,868 | 11,171 | 9,030     | 7,301.51  | 5,854.43  | 4,795.51  | 4,147.06  |
| Cost of Revenue | 2,354  | 2,165  | 1,865  | 1,722  | 1,673  | 1,195     | 1,010.49  | 819.91    | 744.32    | 622.08    |
| Gross Profit    | 17,055 | 15,441 | 13,920 | 11,146 | 9,498  | 7,835     | 6,291.01  | 5,034.52  | 4,051.19  | 3,524.99  |
| EBIT            | 6,912  | 6,120  | 5,818  | 4,292  | 3,362  | 2,883     | 2,212.04  | 1,505.58  | 937.97    | 421.11    |

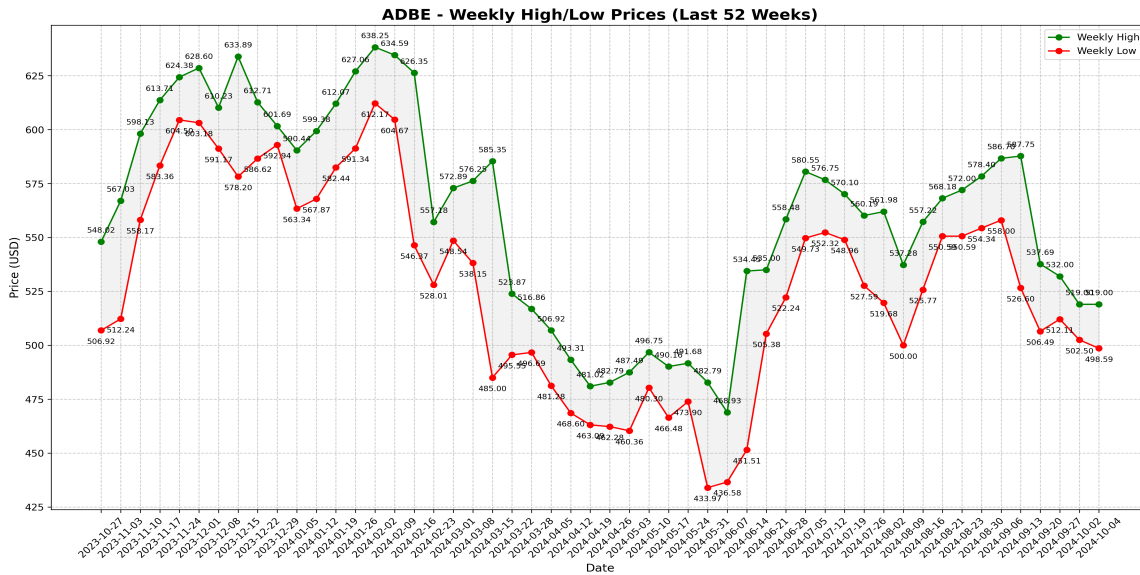
(\* millions, except EPS and dividend)

## BALANCE SHEET, LAST 10 QUARTERS

|                 | 2024 Q2 | 2024 Q1 | 2023 Q4 | 2023 Q3 | 2023 Q2 | 2023 Q1 | 2022 Q4 | 2022 Q3 | 2022 Q2 | 2022 Q1 |
|-----------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Total Assets    | 30,007  | 28,751  | 29,779  | 29,090  | 27,838  | 26,667  | 27,165  | 26,744  | 26,326  | 25,976  |
| Total Debt      | 6,090   | 4,086   | 4,080   | 4,096   | 4,113   | 4,126   | 4,633   | 4,641   | 4,658   | 4,665   |
| Shares          | 449     | 453     | 454     | 456     | 458     | 459     | 467     | 469     | 472     | 473     |
| EPS             | 3.50    | 1.37    | 3.25    | 3.07    | 2.83    | 2.72    | 2.53    | 2.42    | 2.50    | 2.68    |
| Dividend        | 0       | 0       | 0       | 0       | 0       | 0       | 0       | 0       | 0       | 0       |
| Revenue         | 5,309   | 5,182   | 5,048   | 4,890   | 4,816   | 4,655   | 4,525   | 4,433   | 4,386   | 4,262   |
| Cost of Revenue | 598     | 590     | 634     | 580     | 572     | 568     | 568     | 546     | 539     | 512     |
| Gross Profit    | 4,711   | 4,592   | 4,414   | 4,310   | 4,244   | 4,087   | 3,957   | 3,887   | 3,847   | 3,750   |
| EBIT            | 1,971   | 995     | 1,836   | 1,770   | 1,676   | 1,630   | 1,545   | 1,484   | 1,520   | 1,571   |

(\* millions, except EPS and dividend)

### 3. Stock Technical Analysis



Over the past 52 weeks, Adobe Inc.'s (ADBE) stock price has exhibited volatility, influenced by various factors including market sentiment, macroeconomic trends, and company-specific news. The stock initially experienced an upward trend, reaching a peak in mid-November 2023, before undergoing a correction. This decline was partially attributed to investor concerns about the potential impact of AI on Adobe's core business and the FTC's investigation into the company's subscription practices.

Following this pullback, ADBE entered a consolidation phase, trading within a defined range for several months. The stock found support around \$460-480 and faced resistance around \$560-580. This period of sideways movement suggests a period of uncertainty and indecision among investors.

However, the stock price surged significantly in mid-June 2024 following the company's Q2 earnings release. This strong performance was driven by better-than-expected financial results and optimistic management commentary about Adobe's AI strategy. The stock broke through its previous resistance level and established a new high, indicating a shift in investor sentiment towards greater optimism. Despite the recent rally, ADBE remains susceptible to market volatility. Investors will be closely watching the company's future performance, its ability to monetize its AI offerings, and the outcome of the FTC investigation.

## 4. Current Media Coverage & Stories

Adobe Inc. has recently been featured in the news for a variety of reasons, highlighting both its innovation in the creative software space and the challenges it faces in a rapidly evolving market. The company's AI-powered tools, particularly Adobe Firefly, have garnered significant attention, with articles praising their user-friendly interface and potential to revolutionize content creation. Adobe's efforts to make these tools commercially safe by training Firefly models on licensed content have also been positively received, addressing concerns about intellectual property rights and ethical AI development.

However, Adobe's foray into generative AI has also sparked concerns about competition from rivals such as Canva and CapCut, which are also investing heavily in AI-powered features. Articles have pointed out the rising popularity of these platforms, particularly among younger creators, suggesting a potential threat to Adobe's market share.

Adobe's acquisition of Figma, a popular collaborative design platform, has been a subject of much discussion. Initially announced in 2022, the proposed \$20 billion deal faced regulatory scrutiny and was ultimately terminated in December 2023. The news cycle covered the various aspects of this acquisition, from its potential to strengthen Adobe's position in the design software market to concerns about its impact on competition. The hefty \$1 billion termination fee paid to Figma also made headlines.

Beyond AI and acquisitions, Adobe has been in the news for legal issues related to subscription cancellation practices. The FTC's lawsuit against the company for allegedly making it too difficult to cancel subscriptions has drawn negative attention, highlighting the need for more transparent and consumer-friendly policies. Additionally, Adobe has faced securities class action lawsuits and shareholder derivative actions alleging that the company made misleading statements about competition from Figma. These legal issues underscore the risks and challenges Adobe faces in a highly competitive market and the importance of maintaining a strong ethical and legal foundation.

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## 5. Financial vs. Stock vs. Media Coverage Situations

The media headlines regarding Adobe Inc. paint a mixed picture, reflecting the company's simultaneous efforts to push the boundaries of creative software with AI while grappling with competitive pressures and regulatory scrutiny. The positive narrative surrounding Adobe Firefly and its potential to empower creators aligns with the company's strong financial performance and the recent surge in its stock price. This suggests that investors are optimistic about Adobe's ability to successfully integrate AI into its offerings and capitalize on the growing demand for generative AI tools.

However, the headlines also highlight the competitive threat from platforms like Canva and CapCut, which are actively targeting younger creators and leveraging AI to offer similar functionalities. This narrative challenges the assumption that Adobe's dominance in the creative software space is unassailable, reminding investors of the need to monitor market share trends and the emergence of new competitors.

The termination of the Figma acquisition reflects the complex regulatory landscape Adobe navigates. While the deal could have potentially strengthened Adobe's position in the collaborative design market, it faced regulatory pushback over concerns about reduced competition. This narrative demonstrates the potential for regulatory actions to disrupt strategic initiatives and impact Adobe's future growth prospects.

The FTC lawsuit and the securities class action lawsuits present a negative narrative, raising questions about Adobe's business practices and their potential financial and reputational consequences. These legal challenges highlight the importance of ethical considerations, transparency, and responsible business conduct for maintaining a positive brand image and investor confidence. Overall, the contrasting narratives surrounding Adobe reveal a company at a critical juncture, navigating the opportunities and challenges presented by technological advancements, competitive pressures, and evolving regulatory frameworks.



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## 6. Industry Analysis

The creative software industry is experiencing a period of dynamic growth and transformation, driven by the increasing demand for digital content, the proliferation of creative tools, and the rapid advancements in AI and generative AI. Adobe Inc., as a long-standing leader in this space, is well-positioned to capitalize on these trends but also faces challenges from both established competitors and emerging startups.

Key drivers for the industry include the rise of social media marketing, the growing popularity of video content, and the increasing need for businesses to create engaging and personalized digital experiences. The emergence of AI and generative AI is further accelerating these trends, empowering creators with new tools and workflows for producing high-quality content more efficiently. This has led to a surge in investment and innovation, with companies vying to offer the most advanced and user-friendly AI-powered features.

Adobe faces competition from a range of companies, each targeting different segments of the creative market. Canva, with its user-friendly interface and extensive template library, has gained significant traction among novice creators and small businesses. CapCut, backed by ByteDance, is making inroads with its mobile-first video editing tools, particularly appealing to younger creators familiar with TikTok's editing style. Other established players like Microsoft and Google are also expanding their creative software offerings, leveraging their cloud infrastructure and AI capabilities to compete with Adobe.

The regulatory landscape is also evolving rapidly, with governments increasingly focused on data privacy, security, and responsible AI development. This presents both opportunities and challenges for the industry, requiring companies to navigate complex compliance requirements while also ensuring that their AI offerings are ethically sound and commercially safe. Overall, the creative software industry is characterized by intense competition, rapid innovation, and a dynamic regulatory environment. Adobe's ability to adapt to these changes, leverage its strengths in AI and generative AI, and maintain its brand reputation will be crucial for its continued success in this evolving landscape.

## 7. Drivers & Challenges

Adobe Inc. faces a confluence of drivers and challenges that will shape its future trajectory. The most prominent driver is the rapid advancements in AI and generative AI, which are revolutionizing the creative software landscape. Adobe is well-positioned to capitalize on this trend, having already integrated AI-powered features into its flagship products and launched innovative offerings like Adobe Firefly. The increasing demand for generative AI tools, particularly for content creation and marketing, presents a significant growth opportunity for Adobe.

Another driver is the continued shift towards cloud-based subscription models. This transition has provided Adobe with a more predictable and recurring revenue stream, enabling them to invest heavily in research and development and strategic acquisitions. The growing adoption of cloud computing across various industries further strengthens this trend.

The increasing need for businesses to deliver personalized digital experiences is also a major driver for Adobe. The company's Digital Experience segment, powered by Adobe Experience Cloud, is designed to help businesses manage, analyze, and personalize customer journeys. This segment is expected to grow significantly as businesses prioritize digital transformation and seek to enhance customer engagement.

However, Adobe also faces several challenges. The competitive landscape is intensifying, with rivals like Canva and CapCut actively targeting different segments of the creative market. The emergence of new AI-powered creative tools also poses a potential threat to Adobe's market share. Adobe will need to continue innovating and differentiating its offerings to maintain its leadership position.

Regulatory scrutiny is another challenge. The FTC lawsuit and the securities class action lawsuits highlight the risks associated with data privacy, security, and compliance with evolving legal frameworks. Adobe will need to navigate this landscape carefully to mitigate potential financial and reputational consequences.

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## 8. Bull Case

The bull case for Adobe Inc. rests on its ability to leverage its strengths in AI and generative AI to expand its customer base, enhance its product offerings, and capitalize on the growing demand for digital content and experiences. Adobe's early investments in AI research and development have already yielded tangible results, with AI-powered features integrated into its flagship products and innovative offerings like Adobe Firefly gaining traction in the market. The company's deep understanding of creative workflows, combined with its vast repository of licensed content, enables it to develop generative AI tools that are both commercially safe and user-friendly.

The increasing demand for generative AI tools across various industries, including marketing, advertising, and entertainment, is a major tailwind for Adobe. The company's position as a leading provider of creative software, coupled with its strong brand recognition and established customer base, provides it with a significant competitive advantage. As businesses and individuals seek to leverage generative AI to enhance their creativity and productivity, Adobe is well-positioned to capture a substantial share of this growing market.

Adobe's successful transition to a cloud-based subscription model has also created a strong foundation for future growth. The recurring revenue stream generated by Creative Cloud, Document Cloud, and Adobe Experience Cloud provides the company with financial stability and enables it to invest aggressively in innovation and strategic acquisitions. The increasing adoption of cloud computing across various industries further strengthens this trend, providing a favorable backdrop for Adobe's continued expansion.

The bull case for Adobe is further supported by its strong financial performance, its track record of consistent innovation, and its commitment to responsible AI development. As the company continues to invest in emerging technologies, expand its product portfolio, and strengthen its relationships with customers and partners, it is well-positioned to maintain its leadership position in the creative software industry and deliver strong shareholder returns.

## 9. Bear Case

The bear case for Adobe Inc. revolves around concerns about intensifying competition, the potential for AI to disrupt its core business, and the lingering impact of regulatory scrutiny. While Adobe remains a dominant force in the creative software industry, rivals like Canva and CapCut are rapidly gaining market share by offering similar functionalities at lower prices or targeting niche segments more effectively. The emergence of new AI-powered creative tools further intensifies this competition, putting pressure on Adobe to differentiate its offerings and demonstrate the value proposition of its AI capabilities.

The rapid advancements in AI, while presenting growth opportunities, also pose a potential threat to Adobe's core business. The widespread availability of free or low-cost AI tools could lead to commodification of certain creative functionalities, eroding Adobe's pricing power and reducing the perceived value of its premium products. The company's ability to successfully monetize its AI offerings and maintain a clear competitive advantage in this evolving landscape remains a key uncertainty for investors.

The ongoing FTC investigation into Adobe's subscription cancellation practices and the securities class action lawsuits alleging misleading statements about competition from Figma cast a shadow over the company's future prospects. These legal challenges could result in significant financial penalties, damage Adobe's brand reputation, and divert management's attention and resources away from core business initiatives.

The bear case for Adobe is further fueled by concerns about the company's ability to retain key talent in a highly competitive market for AI and cybersecurity expertise. The increasing adoption of hybrid or remote working arrangements may also pose challenges to maintaining a cohesive and innovative workplace culture. In addition, Adobe's reliance on third-party service providers for critical aspects of its operations introduces vulnerabilities, as evidenced by the potential disruptions from cyberattacks and data breaches. The bear case for Adobe suggests that the company faces significant headwinds, and its ability to navigate these challenges and maintain its growth trajectory is far from certain.

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## 10. Forward Valuation

Adobe Inc.'s forward valuation incorporates various financial, stock market, and media insights, as well as our in-depth analysis, to provide a range of potential outcomes for the company's stock price. We employ four distinct valuation methods: discounted cash flow (DCF), relative valuation, sum-of-the-parts (SOTP), and option pricing models, each offering unique perspectives on Adobe's intrinsic value.

The DCF model projects future cash flows based on revenue growth assumptions, profitability margins, and capital expenditures. Our bullish scenario assumes continued strong growth in subscription revenue, driven by AI innovation and expanding market penetration. We also factor in the positive impact of Adobe's cloud transition and its commitment to research and development. The bearish scenario incorporates more conservative growth estimates, reflecting concerns about intensifying competition and the potential for AI to disrupt Adobe's core business.

Relative valuation utilizes multiples based on comparable companies in the creative software industry. We consider revenue multiples, earnings multiples, and enterprise value multiples to determine a range of potential valuations. The bullish scenario reflects Adobe's strong market position, its consistent profitability, and its growth prospects in the generative AI market. The bearish scenario incorporates lower multiples, reflecting concerns about competition and potential risks associated with regulatory scrutiny.

SOTP valuation analyzes Adobe's individual business segments separately, such as Digital Media, Digital Experience, and Publishing and Advertising, assigning separate valuations based on their specific growth prospects, profitability, and competitive dynamics. Our bullish scenario assumes strong performance across all segments, driven by AI innovation, cloud adoption, and the increasing demand for personalized digital experiences. The bearish scenario incorporates more conservative growth estimates for certain segments, reflecting potential challenges from competition and the uncertain monetization pathways for AI offerings.

Option pricing models utilize option market data to infer a range of potential outcomes for Adobe's stock price. This method considers the implied volatility of options, the time to expiration, and the risk-free interest rate to determine a probability distribution of future stock prices. Our bullish scenario reflects a high probability of positive outcomes, driven by optimism about Adobe's AI strategy and its long-term growth prospects. The bearish scenario incorporates a wider range of potential outcomes, reflecting uncertainty about competition, regulatory scrutiny, and the overall market volatility.

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## 11. Executive Summary

Adobe Inc. is strategically positioned at the forefront of the dynamic and rapidly evolving creative software industry, driven by the increasing demand for digital content and the transformative power of AI. The company's strengths lie in its industry-leading products, its successful transition to a cloud-based subscription model, and its commitment to innovation in AI and generative AI.

The company faces significant opportunities in leveraging AI and generative AI to expand its customer base, enhance its product offerings, and capture a substantial share of the growing market for creative tools. Adobe Firefly, its family of creative generative AI models, is already gaining traction, demonstrating the company's ability to develop user-friendly and commercially safe AI tools. The increasing need for businesses to deliver personalized digital experiences also presents a significant growth opportunity for Adobe Experience Cloud, which empowers businesses to manage, analyze, and personalize customer journeys.

However, Adobe also faces challenges from intensifying competition, the potential for AI to disrupt its core business, and the lingering impact of regulatory scrutiny. Rivals like Canva and CapCut are actively targeting different segments of the creative market, while the emergence of new AI-powered creative tools could erode Adobe's pricing power and market share. The FTC lawsuit and the securities class action lawsuits highlight the risks associated with data privacy, security, and compliance with evolving legal frameworks. Adobe's ability to navigate these challenges effectively will be crucial for its continued success.

Adobe's financial performance in fiscal year 2023 reflects its strength and resilience, with strong revenue growth driven by its subscription offerings and strategic investments in AI. The company's outlook for fiscal year 2024 remains positive, with anticipated continued growth in ARR and its expanding customer base. However, the company's ability to effectively monetize its AI offerings, differentiate itself from competitors, and mitigate the impact of regulatory scrutiny will be critical for delivering sustained growth and shareholder returns.

Overall, Adobe's future trajectory will be determined by its ability to successfully navigate a complex and dynamic landscape characterized by rapid technological advancements, evolving customer preferences, and intensifying competition. The company's commitment to innovation, its strong financial position, and its established market leadership provide a solid foundation for future growth, but its ability to effectively address the challenges ahead will ultimately shape its long-term success.