



RESEARCH & STRATEGY

Industry Initiation:

Security Software

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Security Software – Summary Metrics & Valuations



\$'s in millions (except per share)

Company	Ticker	Analyst	Rating	25-Mar	% Chng	% Chng	Market	Ent	Revenue		Rev Growth		EV/Revs		EV/FCF	
				Price	YTD	52 Wk			Cap	Value	2020	2021	2020	2021	2020	2021
Security Software																
Check Point Software Technologies Ltd.	CHKP	Gray	Buy	\$93.86	-17%	-27%	\$13,901	\$9,952	\$2,006	\$2,081	0.6%	3.7%	5.0x	4.8x	9.8x	9.3x
Cloudflare Inc Class A	NET	Gray	Neutral	\$21.66	31%	NA	\$7,165	\$6,528	\$391	\$497	36.2%	27.0%	16.7x	13.1x	NMF	NMF
CrowdStrike Holdings, Inc. Class A	CRWD	Gray	Buy	\$55.78	15%	NA	\$13,363	\$12,529	\$709	\$931	53.5%	31.4%	17.7x	13.5x	NMF	NMF
CyberArk Software Ltd.	CYBR	NA	NR	\$90.09	-25%	-23%	\$3,527	\$2,523	\$434	\$516	26.4%	18.8%	5.8x	4.9x	25.8x	15.0x
FireEye, Inc.	FEYE	NA	NR	\$11.43	-34%	-34%	\$2,801	\$2,772	\$935	\$999	5.1%	6.9%	3.0x	2.8x	66.5x	37.3x
Fortinet, Inc.	FTNT	Gray	Neutral	\$96.94	-7%	17%	\$16,984	\$14,792	\$2,525	\$2,918	17.1%	15.5%	5.9x	5.1x	21.7x	16.6x
Mimecast Limited	MIME	NA	NR	\$33.77	-22%	-25%	\$2,178	\$1,995	\$486	\$581	19.9%	19.6%	4.1x	3.4x	27.8x	18.7x
NortonLifeLock Inc.	NLOK	NA	NR	\$17.89	15%	30%	\$12,560	\$10,592	\$2,471	\$2,521	2.5%	2.0%	4.3x	4.2x	14.0x	12.5x
Okta, Inc. Class A	OKTA	Gray	Buy	\$117.77	7%	53%	\$16,177	\$15,954	\$777	\$1,010	32.6%	30.0%	20.5x	15.8x	NMF	NMF
OneSpan Inc.	OSPN	Gray	Neutral	\$15.54	-7%	-15%	\$638	\$528	\$259	\$286	1.7%	10.5%	2.0x	1.8x	NMF	NMF
Palo Alto Networks, Inc.	PANW	Gray	Neutral	\$166.01	-30%	-34%	\$16,784	\$14,793	\$3,626	\$4,323	16.2%	19.2%	4.1x	3.4x	14.3x	11.7x
Ping Identity Holding Corp.	PING	Gray	Buy	\$19.48	-18%	NA	\$1,580	\$1,564	\$268	\$307	10.3%	14.7%	5.8x	5.1x	NMF	180.6x
Proofpoint, Inc.	PFPT	Gray	Buy	\$99.81	-8%	-12%	\$6,498	\$6,527	\$1,060	\$1,255	19.4%	18.3%	6.2x	5.2x	36.5x	21.6x
Qualys, Inc.	QLYS	NA	NR	\$80.88	-2%	-1%	\$3,380	\$3,081	\$365	\$419	13.6%	14.8%	8.4x	7.4x	21.6x	18.8x
Rapid7 Inc.	RPD	NA	NR	\$42.37	-26%	-16%	\$2,573	\$2,518	\$399	\$483	22.1%	21.0%	6.3x	5.2x	NMF	264.8x
SailPoint Technologies Holdings, Inc.	SAIL	NA	NR	\$16.11	-27%	-41%	\$1,485	\$1,344	\$317	\$360	9.9%	13.5%	4.2x	3.7x	63.2x	29.7x
Tenable Holdings, Inc.	TENB	NA	NR	\$21.70	-16%	-34%	\$2,391	\$2,179	\$438	\$521	23.4%	19.0%	5.0x	4.2x	NMF	44.3x
Zscaler, Inc.	ZS	Gray	Neutral	\$59.13	34%	-6%	\$8,217	\$7,832	\$472	\$608	31.1%	28.9%	16.6x	12.9x	NMF	NMF
Mean					-8%	-11%	\$7,345	\$6,556	\$997	\$1,145	19.0%	17.5%	7.9x	6.5x	30.1x	52.4x
Median					-12%	-16%	\$5,012	\$4,804	\$479	\$595	18.2%	18.6%	5.8x	5.0x	23.8x	18.8x
NASDAQ Composite	COMP			\$7,384	-17%	-3%		\$8,026	3,005	3,231	6.7%	7.5%	2.7x	2.5x	20.1x	16.9x
S&P 500	SP50			\$2,476	-24%	-13%		\$3,176	1,441	1,516	4.0%	5.2%	2.2x	2.1x	17.1x	14.5x

Note: COMP and SP50 Indices reflect Price to FCF Multiples which should approximate EV/FCF given that they have positive net debt.

Source: BTIG Research Estimates, FactSet and company reports

- The security software space has historically traded at **just over 6.0x NTM EV/sales** but was dominated by license hardware models with attached subscriptions.
- An equivalent pure play SaaS model would be worth closer to **8.5x NTM EV/sales**

Source: Company Filings

Summary of Estimates – BTIG vs Street

\$'s in millions (except per share)



Company	Key Metric	CY 2020			CY 2021		
		BTIG	Street	% Diff	BTIG	Street	% Diff
Buy Rated Stocks							
CRWD (1,2)	ARR	\$832	\$837	-0.6%	\$1,105	\$1,073	3.0%
	Revenue	\$728	\$730	-0.2%	\$979	\$950	3.1%
OKTA (1)	Billings	\$920	\$920	0.0%	\$1,177	\$1,160	1.5%
	Revenue	\$777	\$775	0.3%	\$1,010	\$1,005	0.5%
PING	ARR	\$266	\$266	0.0%	\$313	\$311	0.6%
	Revenue	\$268	\$269	-0.2%	\$307	\$317	-3.0%
PFPT	Billings	\$1,257	\$1,270	-1.1%	\$1,470	\$1,494	-1.6%
	Revenue	\$1,060	\$1,063	-0.3%	\$1,255	\$1,261	-0.5%
CHKP	Billings	\$2,014	\$2,118	-4.9%	\$2,121	\$2,174	-2.5%
	Revenue	\$2,006	\$2,043	-1.8%	\$2,081	\$2,111	-1.4%
	FCF	\$1,012	\$1,044	-3.1%	\$1,070	\$1,068	0.1%
Neutral Rated Stocks							
FTNT	Billings	\$3,025	\$3,056	-1.0%	\$3,449	\$3,487	-1.1%
	Revenue	\$2,525	\$2,527	-0.1%	\$2,918	\$2,921	-0.1%
	FCF	\$681	\$724	-5.9%	\$890	\$1,030	-13.6%
NET	Billings	\$387	\$403	-4.0%	\$503	\$527	-4.6%
	Revenue	\$391	\$391	0.0%	\$497	\$512	-3.1%
OSPN	Revenue	\$258	\$259	-0.3%	\$288	\$286	0.7%
	EBITDA	\$26	\$27	-3.4%	\$39	\$36	9.0%
		July 2020 Year End			July 2021 Year End		
PANW (3)	Billings	\$4,077	\$4,104	-0.7%	\$4,810	\$4,862	-1.1%
	Revenue	\$3,352	\$3,363	-0.3%	\$3,985	\$4,010	-0.6%
	FCF	\$770	\$868	-11.3%	\$1,157	\$1,191	-2.8%
ZS	Billings	\$515	\$514	0.2%	\$649	\$640	1.5%
	Revenue	\$416	\$416	-0.1%	\$536	\$539	-0.6%

Note: (1) OKTA and CRWD run FY end Jan. CY 2020 = FY 2021

(2) CRWD street Jan 21 and Jan 22 ARR excludes one outlier at \$960MM and \$1,340MM respectively.

(3) PANW - We model \$770MM reported FCF and \$922.4MM normalized for FY20. Street ests appear to be a mix of normalized and reported FCF.

Source: BTIG, FactSet

How We Differentiate Our Research



Primary Focus = INDEPENDENT FIELDWORK

- Every company looks good on PowerPoint. So....
- We focus on channel partners, consultants and customers

As Part of This Sector Launch, We Held Discussions With:

- 8 Channel Partners – Visibility on ~\$7B in Security Spending
- 7 CISO / customer contacts – skewed towards companies with 10,000+ employees

Most Positive Commentary

- OKTA, PING and CRWD

Most Cautious Commentary

- PANW

Source: Company Filings

Key Themes and Points of Discussion



Our Thoughts on the COVID-19 Outbreak and Impact to Security Software

- Security is not discretionary but budgets can shift
- Technologies enabling remote workforce clearly a big theme – OKTA, PING, ZS, CRWD, NET
- Favor recurring revenue models and large enterprise exposure
- Cheap defensive stocks – CHKP
- Cautious on license and hardware models
- **TOP IDEAS = CRWD, OKTA, PING**

Shift to Cloud Driving Adoption of Zero Trust Architectures

- Key technologies to benefit are identity, secure access service edge (SASE) and endpoint

Perimeter Security and Appliance Models Likely Face Pressure as Cloud Adoption Grows

- We are cautious on the firewall space – PANW, FTNT and CHKP.

Platform Plays vs Best in Class Products? We Favor Best in Class

- CRWD and OKTA are dominating their target markets

Microsoft Can No Longer Be Ignored in the Security Space

- We are not seeing any major changes in competitive trend lines. But MSFT is clearly more focused on security today than ever before

COVID-19 – Analysis of Downward Sales Revision in the 2008 - 2009 Recession



	Reference Year	7/30/08		% Diff	Impact to Growth Outlook		
		Rev Est	Rev Act		Orig Est Yr./Yr.	Act Yr./Yr.	Abs Diff
Large Cap Established Software							
MSFT	Jun '09	\$67,400	\$58,400	-13.4%	11.6%	-3.3%	-14.9%
ORCL	May '09	\$26,100	\$23,200	-11.1%	16.4%	3.4%	-12.9%
High Growth Software							
CRM	Jan '10	\$1,409	\$1,306	-7.3%	30.8%	21.2%	-9.6%
VMW	Dec '09	\$2,446	\$2,024	-17.3%	30.0%	7.6%	-22.4%
Hardware - Network Equipment							
CSCO	Jul '09	\$43,800	\$36,100	-17.6%	10.8%	-8.7%	-19.5%
CDN							
AKAM	Dec '09	\$950	\$860	-9.5%	20.1%	8.7%	-11.4%
Security							
CHKP (1)	Dec '09	\$865	\$824	-4.7%	7.1%	2.0%	-5.1%
SYMC (now NLOK)	Mar '10	\$6,851	\$5,985	-12.6%	11.4%	-2.7%	-14.1%
Mean				-11.7%			-13.7%
Median				-11.9%			-13.5%
Nasdaq Composite							
Sales / Share	Dec '09	\$1,399	\$1,182	-15.5%	18.1%	-0.2%	-18.3%
EPS	Dec '09	\$152.73	\$94.13	-38.4%	NA	NA	NA

Note: (1) CHKP 2009 revenue = \$924MM and included \$100MM from the acquisition of Nokia's security business which closed in April 2009.

Source: BTIG, FactSet

Key Insights

- Everyone in software missed estimates during the last downturn – even large established players.
- Hardware centric companies fared the worst. CSCO missed revs by 18%
- High growth recurring models (CRM) fared much better than high growth license (VMW).
- Security companies performed slightly better than average.
 - CHKP only missed by 5%.
 - SYMC was not a pure play

COVID-19 – Assessing Risk – Favor Recurring Models & Enterprise Exposure



Rank Ordering Security Software Risk Profiles

	Business Model / Segment Exposure	Companies
Lowest Risk	Cloud / SaaS Model / Large Enterprise	ZS, CRWD, PFPT
	Cloud / SaaS Model / Mid Market	OKTA
	Hybrid (Term License / SaaS) / Larger Enterprise	PING
	SaaS Model / SMB Exposure	NET
	License Hardware / Large Enterprise	CHKP, PANW, OSPN
Highest Risk	License Hardware / Mid Enterprise	FTNT

Source: BTIG

Source: Company Filings

Shift to Cloud Driving Adoption of Zero Trust Architectures



In the Legacy Security World

- All applications resided inside the corporate data center on physical servers that were owned by the customer
- The network perimeter was protected by appliances – firewalls, web gateways, IPS / IDS, Sandboxes etc
- Internal traffic was deemed to be “safe” after passing inspection of perimeter security

Today’s World – Cloud Breaks the Legacy Model – Drives Zero Trust

- Applications in 3rd party data centers on someone else’s infrastructure
- Can NOT be protected by perimeter technology
- Zero Trust is important – i.e., do not trust anything until you identify the user and the application

Key Technologies Required = Identity, Secure Access Edge (CASB / Cloud Proxy), and Endpoint.

Source: Company Filings

Perimeter Security and Appliance Models Under Pressure



Firewall Product Revenue Growth is Decelerating

Street Estimates Are Probably Too High In 2020 And 2021

\$'s in millions

	CY2013	CY2014	CY2015	CY2016A	CY2017A	CY2018A	CY2019A	CY2020E	CY2021E
<u>Product Revenue</u>									
PANW	282.6	400.9	593.2	686.0	764.7	996.0	1,062.0	1,084.0	1,169.0
CHKP	496.9	520.3	555.8	573.0	559.0	526.0	511.0	491.0	478.0
FTNT	<u>278.0</u>	<u>360.6</u>	<u>476.8</u>	<u>548.1</u>	<u>577.2</u>	<u>674.4</u>	<u>788.5</u>	<u>892.0</u>	<u>984.0</u>
Total Public Firewall Vendors	1,057.5	1,281.8	1,625.7	1,807.1	1,900.9	2,196.4	2,361.5	2,467.0	2,631.0
<u>Reported Yr./Yr. Growth</u>									
PANW	34.3%	41.9%	47.9%	15.7%	11.5%	30.2%	6.6%	2.1%	7.8%
CHKP	-0.1%	4.7%	6.8%	3.1%	-2.4%	-5.9%	-2.9%	-3.9%	-2.6%
FTNT	<u>11.7%</u>	<u>29.7%</u>	<u>32.2%</u>	<u>15.0%</u>	<u>5.3%</u>	<u>16.8%</u>	<u>16.9%</u>	<u>13.1%</u>	<u>10.3%</u>
Total Public Firewall Vendors	10.5%	21.2%	26.8%	11.2%	5.2%	15.5%	7.5%	4.5%	6.6%
<u>Acquisition / One Time Contribution</u>									
PANW	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CHKP	0.0	0.0	0.0	(35.0)	0.0	0.0	0.0	0.0	0.0
FTNT	<u>0.0</u>	<u>0.0</u>	<u>22.0</u>	<u>28.0</u>	<u>0.0</u>	<u>19.5</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>
Total Public Firewall Vendors	0.0	0.0	22.0	(7.0)	0.0	19.5	0.0	0.0	0.0
<u>Organic Yr./Yr. Growth - Product</u>									
PANW	34.3%	41.9%	47.9%	15.7%	11.5%	30.2%	6.6%	2.1%	7.8%
CHKP	-0.1%	4.7%	6.8%	9.4%	-2.4%	-5.9%	-2.9%	-3.9%	-2.6%
FTNT	<u>11.7%</u>	<u>29.7%</u>	<u>26.1%</u>	<u>9.1%</u>	<u>5.3%</u>	<u>13.5%</u>	<u>16.9%</u>	<u>13.1%</u>	<u>10.3%</u>
Total Public Firewall Vendors	10.5%	21.2%	25.1%	11.6%	5.2%	14.5%	7.5%	4.5%	6.6%

Note: FTNT figures reflect Meru acquisition impact late 2015 / 2016 and ASC 606 in 2018 .

CHKP figures reflect change in accounting / deferral of product revenue with new ATP bundles.

Source: FactSet Research and BTIG

We Favor Best in Class Stories Over Platform Plays

What Winning Looks Like in Security Software



\$'s in millions

Past Best in Class Products - Tangential Expansion Stories							
PANW - Dominate Firewall Expand in Network Security							
Fiscal Year	FY'12	FY'13	FY'14	FY'15	FY'16	FY'17	FY'18
Revenue	\$255.0	\$396.1	\$598.2	\$928.0	\$1,379.0	\$1,762.0	\$2,273.0
Yr./Yr. Growth	114.3%	55.3%	51.0%	55.1%	48.6%	27.8%	29.0%
PFPT - Dominate Email - Upsell Advanced Threat Modules							
Calendar Year	2012	2013	2014	2015	2016	2017	2018
Revenue	\$106.0	\$138.0	\$196.0	\$265.0	\$375.0	\$515.0	\$717.0
Yr./Yr. Growth	29.3%	30.2%	42.0%	35.2%	41.5%	37.3%	39.2%
New Best in Class Products - Tangential Expansion Stories							
CRWD - Dominating Endpoint - VM and IT Ops are Natural Adjacencies							
Fiscal Year	FY'17	FY'18	FY'19	FY'20	FY'21E	FY'22E	FY'23E
Revenue	\$52.7	\$118.8	\$249.8	\$481.4	TBD	TBD	TBD
Yr./Yr. Growth	-55.7%	125.1%	110.4%	92.7%	TBD	TBD	TBD
OKTA - Dominating Workforce Identity - Expanding Customer Identity, PAM, and Governance							
Fiscal Year	FY'16	FY'17	FY'18	FY'19	FY'20	FY'21E	FY'22E
Revenue	\$85.9	\$160.8	\$256.5	\$399.3	\$586.1	TBD	TBD
Yr./Yr. Growth	109.5%	87.2%	59.5%	55.7%	46.8%	TBD	TBD
ZS - Dominating SWG. VPN, DLP and CASB Natural Extension. Broader Firewall Use Case TBD							
Fiscal Year	FY'16	FY'17	FY'18	FY'19	FY'20E	FY'21E	FY'22E
Revenue	\$80.3	\$125.7	\$190.2	\$302.8	\$416.0	TBD	TBD
Yr./Yr. Growth	50.0%	56.5%	51.3%	59.2%	37.4%	TBD	TBD

Source: BTIG, Company Filings

Microsoft Security Can No Longer Be Ignored



MSFT's scale is unmatched and the company has become more focused on security the last few years.

- Office 365 scans 470 billion emails per month
- MSFT analyzes 6.5 trillion security signals in its cloud per day.
- Over 800 million devices are running Windows 10 where Microsoft Defender is natively installed

Pure Play vs MSFT Security Software R&D Spending

\$'s in millions

Company	R&D Budget	Revenue 2020E
Microsoft	\$1,700	NA
PANW	\$508	\$3,645
FTNT	\$285	\$2,540
CHKP	\$235	\$2,051
PFPT	\$230	\$1,065
OKTA	\$160	\$762
CRWD	\$150	\$665
CYBR	\$84	\$515
MIME	\$80	\$491
Total Security Company's Sampled	\$1,732	\$11,734

Source: BTIG and FactSet

MSFT Gartner Ranking in Key Security Categories

Security Category	Gartner Magic Quadrant Rank
Identity and Access Management	#2
Cloud Access Security Broker	Top 3
Endpoint Protection Platforms	Top 2
Network Firewall	Around 15th
Web Application Firewall	12th or worse
Secure Email Gateway (1)	No recent GMQ Probably top 4 - 5

Note: (1) The last GMQ for SEG was in 2015. Based on our customer discussions, we think MSFT is at least top 5.

Source: Gartner and BTIG

Buy Rated Stocks and Summaries



CRWD – Top Pick

- Dominating core target market - endpoint security. Favorable competitive environment. Natural adjacent markets. Highly confident in growth forecasts

PING

- Story not well understood. Supporting large complex hybrid IT environments is difficult and creates high barrier to entry.

OKTA

- Dominating core workforce identity target market. Natural areas of expansion – customer identity, PAM and governance – create large TAM. Highly confident in growth forecasts.

PFPT

- Good GARP play and favorable risk reward. Growth stabilizing in mid to high teens. Share gains against SYMC a tangible opportunity.

CHKP

- Somewhat of a contrarian call. No turn around insight. But CHKP is defensive and too cheap to ignore.

Source: Company Filings for pages 12 to 23

CrowdStrike – Market Dominating Growth Profile

CRWD, Buy, Price Target: \$67



Market Cap: \$14 Billion

Revenue: FY21E \$728MM FY22E \$979MM

Investment Positives

- **Potentially the best all time growth profile ever seen in the security space.** The closest company to match CRWD's current level of growth at scale was Palo Alto Networks back in 2013.
- **Best in class cloud based endpoint security platform.** CRWD held 6% of its \$7B+ endpoint security target market in 2019 but is taking 30%+ of the market's incremental growth.
- **Very favorable competitive landscape.** Key competitors – SYMC, CBLK, and Cylance have all been acquired and are distracted.
- **Real tangential market opportunities** – Vulnerability management and IT Ops are natural adjacencies
- **Highly confident in growth profile.** 35%+ long term revenue growth seems very reasonable

Investment Risks

- Covid-19 outbreak likely creates some pressure in demand environment
- MSFT a real player in endpoint security
- High investor expectations

Okta – Securing Digital Transformation

OKTA, Buy, Price Target: \$144



Market Cap: \$17 Billion

Revenue: FY21E \$777MM FY22E \$1,010MM

Investment Positives

- **Security budgets shifting towards identity as customer adopts cloud.** Almost every CISO contact we have spoken with this year cited identity as a top two spending priority and a critical choke point for any customer adopting cloud architectures.
- **Dominating its core identity target market.** OKTA held about 10% share of its core \$6B target market in 2019 but won 35% of the market's incremental growth.
- **Customer identity is clear and natural expansion area** from OKTA's core workforce identity solution.
- **OKTA is expanding product sets and TAM** - moving into governance, PAM, and offering on-prem support. TAM could easily expand to \$25B over the next few years.
- **Highly confident in growth forecasts.** OKTA could conceivably grow at a 35% pace through 2024 and still only hold ~10% market share of things it can really do.

Investment Risks

- Competition against MSFT – Identity is a strategic focus area
- COVID-19 demand related risk
- High expectations – OKTA is a beat and raise story. In-line not good enough

Ping Identity – High Barrier to Entry Not Well Understood

PING, Buy, Price Target: \$25



Market Cap: \$1.7B

Revenue: 2020E \$268MM 2021E \$307MM

Investment Positives

- **Security budgets shifting towards identity as network perimeter dissolves.** Almost every CISO contact we have spoken with this year cited identity as a top two spending priority and a critical choke point for any customer adopting cloud architectures.
- **Remote workforce play and large enterprise exposure should provide some cushion against COVID-19 headwinds**
- **Solving complexity in large enterprise environments creates high barrier to entry.** Partners and buyers agree that what PING does is complex and difficult to replicate. MSFT can NOT even do it themselves and is forced to partner with PING to connect on prem.
- **Steadily improving competitive landscape.** Legacy on-prem identity solutions (Oracle, CA, IBM, etc) are stale and partners indicate customers increasingly looking to modernize.
- **Good growth and reasonable price.** Street expecting high teens ARR growth. 20%+ reasonable in upside scenario. Not an expensive stock at 5.x 2020E EV/sales

Investment Risks

- Term license model creates headline revenue volatility
- Less mature SaaS model
- Comparisons to OKTA – which is growing much faster than PING.

Proofpoint Inc. – Stable Growth in a Volatile Market

PFPT, Buy, Price Target: \$125



Market Cap: \$6.6 Billion

Revenue: 2020E \$1,060MM FY2021E \$1,255MM

Investment Positives

- **Best in class cloud based email security provider.** We roughly estimate that PFPT holds about 30% market share in email security.
- **Email is a key threat vector and continues to be a spending priority.** Email is the most common threat vector. 93% of successful breaches start with email. But only 7% of enterprise IT security spending is dedicated to email.
- **Broadcom's acquisition of SYMC creates incremental share gain potential.** We estimate that incremental SYMC churn could create a 10% uplift to PFPT revenue over the next 3 – 4 years.
- **We think growth has stabilized.** We feel confident in PFPT's ability to grow revenue at a mid to high teens pace the next few years.

Investment Risks

- COVID-19 related demand risk
- MSFT email security gradually improving
- Growth decelerated in 2018 and 2019. Less upside to Street estimates the last 18 months.

Source: Company Filings

Checkpoint – A Defensive Play for Volatile Times

CHKP, Buy, Price Target: \$117



Market Cap: \$14 Billion

Revenue: 2020E \$2,006MM FY2021E \$2,081MM

Investment Positives

- **Partner commentary remained cautious but not getting worse (prior to COVID-19).** To be clear - partner commentary has been negative on CHKP the last two years. It did not get incrementally worse in recent discussions.
- **Less volatile growth profile vs peers.** CHKP relies more on refresh of existing customers and is less dependent on winning new logs.
- **FCF profile generally stable even with top line volatility.** CHKP consistently manages to hit EPS and FCF targets even when missing on top line.
- **A lot of negative is already baked in.** Stock trades at ~9.0x 2021E EV/FCF. Lowest in seven years. Hist ave = 12.5x.

Investment Risks

- COVID-19 outbreak likely pressures appliance models
- Migration to cloud places pressure on legacy appliance models and broader firewall space
- Fieldwork negative no turn around in sight
- FCF risk harder to manage as billings growth slows and CHKP potentially invests more in S&M

Source: Company Filings

Neutral Rated Stocks and Summaries



ZS

- Tempting to be more constructive because ZS benefits from the adoption of cloud architectures and facilitates remote workforce solutions. But we see increased competition and growth slowed too early in the company's lifecycle relative to broader market opportunity.

FTNT

- Best growth and execution in the firewall space. Concerns on hardware model – both around COVID-19 and as workloads move to cloud keep us at a Neutral.

NET

- Good cloud security story. But too much SMB exposure. Plus, NET is not the best at any one thing they do.

OSPN

- Cheap stock and compelling long term growth targets during mix shift from hardware to recurring. But 50% of revenue today is hardware and only 30% is recurring. 75%+ of revenue is from Europe and APAC – most susceptible to macro pressure. And growth targets are back end loaded.

PANW – Most Cautious Checks

- Cheap stock but greatest potential risk to forecasts. Company has lost focus on core firewall business. The new growth driver – Next Generation Security – is essentially a bet on multiple acquired assets.

Zscaler – Can Growth Really Reaccelerate?

ZS, Neutral

Market Cap: \$8.2 Billion

Revenue: FY20E \$416MM FY21E \$536MM

Fair Value: \$60



Investment Positives

- **Strong secular drivers – cloud security and digital transformation.** The company's cloud based security platform enables customers to connect directly into SaaS applications and reduce infrastructure costs.
- **Remote workforce play – potentially offsets COVID-19 pressure.** ZS's emerging product – Zscaler Private Access (ZPA) – directly enables remote workforce.
- **Strong position and rapid share gains in core secure web gateway market.** ZS holds about 8% of its target market and is winning a high 20% to low 30% share of incremental growth.
- **Attractive long term growth profile.** ZS should be able to grow at a 25%+ pace the next few years

Investment Risks

- **COVID-19 outbreak likely creates pressure on demand.** Roughly 50% of ZS revenue is from Europe and APAC regions
- **The company's growth profile decelerated too early in its lifecycle.** Normalized billings growth slowed from 57% in FY'19 to 33% yr./yr. in 1H'F20.
- **Competitive alternatives increasingly viable.** Most notably PANW.
- **High investor expectations** – beat raise still required.

Fortinet – Solid Growth in a Challenged Market

FTNT, Neutral



Market Cap: \$18 Billion

Revenue: 2020E \$2,525MM FY21E \$2,918MM

Fair Value: \$99

Investment Positives

- **Gaining better traction with larger enterprise customers**
- **Winning incremental share in network security.** FTNT holds about 9% share in the network security market and is taking almost 15% of the market's growth.
- **SD-WAN is a real supplemental growth opportunity.** FTNT was first to market among firewall vendors with an SD-WAN offering in mid 2018. Helped drive 7% points improvement in product revenue growth in 2019 (i.e. core FW = +10% yr./yr and total product = +17% yr./yr.)
- **Fabric and cloud products gaining traction.** Represents 20% of billings and growing 30%+.

Investment Risks

- **Covid-19 outbreak likely places near term pressure on appliance models.** FTNT also generates 60% of sales from EMEA and APAC region and has more exposure to SMB than peers.
- **Appliance centric model likely faces headwinds as workloads move to cloud.**
- **Long term contract duration reduces FCF quality.** Upfront payments on multi-year deals account for 30%+ of FCF.

Source: Company Filings

Cloudflare – SMB Exposure is Our Main Concern

NET, Neutral



Market Cap: \$7.2 Billion

Revenue: 2020E \$391MM 2021E \$497MM

Fair Value: \$23

Investment Positives

- **Strong secular tailwinds** – digital transformation and driving cloud security adoption
- **Solid share gains in core target market.** NET's target market is debatable. But we define it as DDoS, WAF and CDN. NET held about 5% share of spending in 2019 and is winning 15%+ of the market's incremental growth
- **Successfully winning larger enterprise accounts.** Net ended 2019 with 550 customers spending \$100K/year – an increase of 76% yr./yr.
- **Growth accelerated in Q4'19 – 2020 estimates look reasonable.** 51% rev growth in Q4'19. Street 2020E of 36% yr./yr. not aggressive under normal conditions.

Investment Risks

- **COVID-19 risk likely pressures demand environment.** SMB likely around 30% - 40% revenue. Also – 43% of revenue derived from Europe and APAC.
- **Current addressable market is hard to define.** Our checks indicate that NET is not the best at any one thing they do. Customers need to buy the platform.
- **Debatable exposure to a commoditized CDN space.** Call it one third of NET's value prop is CDN related.

Source: Company Filings

OneSpan – Transition in Progress

OSPN, Neutral

Market Cap: \$624MM

Revenue: FY21E \$282M FY22E \$324M

Fair Value: \$17



Investment Positives

- **Powerful secular drivers behind OSPN's identity security portfolio.** A shift towards mobile banking and continued regulatory pressure (GDPR, PSD2, CCPA) is driving business.
- **Proven track record and deep relationships with large global banks.**
- **Shift towards software and recurring revenue should drive higher GMs and help stabilize the model.** The software transition is well underway but still far from over.
- **Depressed valuation is relatively forgiving.** ~2x EV/F20E revenues arguably reflects poor investor sentiment.

Investment Risks

- **Hardware and non-recurring software revenue can create meaningful quarterly volatility.** Recurring revenue is only 25%-30% of total revenue today (our est.). This presents meaningful risk in the newly uncertain environment investors now must navigate.
- **Transition towards recurring revenue unlikely to occur in a straight line.** The company's transitional progress is often called into question on a quarterly basis.
- **FCF generation has been lumpy.**

Palo Alto Networks – Too Much Internal and External Uncertainty

PANW, Neutral



Market Cap: \$17 Billion

Revenue: FY20E \$3,352MM FY21E \$3,985MM

Fair Value: \$169

Investment Positives

- ***Still recognized as the leader in network security.*** PANW's NGFW platform revolutionized the market and the company dominated the firewall space from 2012 - 2018
- ***Aggressive investment in cloud and Next Generation Security Products.*** PANW has been the most proactive of legacy firewall vendors to address the shift in security spending to cloud based architectures.
- ***Compelling mid term growth targets and FCF profile.*** PANW is targeting 20%+ revenue growth through FY22 and indicated that FCF margins should remain stable.

Investment Risks

- **Shift from best in class provider to platform play.** We think PANW is trying to do too many things to extend its growth profile. ***Platform play = slower growth!***
- ***A slowing traditional firewall business likely very hard to turn around.*** Checks indicate PANW has lost focus on its core. We have seen heightened executive departures too.
- ***We are very skeptical on growth outlook.*** Firewall turn around unlikely and next gen security is a bet on acquired assets. Plus, Covid-19 headwinds.
- **FCF is low quality.** Upfront payments for multi-year deals account for 20% - 30%+ of FCF.

Team Background

Gray Powell

- 20 years experience as a sell side analyst
- Most recently worked on Deutsche Bank's #5 ranked II software team. Led coverage of security software space.
- Previously at Wells Fargo. Covered multiple sectors across TMT including security software, cloud infrastructure, data centers, CDN, and telecom services.
- Alabama football fan. This is offset by being a Wake Forest basketball fan.

Kingsley Crane

- B.A. CS/Stats Columbia University
- Experience supporting security, application, and infrastructure software.
- Data science experience in prior roles.

John Gonser

- B.S. Business Administration UC Berkeley
- Experience supporting security, application, and infrastructure software.
- Capital markets experience in prior roles.

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