BUY

Current Price	$0.69
Target Price	$0.88

Ticker:		FZO.ASX
Sector:		Software
Shares on Issue (m):		704.5
Market Cap ($m):		482.6
Net Debt / (Cash) ($m):		-27.1
Enterprise Value ($m):		455.5
52 wk High/Low:	0.700	0.392
12m Av Daily Vol (m):		1.3

Key Metrics

	22F	23F
EV/EBITDA (x)	-201.4	35.6
EV/EBIT (x)	-109.2	45.1
P/E (x)	-91.9	47.2

Ratios

	21F	22F	23F
ND / Equity	-102.5%	-10.3%	-11.8%
EBITDA Mgn	-132.3%	-4.2%	16.7%
RoA	-195.3%	-4.8%	6.0%
RoE	-84.0%	-4.1%	5.8%

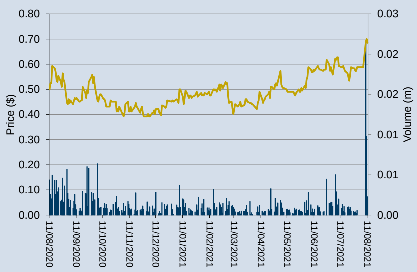
Financials*:

	21F	22F	23F
Revenue ($m)	10.9	53.9	76.3
EBITDA ($m)	-14.4	-2.3	12.8
EBIT ($m)	-16.5	-4.2	10.1
NPAT ($m)	-16.5	-4.2	10.1
** Underlying*			
Net Assets ($m)	34.9	168.1	178.2
Op CF ($m)	-13.4	-7.6	8.0

Per Share Data:

	21F	22F	23F
Norm. EPS (cps)	-4.56	-0.75	1.45
DPS (cps)	0.00	0.00	0.00
Div Yield	0.0%	0.0%	0.0%
NTAPS (cps)	9.64	4.13	4.79
CFPS (cps)	-3.70	-1.35	1.16

Share Price Graph



Please refer to important disclosures at end of the report (from page 9)

Wednesday, 11 August 2021

Family Zone (FZO)

Complementary acquisition adds scale

Analyst | Ian Christie

Quick Read

FZO has added a significant and complementary acquisition to its already impressive organic growth. It brings geographic and product diversification, reducing risk, and enhancing the combined entity's opportunity set. With major tailwinds behind cyber security the prize is large for successful solution providers.

Smoothwall acquisition

Acquisition summary: FZO is acquiring Smoothwall, a provider of digital safety solutions primarily within the UK, for $142M cash consideration. The business has a mature filtering offering, and a market leading analytics and monitoring product. Smoothwall has been operating for over 20 years, provides services to 6M students, and delivered $30M annual recurring revenue (ARR) and proforma unaudited EBITDA of ~$7M last financial year. FZO is funding the acquisition with a $146M capital raise at $0.55.

Complementary: The cyber safety offerings of the businesses are highly complementary, with FZO's strengths in filtering and parental controls dovetailing with Smoothwall's monitoring product. Market penetration provides solid product validation for filtering and monitoring, while the premium parental control product offers significant upside if the imminent launch in the US is successful. Importantly, the group's sales personnel in both jurisdictions will now have a full suite of products with which to target a greater portion of a potential client's wallet.

Forecasts: The combined group enters FY22 with ARR of ~$44M, and we adjust forecasts significantly to account for Smoothwall. We expect EBITDA breakeven occurring earlier than under a standalone FZO model, although a lot will depend on how aggressively FZO chases, and invests in anticipation of, the growth opportunity. We provide more detail behind our assumptions in the forecasts section of this report.

Managing growth: Success in achieving significant organic and inorganic growth in a short period comes with risks that need managing. FZO is a very different business to what it was even a year ago, so it is a positive that Smoothwall is expected to not only be a good cultural fit but brings additional breadth and depth to the team. While there will be challenges, a need to manage a strong growth profile is a good problem to have.

Recommendation

It is difficult valuing a young, high growth, acquisitive business. As explained in the valuation section of this report, we have done so with reference to strongly-growing peers and back it up with a DCF-based valuation (while acknowledging a high degree of forecasting risk around future cash flows). The Smoothwall acquisition provides product and geographic diversification, reducing risk, and our blended valuation increases to $0.88 (prior $0.78). We upgrade our recommendation to BUY (previously SPEC BUY).

Family Zone

Equity Research

Ian Christie, CFA

Recommendation	BUY
Current Price ($)	0.69
Valuation ($)	0.88

Sector	Software
Market Cap ($m)	482.6
Enterprise Value ($m)	455.5
Date	11 August 2021

Trading Metrics	FY21F	FY22F	FY23F	FY24F
EV / EBITDA (x)	(31.7)	(201.4)	35.6	12.7
EV / EBIT (x)	(27.7)	(109.2)	45.1	14.1
P/E (x)	(15.0)	(91.9)	47.2	14.8
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%

Per Share Data	FY21F	FY22F	FY23F	FY24F
Reported EPS (cps)	-4.56	-0.75	1.45	4.64
Adjusted EPS (cps)	-4.56	-0.75	1.45	4.64
Div. per share (cps)	0.00	0.00	0.00	0.00
NTA per share (cps)	9.64	4.13	4.79	9.43
CF per share (cps)	-3.70	-1.35	1.16	4.09

Valuation	Calcs.	$m	$ps
DCF Valuation:			
Discount Rate / WACC (%)	11.0%		
PV Free Cash Flow ($m)		637.9	
Less Net Debt / Plus Cash ($m)		27.1	
Plus Unpaid Cap ($m)		-	
Equity Value ($m)		665.0	0.94
Capitalisation Valuation:			
FY21 ARR multiple	12.5	578.4	0.82
Valuation ($/share)			*0.88*

P&L ($m)*	FY21F	FY22F	FY23F	FY24F
Revenue	10.9	53.9	76.3	111.9
EBITDA	(14.4)	(2.3)	12.8	35.8
D&A	(2.1)	(1.9)	(2.7)	(3.5)
EBIT	(16.5)	(4.2)	10.1	32.3
PBT	(16.5)	(4.2)	10.1	32.2
NPAT	(16.5)	(4.2)	10.1	32.2

** Underlying*

P&L ($m)*	1H20A	2H20A	1H21A	2H21F
Revenue	2.4	2.6	4.4	6.5
EBITDA	(5.9)	(6.9)	(7.7)	(6.7)
D&A	(2.3)	(1.8)	(1.7)	(0.4)
EBIT	(8.3)	(8.7)	(9.3)	(7.1)
PBT	(8.3)	(8.9)	(9.3)	(7.2)
NPAT	(8.3)	(8.9)	(9.3)	(7.2)

** Underlying*

Cash Flow ($m)	FY21F	FY22F	FY23F	FY24F
Receipts	11.3	45.0	70.8	103.1
Payments	(29.6)	(56.5)	(65.8)	(76.7)
Other / Prepayments	4.9	4.0	3.0	2.0
Cash from Operations	(13.4)	(7.6)	8.0	28.4
Property, Plant & Equip	(2.4)	(3.3)	(4.4)	(5.2)
Payment for Subsidiary	-	(144.9)	-	-
Other	-	-	-	-
Cash From Investing	(2.4)	(148.2)	(4.4)	(5.2)
Issue of Shares	47.0	137.4	-	-
Net Borrowing	(1.3)	-	-	-
Dividends / Other	-	-	-	-
Cash From Financing	45.7	137.4	-	-
Net Cash Flow	30.0	(18.4)	3.6	23.2
Ending Cash	35.8	17.3	21.0	44.2

Cash Flow ($m)	1H20A	2H20A	1H21A	2H21F
Receipts	2.7	3.2	6.4	4.8
Payments	(8.7)	(7.4)	(12.1)	(17.4)
Other / Prepayments	1.9	0.0	2.2	2.7
Cash from Operations	(4.1)	(4.2)	(3.5)	(9.9)
Property, Plant & Equip	(0.4)	(1.1)	(0.8)	(1.5)
Payment for Subsidiary	-	-	-	-
Other	-	-	-	-
Cash From Investing	(0.4)	(1.1)	(0.8)	(1.5)
Issue of Shares	4.5	6.0	26.0	21.1
Net Borrowing	(0.6)	0.6	(1.5)	0.2
Dividends / Other	-	-	-	-
Cash From Financing	3.9	6.6	24.5	21.3
Net Cash Flow	(0.6)	1.3	20.1	9.8
Ending Cash	4.5	5.8	25.9	35.8

Balance Sheet ($m)	FY21F	FY22F	FY23F	FY24F
Cash	35.8	17.3	21.0	44.2
Receivables	4.3	13.3	18.8	27.6
Inventory / Other	0.6	1.0	1.1	1.3
Current Assets	40.7	31.7	40.9	73.1
Property, Plant & Equip	3.1	4.5	6.2	7.9
Other NC Assets	0.4	145.3	145.3	145.3
Non-Current Assets	3.6	149.9	151.6	153.2
Total Assets	44.3	181.5	192.5	226.3
Payables	4.3	8.4	9.3	10.9
Borrowings	-	-	-	-
Provisions / Other	5.0	5.0	5.0	5.0
Total Liabilities	9.3	13.4	14.3	15.9
Net Assets	34.9	168.1	178.2	210.4
Ordinary Equity	103.7	241.1	241.1	241.1
Reserves	10.0	10.0	10.0	10.0
Retained Earnings	(78.8)	(83.0)	(72.9)	(40.7)
Total Equity	34.9	168.1	178.2	210.4

Financial Ratios	FY21F	FY22F	FY23F	FY24F
Growth				
Revenue growth (%)	119.5%	396.3%	41.6%	46.6%
EBITDA growth (%)	N/A	N/A	N/A	179.9%
NPAT growth (%)	N/A	N/A	N/A	219.8%
Profitability Ratios				
EBITDA Margin (%)	-132.3%	-4.2%	16.7%	32.0%
Return on Assets (%)	-195.3%	-4.8%	6.0%	18.2%
Return on Equity (%)	-84.0%	-4.1%	5.8%	16.6%
ROIC (%)	-226.4%	-3.6%	4.4%	13.5%
Balance Sheet Ratios				
Net Debt (ND) / Equity (%)	-102.5%	-10.3%	-11.8%	-21.0%
ND / ND + Equity (%)	4106.9%	-11.5%	-13.3%	-26.6%
Current Ratio (x)	5.7	2.8	3.4	5.3
Net Interest Cover (x)	-249.6	-278.0	672.9	2,150.0
Cash Flow Ratios				
Free Cash Flow Yield (%)	-6.4%	-40.5%	0.8%	4.9%
Cash Conversion (x)	0.9	3.3	0.6	0.8

Acquisition of Smoothwall

FZO has acquired UK-based Smoothwall for $142M

Smoothwall background

The $142M acquisition of UK-based Smoothwall follows a lengthy due-diligence process which highlighted the complementary nature and cultural fit of the two businesses. Smoothwall has grown its position primarily in the UK over the last twenty years and is of a scale that generates pro forma Annual Recurring Revenue (ARR) of ~$30M and EBITDA of ~$7M. It services ~38% of the UK market, 6M students, and has long-term contracts and relationships.

Smoothwall has around 38% of the UK market, servicing 6.1M students

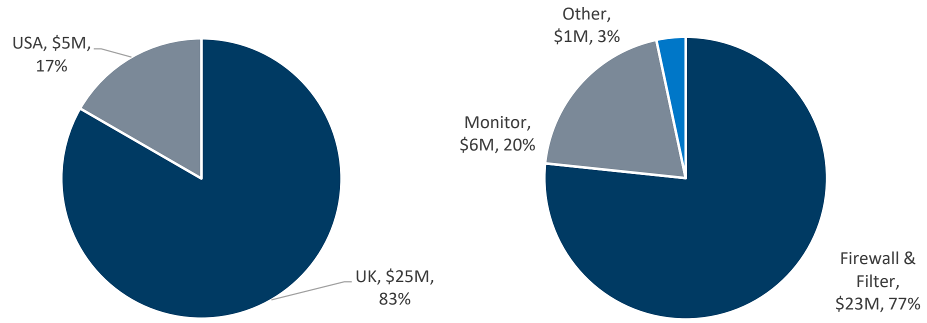
Its portfolio of digital safety products includes filtering, firewalls, monitoring, and digital record keeping. FZO draws attention to Smoothwall's cloud-based "Monitor" product, a leader in the growing cyber-safety segment of data analytics and monitoring. It combines artificial intelligence (AI) and human moderation to identify and intervene in situations that threaten child safety (such as bullying, self-harm, violence, suicide, and exploitation). It is a response to rapidly evolving duty of care requirements, which in the UK has become an obligation under the Keeping Children Safe in Education (KCSIE) legislation.

Acquisition rationale

FZO identifies Smoothwall's scale, complementary product offerings, the opportunities available to the combined group, and an increased pool of talent amongst key strategic drivers. We find the product and geographic synergies highly compelling. Smoothwall provides FZO with immediate and meaningful exposure to the UK market, while complementary product strengths allow for cross-selling across and within jurisdictions.

Smoothwall generated ARR of ~$30M and EBITDA of ~$7M last financial year

Figure 1. Smoothwall's geographic and product revenue splits



Source: FZO, Argonaut

FZO and Smoothwall have complementary product offerings and a good cultural fit

Figure 2. Smoothwall's and Family Zone's product strengths

	Filtering & Compliance	Classroom Management	Data Analytics & Monitoring	Parental Controls
Family Zone	"School Manager"	"Classwize"	"Case Manager"	"Premium"
Smoothwall	"Filter"	(In Development)	"Monitor"	

	Market Leading
	Competing
	In Development

Source: FZO, Argonaut

Consolidated business profile

The combined entity becomes a meaningful global player in cyber safety

On a consolidated basis, the combined group becomes a meaningful global player in cyber safety. FZO had already been rapidly penetrating the US market, and with 3M students on its platform after the recent acquisition of NetRef, had quickly and impressively penetrated more than 5% of the US student market.

Importantly, the combination of FZO and Smoothwall products will give the group's sales personnel a full suite of products with which to target all a client's potential spend, not just a portion. FZO's filtering product has been strongly endorsed by the uptake in the US, while Smoothwall's market share in the UK speaks to the performance of its product suite.

The duty of care regarding online safety is increasingly in focus, providing strong industry tailwinds

The spend across the cyber security space provides strong tailwinds for a Company with validated products that meet the growing market need. The duty of care component of a child's online safety is increasingly important and an exciting growth opportunity for the business.

The premium parental control product, which retails at a much higher price per account than student products, provides a high growth opportunity both in the US and the UK. Launch in the US is imminent.

The broader suite of products provides the sales team with an opportunity to capture a greater share of customer wallet

Figure 3. Consolidated business profile

	smoothwall	family zone	MergeCo
Geographic presence			
UK	Y		Y
US	Y	Y	Y
ANZ		Y	Y
Products			
Filter (cloud & on-premise)	Competing	Market leading	Market leading
Monitoring	Market leading	In development	Market leading
Classroom management	In development	Competing	Competing
Parental controls		Market leading	Market leading
Metrics			
Employees (heads)	113	190	**+ 300**
Students #s	6,100,000	3,000,000	**+ 9 million**
School #'s	12,400	5,600	**+ 18 thousand**
Estimated ARR at 30 Jun '21[1]	~ A$ 30 million	~ A$ 14 million	**+ A$ 44 million**

1. Converted to AUD based on AUD:GBP of 0.54 as at 15 July 2021. Shown on a UK Financial Year basis

Source: FZO

Acquisition funding

The acquisition is being funded by a $146M capital raising at $0.55

The cash acquisition of Smoothwall has been funded by a fully underwritten $146.3M capital raising at $0.55 comprising:

- A placement to raise $71.0M (concluded)
- A 5-for-16 entitlement offer comprising:
  - An accelerated institutional component to raise $37.1M (concluded)
  - A retail component to raise $38.2M (in process)

Following the capital raise, acquisition, and related expenses FZO will have cash available of $27.1M, slightly below the $32.1M on 31 July (which we assume was down on the $35.6M at June quarter end in part due to the NetRef acquisition). Shares in issue will have climbed from 438.4M to 704.5M.

Forecasts

We have reviewed and adjusted our prior standalone FZO forecasts, prior to adding the anticipated contribution from Smoothwall

We reviewed and adjusted our prior FZO standalone forecasts, primarily to reflect updated product pricing, and then combined these numbers with Smoothwall's contribution based on FY22 opening ARR of $30M and $7M EBITDA.

Given the significant forecasting risk (to both the upside and the downside), we highlight some of our key thoughts below:

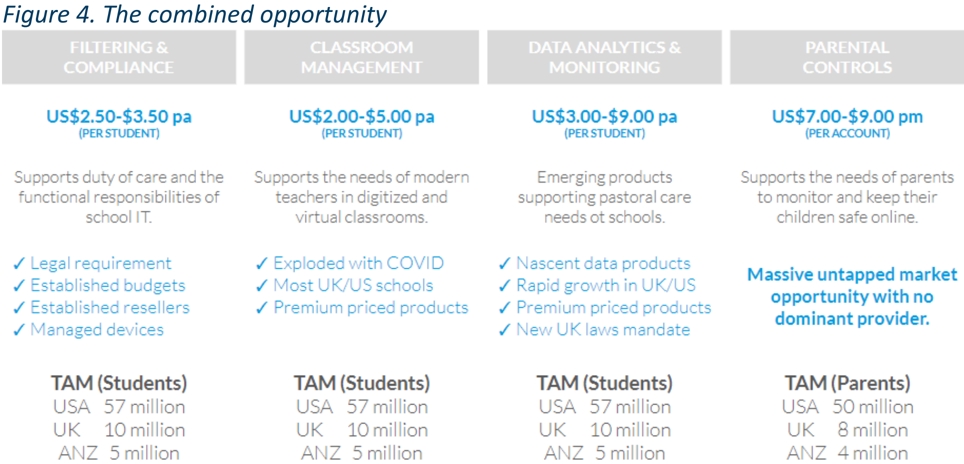
- In the US:
  - We continue to factor in strong growth in licensed student numbers for FZO's filtering & compliance software given success to date. We believe FZO has the potential to break 10% student market share by FY25.
  - Our forecasts for classroom management tools, and data analytics & monitoring are more circumspect until FZO builds its track record. As a result, if FZO demonstrates success selling Smoothwall's Monitor in the US we see potential upside to our US numbers from this product.
  - The sale of premium parental controls provides the biggest forecasting risk. We currently assume relatively small penetration by FY25 in comparison to student penetration (roughly 1 parent per 15 licensed students). However, given product revenue per account is so much higher (see below), by FY25 our forecast revenue from premium product sales exceeds student revenue. The success of the launch of this product, which is currently underway, will therefore be critical.

We pencil in continued strong growth in the market leading filtering and monitoring products, but are more circumspect with other product lines

- In the UK:
  - We forecast lower growth overall than in the US, primarily because of the large existing market share, although within the product suite we assume Smoothwall's Monitor product achieves solid growth and increased market share.
  - We have been cautious with assumptions regarding the premium parental control product rollout in the UK pending the success of the launch in the US. It provides significant upside potential to our current forecasts.
- In Australia & New Zealand:
  - We assume lower growth compared to overseas, and with its smaller size, believe the region's contribution will become increasingly insignificant over time.

The premium parental control product provides strong upside potential to forecasts given its higher pricing, so the success of its launch in the US will be critical

Figure 4. The combined opportunity



Forecasting risk is high

Source: FZO, (TAM = Total Addressable Market)

A summary of key assumptions and forecasts are shown in the table overleaf.

Family Zone (FZO)		FY21E	FY22F	FY23F	FY24F	FY25F	1H22F	2H22F	1H23F	2H23F
Students										
Student Numbers:										
US (average over period)	#M	1.4	3.1	4.5	5.9	7.3	2.8	3.4	4.3	4.7
UK (average over period)	#M	-	4.1	4.3	4.5	4.5	4.0	4.1	4.3	4.4
Other (average over period)	#M	0.1	0.1	0.2	0.2	0.2	0.1	0.2	0.2	0.2
Total (average over period)	#M	1.5	7.3	9.0	10.6	12.0	6.9	7.6	8.7	9.2
Student Revenue:										
US	A$M	6.4	19.8	28.5	37.9	47.4	9.2	10.6	13.8	14.7
UK	A$M	-	27.1	31.5	35.0	36.5	13.1	13.9	15.4	16.2
Other	A$M	3.2	4.3	5.0	5.5	6.0	2.1	2.2	2.4	2.6
Total	A$M	9.7	51.2	65.1	78.4	90.0	24.5	26.7	31.6	33.5
ARR (at start of period)	A$M		43.8	57.5	70.2	81.8	43.8	48.0	57.5	60.8
Student Revenue/User:										
US	A$ p.a.	4.5	6.4	6.3	6.5	6.5	6.7	6.2	6.4	6.2
UK	A$ p.a.		6.7	7.3	7.8	8.1	6.6	6.8	7.2	7.4
Parents										
Parent Numbers:										
US (average over period)	#M	-	0.0	0.1	0.2	0.4	0.0	0.0	0.0	0.1
UK (average over period)	#M	-	-	0.0	0.0	0.0	-	-	0.0	0.0
Other (average over period)	#M	0.0	0.0	0.0	0.1	0.1	0.0	0.0	0.0	0.0
Total (average over period)	#M	0.0	0.0	0.1	0.3	0.5	0.0	0.1	0.1	0.1
Parent Revenue:										
US	A$M	-	1.0	8.0	28.9	54.4	0.2	0.8	2.4	5.6
UK	A$M	-	-	1.0	2.0	3.1	-	-	0.5	0.5
Other	A$M	1.1	1.8	2.2	2.6	2.9	0.8	0.9	1.1	1.2
Total	A$M	1.1	2.7	11.2	33.5	60.4	1.0	1.7	4.0	7.3
ARR (at start of period)	A$M		-	2.1	10.8	23.9	-	0.6	2.1	5.3
Parent Revenue/User:										
US	A$ p.a.		128.0	128.0	128.0	128.0	128.0	128.0	128.0	128.0
UK	A$ p.a.			128.0	128.0	128.0			128.0	128.0

** Note that we assume students may be licensed for more than one product (as reflected by revenue per user)*

Gross Profit		FY21E	FY22F	FY23F	FY24F	FY25F	1H22F	2H22F	1H23F	2H23F
Revenue:										
Students	A$M	9.7	51.2	65.1	78.4	90.0	24.5	26.7	31.6	33.5
Parents	A$M	1.1	2.7	11.2	33.5	60.4	1.0	1.7	4.0	7.3
Total	A$M	10.8	53.9	76.3	111.9	150.4	25.5	28.5	35.6	40.7
Direct Expenses:										
Data Hosting	A$M	(2.9)	(11.7)	(12.2)	(14.6)	(16.8)	(5.6)	(6.2)	(5.9)	(6.3)
Other Direct	A$M	(3.8)	(7.6)	(10.7)	(15.7)	(21.3)	(3.6)	(4.0)	(5.0)	(5.7)
Total	A$M	(6.7)	(19.3)	(22.9)	(30.2)	(38.1)	(9.2)	(10.2)	(10.9)	(12.0)
Data Hosting / User	A$ p.a.	(1.9)	(1.6)	(1.3)	(1.3)	(1.3)	(0.8)	(0.8)	(0.7)	(0.7)
Gross Profit:										
Gross Profit	A$M	4.1	34.6	53.5	81.7	112.4	16.3	18.3	24.7	28.7
Gross Profit Margin	%	38%	64%	70%	73%	75%	64%	64%	69%	71%
EBITDA:										
Other Income	A$M	5.0	4.0	3.0	2.0	-				
Other Expenses	A$M	(23.5)	(40.8)	(43.7)	(47.9)	(50.6)				
EBITDA	A$M	(14.5)	(2.3)	12.8	35.8	61.7				
EBITDA Margin	%			17%	32%	41%				

Valuation

We look at an ARR multiple and a DCF valuation to determine a valuation

Valuing rapidly growing, early stage companies is challenging. We have done so by:

- Using an EV multiple of current ARR multiple with reference to peers' trading multiples
- Backing this up with a DCF valuation based on the earnings assumptions as highlighted above

Multiple analysis

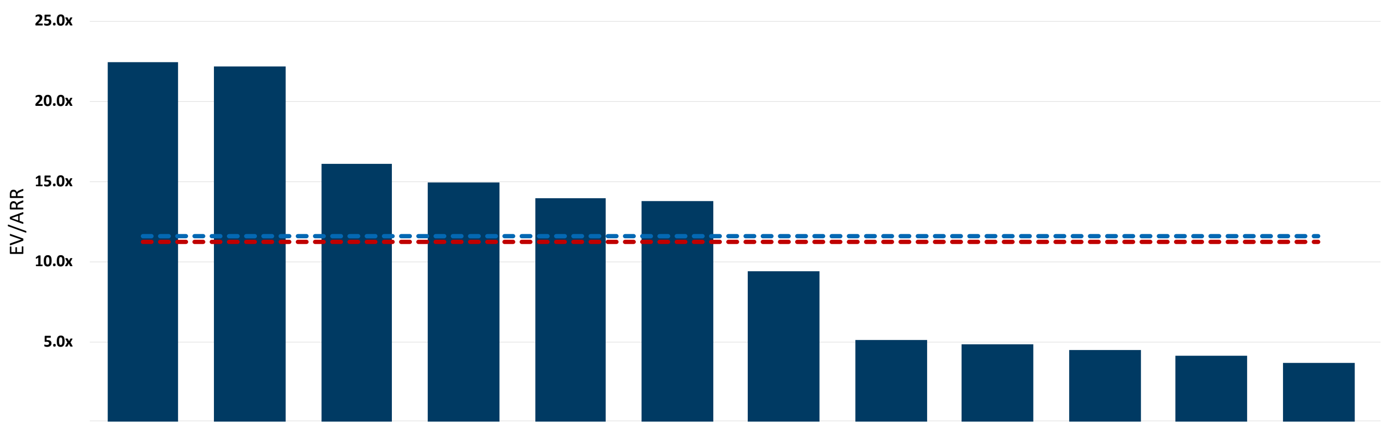
Using a 12.5x multiple of current ARR we get a valuation of $0.82

We analysed 30 predominantly software as a service (SaaS) ASX-listed companies, capturing current enterprise values (EVs), current ARR, and annual ARR growth. They trade on a very wide range of EV/ARR multiples, which is not helpful. However, we assume the multiple in part reflects growth potential, so filtered out all companies that did not grow ARR by at least 30% over the last year. This was with reference to FZO and Smoothwall's combined ARR growth of 31%.

This narrowed the field of comparable companies down to 12 as shown below. The range in EV/ARR multiples remains wide. However, the average and median EV/ARR's fall within the 11-12x band, which we find reasonable.

Figure 5. Peer comparisons

Selected comparable companies are majority SaaS companies with ARR growth +30%



Company	DUB	ALC	M7T	IHR	ART	5GG	K2F	MPA	PRO	ELO	BID	SKF
EV	$875.5m	$352.3m	$215.8m	$58.4m	$357.8m	$159.3m	$31.7m	$22.4m	$36.8m	$372.1m	$63.1m	$51.6m
ARR	$39.0m	$15.9m	$13.4m	$3.9m	$25.8m	$11.6m	$3.4m	$4.4m	$7.6m	$84.0m	$15.2m	$14.0m
ARR Growth	142%	118%	105%	100%	33%	132%	50%	144%	77%	52%	83%	40%
EV/ARR	22.4x	22.2x	16.1x	14.9x	13.9x	13.7x	9.4x	5.1x	4.8x	4.4x	4.2x	3.7x

Source: Argonaut, FactSet, Company announcements

Given the size of FZO's addressable global market, growth exhibited to date, and potential opportunities, we use a 12.5x ARR multiple in valuing FZO, slightly above this peer group average.

On this basis, using the current $44.1M ARR we derive a multiple-based valuation of $0.82.

We show the valuation sensitivity to different EV/ARR multiples below.

A multiple valuation is relative, and a sensitivity to various multiples shows a wide range of valuation outcomes

Figure 6. EV/ARR valuation sensitivity

Multiple (x)	7.5	10.0	12.5	15.0
Comb. ARR	$44.1m	$44.1m	$44.1m	$44.1m
EV	$330.8m	$441.0m	$551.3m	$661.5m
Net Cash	$27.1m	$27.1m	$27.1m	$27.1m
Equity Value	$357.9m	$468.1m	$578.4m	$688.6m
Shares (M)	704.5m	704.5m	704.5m	704.5m
Val / Share	$0.51	$0.66	$0.82	$0.98

Source: Argonaut, FactSet, Company announcements

DCF valuation

Our DCF valuation comes out at $0.94, although we acknowledge there is a high level of risk with forecast cash flows

We are conscious of the significant risks in forecasting cash flows for FZO, however have derived a DCF based valuation based on the assumptions highlighted previously in this document. Reality is likely to differ significantly from our forecasts, and this could be in either direction. We have discounted these cashflows at 11%. Previously we provided a DCF valuation range based on discount rates between 11% and 13%, however the acquisition of EBITDA-positive Smoothwall helps de-risk the business.

Our DCF_{11}-based valuation of $0.94 provides backup to our multiple-based valuation. At a 13% discount rate, our valuation would fall to $0.72.

Combined

We combine the two valuation methodologies to set a blended valuation of $0.88.

Risks

There are significant opportunities ahead of FZO, although management will face challenges and risks around managing the growth and successfully integrating the new businesses

We see significant opportunity for FZO as it capitalises on the very strong tailwinds in cyber-safety. There are however risks to achieving the potential, key in our view being:

- **Managing growth:** FZO entered the US market in late 2018 and on a standalone basis has grown impressively from less than 0.5M to 2.4M student licenses over the last two years, nearly all in the US. With the recent acquisitions, student numbers have climbed to ~9M at 18,000 schools. Acquisitions bring skills to the group but managing growth and addressing significant opportunities within a much bigger business will pose new challenges to FZO management.
- **Integration:** FZO notes that considerable time was spent on assessing the Smoothwall acquisition, convincing management of both businesses that there was cultural fit and complementary services. This is important and provides comfort, although business integrations invariably come with unforeseen challenges.
- **Competition:** The strong tailwinds in the cyber security space are well understood and existing and new competitors will also be endeavouring to take market share. This does, however, make FZO's performance even more impressive in our view, validating the products and the potential growth.

Forecasting and valuation risk remains high until FZO establishes more of a track record

- **Forecasting and valuation risk:** We have already highlighted the risks involved with forecasting for a young, high-growth company. Actual outcomes can be very different to forecasts. A multiple based valuation is relative, not absolute, so depends on market sentiment toward the sector, while a DCF valuation is only as good as the cash flow forecasts from which it is derived.

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