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an EFG company

Family Zone Cyber Safety Ltd (FZO)

Rating: Buy | Risk: High | Price Target: $1.00

Building a Wall of ARR

Key Information

Current Price ($ps)	0.78
12m Target Price ($ps)	1.00
52 Week Range ($ps)	0.40 - 0.83
Target Price Upside (%)	28.2%
TSR (%)	28.2%
Reporting Currency	AUD
Market Cap ($m)	549.6
Sector	Information Technology
Avg Daily Volume (m)	1.4
ASX 200 Weight (%)	0.02%

Fundamentals

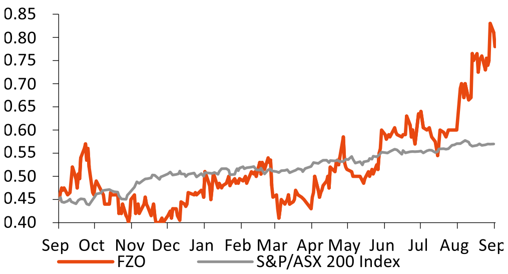
YE 30 Jun (AUD)	FY21A	FY22E	FY23E	FY24E
Sales ($m)	9.0	41.4	60.4	76.9
NPAT ($m)	(22.5)	(17.9)	(10.3)	2.4
EPS (cps)	(6.1)	(2.9)	(1.5)	0.3
EPS Growth (%)	13.8%	52.0%	50.2%	123.1%
DPS (cps) (AUD)	0.0	0.0	0.0	0.0
Franking (%)	0%	0%	0%	0%

Ratios

YE 30 Jun	FY21A	FY22E	FY23E	FY24E
P/E (x)	(9.9)	(26.7)	(53.5)	nm
EV/EBITDA (x)	(26.1)	(39.1)	(108.7)	64.1
Div Yield (%)	0.0%	0.0%	0.0%	0.0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%

Price Performance

YE 30 Jun	1 Mth	2 Mth	3 Mth	1 Yr
Relative (%)	30.1%	19.1%	28.8%	46.7%
Absolute (%)	30.0%	21.9%	32.2%	73.3%
Benchmark (%)	(0.1%)	2.8%	3.4%	26.6%



Price performance indexed to 100 *Source: FactSet*

Major Shareholders

McCusker Holdings Pty Ltd.	11.8%
Regal Funds Management Pty Ltd.	9.8%
LEVY TIM /FAMILY/	2.5%
Twynam Investments Pty Ltd.	2.3%
PAWLOWITSCH PETER EDWARD	2.3%

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Event

Family Zone (FZO) announcement and completion of Smoothwall, FY21 results to market.

Highlights

- **Significant and strategic acquisition** – FZO has acquired Smoothwall, a leading digital cybersecurity provider operating in the US and UK education markets for $142m or an attractive 4.7x ARR, which is accretive at both revenues and EBITDA. Smoothwall boasts $30m in ARR and 6.1m students on its platform across >12k schools and is market leading. This drives significant scale with FZO now at $44m ARR (3x prior), with Shaw expectations of $100m by FY25e. Importantly, FZO has acquired a leading monitoring product with an opportunity to launch into ~3m US students (>$20m ARR opportunity).
- **ARR growth expectations point to $1bn+ potential** – Post the acquisition of Smoothwall, our ARR is upgraded by +130% to $58m in FY22e and $73m in FY24e (+$15m). FZO is likely to be the next $1bn+ market cap tech player on the ASX in our view. Despite initial growth dilution growth after acquiring more mature Smoothwall, we expect a convergence in growth in later years upon conversion of core Filtering students into Classroom, Monitoring and Parental Control products. Our analysis on the business at scale, ex-growth produces a mid and high case EBITDA of $68m and $100m respectively and valuation of $1.29 and $1.71 respectively.
- **Early signs of Smoothwall outperformance** – Smoothwall is showing signs of early success with a $1.4m TCV contract in Wales (UK) in Cloud Reporting. Further, FZO updated the market last week stating that integration of Smoothwall is well underway including development of cross and upsell strategies. Furthermore, the USA is into peak sales season with ARR of $48m expected in 1Q22e (+10%) with potential for further large deals across multiple districts and cross-sell available.
- **Preferred platform for further accretive acquisitions** – Now having acquired Smoothwall and NetRef with a significant and expanding footprint in the US, UK, ANZ and Canada, FZO becomes the natural acquirer of further edu-tech businesses with niche technology or under-monetised student bases which remain plentiful. The student cyber safety space remains in its infancy especially across products with legislated requirements (i.e. Monitoring under KCSIE in the UK, Filtering under CIPA in the US) with ~10 years of growth runway and structural tailwinds remaining in our view. Given scale, track record and breadth of product offering, FZO offers globally leading exposure to this thematic in the immediate and long term.
- **Catalysts forthcoming to underwrite continued returns** – FZO remains our most catalyst rich stock under coverage with possible forthcoming news flow including:
  - Large agreements in the US with 600k students in POC and 2.4m in the pipeline.
  - US B2C success with imminent launch expected and significant 3m students sell through opportunity, a free hit on CACs and >12x ARPU on Filtering tools.
  - Further M&A potential with $36m in dry powder at 30 June 2021 and FZO now a leading global edu-tech consolidation platform.
  - Traction in UK/US cross-sell sooner than anticipated, in particular Classroom tools which are underpenetrated with a ~5.3m student base in the UK.
- **Key changes** – We have built in the acquisition of Smoothwall and the associated scale benefits. The result is an increase to our estimates including ARR by +130%, +79% and +61% and contracted students by +153%, +105% and +85% across FY22e – FY24e respectively. Our Price Target increases by 30% to $1.00 per share (previously $0.77).

Recommendation

FZO is now a leading global edu-tech player with significantly broadened growth levers and a platform for rapid ARR expansion. The company remains our most catalyst rich stock under coverage with significant upside to growth and ARR. Maintain Buy with upgraded PT.

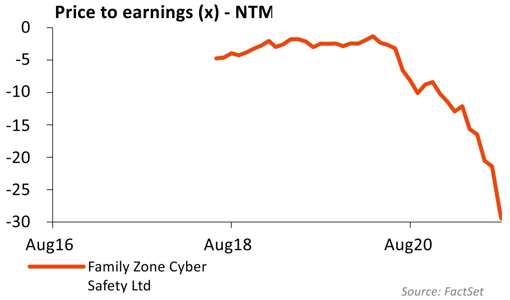
Family Zone Cyber Safety Ltd
Information Technology
Software & Services
FactSet: FZO-AU / Bloomberg: FZO AU

Key Items	Data
Recommendation	BUY
Risk	HIGH
Price ($ps)	0.78
Target Price ($ps)	1.00
52 Week Range ($ps)	0.40 - 0.83
Shares on Issue (m)	704.6
Market Cap ($m)	549.6
Enterprise Value ($m)	532.8
TSR (%)	28.2%

Company Description

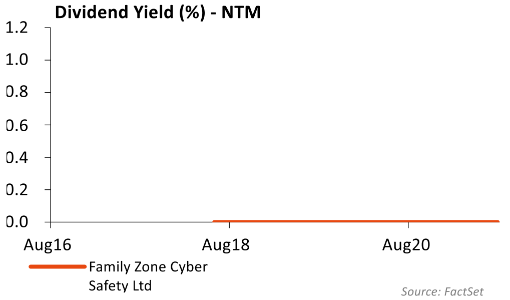
Family Zone Cyber Safety Ltd. engages in the development of parental control platform. It intends to create a system that manages the majority of the parental control functions in a cloud-based application. The company was founded by Tim Levy, Ben Trigger, Paul Robinson, and Crispin Swan in 2014 and is headquartered in West Perth, Australia.

Price to earnings (x) - NTM



Source: FactSet

Dividend Yield (%) - NTM



Source: FactSet

Financial Year End: 30 June

Investment Summary (AUD)	FY20A	FY21A	FY22E	FY23E	FY24E
EPS (Reported) (cps)	**(7.1)**	**(6.1)**	**(2.9)**	**(1.5)**	**0.3**
EPS (Underlying) (cps)	**(7.1)**	**(6.1)**	**(2.9)**	**(1.5)**	**0.3**
EPS (Underlying) Growth (%)	29.3%	13.8%	52.0%	50.2%	123.1%
PE (Underlying) (x)	**(2.8)**	**(9.9)**	**(26.7)**	**(53.5)**	**nm**
EV / EBIT (x)	**(32.2)**	**(23.1)**	**(29.8)**	**(52.1)**	**218.3**
EV / EBITDA (x)	**(42.8)**	**(26.1)**	**(39.1)**	**(108.7)**	**64.1**
DPS (cps) (AUD)	0.0	0.0	0.0	0.0	0.0
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	0%	0%	0%	0%	0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Free Cash Flow Yield (%)	(20.1%)	(8.2%)	(35.6%)	(0.4%)	3.0%

Profit and Loss (AUD) (m)	FY20A	FY21A	FY22E	FY23E	FY24E
Sales	5.1	9.0	41.4	60.4	76.9
Sales Growth (%)	*21.6%*	*76.1%*	*361.5%*	*46.1%*	*27.3%*
Other Operating Income	3.4	4.3	4.3	4.3	4.3
EBITDA	**(12.7)**	**(19.7)**	**(13.6)**	**(4.9)**	**8.1**
EBITDA Margin (%)	*nm*	*nm*	*(32.9%)*	*(8.1%)*	*10.5%*
Depreciation & Amortisation	(4.2)	(2.6)	(4.2)	(5.3)	(5.7)
EBIT	**(16.9)**	**(22.3)**	**(17.9)**	**(10.3)**	**2.4**
EBIT Margin (%)	*nm*	*nm*	*(43.2%)*	*(17.0%)*	*3.1%*
Net Interest	(0.2)	(0.2)	0.0	0.0	0.0
Pretax Profit	(17.1)	(22.5)	(17.9)	(10.3)	2.4
Tax	0.0	0.0	0.0	0.0	0.0
Tax Rate (%)	*0.0%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*
NPAT Underlying	**(17.1)**	**(22.5)**	**(17.9)**	**(10.3)**	**2.4**
Significant Items	(0.1)	0.0	0.0	0.0	0.0
NPAT Reported	**(17.2)**	**(22.5)**	**(17.9)**	**(10.3)**	**2.4**

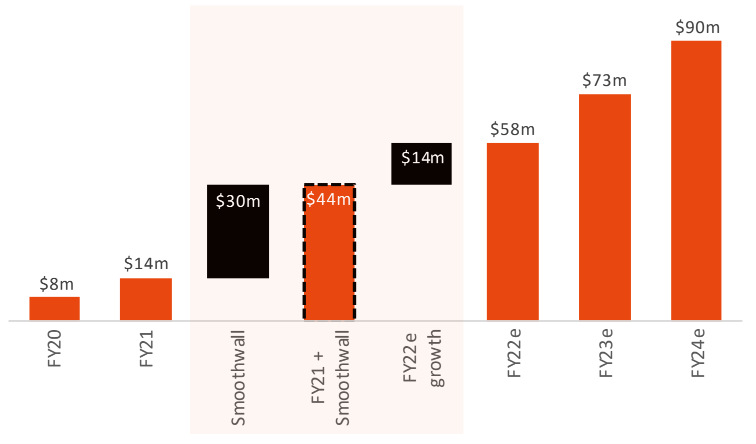
Cashflow (AUD) (m)	FY20A	FY21A	FY22E	FY23E	FY24E
EBIT	(16.9)	(22.3)	(17.9)	(10.3)	2.4
Tax Paid	0.0	0.0	0.0	0.0	0.0
Net Interest	(0.2)	(0.2)	0.0	0.0	0.0
Change in Working Capital	0.0	4.4	(2.3)	6.8	13.3
Depreciation & Amortisation	4.2	2.6	4.2	5.3	5.7
Other	1.5	1.7	3.8	2.0	2.4
Operating Cashflow	**(8.3)**	**(15.6)**	**(12.2)**	**3.8**	**23.8**
Capex	(1.4)	(2.2)	(6.0)	(6.0)	(6.0)
Acquisitions and Investments	0.0	0.0	(146.0)	0.0	0.0
Disposal of Fixed Assets/Investments	0.0	0.0	0.0	0.0	0.0
Investing Cashflow	**(1.4)**	**(2.2)**	**(152.0)**	**(6.0)**	**(6.0)**
Free Cashflow	**(9.7)**	**(17.7)**	**(164.2)**	**(2.2)**	**17.8**
Equity Raised / Bought Back	10.4	47.8	146.4	0.0	0.0
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Change in Debt	0.0	(0.8)	0.0	0.0	0.0
Other	0.0	(0.4)	0.0	0.0	0.0
Financing Cashflow	**10.4**	**46.6**	**146.4**	**0.0**	**0.0**
Net Change in Cash	**0.7**	**28.9**	**(17.8)**	**(2.2)**	**17.8**

Balance Sheet (AUD) (m)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash	5.8	34.9	17.2	15.0	32.8
Accounts Receivable	4.7	9.0	39.2	49.8	62.5
Inventory	0.2	0.4	2.0	2.5	3.2
Other Current Assets	0.2	1.9	1.9	1.9	1.9
PPE	1.5	2.8	3.4	3.2	3.1
Goodwill & Intangibles	1.3	6.0	153.1	153.9	154.4
Other Non Current Assets	0.4	2.6	2.6	2.6	2.6
Total Assets	**14.2**	**57.5**	**219.4**	**228.9**	**260.4**
Accounts Payable	3.3	6.1	29.4	37.3	46.9
Short Term Debt	1.3	0.4	0.4	0.4	0.4
Long Term Debt	0.0	0.0	0.0	0.0	0.0
Income Taxes Payable	0.0	0.0	0.0	0.0	0.0
Other	5.2	17.6	27.6	39.6	59.1
Total Liabilities	**9.8**	**24.2**	**57.5**	**77.3**	**106.5**

Ratios	FY20A	FY21A	FY22E	FY23E	FY24E
Gearing (%)	3,541.7%	2,991.0%	(11.5%)	(10.6%)	(26.6%)
Net Debt / EBITDA (x)	0.4	1.7	1.2	3.0	(4.0)

Creating a Global Leader in Cyber Safety

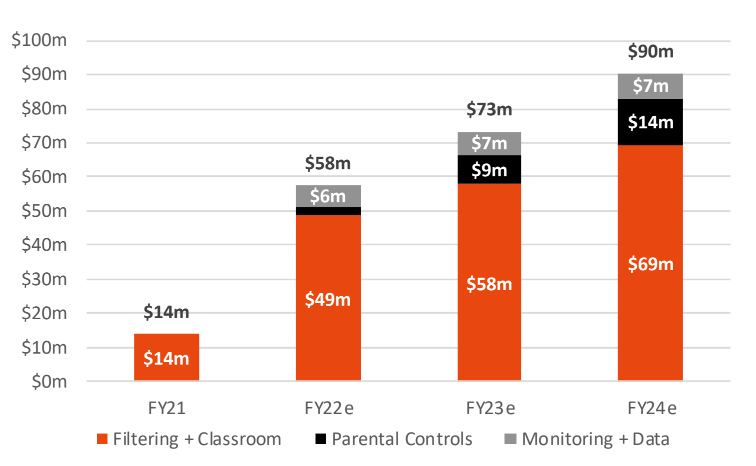
Figure 1: ARR bridge – FZO and Smoothwall



Source: Company data, Shaw and Partners analysis

- Smoothwall is a leading digital and safeguarding services provider operating in the US and UK education markets, with $30m in ARR and 6.1m students on its platform across >12k schools.
- Including FZO's ARR base of $14m, group ARR is now $44m with Shaw forecasting an increase to **$58m in FY22e, $73m in FY23e and $90m in FY24e**. Contracted students rises from 2.4m at FY21 to >10m at FY22e on our estimates.
- The company is **accelerating towards >$100m in ARR and in our view may well be the next $1bn+ market cap tech player on the ASX**.

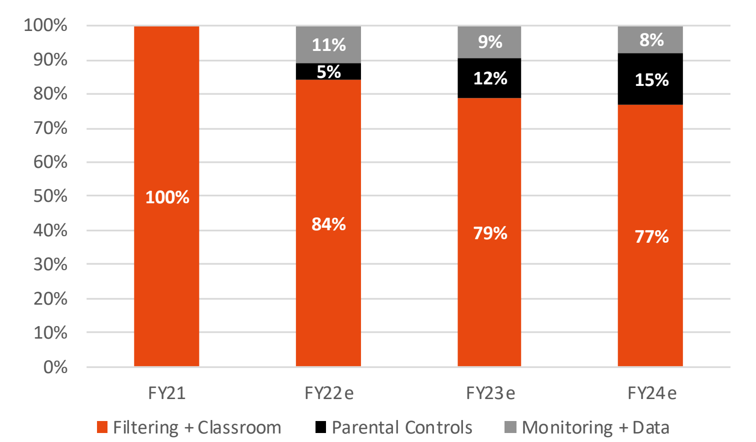
Figure 2: ARR by product – growth across multiple products



Source: Company data, Shaw and Partners analysis

- Before the acquisition of Smoothwall, FZO was predominantly focussed on Filtering and Classroom products, with a launch into Parental Controls slated for the US at a significant premium to core product ARPU and organically marketed to parents through the existing school network.
- Smoothwall has now introduced a Monitoring & Data product to the FZO stable, which is a market leader in the UK and **mandated under KCSIE (Keeping Children Safe in Education) which states that schools "must" have appropriate filters and monitoring systems**.
- In the US, Filtering is mandated whilst Monitoring products in our view are likely to see rising penetration as cyber safety for schools and children becomes increasingly important.

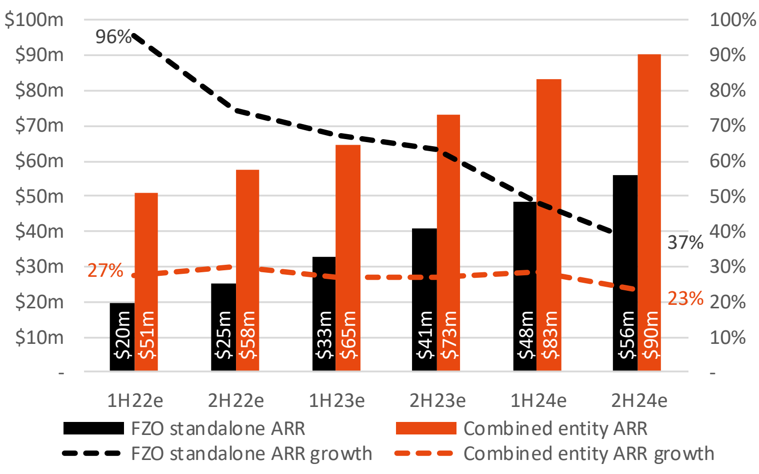
Figure 3: ARR by product – diversifying product base



Source: Company data, Shaw and Partners analysis

- As shown above, we see FZO continuing to further diversify its ARR base from Filtering and Classroom tools into Parental Controls and Monitoring & Data.
- We believe Parental Controls presents a significant opportunity with upside to our estimates if executed upon.
- Preliminary trials in Australia saw ~17.5% conversion of freemium to paid Parental Controls. For comparison, **we conservatively model 0.6%, 1.4% and 1.8% penetration in the US across FY22e – FY24e exiting FY24e at ~$14m ARR. At 10% penetration (company target), ARR for Parental Controls alone would be ~$77m or ~5x our estimate**.

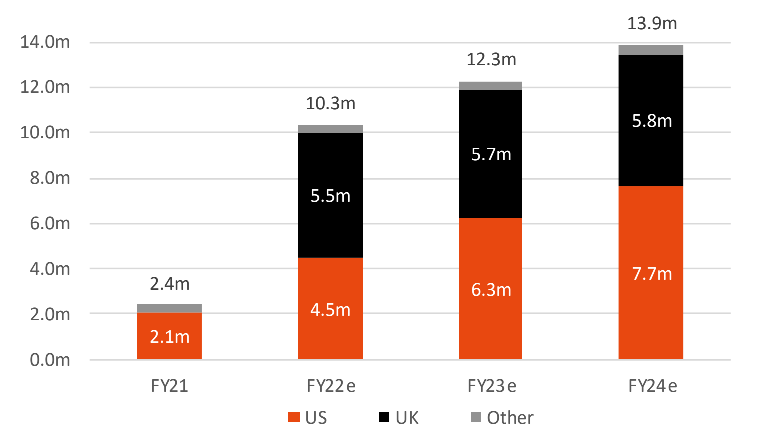
Figure 4: ARR growth converging alongside cross-sell execution



Source: Company data, Shaw and Partners analysis

- We present adjacent our pre-Smoothwall estimates of the FZO standalone business in terms of ARR, versus our updated estimates include Smoothwall.
- The FZO core business exited FY21 at an organic ARR growth rate of 74% YoY, with Shaw now forecasting 27% ARR growth across the combined entity in 1H22e after the acquisition of Smoothwall.
- Whilst growth in percentage terms is diluted, we note **absolute ARR is significantly expanded and see growth rates converging over time as cross-sell and up-sell opportunities are executed upon**.
- We see our estimates as broadly conservative under the combined entity and in line with standard practice will pass through changes when we observe tangible penetration.

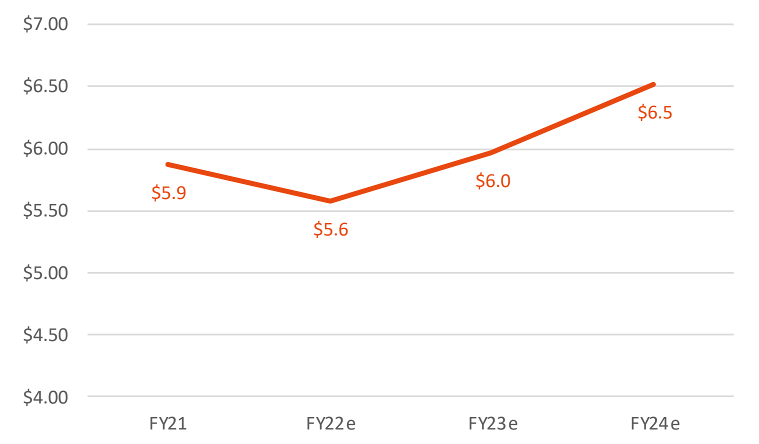
Figure 5: Contracted students by geography – majority growth in US



Source: Company data, Shaw and Partners analysis

- FZO reached 5.2% district share of US schools in FY21 with 3.0m students on its platform and has now acquired a further 6.1m students (we assume 5.3m in the UK and 800k in the US).
- The **cross-sell and up-sell opportunities coming out of the Smoothwall acquisition are incredibly vast both into the core FZO business and out of the Smoothwall product base**, with key opportunities in our view being:
  - <u>Classroom tools</u> into the UK student base.
  - <u>Data and Monitoring</u> tools into the US student base.
  - <u>Parental Controls</u> into the US and UK.

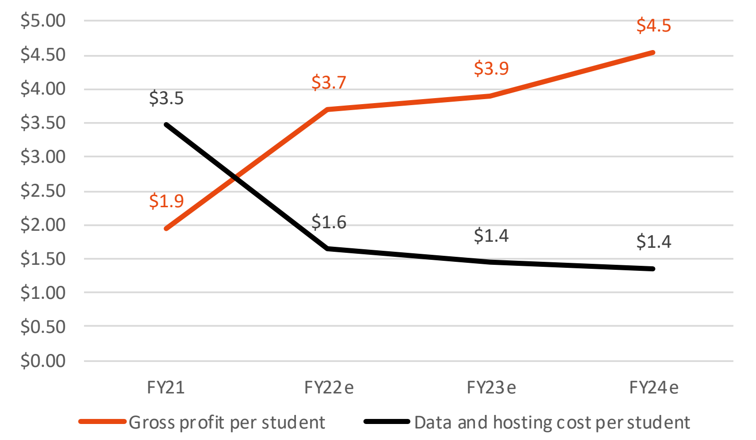
Figure 6: Blended ARPU – rising as Parental Controls penetrates



Source: Company data, Shaw and Partners analysis

- With core ARPUs across the FZO business sitting around $5.90 per student exiting FY21, we see some moderation to $5.60 in FY22e as we blend through Smoothwall ARPUs.
- Post-FY22e, we forecast **expansion to $6.00 in FY23e and $6.50 in FY24e broadly driven by penetration in Parental Controls** which has a significantly greater ARPU when compared to other products (we assume $100 per family versus $4.70 for Filtering + Classroom products).
- We anticipate some pressure across corer Filtering ARPUs, however with **FZO leading the market on product breadth and expertise, we expect ARPUs to rise across its basket of students over time as reflected in our blended ARPU estimates**.

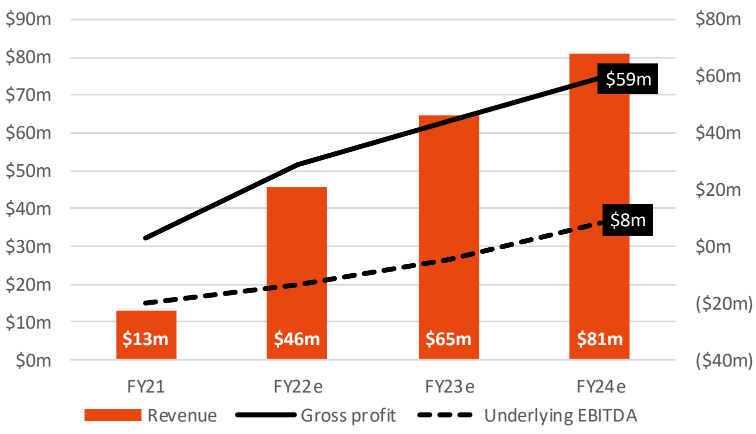
Figure 7: Gross profit / data and hosting costs per student



Source: Company data, Shaw and Partners analysis

- We present gross profit per student as revenues less our assumptions on data and hosting costs per student (versus a broader definition in the reported accounts).
- Our forecasts imply **growth in GP per student from $1.90 in FY21 to $4.50 by FY24e**, which we see as conservative and based on the following:
  - Exit run rate data and hosting costs of $1.50 per June 2021, and a company target of <$1.30 per students by the end of FY22e.
  - Scale benefits across the recent Google Cloud Platform (GCP) transition.
  - Rising penetration in value-add products (i.e. Classroom, Parental Controls).

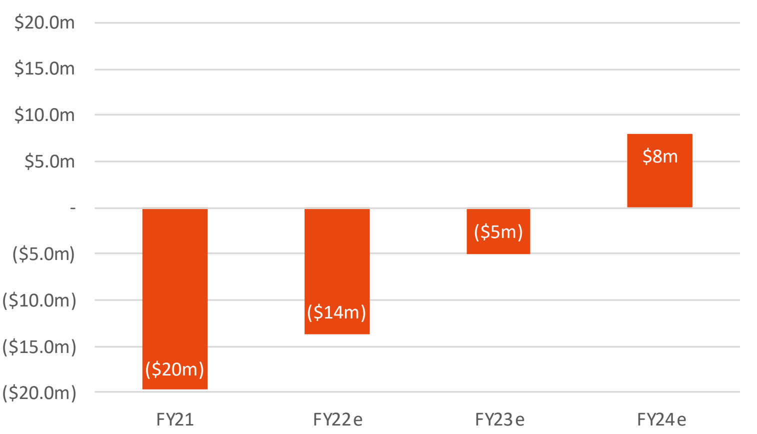
Figure 8: Revenue, gross profit and expenses – investing in future growth



Source: Company data, Shaw and Partners analysis

- Based on group ARR and our assumptions across a conversion lag factor, we estimate total **revenue (including R&D and other income) of $46m in FY22e, $65m in FY23e (+41% YoY) and $81m in FY24e (+25% YoY)**.
- Additionally, we have rolled through our estimate of Smoothwall expenses based on underlying EBITDA of $7m and revenues of $30m from the date of completion (middle of August 2021).
- On top of Smoothwall opex, we have assumed 5% HoH growth on FZO's 2H21 expense base moving into 1H22e to arrive at FY22e operating expenses of ~$47m (+71% YoY from ~$27m in FY21).

Figure 9: Underlying EBITDA – maiden positive in FY24e



Source: Company data, Shaw and Partners analysis

- Based on our estimates across revenues and conservative operating expenses, we **anticipate FZO reaching maiden underlying EBITDA positive in FY24e ($8m)**.
- Broadly we expect to see **significant operating leverage across the employee base, with the combined entity now employing >300 heads after adding 113 from Smoothwall**.
- Based on our modelling, we continue to hold the view that **FZO has the potential to deliver ~50% underlying EBITDA margins** in the long term whilst continuing to grow ARR and revenues.

Refreshed company overview and product

- The core strategy of FZO continues to be seeking to support and protect every child's digital journey.
- After the acquisition of Smoothwall, FZO commands a market leading proposition across a variety of products in both the B2B and B2C space predominantly across the US and UK.
- Our forecasts and expectations are now materially de-risked given the opportunity to cross-sell and up-sell through a larger student base (~9m students vs 2.4m previously), broadened product set (in particular a leading Monitoring tool) and geographic expansion and diversification.

Figure 10: Company overview and markets post-Smoothwall acquisition

		Filtering	Classroom	Monitoring	Parental Controls
	Product	Core filtering and compliance tool typically sold under "Linewize" in the US.	Classroom visibility and control tool typically sold under "Classwize".	Real-time, proactive, AI driven digital monitoring tool typically sold under "Monitor" in the UK.	Management of access limits, and study time with reporting and alerts for families in the home.
	Function	Dashboard/reporting controls used by IT teams to control school content environment.	Monitor screens in classrooms and control content for maximum teaching efficiency.	Safeguard against cyberbullying, self-harm and more with keylogging, screen capturing.	Protect devices on home network and beyond, including app restriction and time limits.
	Channel	B2B	B2B	B2B	B2C
	ARPU per student (per company, AUD)	$3 - $5	$3 - $7	$4 - $12	$112 - $144
Penetration	**US**	~5.2% district market share, rapidly accelerating. Mandated under CIPA legislation.	Sold as add-on with penetration and functionality rising, augmented by NetRef.	No presence as yet, significant opportunity to cross-sell Smoothwall Monitor.	Launch underway, significant growth opportunity with large ARPU and zero CAC.
Penetration	**UK (Smoothwall)**	Dominant market share with 38% of schools.	Significant cross-sell opportunity given minimal penetration into school base.	Leader and mandated under KCSIE legislation.	No presence under Smoothwall, opportunity to cross-sell FZO product over time.
	Company target	Continue to take market share, cross-sell/up-sell complementary products.	50% take-up of Smoothwall (UK) schools in medium term.	50% take-up of K-12 US districts in medium term.	10% parent take-up in the medium term.

Source: Company data, Shaw and Partners analysis

Key assumptions and financials

In general, we model FZO on a quarterly basis over ~10 financial years. We utilise several drivers based upon number of schools, students and ARPU to generate our financial forecasts.

Figure 11: Key assumptions and forecasts

	1H21 Dec20	2H21 Jun21	FY21 Jun21	1H22e Dec21	2H22e Jun22	FY22e Jun22	1H23e Dec22	2H23e Jun23	FY23e Jun23	1H24e Dec23	2H24e Jun24	FY24e Jun24
Core drivers												
ARR by product												
Filtering + Classroom	$10.0m	$14.1m	**$14.1m**	$43.8m	$48.6m	**$48.6m**	$52.9m	$57.8m	**$57.8m**	$65.2m	$69.4m	**$69.4m**
Parental Controls	-	-	-	$1.1m	$2.7m	**$2.7m**	$5.3m	$8.8m	**$8.8m**	$11.1m	$13.8m	**$13.8m**
Monitoring + Data	-	-	-	$6.1m	$6.4m	**$6.4m**	$6.6m	$6.9m	**$6.9m**	$7.1m	$7.3m	**$7.3m**
Total ARR	**$10.0m**	**$14.1m**	**$14.1m**	**$51.0m**	**$57.7m**	**$57.7m**	**$64.8m**	**$73.4m**	**$73.4m**	**$83.3m**	**$90.4m**	**$90.4m**
ARR growth	*72%*	*74%*	***74%***	*410%*	*309%*	***309%***	*27%*	*27%*	***27%***	*28%*	*23%*	***23%***
ARPU by product												
Filtering + Classroom	$6.6	$5.9	**$5.9**	$4.7	$4.7	**$4.7**	$4.7	$4.7	**$4.7**	$5.0	$5.0	**$5.0**
Parental Controls	-	-	-	$100.0	$100.0	**$100.0**	$100.0	$100.0	**$100.0**	$100.0	$100.0	**$100.0**
Monitoring + Data	-	-	-	$4.0	$4.0	**$4.0**	$4.0	$4.0	**$4.0**	$4.0	$4.0	**$4.0**
Blended ARPU	**$6.6**	**$5.9**	**$5.9**	**$5.5**	**$5.6**	**$5.6**	**$5.8**	**$6.0**	**$6.0**	**$6.4**	**$6.5**	**$6.5**
Students contracted												
US students contracted	1.2m	2.1m	**2.1m**	3.6m	4.5m	**4.5m**	5.3m	6.3m	**6.3m**	6.9m	7.7m	**7.7m**
UK students contracted	0.0m	0.0m	**0.0m**	5.4m	5.5m	**5.5m**	5.6m	5.7m	**5.7m**	5.7m	5.8m	**5.8m**
Aus, NZ, Canada students contracted	0.3m	0.3m	**0.3m**	0.3m	0.3m	**0.3m**	0.4m	0.4m	**0.4m**	0.4m	0.4m	**0.4m**
Total students contracted	**1.5m**	**2.4m**	**2.4m**	**9.3m**	**10.3m**	**10.3m**	**11.3m**	**12.3m**	**12.3m**	**13.0m**	**13.9m**	**13.9m**
Students contracted growth	*145%*	*164%*	***164%***	*519%*	*331%*	***331%***	*21%*	*19%*	***19%***	*16%*	*13%*	***13%***
Financials												
Profit and loss												
Sales revenue	$4.4m	$4.6m	**$9.0m**	$16.9m	$24.5m	**$41.4m**	$29.3m	$31.1m	**$60.4m**	$37.8m	$39.1m	**$76.9m**
Gross profit	$1.6m	$1.6m	**$3.2m**	$11.5m	$17.2m	**$28.6m**	$21.1m	$23.0m	**$44.1m**	$28.8m	$30.5m	**$59.2m**
Underlying EBITDA	($7.7m)	($12.0m)	**($19.7m)**	($8.1m)	($5.5m)	**($13.6m)**	($2.8m)	($2.2m)	**($4.9m)**	$3.3m	$4.8m	**$8.1m**
Underlying NPAT	($9.3m)	($13.2m)	**($22.5m)**	($9.6m)	($8.3m)	**($17.9m)**	($5.1m)	($5.1m)	**($10.3m)**	$0.4m	$2.0m	**$2.4m**
Cashflow												
Operating cashflow	($3.5m)	($12.1m)	**($15.6m)**	($5.4m)	($6.8m)	**($12.2m)**	$17.0m	($13.2m)	**$3.8m**	$27.3m	($3.5m)	**$23.8m**
Free cashflow	($4.4m)	($13.4m)	**($17.7m)**	($154.4m)	($9.8m)	**($164.2m)**	$14.0m	($16.2m)	**($2.2m)**	$24.3m	($6.5m)	**$17.8m**
Balance sheet												
Cash balance	$25.9m	$34.9m	**$34.9m**	$26.9m	$17.2m	**$17.2m**	$31.2m	$15.0m	**$15.0m**	$39.3m	$32.8m	**$32.8m**
Contributed equity	$82.8m	$106.1m	**$106.1m**	$252.5m	$252.5m	**$252.5m**	$252.5m	$252.5m	**$252.5m**	$252.5m	$252.5m	**$252.5m**
Growth and margins												
Growth rates (YoY)												
Sales revenue growth	85%	68%	**76%**	284%	436%	**362%**	74%	27%	**46%**	29%	26%	**27%**
Underlying EBITDA growth	(32%)	(73%)	**(55%)**	(6%)	54%	**31%**	66%	61%	**64%**	na	na	**na**
Margins												
Gross profit margin	36%	36%	**36%**	68%	70%	**69%**	72%	74%	**73%**	76%	78%	**77%**
Underlying EBITDA margin	(176%)	(262%)	**(220%)**	(48%)	(22%)	**(33%)**	(9%)	(7%)	**(8%)**	9%	12%	**10%**

Source: Company data, Shaw and Partners analysis

Valuation

- In undertaking our valuation, we rely upon an equal weighting of:
  1) Target ARR multiple having regard to our comparable company analysis with respect to ASX-listed companies – output of $1.04 per share.
  2) Cashflow based valuation through a discounted cash flow (DCF) model – output of $0.96 per share.
- **The net result of our equal-weighted valuation methodologies is a 12-month Price Target of $1.00 per share (+30% on our prior Price Target of $0.77 per share).**

Target ARR multiple (comparable peers' analysis)

- We present below a domestic comparable peers table across a diverse range of sectors and characteristics, with a focus on the core ARR metric.
- We note that FZO trades at an EV/ARR of 12.4x which is broadly in line with the peer set average, however in our view has significantly greater growth prospects, especially in the context of growth in market share (globally), product expansion and cross-sell opportunities in the US and UK.
- The Nasdaq Emerging Cloud Index trades on average revenue multiple of 23.0x which is a material premium to our generally high quality ASX-listed peer set (*source: BVP*).

Figure 12: Peers table

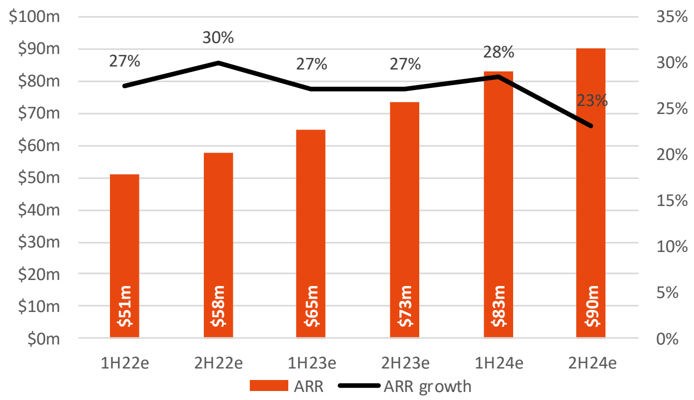
Company	Sector / focus	Last price	Market cap	EV	EV/ARR			EV/Sales			EV/EBITDA		
					Latest	FY+1	FY+2	FY	FY+1	FY+2	FY	FY+1	FY+2
Family Zone[1]	**Cyber safety software**	**$0.78**	**$550m**	**$515m**	**11.7x**	**8.9x**	**7.0x**	**36.5x**	**8.9x**	**7.0x**	**na**	**na**	**na**
9 Spokes	Data mgmt software	$0.01	$19m	$11m	2.6x			2.1x	1.3x	1.0x	na	na	na
Altium[1]	Software solutions	$32.93	$4.3bn	$4bn	29.1x			16.9x	14.3x	12.2x	51.0x	40.6x	34.3x
Bigtincan	Sales and marketing	$1.37	$746m	$713m	13.4x			9.1x	6.6x	5.4x	na	na	na
Catapult	Sports solutions	$1.96	$452m	$415m	7.8x			3.8x	3.5x	2.9x	112.0x	na	40.6x
Class[1]	SMSF software	$1.90	$236m	$231m	4.6x			4.6x	3.9x	3.5x	11.6x	10.1x	9.1x
Damstra[1]	Workforce mgmt	$0.91	$170m	$160m	4.6x			6.0x	4.8x	3.8x	145.7x	19.7x	13.7x
Dropsuite[1]	Data backup solutions	$0.20	$132m	$130m	11.8x			17.3x	7.2x	4.6x	na	88.5x	25.5x
Dubber[1,2]	Call recording software	$3.99	$1.2bn	$1.2bn	30.3x			45.3x	26.2x	17.5x	na	na	165.4x
Elmo[1]	HR technology	$5.10	$456m	$427m	5.1x			6.1x	4.8x	3.9x	na	308.3x	53.5x
FINEOS[1]	Software solutions	$4.40	$1.3bn	$1.3bn	18.3x			7.5x	6.4x	5.7x	130.3x	59.0x	39.8x
ImExHS	Healthcare software	$1.38	$42m	$36m	2.8x			3.0x	2.1x	1.2x	na	na	5.5x
IRESS[1]	Fintech software	$14.53	$2.8bn	$3bn	5.8x			5.5x	4.8x	4.5x	22.7x	20.3x	18.5x
LiveHire	HR technology	$0.37	$109m	$91m	22.0x			16.9x	11.1x	6.1x	na	na	na
LiveTiles	HR technology	$0.15	$132m	$133m	2.1x			2.5x	na	na	na	na	na
Mach7	Healthcare software	$0.99	$233m	$218m	20.8x			11.2x	7.4x	5.3x	na	49.6x	16.1x
Megaport	Software solutions	$18.00	$2.8bn	$2.6bn	29.0x			34.1x	24.2x	17.0x	na	1195.0x	93.1x
MSL Solutions	Sales and marketing	$0.24	$78m	$76m	4.4x			3.3x	na	na	23.1x	na	na
Nearmap	Software solutions	$2.04	$1bn	$935m	8.8x			7.7x	6.5x	5.3x	36.8x	40.2x	21.9x
Nitro[1]	Software solutions	$3.42	$682m	$558m	16.5x			10.0x	7.9x	6.1x	na	na	na
PayGroup	HR technology	$0.46	$53m	$41m	1.5x			1.5x	1.3x	na	19.2x	6.1x	na
RightCrowd	Workforce mgmt	$0.29	$75m	$68m	8.5x			3.7x	na	na	na	na	na
RPMGlobal	Mining solutions	$1.85	$425m	$412m	18.8x			5.8x	4.9x	4.2x	210.0x	47.2x	20.7x
Technology One[1]	Software solutions	$11.19	$3.6bn	$3.4bn	14.6x			11.6x	10.0x	9.1x	30.3x	25.3x	22.4x
Whispir[1]	Telco software	$2.31	$270m	$230m	4.3x			4.3x	4.2x	3.5x	na	na	na
Xero	Accounting software	$153.76	$22.8bn	$22.7bn	23.6x			28.9x	17.1x	14.1x	125.4x	82.7x	61.2x
Peers													
Average					12.4x			10.7x	8.2x	6.5x	76.5x	142.3x	40.1x
Median					8.8x			6.1x	6.4x	5.3x	43.9x	43.9x	23.9x
FZO premium/(discount) to peers													
Premium/(discount) to average					(5.9%)			240.2%	8.8%	7.5%	na	na	na
Premium/(discount) to median					33.3%			502.1%	38.7%	33.2%	na	na	na

Source: FactSet consensus estimates, company announcements, Shaw and Partners analysis.

Notes: [1] Under coverage by Shaw and Partners; [2] Shaw and Partners currently restricted on DUB post-capital raising, estimates are pre-update.

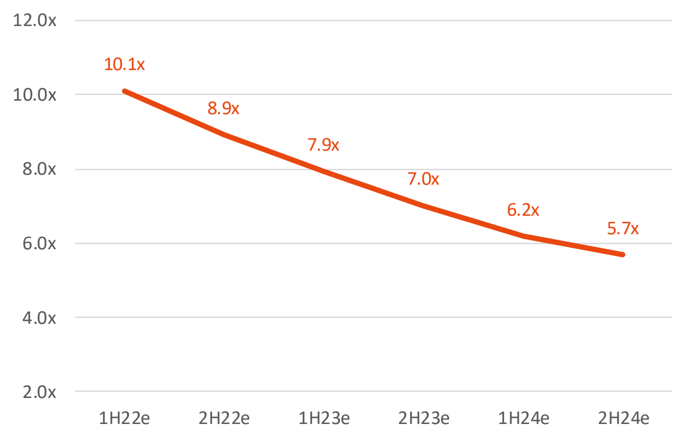
- Further, we expect FZO to de-lever its EV/ARR multiple over time and forecast a multiple of 8.9x at the end of FY22e and 7.0x at the end of FY23e, which would likely see the company trading at a material discount to peers in our view.
- We also expect an acceleration in ARR growth over time versus the core business, even off a larger base as penetration in Classroom and Monitoring products rises.

Figure 13: ARR and ARR growth



Source: Company data, Shaw and Partners analysis

Figure 14: EV/ARR de-levering over time



Source: Company data, Shaw and Partners analysis

- We have applied what we view to be a conservative ARR multiple of 10.0x (versus ASX peers on 12.4x and Nasdaq Emerging Cloud peers on 23.0x) against FY25e ARR of $115m, discounted at our WACC of 11.7% to produce our valuation of $1.04 per share on a fully diluted basis.

Figure 15: Target ARR assumptions and output

Variable	Value
FY25e ARR	$115m
Target ARR multiple	10.0x
Enterprise value (EV)	**$1,145m**
Net (debt)/cash	$53m
Fully diluted shares	753m
Value per share	$1.59
Time	3.8 years
WACC	11.7%
Valuation (per share)	**$1.04**

Source: Shaw and Partners analysis

Discounted cash flow (DCF)

- We undertake ~10 years of financial forecasts and apply a terminal value to our valuation to form our DCF output to produce our valuation of $0.96 per share.
- We expect that FZO has the potential to deliver 50%+ EBITDA margins at scale and present our DCF key assumptions and output below figures.

Figure 16: DCF assumptions and output

Variable	Value
Cost of equity	13.0%
Cost of debt (post tax)	5.3%
WACC	**11.7%**
Inflation	2.5%
Terminal growth rate	2.5%
Operational NPV	$706m
Net (debt)/cash	$17m
Total NPV	$722.9m
Fully diluted shares on issue	753.0m
Valuation (per share)	**$0.96**

Source: Shaw and Partners analysis

Cross-check valuation (ex-growth)

- As a cross check to our primary valuation methodologies, we have also conducted analysis of FZO at scale (ex-growth), utilising target contracted students, gross and EBITDA margins and a consistent capitalisation earnings multiple of 25.0x.
- At our assumed 25.0x EBITDA multiple (more than supported by our comparable analysis above and a suitable multiple in our view for a relatively mature SaaS company producing high GMs and EBITDA margins) and discounted at our WACC of 11.7%, we arrived at a spectrum of fully diluted NPV valuations per share as follows:
  - **Low case:** $0.91 and marginally above current trading.
  - **Mid case:** $1.29 and well ahead of our current Price Target.
  - **High case:** $1.71 and significantly ahead of our current Price Target.

Figure 17: High level scenario analysis of FZO at scale, ex-growth

	Scenario		
Metric	**Low**	**Mid**	**High**
Assumptions			
Students at maturity	16.0m	18.0m	20.0m
Years to maturity	4 years	5 years	6 years
GP per student	$5.00	$6.00	$7.00
GP at maturity	**$80m**	**$108m**	**$140m**
GP margin	75%	80%	85%
Data and hosting costs	($27m)	($27m)	($25m)
EBITDA margin	40%	50%	60%
Operating costs	($37m)	($41m)	($40m)
EBITDA	**$43m**	**$68m**	**$100m**
Valuation			
EBITDA multiple (ex-growth)	25.0x	25.0x	25.0x
WACC	11.7%	11.7%	11.7%
EBITDA multiple valuation	$1,067m	$1,688m	$2,491m
NPV valuation	$686m	$972m	$1,285m
Fully diluted shares	*753.0m*	*753.0m*	*753.0m*
NPV (price per share)	**$0.91**	**$1.29**	**$1.71**

Source: Company data, Shaw and Partners analysis

Estimate revisions

- As a result of the Smoothwall acquisition, significant cross-sell opportunity, capital raising and FY21 results, we have revisited our forecasts and provide our changes below.
- Our students contracted increases by 6.2m, 6.3m and 6.4m across FY22e – FY24e respectively as a result of the significant student acquisition mainly in the UK.
- Our ARR increases by 130%, 79% and 61% across FY22e – FY24e respectively, as the number of students, product penetration and cross-sell opportunity rises.

Figure 18: Estimate revisions

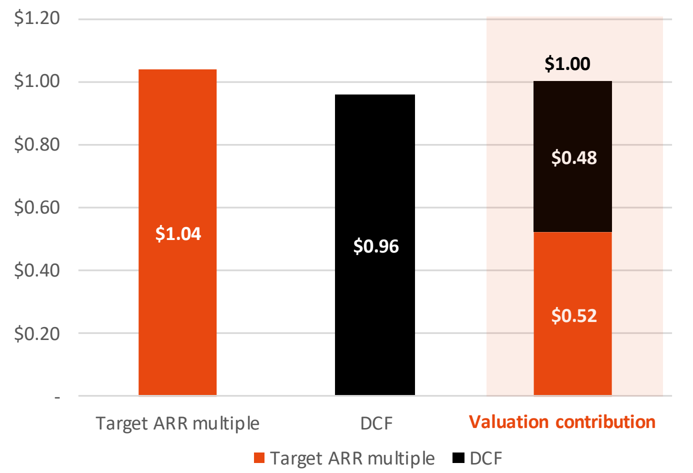
	FY22e			FY23e			FY24e		
Metric	**Old**	**New**	**Change**	**Old**	**New**	**Change**	**Old**	**New**	**Change**
Students contracted	4.1m	**10.3m**	153%	6.0m	**12.3m**	105%	7.5m	**13.9m**	85%
ARR	$25.1m	**$57.7m**	130%	$41.0m	**$73.4m**	79%	$56.3m	**$90.4m**	61%
Sales revenue	$22.3m	**$41.4m**	85%	$36.2m	**$60.4m**	67%	$50.9m	**$76.9m**	51%
Underlying EBITDA	($6.1m)	**($13.6m)**	(123%)	$3.7m	**($4.9m)**	na	$14.5m	**$8.1m**	(44%)
Underlying NPAT	($7.5m)	**($17.9m)**	(138%)	$2.5m	**($10.3m)**	na	$13.5m	**$2.4m**	(82%)

Source: Company data, Shaw and Partners analysis

Valuation change

- As a result of our estimate revisions and utilising an equal weighted target ARR multiple and DCF methodologies, we make revise our 12-month Price Target to $1.00 per share from our prior Price Target of $0.77 per share (+30%).

Figure 19: Price Target buildup



Source: Shaw and Partners analysis

Figure 20: Price Target changes

Methodology	Output	Weight	Contribution
Target ARR multiple	$1.04	50%	$0.52
DCF	$0.96	50%	$0.48
Valuation (per share)			**$1.00**

Variable	Valuation
Previous Valuation	$0.77
New Valuation	$1.00
Change	**30%**

Source: Shaw and Partners analysis

Core drivers and catalysts

Our investment thesis is driven by the following and should be read in conjunction with our key risks:

Acceleration of student licenses into international markets – FZO is gaining material market share into the large and material US and UK markets. We expect that the acceleration of US and UK ARR is likely to continue and strengthen. Over time we expect FZO market share to grow to north of 10% in the US.

Material above market growth profile to ARR – FZO is likely to have a growth profile to ARR materially above the market. We expect that over the medium to long term FZO ARR has the potential to grow to ~$100m+.

Upside to ARR from further product and market entries – FZO is likely to launch further value-added products into market, particularly within the US and UK. These including Classroom, Monitoring and Parental Control products. Successful expansion and mainstream adoption of these products could result in FZO achieving revenue materially above our estimates.

Structural industry tailwinds driving growth – There is significant tailwinds towards the adoption of public cloud-based products. Further the educational market for cyber protection products for schools and families is large and growing, as government funding allocations to the industry rise. We see these positive industry tailwinds supporting FZO's growth.

Product competitive advantages – FZO has a best in breed solution in our view and is supported by a desire to lead from a technology point of view. With a strong back end, large body of work with integrations and public cloud hosting, FZO's product exhibits significant advantages over competitors in market.

Potential M&A and inbound interest – FZO may be of potential interest to strategic buyers and is likely to see significant interest as the company gains US market share. There are several modern and legacy companies that provide cyber products targeted at educational and family markets, and there may be an opportunity for FZO to be an active consolidator in the market.

Key risks

Risks to our investment thesis include although are not limited to:

Technological change – We see FZO's application as purpose built and technologically competitive with other products in market. However, this may not always be the case due to technological changes. These changes may lead to a requirement for FZO to redevelop its products in order to meet dynamic customer requirements. We flag that FZO must continue to invest in value added services and other products to overlay on its core filtering product.

Competition – Whilst FZO's product is one of several available in its key markets, new competition or intensified competition from existing operators may result in margin erosion, or even a loss of existing contracts.

Growth aspirations – FZO has global ambitions and has attained a level of penetration amongst schools in the US, Australia, New Zealand and the UK. The company has ambitions to continue to grow materially and deliver a step change in growth. There is no guarantee that FZO has the team in place or skills to navigate its growth aspirations.

M&A integration – Given FZO's acquisitive nature, there is a risk that such acquisitions are unsuccessfully integrated into the group, or do not perform in line with management expectations.

Key board and management risk – FZO's CEO is a co-founder of the business and one of the largest shareholders of the group. Failure to retain and grow executive talent may adversely impact the group's growth. Moreover, this risk is elevated for businesses experiencing material growth over a short time horizon, such as FZO.

Cash burn – FZO has historically delivered negative cash flows and is forecast to reach positive cash flows in FY23. There is risk that positive cashflow is not achieved in line with forecast, and companies that have negative cash flows typically exhibit greater volatility and there is no guarantee that FZO will be able to continue financing the business or that the group will reach profitability.

Data failure – FZO utilises cloud-based storage for the majority of school and student data. However, FZO may experience hacking or stolen information that could adversely affect the operations and reputation of the group.

Churn, stickiness, and LTV – FZO is still at the inception of growth and its customer base. Currently the group exhibits relatively low churn and a consistently growing user base. There is no guarantee that these users will continue with the group. Higher churn may in turn decrease the total LTV of FZO, which may impact valuation considering FZO is likely being valued on its ARR and a consistent growth trajectory.

International operations – The company offers products and services via the cloud, but services these operations through sales and support across multiple countries across several geographic regions. As such FZO is subject to an elevated level of currency, execution and cost risk.

Small cap liquidity and volatility – As a small cap company, FZO exhibits higher levels of volatility and lower liquidity than the broader market in general. This beta is magnified during periods of market upheaval, such as the current COVID environment.

Revenues and cash flows – FZO delivers products and services predominantly to schools, students and parents globally. As such, FZO may from time to time see delays to cash flows or potential differences to revenue recognition from ARR stemming from various revenue profiles of its income streams. This is likely to be magnified through periods of extreme user growth wherein POC or trial periods are not immediately billed.

COVID – We view COVID as a far-reaching global event that has caused a global recession and material upheaval across all markets, products and services. Whilst COVID has been a change event and positive for FZO in our view, the pandemic elevates the risk profile of all listed companies. Further, FZO has experienced a step change of user growth associated with COVID and this demand may subside in a more normalised economic environment.

Rating Classification

Buy	Expected to outperform the overall market
Hold	Expected to perform in line with the overall market
Sell	Expected to underperform the overall market
Not Rated	Shaw has issued a factual note on the company but does not have a recommendation

Risk Rating

High	Higher risk than the overall market – investors should be aware this stock may be speculative
Medium	Risk broadly in line with the overall market
Low	Lower risk than the overall market

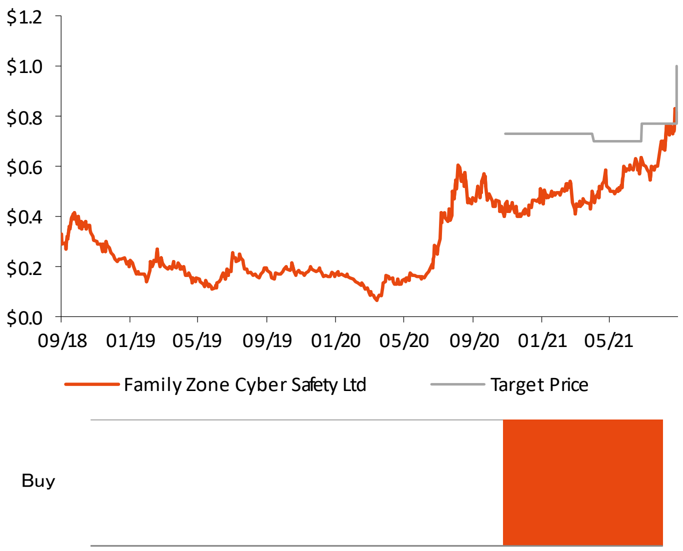
RISK STATEMENT: Where a company is designated as 'High' risk, this means that the analyst has determined that the risk profile for this company is significantly higher than for the market as a whole, and so may not suit all investors. Clients should make an assessment as to whether this stock and its potential price volatility is compatible with their financial objectives. Clients should discuss this stock with their Shaw adviser before making any investment decision.

Distribution of Investment Ratings

Rating	Count	Recommendation Universe
Buy	75	82%
Hold	15	16%
Sell	1	1%

History of Investment Rating and Target Price - Family Zone Cyber Safety Ltd

Date	Closing Price ($)	Target Price ($)	Rating
6-Sep-21	0.81	1.00	Buy
6-Jul-21	0.63	0.77	Buy
12-Apr-21	0.47	0.70	Buy
6-Nov-20	0.45	0.73	Buy



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