

# KAPE TECHNOLOGIES

## SOFTWARE AND COMPUTER SERVICES

12 September 2022

### KAPE.L

259p

Market Cap: £931.1m

#### SHARE PRICE (p)



12m high/low

455p/256p

Source: LSE Data (priced as at prior close)

#### KEY DATA

Net (Debt)/Cash	\$(391.1)m (at 30/06/22)
Enterprise value	£1216.6m
Index/market	AIM
Next news	Trading update, Jan. '23
Shares in Issue (m)	359.5
Chairman	Don Elgie
Chief Executive	Ido Erlichman
CFO	Oded Baskind

#### COMPANY DESCRIPTION

Kape is a cyber security company focused on digital privacy and protection.

[www.kape.com](http://www.kape.com)

KAPE TECHNOLOGIES IS A RESEARCH CLIENT OF PROGRESSIVE

#### ANALYSTS

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## The growth charge continues

Kape's Interim Results for the 6 months to 30 June published today follow the Trading Update in July and are comfortably in line with full-year expectations. Strong cash generation, coupled with revenue growth of 217% and 210% pro forma Adj EBITDA growth, is consistent with the update, and management remains confident of full-year results in line with market expectations. We are towards the lower end of the range and continue to see risk to forecasts on the upside.

- **Digital Privacy – ExpressVPN – an exceptional deal** 19% pro forma revenue growth in privacy is a result not just of new customers but also of material upsell. The costs savings anticipated are coming through, and this earnings accretive deal has not only transformed Kape as an operating business, but also transformed its scale and standing within the consumer digital security and privacy industry.
- **Digital Content - 25% pro forma revenue growth.** Growth is being delivered both in mature verticals and now via substantial expansion into new verticals. This is in addition to the contribution of skills and knowhow across the broader group.
- **Guidance and forecasts unchanged.** Management has maintained its guidance for FY22 (revenues range \$620m-\$624m and pro forma Adjusted EBITDA range \$166m - \$172m). Our forecasts are towards the lower end of these ranges and the strong H1 adds to our belief that risks to our forecasts are clearly on the upside.
- **Back on the deal trail?** We had previously expected that 2022 might be a year of 'consolidation', however, it is clear from the results statement that management are anxious to maintain the strategic momentum.

The Kape investment case is not just about the dynamic growth of the digital privacy and security industries. It is about management's ability to identify both organic and acquisition driven growth and to execute. The ExpressVPN and Webselense deals demonstrate this capability. Management have delivered considerable revenue growth and the execution on the cost savings process is also working well. Trading on a current year P/E of 9.0 and with market growth, scale benefits, and cost savings, and potential for more deals all available to drive earnings growth in the short, medium and long-term, we question whether the market has understood the scale and speed of Kape's ambition and potential.

FYE DEC (\$M)	2019	2020	2021	2022E	2023E
Revenue	66.1	122.2	230.7	615.5	699.6
Adjusted EBITDA	14.6	39.0	86.0	167.7	190.2
Adjusted PBT	10.6	30.8	75.2	158.5	180.9
Adjusted Dil EPS (c)	6.5	13.5	23.1	39.1	44.6
EV/Sales	25.2x	13.6x	7.2x	2.7x	2.4x
EV/ Adj. EBITDA	114.5x	42.8x	19.4x	9.9x	8.8x
P/E	54.9x	26.2x	15.3x	9.1x	8.0x

Source: Company Information and Progressive Equity Research estimates.

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Please refer to important disclosures at the end of the document.

## The growth charge continues

### H1 2022 – in line with trading update, but perhaps under-appreciated

H1 2022 revenues of \$302.4m were 217% above those in H1 2021, 19% more on a pro forma organic basis, and within this 89% was on a recurring basis. The pro forma adjusted EBITDA of \$88.9m was 210% more than H1 2021 – and 17% up on a pro forma basis. Diluted Adjusted EPS increased by 279% to 34.1c (H1 2021 9c). With the balance sheet settling down post the acquisitions the net debt figure was \$391.1m (vs \$475.5m at 31 Dec 2021) and the H1 2022 cashflow from operations was \$90.1m – a 101% conversion from pro forma Adjusted EBITDA. As noted above, following the trading update in July the market expected these results and this growth trajectory – but the P/E and strident statement suggest that the market might not fully appreciate or understand this performance.

#### H1 2022 Segment revenues and results

	Revenue		Segment result	
	H1 2022	H1 2021	H1 2022	H1 2021
	\$m	\$m	\$m	\$m
<b>Privacy*</b>	253.5	49.6	129.7	27.7
<b>Security</b>	21.4	18.5	7.9	6.7
<b>Content</b>	27.5	27.5	4.5	12.1
<b>Total</b>	302.4	95.5	142.2	46.5

Source: Kape

\*Privacy Segment result is adjusted for deferred contract expenses related to ExpressVPN acquisition

### Digital Privacy (84% group revenue H1 2022)

The 412% increase in revenues H1 2022 vs H1 2021 was principally driven by the acquisition of ExpressVPN in December 2021 for \$926m, augmented by strong year-on-year organic growth. The 19% pro forma revenue growth in Digital Privacy is a result not just of new customers but also upsell. The costs savings anticipated with the acquisition are coming through. Perhaps even more importantly, this earnings accretive deal has not only transformed Kape as an operating business, it has transformed the group in terms of scale and standing within the consumer digital security and privacy industry.

The statement shows that Kape is on course to realise \$9m in synergies by the end of the year from bringing its Privacy businesses together and that it is on course to achieve the \$30m anticipated savings in FY22. These cost savings are coming across the business – in customer support, R&D and marketing. Furthermore the gains are not just in basic direct costs, there are gains to be main from better management and coordination of brands to yield reductions to customer acquisition costs and even stronger growth.

### **Digital Content (7% group revenue H1 2022)**

Webselenese's revenues of \$27.5m showed 25% pro forma revenue growth on H1 2021. The acquisition of Webselenese in March '21 was a move into a parallel market that gave Kape increased exposure to its end customers. The deal provides the group better insights into the consumers in the digital privacy and security spaces, as well as enhanced understanding of digital marketing organic channels. Content businesses are not software businesses, but Kape's management have demonstrated that they can both grow the content business and use its knowhow to reduce customer acquisition costs across a range of the group's product segments. In these ways, Webselenese provides insight, potential customers, and lower customer acquisition costs across the business. Kape's content reaches more than 120m unique readers each year – a huge potential market for Kape's products, both current and future.

Moves into new verticals were a primary driver to the revenue growth, although as new markets these have suppressed the overall segment margins – initial investment has been required to set up these new verticals, and we expect margins to widen as these segments mature.

### **Digital Security (9% group revenue H1 2022)**

The Security segment saw revenue growth of 15.7% vs H1 2021 to \$21.4m. This segment has demonstrated growth over the past two years, primarily through the expansion of Intego as a fully subscription-based offering. The long term fundamentals and attractions remain firmly in place. Key factors in this growth included nearly 20% growth in Intego's endpoint security products and 15% improvement for PC performance products.

### **More than just marketing and cost savings that drive growth**

Whilst the growth figures may grab our attention and comments on cost savings confirm our view on management, the statement also reminds us that Kape continues to launch new products, develop new solutions and invest in servers to ensure that its customers get the speed and resilience of VPN service they expect.

### **Confident management, guidance unchanged, forecasts left alone**

Management has maintained its guidance for FY22 (revenues range \$620m-\$624m and pro forma Adjusted EBITDA range \$166m - \$172m). Our forecasts are towards the lower end of these range and the risks to our forecasts are clearly on the upside, but for now we look to the investor and analyst presentations as opportunities to understand more about the drivers to growth and just how far and in which directions this ambitious team go.

### **Back on the M&A trail?**

We had previously expected that, following two transformational deals in 2021, 2022 might be a year of what is often described as 'consolidation'. However, it is clear from the results statement that management are anxious to maintain the strategic momentum. The comment of Ido Erlichman, the CEO, that 'Our growing profitability and the sheer scale of our customer base combined with the current market conditions pose a prime opportunity for Kape on the M&A front' leaves us in no doubt. Management want 2022 to be a year of further strategic progress, not just one of operational and financial development.

### Conclusion

The Kape investment case is not just about the dynamic growth of the digital privacy and security industries. It is about the management's ability to identify both organic and acquisition driven growth and to execute. The ExpressVPN and Webselenese deals demonstrate that the group has delivered to date, and we expect that more can be done. Management have driven and enabled considerable revenue growth and the execution on the cost savings process is also working well. Trading on a current year P/E of 9.0 and with market growth, scale benefits, and cost savings, as well as the potential for more deals all available to drive earnings growth in the short, medium and long-term, we question whether the market has understood the scale and speed of Kape's ambition and potential.

**Financial Summary: Kape Technologies**

Year end: December (\$m unless shown)

	2019	2020	2021	2022E	2023E
<b>PROFIT &amp; LOSS</b>					
Revenue	66.1	122.2	230.7	615.5	699.6
Adj EBITDA	14.6	39.0	86.0	167.7	190.2
Adj EBIT	11.9	34.1	81.7	162.5	184.9
Reported PBT	2.8	7.3	44.6	80.2	102.7
Fully adj PBT	10.6	30.8	75.2	158.5	180.9
NOPAT	11.1	31.9	73.5	146.2	166.5
Reported Dil EPS (c)	1.7	14.8	14.2	19.8	25.3
Fully adj Dil EPS (c)	6.5	13.5	23.1	39.1	44.6
Dividend per share (c)	0.0	0.0	0.0	0.0	0.0
<b>CASH FLOW &amp; BALANCE SHEET</b>					
Operating cash flow	(1.7)	37.6	77.2	144.6	256.5
Free Cash flow (\$m)	(5.4)	8.4	(389.3)	(40.3)	71.6
FCF per share (c)	(3.6)	4.2	(156.4)	(11.0)	19.6
Acquisitions	(64.3)	(58.5)	(165.1)	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	0.0	113.2	348.4	0.0	0.0
Net cash flow	(70.9)	45.7	(209.2)	(40.3)	71.6
Overdrafts / borrowings	(40.2)	(38.8)	(117.4)	(110.7)	(104.0)
Cash & equivalents	8.2	49.9	27.0	0.0	64.9
Net (Debt)/Cash	(32.0)	11.1	(90.4)	(110.7)	(39.1)
<b>NAV AND RETURNS</b>					
Net asset value	155.0	228.8	863.4	1,167.7	1,260.1
NAV/share (c)	99.2	102.9	240.7	325.5	351.3
Net Tangible Asset Value	(87.9)	0.8	(621.1)	(1,174.8)	(1,004.3)
NTAV/share (c)	(56.2)	0.4	(173.1)	(327.5)	(279.9)
Average equity	114.0	191.9	546.1	1,015.6	1,213.9
Post-tax ROE (%)	1.8%	15.0%	6.5%	7.1%	7.6%
<b>METRICS</b>					
Revenue growth	26.9%	85.0%	88.7%	166.8%	13.7%
Adj EBITDA growth	40.3%	167.7%	120.8%	94.9%	13.4%
Adj EBIT growth	43.5%	186.8%	139.2%	98.9%	13.8%
Adj PBT growth	28.1%	191.2%	144.4%	110.8%	14.2%
Adj EPS growth	28.8%	109.1%	71.1%	68.8%	14.2%
Dividend growth	N/A	N/A	N/A	N/A	N/A
Adj EBIT margins	18.0%	27.9%	35.4%	26.4%	26.4%
<b>VALUATION</b>					
EV/Sales	25.2	13.6	7.2	2.7	2.4
EV/EBITDA	114.5	42.8	19.4	9.9	8.8
EV/NOPAT	150.5	52.2	22.7	11.4	10.0
PER	54.9	26.2	15.3	9.1	8.0
Dividend yield	N/A	N/A	N/A	N/A	N/A
FCF yield	(1.0%)	1.2%	(44.1%)	(3.1%)	5.5%

Source: Company information and Progressive Equity Research estimates

**Disclaimers and Disclosures**

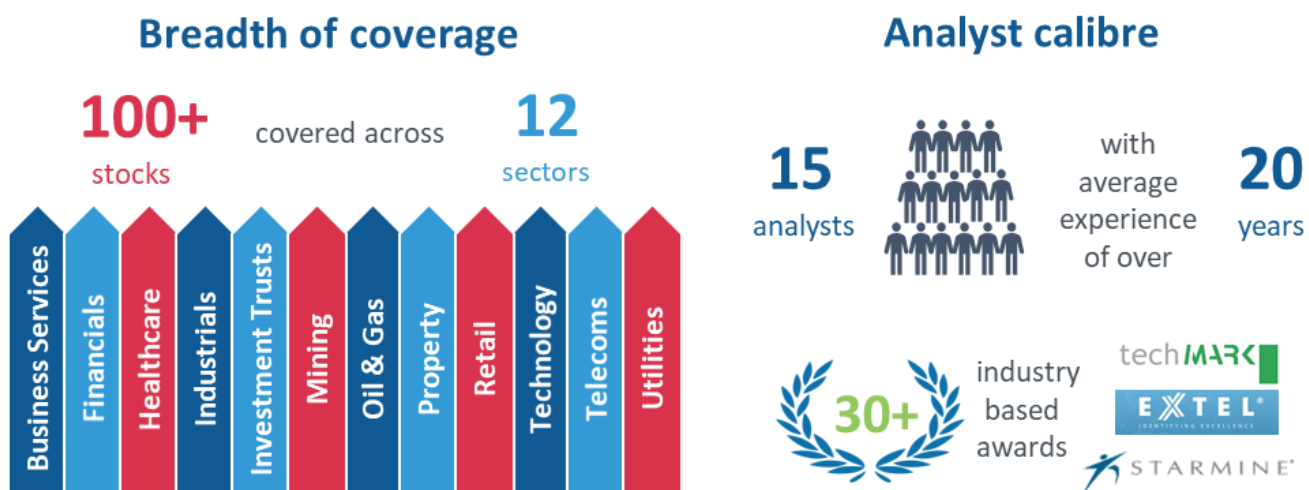
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