

## Family Zone (FZO) | Acquires NZ cyber security company

Rating: **BUY**  
 Target Price<sup>1</sup>: **\$1.34**  
 Projected Return: **57%**

<sup>1</sup> 12 month target

### Company Statistics

Share Price (A\$)	0.855
Market Cap (A\$m)	84.5
Enterprise Value (A\$m)	76.4
Issued Shares (mil)	98.8
Options (mil)	26.9
Cash (A\$m)	8.1
Debt (A\$m)	0.0

### Earnings Summary

FY End (June)	2017	2018e	2019e	2020e
Revenue (A\$m)	1.6	6.0	21.3	37.3
EBITDA (A\$m)	-7.7	-3.5	11.0	20.8
NPAT adj (A\$m)	-8.8	-4.5	10.1	14.1
EV/EBITDA	N/A	N/A	8.0x	3.6x

### Share Price (A¢ps)



### Company Description

Family Zone is a parental control software product aimed at protecting children against inappropriate online content as well as helping parents control the time their children spend on their devices.

#### Analyst

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\*see research dated 09/08/2017

## FZO acquires Linewize

### Investment Summary

Family Zone has announced that it has acquired New Zealand cyber security and safety services company, Linewize.

### Investment Highlights

- Linewize is the leading cyber security and safety services provider in New Zealand with 260 schools and 130k students (out of 2,500 schools and 900k students countrywide)
- The acquisition consists of a NZ\$200k deposit, plus 9.5m FZO shares, plus 9.5m performance shares (subject to shareholder approval). At the current FZO share price of A\$0.855 the deposit and share consideration would value the acquisition price at c.A\$16.5m.
- FZO announced in July that it had entered into a partnership with Linewize to integrate the FZO and Linewize platforms
- Linewize's revenue in FY17 was c.A\$1m, which has grown from c.A\$200k in FY16
- Linewize was founded in 2013 and provides cloud managed fire wall services – primarily for the education sector. FZO believes Linewize's technology is world class.
- FZO expects a technical effort to commence during November
- We have updated our model to now include revenues from NZ, which adjusts our earnings in FY18E/19E/20E by +0.2¢/+0.6¢/+2.3¢
- We expect FZO to secure 200 NZ schools by FY20E, with this lifting by 50 schools in each of FY21E and FY22E.

### Investment Recommendation

**Maintain Buy Rating and increase our 12 month Target Price to \$1.34 (was A\$1.33\*) due to the higher school numbers in ANZ, which is offset by the increased share base.**

Our price target methodology is now based on an FY20E P/Sales multiple of 4.45x. Our target price reflects a 57% premium to the last traded price.

Today we have updated our model for the Linewize deal, which results in changes to our earnings in 18E/19E/20E of +0.2¢/+0.6¢/+2.3¢ to – A4.4¢/+A8.5¢/+A11.7¢.

We model Family Zone on the assumption that it achieves 20,000 consumer direct subscriptions and 120 school sign-ups in ANZ by the start of the 2018 school year. We also assume the company generates c.A\$3.9m in wholesale revenue within Asia by FY19E and A\$2.7m revenue within the US by FY19E. This results in FY19E revenue of A\$21.3m at an EBITDA margin of 52%.

The key risk to our view is competition within the parental control software market (leading to limited sign ups – particularly overseas), as well as cyber-crime.

## Summary Financials

P&L (A\$m)					Balance sheet (A\$m)				
	FY17	FY18E	FY19E	FY20E		FY17	FY18E	FY19E	FY20E
<b>Total Revenue</b>	<b>1.6</b>	<b>6.0</b>	<b>21.3</b>	<b>37.3</b>	Cash & equivalents	1.4	3.1	13.7	28.4
COGS	1.0	6.5	8.3	11.5	Receivables	1.0	7.3	25.9	45.3
Corporate	6.8	3.0	2.0	5.0	Inventory	0.2	0.7	2.4	4.2
Other	1.5	0.0	0.0	0.0	Other	0.0	0.0	0.0	0.0
<b>EBITDA</b>	<b>-7.7</b>	<b>-3.5</b>	<b>11.0</b>	<b>20.8</b>	<b>Total current assets</b>	<b>2.5</b>	<b>11.1</b>	<b>42.0</b>	<b>0.0</b>
D&A	1.1	1.0	1.0	1.1	Net PP&E	0.2	-0.8	-1.3	-1.8
<b>EBIT</b>	<b>-8.8</b>	<b>-4.5</b>	<b>10.0</b>	<b>19.7</b>	Other	4.3	4.0	9.2	92.4
Net interest	0.0	0.1	0.1	0.4	<b>Total non-current assets</b>	<b>4.5</b>	<b>3.3</b>	<b>7.9</b>	<b>90.6</b>
<b>Pretax profit</b>	<b>-8.8</b>	<b>-4.5</b>	<b>10.1</b>	<b>20.1</b>	<b>Total assets</b>	<b>7.1</b>	<b>14.4</b>	<b>49.9</b>	<b>90.6</b>
Tax	0.0	0.0	0.0	6.0	Payables	3.5	10.0	35.4	62.0
Minorities	0.0	0.0	0.0	0.0	Short term debt	0.0	0.0	0.0	0.0
<b>NPAT (adj)</b>	<b>-8.8</b>	<b>-4.5</b>	<b>10.1</b>	<b>14.1</b>	Other	0.2	0.2	0.2	0.2
Abnormal items	0.0	0.0	0.0	0.0	<b>Total current liabilities</b>	<b>3.7</b>	<b>10.2</b>	<b>35.6</b>	<b>62.2</b>
<b>NPAT (rep)</b>	<b>-8.8</b>	<b>-4.5</b>	<b>10.1</b>	<b>14.1</b>	Long term debt	0.0	0.0	0.0	0.0
<b>Ave shares (diluted)</b>	<b>60.1</b>	<b>100.3</b>	<b>119.3</b>	<b>120.3</b>	Other	0.8	0.8	0.8	0.8
EPS adj (A¢)	-14.6	-4.4	8.5	11.7	<b>Total long term liabilities</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>
<b>DPS (A¢)</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>Total liabilities</b>	<b>4.5</b>	<b>11.0</b>	<b>36.4</b>	<b>63.0</b>
					<b>Total common equity</b>	<b>2.6</b>	<b>3.4</b>	<b>13.5</b>	<b>27.6</b>
Cash Flow (A\$m)					Ratios & Valuations				
	FY17	FY18E	FY19E	FY20E		FY17	FY18E	FY19E	FY20E
Cash receipts	1.3	6.0	21.3	37.3	ROE (%)	na	na	75%	51%
Cash payments	-7.4	-9.5	-10.3	-16.5	ROA (%)	na	na	20%	16%
Net interest	0.0	0.1	0.1	0.4	Net debt/equity (%)	na	na	na	na
Tax paid	0.0	0.0	0.0	-6.0	Interest cover - EBIT (x)	na	na	na	na
Other	0.7	0.0	0.0	0.0	P/E (x)	na	na	10.1	7.3
<b>Cash flow from operations</b>	<b>-5.3</b>	<b>-3.5</b>	<b>11.1</b>	<b>15.1</b>	P/B (x)	na	25.5	7.6	3.7
Total capital	0.0	0.0	-0.5	-0.5	EV/EBITDA (x)	na	na	8.0	3.6
Acquisitions	-3.0	0.0	0.0	0.0	Dividend yield (%)	na	0.0%	0.0%	0.0%
Divestitures	0.0	0.0	0.0	0.0	Free cash flow yield (%)	na	na	10%	14%
Other	0.0	0.0	0.0	0.0	Sales growth (%)	na	na	254%	75%
<b>Cash flow from investments</b>	<b>-3.1</b>	<b>0.0</b>	<b>-0.5</b>	<b>-0.5</b>	EBITDA growth (%)	na	na	na	na
Dividends paid	0.0	0.0	0.0	0.0	EPS growth (%)	na	na	na	na
Capital raised	9.1	5.2	0.0	0.0	Gross margin (%)	na	-9%	61%	69%
Repaid debt/borrowed funds	0.0	0.0	0.0	0.0	EBITDA margin (%)	na	-59%	52%	56%
Other	0.0	0.0	0.0	0.0	EBIT margin (%)	na	-75%	47%	53%
<b>Cash flow from financing</b>	<b>9.0</b>	<b>5.2</b>	<b>0.0</b>	<b>0.0</b>					
<b>Total cash flow</b>	<b>0.6</b>	<b>1.7</b>	<b>10.6</b>	<b>14.6</b>					

June year end

Ratios calculated using FZO.AX share price of \$ 0.86

Source: Company data, BW Equities Research estimates

## Updating our model

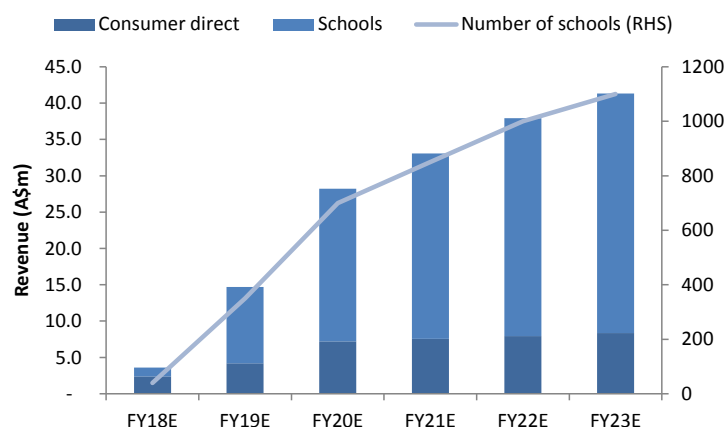
## Upgrading our Australia &amp; NZ estimates

Within Australia, FZO is primarily targeting independent schools to grow its subscription numbers. Of the c.10,000 schools within Australia, c.1,000 are independent schools – and FZO is targeting these independent schools directly.

Within New Zealand all public schools have purchasing discretion within their budget – hence FZO will target all 2,500 schools, not just the private schools.

We model the company's Australia & New Zealand revenue via two streams: (1) consumer direct subscriptions, and (2) school subscriptions. FZO has announced that it has 16,000 consumer direct subscriptions – which we estimate are charged at A\$10/month. The company has also announced that it has signed up 63 schools which have mandated the use by its students. We work off an average of 500 families per school at a cost of A\$5/month per family.

- **We forecast FZO to lift the 16,000 consumer direct subscriptions to 35,000 in FY19E and 60,000 in FY20E.** We then model a 5% growth rate for the following five years (this figure has not changed following the acquisition).
- **We forecast FZO to secure close to 120 mandated schools by the start of the 2018 school year.** We expect the company to grow its mandated school numbers to c.700 schools by FY20E which includes 500 in Australia and 200 in New Zealand.



Source: BW estimates

We have updated our model for the Linewize announcement which results in an increase in school sign ups, offset by the higher share base. We expect the company to make a loss in FY18E before moving to profitability in FY19E. Our earnings changes are summarised below.

	EBITDA (A\$m)			EPS (A¢ps)			DPS (A¢ps)		
	Old	New	Change	Old	New	Change	Old	New	Change
FY17	-7.7	-7.7	0.0	-14.6	-14.6	0.0	0.0	0.0	na
FY18E	-3.5	-3.5	0.0	-4.7	-4.4	0.2	0.0	0.0	na
FY19E	9.5	11.0	1.5	7.9	8.5	0.6	0.0	0.0	na
FY20E	15.4	20.8	5.3	9.4	11.7	2.3	0.0	0.0	na
				Old	New	Change			
DCF Valuation (A\$ps)				\$ 1.05	\$ 1.14	8.6%			
12 mo Price Target (A\$ps)				\$ 1.33	\$ 1.34	0.8%			

Source: BW estimates, Company Data

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