

March 16, 2018

## Qualys, Inc. : QLYS

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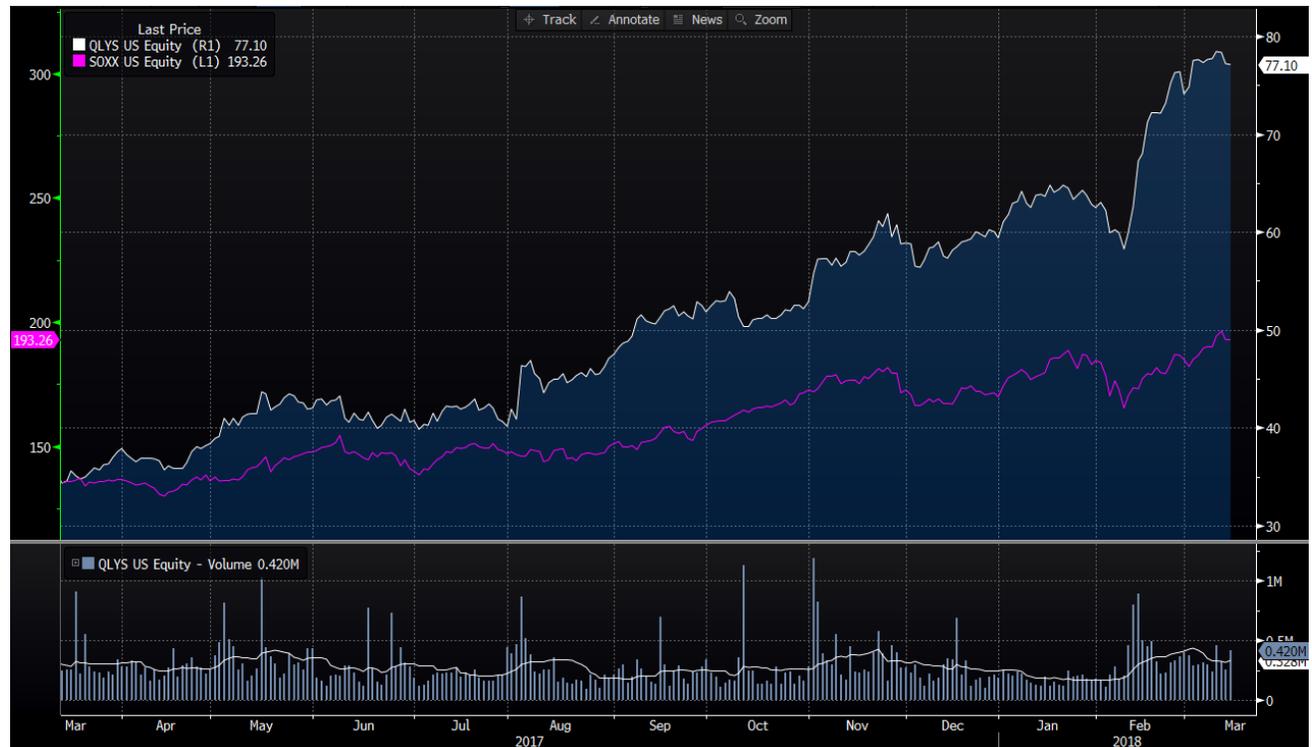
Sector: Information Technology

Industry: Infrastructure Software

Current Price: \$77.10

Target Price: \$95.18

Qualys, Inc. provides cloud-based network security software for organizations in various sectors around the world. The software provides organizations with vulnerability management, automatic network monitoring, IT asset identification, and an overall view of security and compliance across the organizations entire IT infrastructure.



### Buy

Current Price:	\$77.10
Target Price:	\$95.18
Market Cap:	2.9B
Average Volume:	328k
ROE:	12.7%
Ke:	8.18%
52 Week Range:	\$33.85 - \$79.40
TTM EBITDA Margin:	25.18%

### Catalysts:

- Short Term:** Recent acquisitions of relevant cloud technology companies integrating into Qualys current solutions; current domination of market through high value partnerships
- Mid Term:** Advancement of cloud tech through rigorous R&D along with active M&A for further acquisitions
- Long Term:** Worldwide transition into cloud technology deployment

## Thesis:

Qualys Inc. is pioneering cloud based cybersecurity and compliance solutions for the global market. Strategically selected acquisitions are providing Qualys with instant injection of technology that compliments their existing product line and helps push it further. Currently, Qualys is leading the market through their unprecedented reputation through partnerships with major companies such as Microsoft, IBM, CISCO, and AVAYA. The company possesses strong revenue growth while maintaining their margins through effective management and superior product. The cloud technology industry is poised for strong growth in the future; industry growth coupled with strategic acquisitions, high level partnerships, and aggressive forward-looking M&A, Qualys is positioned to generate value in the future.

## Product:

Qualys Inc. offers a plethora of security and compliance solutions to their customers through asset management, IT security, compliance monitoring, and web application security. Asset management is a live view into an organizations global IT assets; IT security ranges from vulnerability management to continuous monitoring of networks; compliance monitoring maintains regulatory IT management; web application security includes scanning of and firewalls for internet activity. Below is a further breakdown of their solutions:

# Qualys Cloud Platform Apps

### ASSET MANAGEMENT

- AI Asset Inventory**  
 Maintain full, instant visibility of all your global IT assets
- SYN CMDB Sync**  
 Synchronize asset information from Qualys into ServiceNow CMDB
- CI Cloud Inventory (Beta)**  
 Inventory of all your cloud assets across AWS, Azure, GCP and others
- CRI Certificate Inventory (Beta)**  
 Inventory of TLS/SSL digital certificates on a global scale

### IT SECURITY

- VM Vulnerability Management**  
 Continuously detect and protect against attacks, anytime, anywhere
- TP Threat Protection**  
 Pinpoint your most critical threats and prioritize patching
- CM Continuous Monitoring**  
 Alerts you in real time about network irregularities
- IOC Indication of Compromise**  
 Continuously monitor endpoints to detect suspicious activity
- CS Container Security (Beta)**  
 Discover, track, and continuously protect containers
- CRA Certificate Assessment (Beta)**  
 Assess all your digital certificates for TLS/SSL vulnerabilities

### COMPLIANCE MONITORING

- PC Policy Compliance**  
 Assess security configurations of IT systems throughout your network
- PCI PCI Compliance**  
 Automate, simplify and attain PCI compliance quickly
- FIM File Integrity Monitoring**  
 Log and track file changes across global IT systems
- SCA Security Configuration Assessment**  
 Automate configuration assessment of global IT assets
- CSA Cloud Security Assessment (Beta)**  
 Get full visibility and control across all public cloud instances
- SAQ Security Assessment Questionnaire**  
 Minimize the risk of doing business with vendors and other third parties

### WEB APPLICATION SECURITY

- WAS Web Application Scanning**  
 Secure web applications with end-to-end protection
- WAF Web Application Firewall**  
 Block attacks and virtually patch web application vulnerabilities

Vulnerability management is the forefront of these technologies that continually scans assets on premise as well as on the cloud at endpoints. There is minimal network impact from VM meaning a high-level of security at an

extremely low efficiency cost. Free trials are offered for potential clients to familiarize them with the company's tech along with free training for current clients. For clients, employing this tech couldn't be easier – there is no software to download, databases to maintain, or servers to put in place; Qualys maintains all of this and the client merely accesses it all through a web browser. The web browser has dashboards on its UI that can search for any IT assets, whether on the premise, cloud, or at endpoints, in two seconds.

Aside from their flagship vulnerability management, Qualys' products are meant to fully secure an entire organization's network. A quote from CISCO's team audit lead Doug Dexter, "We use pretty much every product that Qualys has come out with. I don't think there's a product that Qualys makes that we don't use somewhere." Wholesome IT solutions is the goal for Qualys which is being progressed by internal R&D along with acquisitions of smaller companies that will be discussed further later on.

Products offered by Qualys are normally on an annual subscription service, with another option for small companies on a "pay per scan" basis.

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## Acquisitions:

Qualys recently acquired the assets of NetWatcher and Nevis Networks both in 2017. NetWatcher's technology stack includes solutions for threat intelligence, active monitoring through all on premise, cloud, and endpoint IT assets, insider application vulnerability, and compliance reporting. Based on the previous description of Qualys technology, the assets acquired from NetWatcher will be integrated in the next 12 months seamlessly into Qualys' current stack. Assets acquired from Nevis Networks focus endpoint scanning and security to provide compliance across all endpoints along with mapping of all endpoints for transparent visibility.

Based on the description of the assets acquired from both NetWatcher and Nevis Networks, it's evident that Qualys' M&A strategy is disciplined in progressing their current solutions opposed to just pushing their top line. In the Q4 earnings call, Philippe Courtot (Chairman and CEO) talked about using metrics similar to Microsoft for acquisition pricing – essentially pricing an acquisition in terms of paying a certain dollar amount per engineer that the prospective company has. Qualys is starting to derive their own metrics from the Microsoft model to ensure acquisitions are optimally priced.

The future target companies for Qualys are small cloud based technology firms that already possess the adequate tech stack to integrate into Qualys systems. Even with a lot going on in the company in terms of scaling their cloud tech and pushing out new solutions, M&A is still high in priority to provide customers with solutions they require (Q4 2017 Earnings Call).

Please advise that transaction prices for the aforementioned acquisitions are not public knowledge; an inquiry to a media rep at Qualys for pricing information was not responded to.

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## Earnings:

Revenue compared to EBITDA have both be growing strongly YoY for the last 3 years with projections constant. Strong revenue growth while maintaining margins is attributed to two focuses lead by Qualys'

management: penetration of the high-end untapped market and consistent revival of existing customers solution needs.

The high-end market that Qualys is targeting has an outstanding list of Fortune companies thus far. Qualys customers included 68% of the Fortune 50 in 2016 to 74% at the end of 2017 and 60% of the Fortune 100 in 2016 to 70% in 2017 (Q4 2017

Earnings Call). Growing a substantial customer base is important in the cloud

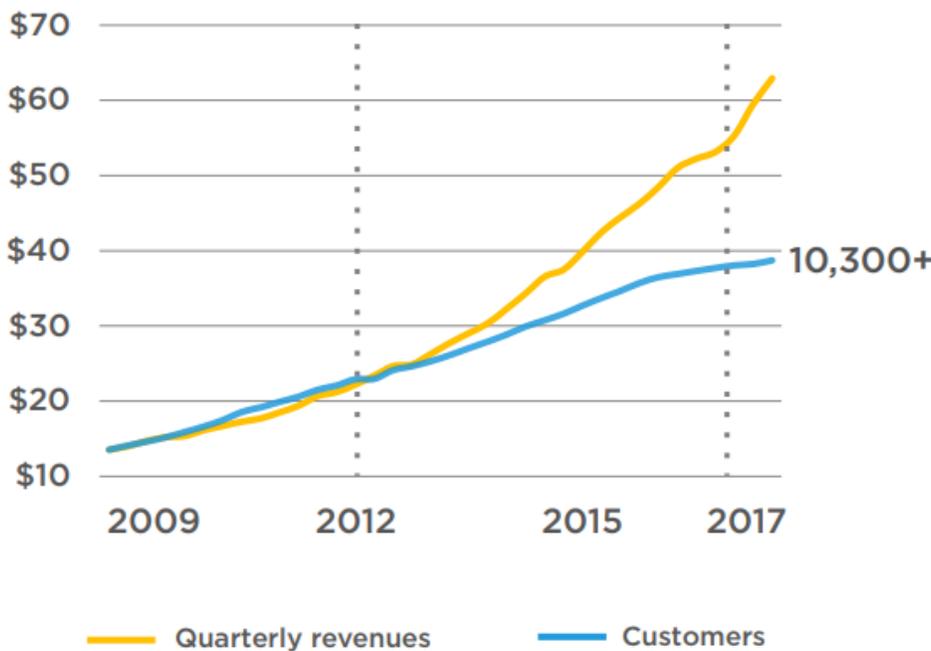
Year	2015	2016	2017	2018	2019
Revenue Growth YoY	23%	20%	17%	20%	17%
EBITDA Growth YoY	79%	20%	25%	17%	20%

technology industry, especially when it comes to security – customers want a company they can trust in such a new and progressive space. Below is a snapshot of YoY growth for revenue and EBITDA sourced from Bloomberg (2018 & 2019 are projections).

It's clear that as Qualys scales their business and generates revenue, they're able to keep their margins. Currently Qualys has over 10,000 customers with 25% in 2016 deploying three or more solutions, which has grown to 32% in 2017 deploying three or more solutions. Revenues are increasing quarter to quarter faster than the amount of customers, indicating retention in current customers purchasing more solutions on top of their initial solution. Below is a graph sourced from the Q4 2017 Earnings Call Slides with revenues in millions on the L1 scale and customers on the R1 scale in actuals:

Be advised that Qualys first pricing was in September of 2012 where revenues start to expand over the

**Quarterly revenues vs. customers**

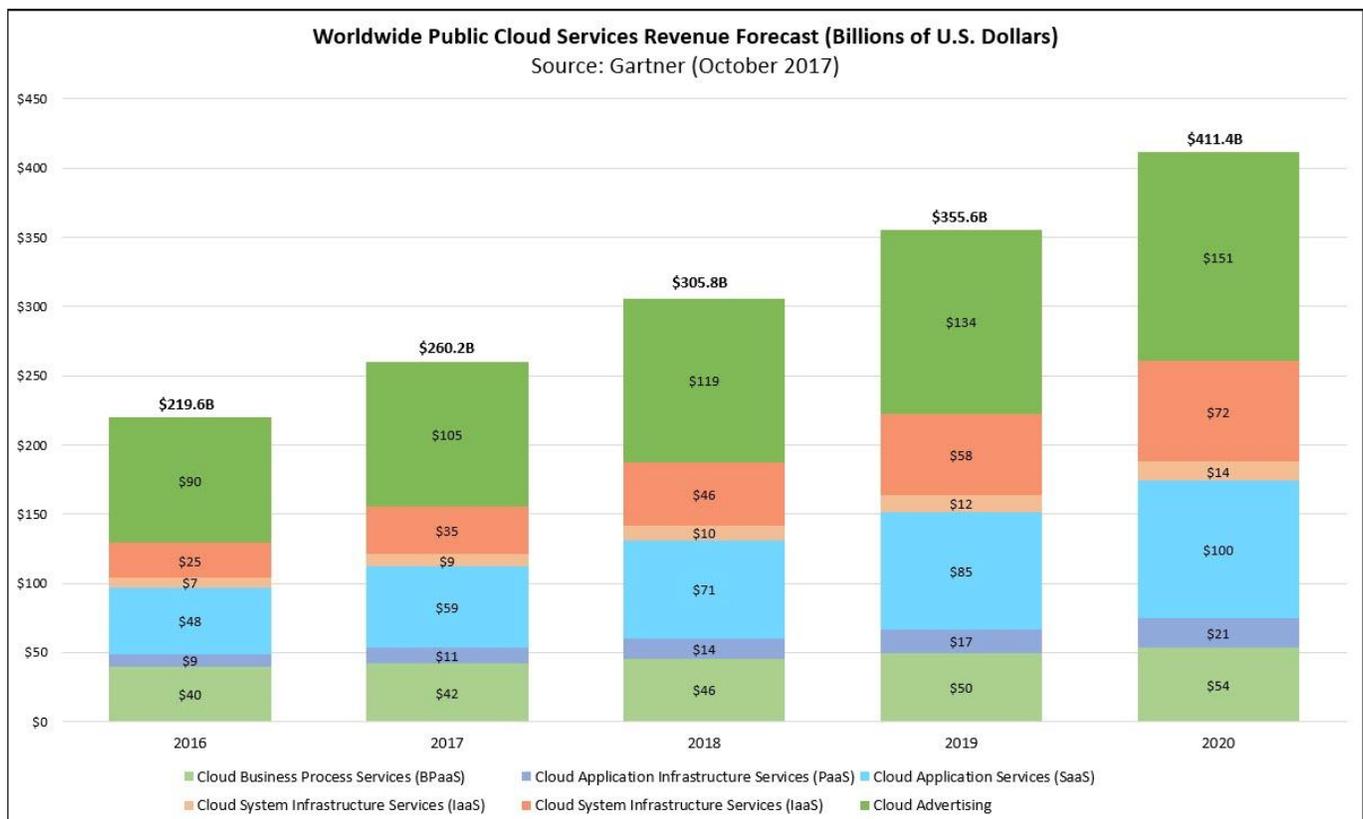


growing customer base. With essentially no debt in their capital structure, revenue is the main driver for shareholder profitability. Currently Qualys has an ROE of 12.7% with a Ke of 8.18%. High sensitivity to operating costs is attributed to heightened R&D for the new cloud space but maintain margins while revenue grows is a clear indication that Qualys can mitigate the OpEx sensitivity. R&D was about 18.5% of revenue in FY 2017, on par with 2015 and 2016 R&D/Revenue figures.

## Industry Outlook:

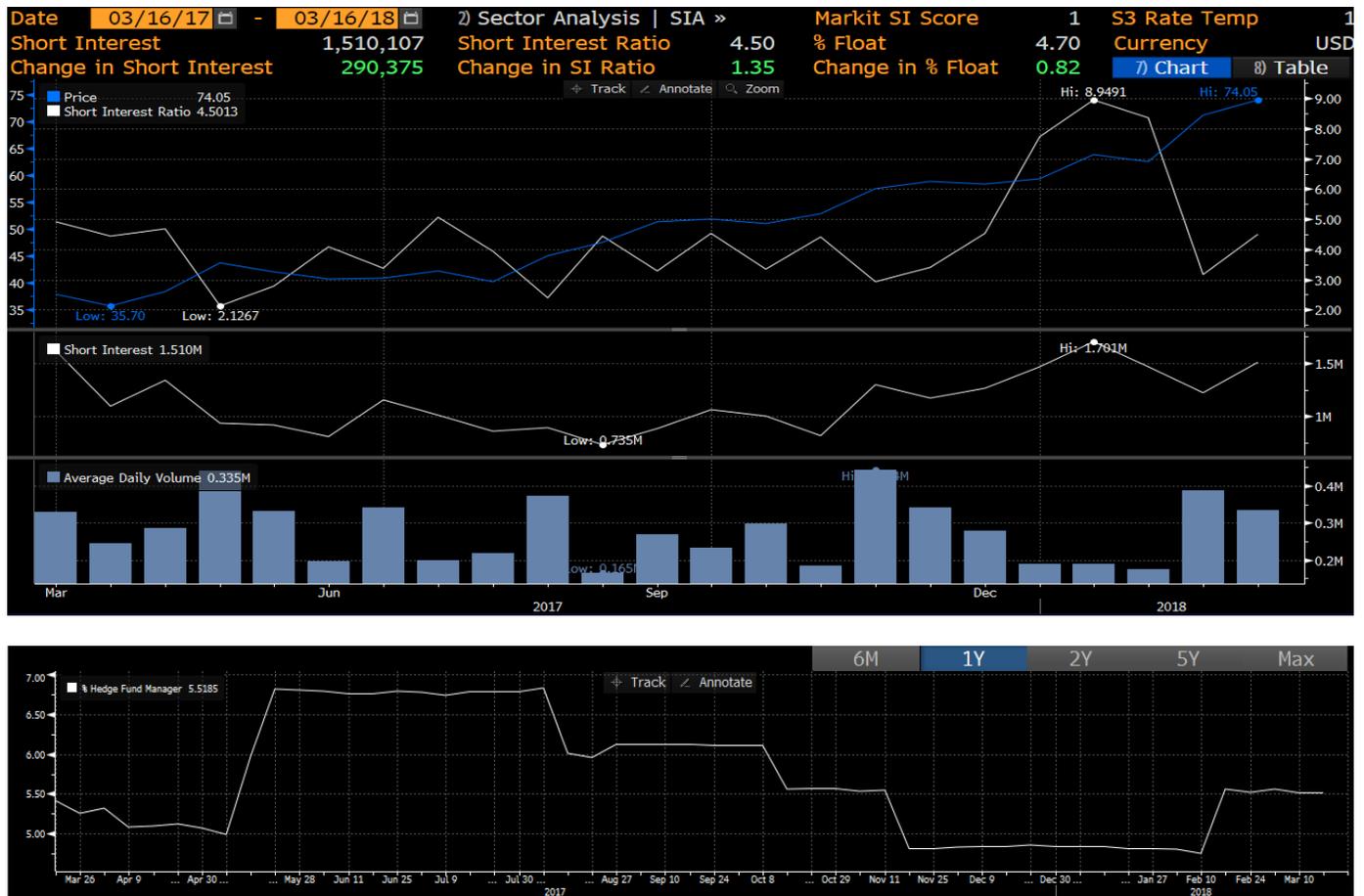
Cloud technology is one of the most prevalent new technologies for organizations looking to lower IT costs and improve efficiency by moving their data to clouds. In terms of cybersecurity, breaches will only be more of a risk when organization information is stored on offsite servers and being accessed remotely. Therefore, as cloud technology grows, IT security will grow along with it.

Looking at the global cloud industry, cloud services revenues grew 18.5% in 2017 while Infrastructure as a Service grew 36.6% in 2017. As illustrated below, these growths won't be surprising in the next three year projections. Main drivers for high growth percentages are due to flexibility in scale, efficiency in accessibility, and reduction in costs. Flexibility in scale is from organizations not needing to store data and servers that maintain a finite amount of storage. Not only do servers have finite storage, they notoriously move slower as more data is pushed onto them. With cloud technology, storage space can be scaled as a company grows so that organizations don't have to buy more servers and can scale at their own pace. Efficiency in accessibility boils down to end points such as mobile devices and other off-site devices being able to access data from the cloud with the only requirement being an internet connection. Being able to access data and applications when not on premise of an organization is a priceless. Spending less on hardware and storage facilities results in reduction of costs despite subscription fees from the cloud. Along with reduction in costs, value is created through automatic updates of the cloud technology on the service providers side.



## Ownership/SI:

The short interest in Qualys recently went up at the beginning of February with an increase in percentage of float by 0.82%. While the short interest has gone up, the price has followed, consistent with hedge fund managers increasing their stake in the company. This bodes unfavorable to potential investors but I believe the market is wrong. Hedge fund managers are known to be in and out of positions for profitability in the short run. With Qualys price the highest it's been in the last 52 weeks, analysts are estimating a slight drop in price and hedge funds are looking to capitalize on this. Regardless, the intrinsic value of Qualys proves that in a long position, returns will be generated past the short-term position of hedge funds.



## Competitors:

Qualys is the best compared to their peer group in terms of maintaining margins while increasing revenue growth. Their revenue growth over the past year of 16.62% is couple with a TTM EBITDA margin of 25.18% and ROE of 16.93%. It's clear that management does an above industry average job managing costs while providing value for the shareholders. Notably, the competition are beating Qualys in revenue growth over the last year but average a negative TTM EBITDA margin and ROE.

Name	Mkt Cap (USD)	Rev - 1 Yr Gr:Y	T12M EBITDA Mrgn:Y	ROE:Y	ROIC/WACC Ratio
Median	2.29B	21.65%	-0.09%	-6.80%	-0.77
100) QUALYS INC	2.29B	16.62%	25.18%	16.93%	1.01
101) FIREEYE INC	2.48B	5.18%	-18.95%	-36.67%	-1.71
102) MIMICAST LTD	1.66B	31.53%	0.81%	-6.80%	-0.77
103) IMPERVA INC	1.36B	21.65%	-0.09%	-3.84%	-0.43
104) PROOFPOINT INC	4.47B	37.23%	-4.79%	-69.15%	-1.10

Compared to their competitors, Qualys possess contracts with the majority of leaders in multiple industries. As stated earlier, the company is currently dominating Forves Global 50 and maintains 47% of the global 500.

## Blue chip global customer base

74% of the Forbes Global 50, 47% of Global 500, and 25% of Global 2000 standardized on Qualys

- 9 of the top 10 in Software
- 8 of the top 10 in Consumer Discretionary
- 8 of the top 10 in Consumer Staples
- 8 of the top 10 in Major Banks
- 8 of the top 10 in Technology
- 8 of the top 10 in Telecommunications
- 7 of the top 10 in Healthcare
- 6 of the top 10 in Industrial & Materials
- 5 of the top 10 in Insurance

Note: Based on Forbes Global 2000 Classification



Domination in the high end market compliments Qualys domination of competitors in terms of margins and returns to shareholders while still growing their revenue adequately. Partnerships with these recognizable companies will only further catapult Qualys past their competition, especially since Qualys maintains excellent retention in furthering existing customer sales as mentioned previously.

A closer look into Qualys most comparable competitor, Imperva Inc., shows operating income loss of \$13.7 million in FY 2017. Recently, Imperva’s Chief Revenue Officer resigned in mid-February of 2018 to “pursue other interests”(source: company new release). It’s evident Imperva is hitting obstacles in their business that’s leading to destruction of value for their shareholders.

## Conclusion:

Qualys Corporation is a buy at its current price due to a competitive advantage compared to their peers due to heightened reputation through high value partnerships, aggressive M&A to further progress their cloud technology, and growth potential through outstanding margins while revenue continues to increase. The cloud technology industry as a whole is poised to grow substantially resulting in a necessity for IT security firms. Qualys, being a pioneer and leader in the IT security space, will ride the forefront of this growth with improvements in revenue growth and margin maintenance.

### Qualys, Inc. (QLYS)

## CENTER FOR GLOBAL FINANCIAL STUDIES

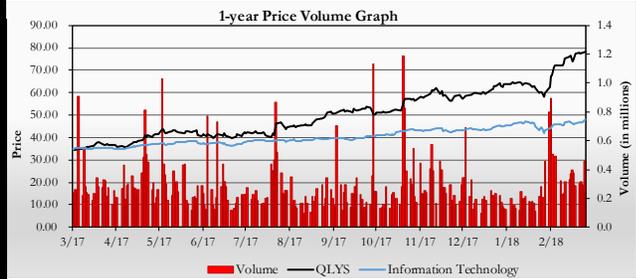
**BULLISH**

Analysis by Zachary DeLeonardo  
3/16/2018

Current Price: **\$77.25**  
Divident Yield: **0.0%**

Intrinsic Value: **\$80.29**  
Target Price: **\$95.21**

Target 1 year Return: 23.25%  
Probability of Price Increase: 99%



<b>Description</b>		<b>Market Data</b>	
Qualys, Inc. provides cloud-based security and compliance solutions in the United States and internationally.		Market Capitalization	\$2,984.05
<b>General Information</b>		Daily volume (mil)	0.26
Sector	Information Technology	Shares outstanding (mil)	38.63
Industry	Software	Diluted shares outstanding (mil)	40.07
Last Guidance	February 12, 2018	% shares held by institutions	109%
Next earnings date	May 2, 2018	% shares held by investments Managers	73%
<b>Market Assumptions</b>		% shares held by hedge funds	6%
Estimated Equity Risk Premium	5.30%	% shares held by insiders	14.96%
Effective Tax rate	22%	Short interest	3.91%
		Days to cover short interest	5.51
		52 week high	\$79.40
		52-week low	\$33.75
		Volatility	41.88%

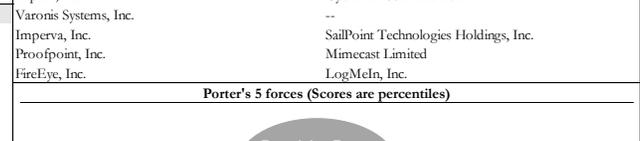
Past Earning Surprises		
Quarter ending	Revenue	EBITDA
12/31/2016	-0.84%	-10.65%
3/31/2017	1.16%	-16.90%
6/30/2017	0.95%	-13.40%
9/30/2017	1.52%	-10.84%
12/31/2017	1.50%	-25.09%
Mean	0.86%	-15.38%
Standard error	1.0%	4.1%

Market and Credit Scores	
Recommendation (STARS) Value--0	Recommendation (STARS) Description--0
Quality Ranking Value--0	Quality Ranking Description--0
Short Score--1	Market Signal Probability of Default % (Non-Ratings)
	-0.028%
	CreditModel Score (Non-Ratings)--b

Industry and Segment Information	
LTN Revenues by Geographic Segments	LTN Revenues by Business Segments
United States--70%	Security Software & Services--100%
Foreign--30%	--
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Management		Total Compensations Growth		Stock Price Growth During Tenure	
Courtot, Philippe	Chairman, CEO & President	70.71% per annum over 5y		0% per annum over 0y	
Fisher, Melissa	CFO & Principal Accounting Officer			-8.44% per annum over 2y	
Posey, Bruce	VP, General Counsel & Corporate Secretary	-100% per annum over 2y		-4.35% per annum over 1y	
Deeba, Amer	Chief Commercial Officer	333.57% per annum over 1y		14.36% per annum over 3y	
Thakar, Sumedh	Chief Product Officer	31.06% per annum over 3y			
Touma-Bruno, Rima	Chief Human Resource Officer				

Porter's 5 forces (Scores are percentiles)	
Bargaining Power of Suppliers-- MIDDLE TIER	38
Bargaining Power of Customers-- MIDDLE TIER	64
Threat of New Competition-- LOWEST TIER	29
Intensity of Existing Rivalry-- MIDDLE TIER	50
Threat of Substitutes-- MIDDLE TIER	58
Overall Position among Peers-- MIDDLE TIER	45

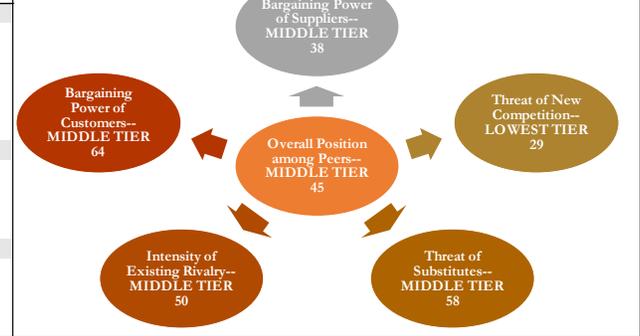


Profitability		QLYS (LTM)	QLYS Historical	Peers' Median (LTM)
Return on Capital (GAAP)		53.9%	34.59%	81.08%
Operating Margin		34%	10.23%	15.80%
Revenue/ Capital (GAAP)		1.59	3.38	5.13
ROE (GAAP)		12.7%	7.9%	28.7%
Net margin		18.2%	8.0%	13.5%
Revenue/Book Value (GAAP)		0.70	0.98	2.12

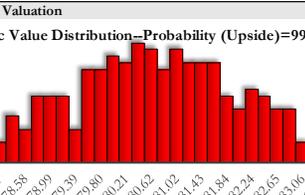
Invested Funds		QLYS (LTM)	QLYS Historical	Peers' Median (LTM)
Cash/ Capital		50.8%	94.6%	57.9%
NWC/ Capital		-19.5%	-15.9%	-33.2%
Operating Assets/ Capital		68.4%	21.1%	10.7%
Goodwill/ Capital		0.3%	0.1%	64.5%

Capital Structure		QLYS (LTM)	QLYS Historical	Peers' Median (LTM)
Total Debt/ Market Capitalization		0.08	0.10	0.23
Cost of Debt		3.9%	4.4%	5.8%
CGFS Rating (F-score, Z-score, and default Probability)		A		
WACC		8.1%	9.4%	11.0%

Valuation	
Forecast Assumptions	Explicit Period (10 years)
Revenue Growth CAGR	16%
Average Operating Margin	32%
Average Net Margin	20%
Growth in Capital CAGR	12%
Growth in Chims CAGR	-3%
Average Return on Capital	13%
Average Return on Equity	13%
Average Cost of Capital	8%
Average Cost of EquityKc	8%



Sensitivity Attribution Analysis	
Revenue	34.1%
Operating costs	49.2%
Capital expenditures	16.3%
Discount Rate	0.4%



Forecast Assumptions	
Continuing Period	2%
	31%
	20%
	2%
	2%
	13%
	13%
	8%
	8%