Dropsuite Limited

An undervalued, profitable growth story – initiating with a BUY

INITIATION

We initiate on Dropsuite (DSE) with a BUY recommendation and $0.33/Sh PT. Our positive view is supported by (1) multiple structural tailwinds which support cloud backup as a thematic, (2) DSE's demonstrable history of prudent and profitable growth (which we expect will continue), (3) a best-in-class product and go-to-market strategy, and (4) M&A optionality – with $25m of funding available. Finally, we believe the sell-off post Microsoft's announcement of its Syntex Backup & Archive product is overdone and see now as an attractive entry point to a multi-year growth story.

A profitable grower at the intersection of three mega-trends

- As a leading provider of cloud-based backup and archiving for businesses, DSE operates at the intersection of three mega-trends, being (1) the rise of cybercrime, (2) the migration of on-premise hosting to the cloud, and (3) MSP industry growth. These themes have long runways and will continue to act as positive tailwinds.
- DSE has delivered extraordinary growth over the past 7-year (a CAGR of >70%) and has managed to do so profitably – delivering positive FCF in each of the past six quarters, while cumulative cash flows are now positive back to 2Q19. Additionally, management are prudent capital allocators, having built a ~$150m business on just ~$43m of outside capital (of which only ~$18m has been spent). We expect this performance to continue.

Microsoft concerns appear overblown

- At its Inspire Conference 2023, Microsoft provided a first look at its *365 Backup and Archive* solution (B&A) – DSE's price fell 22% on the day and has not recovered since. However, based on our work and discussions with industry participants, we conclude that fears of any existential risk to DSE's business are overblow. Accordingly, we believe the market's scepticism is providing an opportunity.

Initiating with a BUY recommendation

- We derive our FTM $0.33/Sh price target via a 10-year DCF. This implies a TSR of 32%, which underpins our BUY recommendation.
- Our PT implies a FTM EV/revenue multiple of 4.3x, well below ASX tech peers, when adjusting for growth and profitability performance.
- **Catalysts.** (1) re-acceleration of net user growth (expected from 1Q24), (2) M&A, (3) lapping of Syntex B&A launch (2H24), (4) IR's fall → tech re-rate.

Year-end December ($)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue ($m)	11.7	20.7	31.5	44.3	57.2
EBITDA ($m)	0.0	1.3	2.2	4.1	7.1
EBIT ($m)	(0.0)	1.2	2.1	3.9	6.9
Reported NPAT ($m)	0.1	1.5	3.1	5.0	8.0
Reported EPS (c)	(0.0)	0.2	0.4	0.7	1.1
Normalised NPAT ($m)	0.1	1.5	3.1	5.0	8.0
Normalised EPS (c)	0.0	0.2	0.4	0.7	1.1
EPS Growth (%)	-	2,129.8	104.8	61.4	62.4
Dividend (c)	-	-	-	-	-
Net Yield (%)	-	-	-	-	-
Franking (%)	-	-	-	-	-
EV/EBITDA (X)	-	-	-	37.8	21.0
Normalised P/E (x)	-	-	61.7	38.3	23.6
Normalised ROE (%)	0.5	6.4	11.8	16.4	21.9

Source: OML, Iress, Dropsuite Limited

Last Price
A$0.25

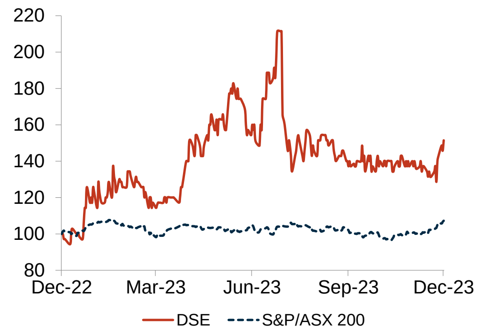
Target Price
A$0.33

Recommendation
Buy

Risk
Higher

IT Services	
ASX Code	DSE
52 Week Range ($)	0.17 - 0.37
Market Cap ($m)	184.5
Shares Outstanding (m)	696.1
Av Daily Turnover ($m)	0.0
3 Month Total Return (%)	10.4
12 Month Total Return (%)	51.4
Benchmark 12 Month Return (%)	7.2
NTA FY23E (¢ per share)	4.6
Net Cash FY23E ($m)	24.6

Relative Price Performance



Source: FactSet

Consensus Earnings

	FY23E	FY24E
NPAT (C) ($m)	2.4	4.3
NPAT (OM) ($m)	3.1	5.0
EPS (C) (c)	0.1	0.2
EPS (OM) (c)	0.4	0.7

Source: OML, Iress, Dropsuite Limited

Lindsay Bettiol, CFA
Senior Research Analyst
(03) 9608 4179
lbettiol@ords.com.au

Milo Ferris
Research Associate
(02) 8216 6691
mferris@ords.com.au

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Figure 1: Financial Summary

Code	**DSE**	Rating:	**Buy**
Analysts	Lindsay Bettiol Milo Ferris	Price Target:	$0.33
Date	20/12/2023	Upside/downside:	30%
Share Price	$0.25	Valuation:	$0.30
Market Capitalisation (A$m)	$174.0	Valuation method:	DCF
Enterprise Value (A$m)	$151.1	Risk:	Higher

PROFIT & LOSS (Dec Year End)		FY21A	FY22A	FY23F	FY24F	FY25F
Revenue	A$m	11.7	20.7	31.5	44.3	57.2
COGS	A$m	-4.2	-7.1	-9.7	-13.4	-16.7
Gross Profit	A$m	**7.5**	**13.6**	**21.7**	**30.9**	**40.5**
Other Income	A$m	0.0	0.0	0.0	0.0	0.0
Expenses	A$m	-7.5	-12.4	-19.6	-26.8	-33.4
EBITDA	A$m	**0.0**	**1.3**	**2.2**	**4.1**	**7.1**
Depreciation & Amortisation	A$m	0.0	-0.1	-0.1	-0.2	-0.3
EBIT	A$m	**0.0**	**1.2**	**2.1**	**3.9**	**6.9**
Net Interest Expense	A$m	0.0	0.3	0.8	1.0	1.2
Minorities	A$m	0.0	0.0	0.0	0.0	0.0
Reported PBT	A$m	0.0	1.5	2.8	5.0	8.0
Tax Expense / (Credit)	A$m	0.0	0.0	0.0	0.0	0.0
Reported NPAT	A$m	**0.1**	**1.5**	**3.1**	**5.0**	**8.0**
Significant Items & FX	A$m	0.1	0.0	0.3	0.0	0.0
Underlying NPAT	A$m	**0.1**	**1.5**	**3.1**	**5.0**	**8.0**

BALANCE SHEET		FY21A	FY22A	FY23F	FY24F	FY25F
Assets						
Cash	A$m	21.6	22.3	24.6	28.4	35.2
Receivables	A$m	2.2	4.1	6.3	8.7	10.8
Prepayment & Other Receivables	A$m	0.2	0.4	0.7	0.7	0.7
PPE	A$m	0.0	0.1	0.1	0.2	0.2
Goodwill & Intangibles	A$m	0.0	0.0	0.0	0.0	0.0
Other Assets	A$m	0.1	0.1	0.1	0.1	0.1
Total Assets	A$m	24.1	26.9	31.9	38.1	47.1
Liabilities						
Payables	A$m	2.0	2.5	3.5	4.7	5.7
Accrued Liabilities	A$m	0.0	0.0	0.0	0.0	0.0
Borrowings	A$m	0.0	0.0	0.0	0.0	0.0
Provisions	A$m	0.0	0.0	0.0	0.0	0.0
Deferred Liability	A$m	0.1	0.1	0.1	0.1	0.1
Other Liabilities	A$m	0.0	0.0	0.5	0.5	0.5
Total Liabilities	A$m	2.2	2.7	4.1	5.3	6.3
Equity						
Share Capital	A$m	43.4	43.4	43.4	43.4	43.4
Other Equity	A$m	0.1	1.0	1.7	1.7	1.7
Retained Earnings	A$m	-21.6	-20.2	-17.4	-12.4	-4.3
Total Shareholders Equity	A$m	21.9	24.2	27.8	32.8	40.8
BV per share	Acps	3.6	3.5	4.0	4.7	5.9
NTA per share	Acps	3.9	3.9	4.6	5.5	6.8

CASH FLOW		FY21A	FY22A	FY23F	FY24F	FY25F
Cash at Start	A$m	2.5	21.6	22.3	24.6	28.4
Cash Flow from Operations	A$m	0.3	0.9	2.4	4.0	7.1
Capex	A$m	-0.1	-0.1	-0.2	-0.2	-0.3
Free Cash Flow	A$m	0.2	0.9	2.2	3.8	6.8
Cash Flow from Investing	A$m	-0.1	-0.1	-0.2	-0.2	-0.3
Cash Flow from Financing	A$m	18.9	0.0	0.0	0.0	0.0
Cash at End	A$m	21.6	22.3	24.6	28.4	35.2
FCF per share (cps)	Acps	0.0	0.1	0.3	0.5	1.0
FCF / Underlying NPAT	%	330%	58%	72%	76%	85%
FCF Yield	%	0.1%	0.5%	1.3%	2.2%	3.9%

EARNINGS		FY21A	FY22A	FY23F	FY24F	FY25F
EPS - Underlying	Acps	0.0	0.2	0.4	0.7	1.1
EPS Growth - Underlying	%	-102%	2125%	105%	61%	62%
EPS - Reported	Acps	0.0	0.2	0.4	0.7	1.1
Diluted shares	m	612.0	684.1	696.1	696.1	696.1
DPS	Acps	0.0	0.0	0.0	0.0	0.0
Dividend Yield	%	0%	0%	0%	0%	0%
Payout Ratio	%	0%	0%	0%	0%	0%

VALUATION		FY21A	FY22A	FY23F	FY24F	FY25F
EV/Revenue	x	13.0	7.3	4.7	3.3	2.4
EV/EBITDA	x	n.m.	121.3	68.7	35.3	19.5
EV/EBIT	x	n.m.	127.4	72.5	37.0	20.2
P/E - Underlying	x	n.m.	119.3	58.2	36.1	22.2
Price/Book	x	7.0	7.1	6.3	5.3	4.3
Price/NTA	x	6.3	6.4	5.5	4.6	3.7
Price/FCF	x	781.1	201.0	78.7	45.9	25.5

GROWTH		FY21A	FY22A	FY23F	FY24F	FY25F
Revenue	%	66%	77%	52%	41%	29%
Total Expenses	%	34%	66%	51%	37%	25%
EBITDA	%	-100%	n.m.	74%	90%	72%
Adjusted EBITDA	%	-112%	n.m.	50%	73%	60%
PBT	%	-99%	n.m.	95%	76%	62%
Reported NPAT	%	-103%	n.m.	110%	61%	62%
Underlying NPAT	%	-103%	n.m.	110%	61%	62%

MARGINS & RETURNS		FY21A	FY22A	FY23F	FY24F	FY25F
Gross Margin	%	64.4%	65.8%	69.0%	69.8%	70.8%
EBITDA Margin	%	0.0%	6.0%	6.9%	9.3%	12.4%
Adj. EBITDA Margin	%	1.5%	10.2%	10.1%	12.4%	15.3%
EBIT Margin	%	-0.3%	5.8%	6.5%	8.9%	12.0%
Underlying NPAT Margin	%	0.5%	7.1%	9.8%	11.2%	14.1%
ROE	%	-0.1%	4.8%	7.7%	11.2%	14.8%
ROA	%	-0.1%	5.4%	8.9%	13.0%	17.1%
Effective Tax Rate	%	0.0%	0.0%	0.0%	0.0%	0.0%

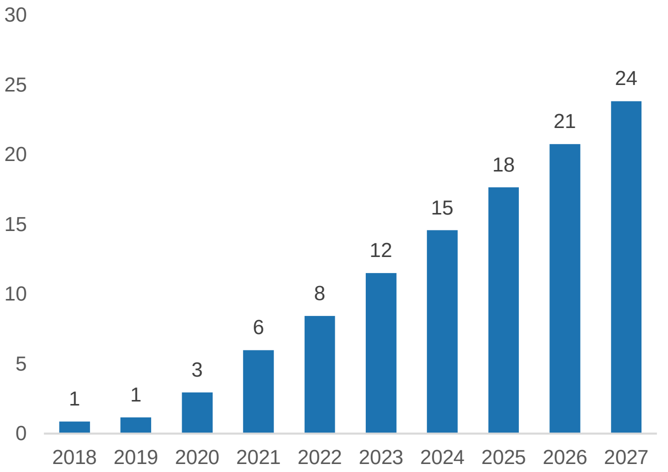
GEARING		FY21A	FY22A	FY23F	FY24F	FY25F
Net Debt / (Cash)	A$m	-21.6	-22.3	-24.6	-28.4	-35.2
Enterprise Value	A$m	152.4	151.7	149.4	145.6	138.8
Net Debt/EV	%	-14.2%	-14.7%	-16.5%	-19.5%	-25.4%
Net Debt/Equity	%	-98.6%	-92.2%	-88.6%	-86.8%	-86.3%
Net Debt/EBITDA	x	n.m.	-17.9	-11.3	-6.9	-4.9
EBITDA/Net Interest	x	0.7	4.8	2.9	4.1	6.0

SEGMENTS		FY21A	FY22A	FY23F	FY24F	FY25F
Revenue	A$m	11.7	20.7	31.5	44.3	57.2

Source: Ord Minnett Research

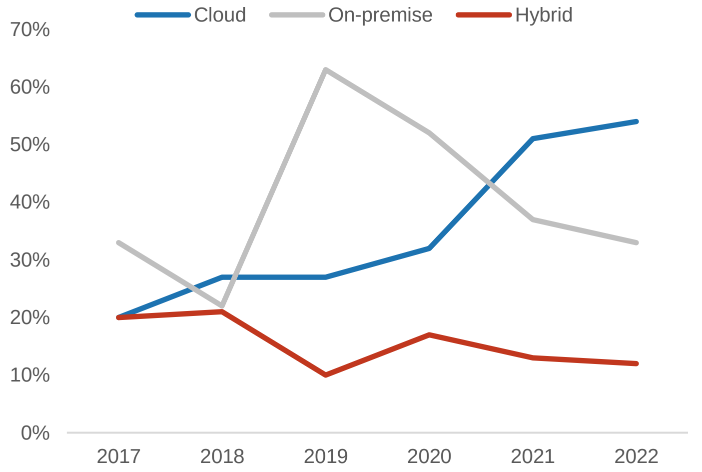
Key Charts

Figure 2: The costs associated with cybercrime continue to rise



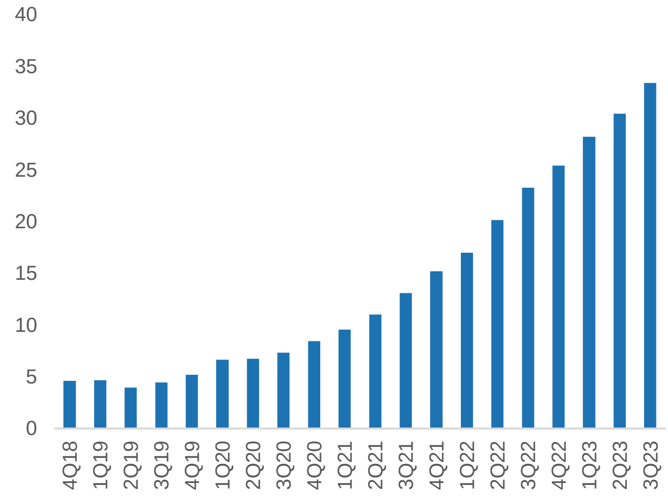
Source: Statista, FBI, IMF
Units: Annual cost of cybercrime, US$tr

Figure 3: Cloud backup is rising in-line with increased adoption



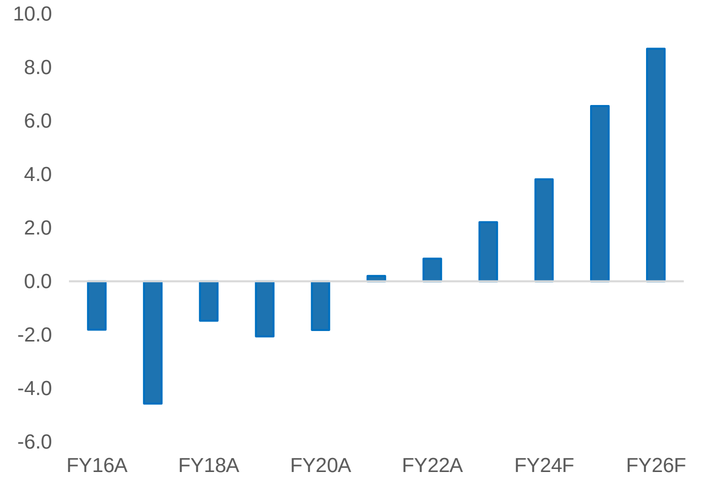
Source: Acronis, 2022
Units: Backup sources, by medium (%)

Figure 4: ARR has grown at a 7-yr CAGR of >70%...



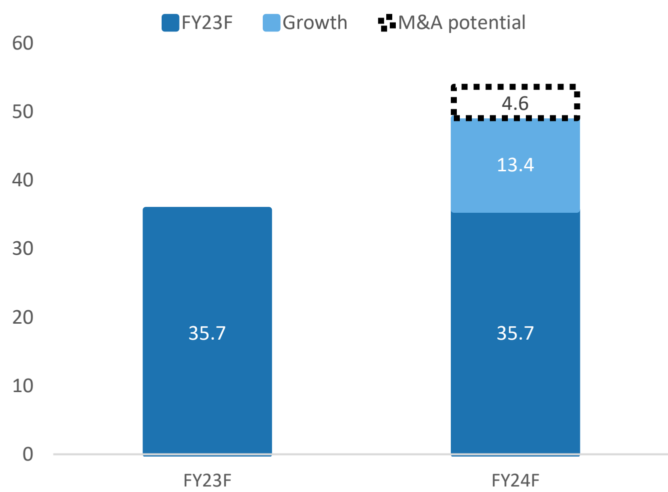
Source: Ord Minnett Limited estimates
Units: ARR, historical (A$m)

Figure 5: …And has done so profitably



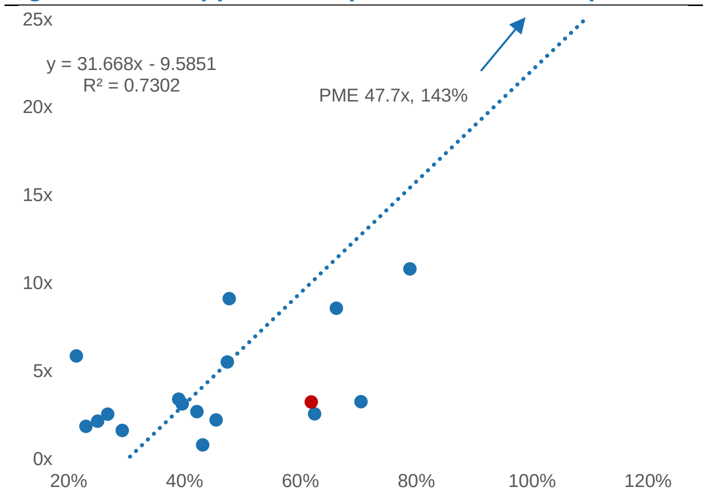
Source: Ord Minnett Limited estimates
Units: FCF, historical and forecast (A$m)

Figure 6: M&A has potential to drive further growth



Source: Bloomberg, Ord Minnett Limited estimates
Units: Impact of potential M&A on FY24 revenues (A$m)

Figure 7: DSE appears inexpensive relative to peers



Source: Bloomberg, Ord Minnett Limited estimates
Units: EV/revenue (Y) vs Rule of 40 (X)

Executive Summary

Founded in Singapore in 2011, Dropsuite is a cloud-based software platform offering backup, archiving, and recovery solutions for businesses. The company specialises in protecting critical data from Microsoft 365, Google Workspace, QuickBooks, and others. Its products are distributed via a network of ~4k IT reseller partners globally.

DSE has delivered rapid top-line growth since its founding, with ARR rising at a 7-year CAGR of >70%, while growth has only fallen below 50% on one occasion. The company now serves >1m end users and is expected to generate >$30m in revenues for FY23F.

We believe the sell-off post Microsoft's Backup & Archiving product announcement in July is overdone, with DSE now trading on an FY24 EV / revenue multiple of just 4.0x, well below ASX tech peers, when adjusting for growth and profitability.

Accordingly, we initiate with a BUY recommendation and $0.33/Sh PT.

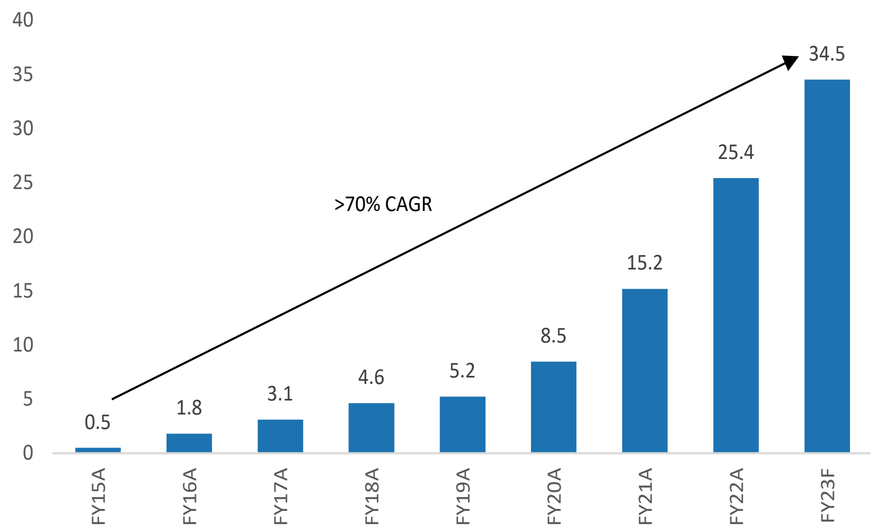
Investment summary

1. **At the intersection of three secular trends [Pgs. 26-31].** As a leading provider of cloud-based backup and archiving for businesses, DSE operates at the intersection of three mega-trends, being (1) the rise of cybercrime, (2) the migration of on-premise hosting to the cloud, and (3) growth of Managed Service Provider (MSP) industry. These themes have long runways and will continue to act as positive tailwinds for growth.

2. **Best-in-class product.** DSE's Microsoft 365 (M365) backup is considered a product leader, as evidenced by its consistent outperformance vs peers on both a qualitative (industry awards) and quantitative (market share) basis. In 2023, DSE ranked #1 of its peer group for product features, satisfaction, experience and capability – for a 4th consecutive year. Further, our discussions with industry participants also highlight DSE as a product leader in the space.

3. **Prudent, profitable growth.** DSE has delivered extraordinary growth over the past 7-year (a CAGR of >70%) and has done so profitably – delivering positive FCF during each of the past six quarters, while cumulative cash flows are also positive dating back to 2Q19. Additionally, management are prudent capital allocators, having raised just ~$42m since inception, of which only ~$18m has been invested.

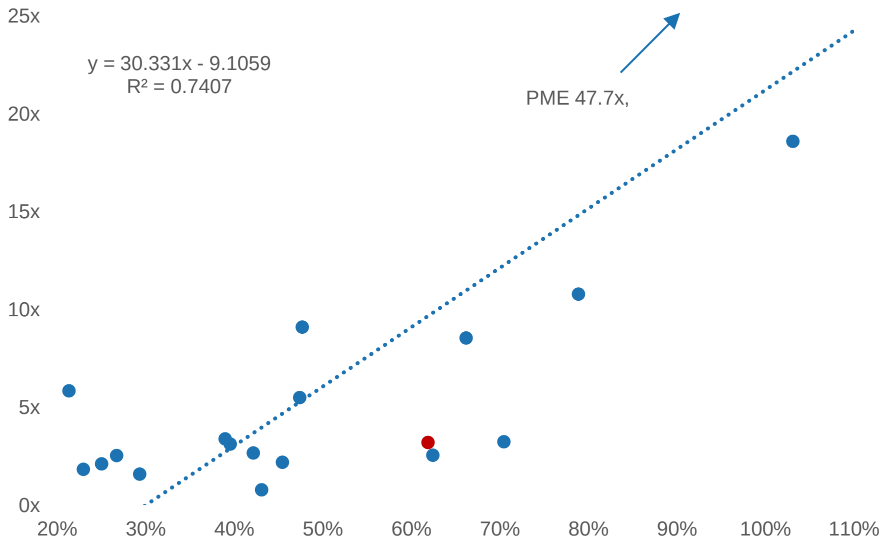
Figure 8: Historical ARR performance (A$m)



Source: Ord Minnett Limited estimates, company presentations

4. **Resource-light G2M strategy.** The majority of DSE's revenues and users come via its channel partners – numbering ~4k. This indirect approach to S&M allows the company to distribute its products in a resource efficient manner. Further, these relationships take time to cultivate and thus, (1) demonstrate a strong product-market fit, and (2) make DSE's products difficult to displace for new entrants.
5. **M&A optionality**. DSE's prudent capital allocation extends to its M&A activity, where the company continues to actively assess inorganic opportunities, yet will not be drawn into overpaying for assets. Accordingly, the company's cash balance remains robust at ~$25m (and growing). We see this as sufficient to increase ARR by ~$5m [assuming an all-cash transaction at ~4x multiple].
6. **Valuation is undemanding.** DSE trades on 4.0x FTM EV / revenue, below its recent history (20% disc.). Additionally, given the company's robust forecast revenue growth (3-yr CAGR ~30%) and profitability (FY24 EBITDA margins = 7%), we believe it screens as inexpensive against high-growth, profitable ASX software names (Figure 9).

Figure 9: Valuation vs high growth, profitable peers



Source: Ord Minnett Limited estimates, company presentations

7. **Key risk: Microsoft B&A threat overblown.** At its Inspire Conference 2023, Microsoft provided a first look at its *365 Backup and Archive* solution (B&A) – DSE's price fell 22% on the day and has never recovered. However, based on our proprietary work and discussions with industry participants, we conclude that fears of any existential risk to DSE's business are overblow. We discuss this theme in greater detail on Pgs. 24-25 of this note.

Estimates Summary

Revenues

We expect top-line growth to moderate, from 52% in FY23F to a (still robust) 41% in FY24 and a 3-year CAGR of 30% through FY26F. Our estimates are predicated on:

- **Gross users:** Gross adds are expected to remain at the recent ~90k/qtr run-rate through FY24 and rise modestly thereafter.
- **Churn:** The recent churn of a legacy, non-core customer is expected to finish in 4Q23, when a further ~40k users come off. We then model a return to base-line ~3%/year in FY24, before a material step-up associated with the launch of Microsoft's B&A product beginning from 1Q25.
- **Net new users:** The above assumptions result in a re-acceleration of net user growth from 1Q24 and drive total users to 2.04m by the end of FY26, up ~900k vs 4Q23F – a 3-year CAGR of 21%.
- **ARPUs:** USD ARPUs rise to $1.90 by FY26F, +$0.23 vs FY23F, a very modest ~4% 3-year CAGR, as recent positive mix benefits (churn-related) subside.

Expenses

- **Gross profits.** Margins rise from 69% in FY23F to 71% in FY26F, driven by ongoing efficiencies and benefits of scale.
- **Cash opex:** Employee Benefits as a percentage of subscriptions fall to 37% (from 42% in FY23F) as a natural consequence of scale. SBP comes down in-line with this growth. All other line items increase broadly with revenue growth rates.
- **Statutory EBITDA:** rises from $2.2m to $10.5m over the same period. Margins rise from +7% to +15%.
- **Adj. EBITDA:** rises from $3.2m in FY23F, to $12.4m by FY26F (margins +10% to +18%). The sole different between statutory and adjusted EBITDA is share-based compensation.

Cash flow and Balance Sheet

- We model FCF for FY23F of $2.2m, rising to $9.0m by FY26.
- OCF / EBITDA cash conversion runs at ~90-100% through FY26, impacted by modest growth-related working capital items.
- **Cash balances** rise from ~$25m at the end of FY23, to ~$44m by FY26. Note: we make no allowance for M&A or capital returns at this time, although suspect both are more-likely than a continued build-up of cash.

Figure 10: Estimates summary

Estimates Summary	Unit	FY21A	FY22A	FY23F	FY24F	FY25F	FY26F	3YR
Users	000s	649	935	1,158	1,519	1,741	2,043	21%
Gross	*000s*	*233*	*320*	*367*	*400*	*432*	*464*	8%
Churn	*000s*	*15*	*34*	*144*	*39*	*210*	*162*	4%
Net	*000s*	*218*	*286*	*223*	*361*	*222*	*302*	11%
ARPU	US$/m	1.40	1.53	1.67	1.75	1.83	1.90	4%
ARR	$m	15.2	25.4	35.7	49.1	58.7	71.6	26%
Revenue	**$m**	**11.7**	**20.7**	**31.5**	**44.3**	**57.2**	**69.0**	**30%**
Gross Profit	$m	7.5	13.6	21.7	30.9	40.5	49.3	31%
Margin %	*%*	*64.4%*	*65.8%*	*69.0%*	*69.8%*	*70.8%*	*71.4%*	
Opex	$m	7.5	12.4	19.6	26.8	33.4	38.8	26%
EBITDA	**$m**	**0.0**	**1.2**	**2.2**	**4.1**	**7.1**	**10.5**	**69%**

Source: Ord Minnett Limited estimates

Valuation is undemanding

Price Target = A$0.33/Share

We derive our 12-month forward A$0.33/Share Price Target via a 10-year DCF, which implies a FTM EV/revenue multiple of 4.3x. We believe this is appropriate given the considerable revenue growth we expect DSE to deliver in the medium-term (3-year CAGR = 30%), its solid gross margins (~70%) and strong FCF profile (FY23F = $2.2m, FY26F = $9.0m).

Our Price Target implies a 32% TSR, which underpins our BUY recommendation.

Figure 11: DCF summary

DCF inputs	
Beta	1.5
Risk Free Rate	4.5%
Market Risk Premium	4.0%
Cost of Equity	10.5%
Cost of Debt (After Tax)	7.5%
WACC	**9.8%**
Terminal Growth Rate	**2.0%**

DCF outputs	
Enterprise Value ($m)	**181.8**
Less: Net Debt (FY23e) ($m)	(24.6)
Equity Value ($m)	**206.4**
Implied Equity Value ($/sh)	**0.30**
Rolled forward at WACC	9.8%
Price Target ($/sh)	**0.33**

RFR % \ Beta	**2.00**	**1.75**	**1.50**	**1.25**	**1.00**
6.5%	0.23	0.24	0.26	0.28	0.31
5.5%	0.25	0.27	0.29	0.32	0.35
4.5%	0.27	0.30	**0.33**	0.36	0.41
3.5%	0.30	0.33	0.37	0.42	0.48
2.5%	0.34	0.38	0.43	0.50	0.59
1.5%	0.40	0.45	0.52	0.62	0.76

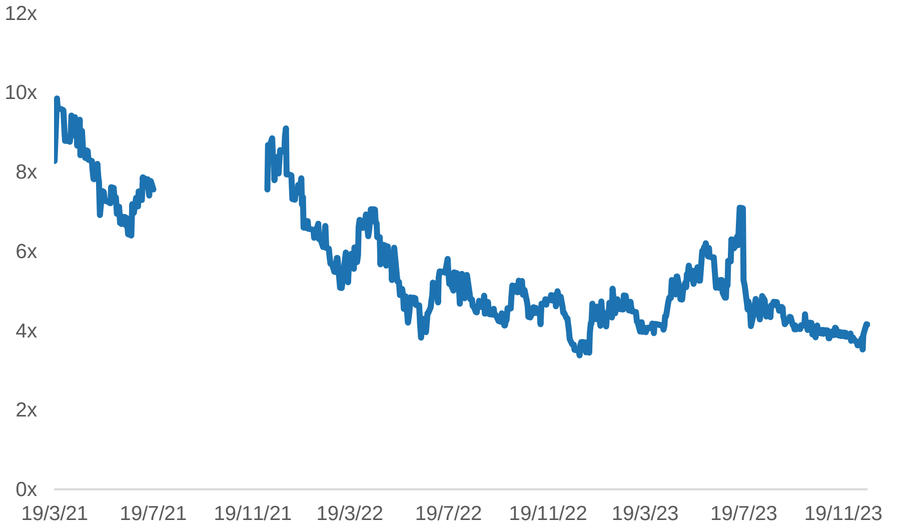
Source: Ord Minnett Limited estimates

Historical context

Following a continual de-rating over the past few years, DSE now trades on a one-year forward EV/revenue multiple of 4.0x. This represents:

- 31% discount to the 3-year average of 5.8x, 9th percentile
- 20% discount/premium to the post-22 (i.e. tech bubble) average of 4.9x, 11th percentile

Figure 12: Absolute EV/revenue



Source: Bloomberg

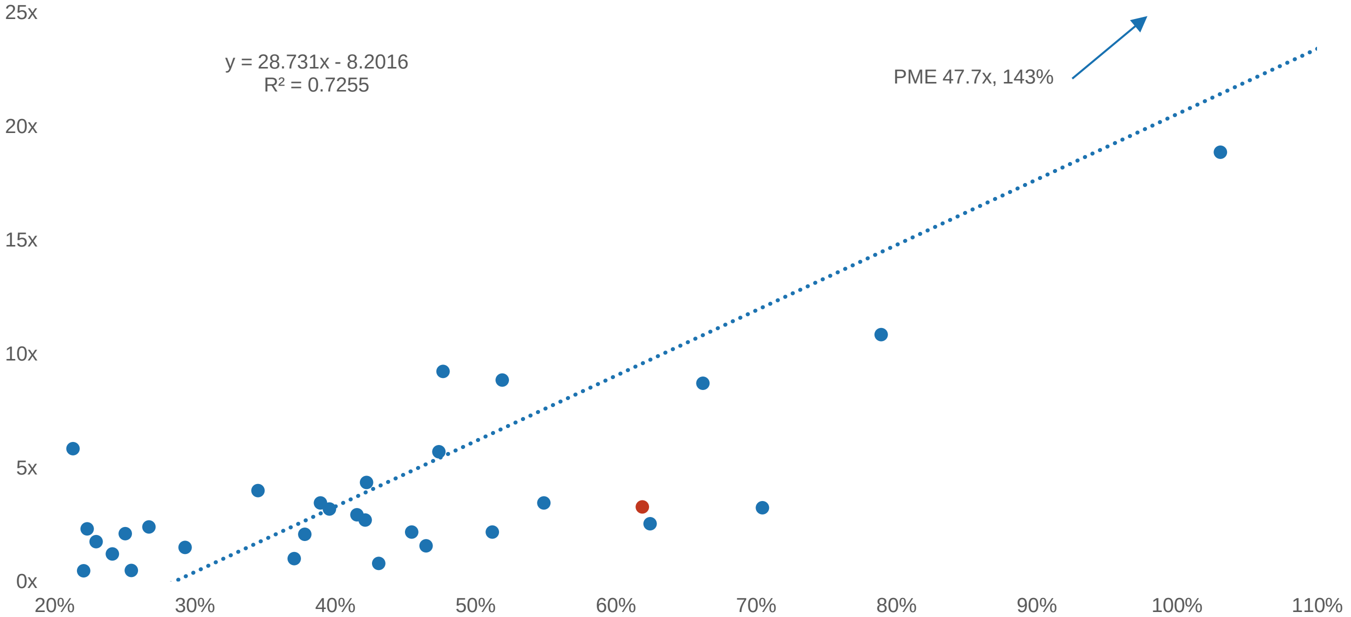
Peer comparison

Below we compare DSE with a group of high growth, profitable ASX-listed software peers on an EV/revenue vs Ro40 basis.

As presented, DSE appears inexpensive given:

- A 2-year revenue CAGR of 46% and FY24F EBITDA margin of 9% sees DSE with a Ro40 of 55% (note: figure is based on consensus estimates). This is broadly in-line with its profitable / high-growth peer set at 53%.
- Current EV/revenue multiple of 4.0x is comfortably below the peer average of 7.3x, despite the abovementioned comparable growth and profitability metrics.

Figure 13: DSE peer valuations



Source: Bloomberg, Ord Minnett Limited estimates
Note: X-axis = EV/revenue (x), Y-axis = Ro40 2yr CAGR
Constituents: ASX listed software. See Figure 58

Additional upside, given M&A optionality

Balance Sheet = ~$25m in available funding

DSE is sufficiently well-funded to support its growth ambitions – with ~$25m in available cash at the end of 3Q23.

Additionally, the company has been demonstrably FCF positive since 2Q22, while cumulative cash flows have also been positive dating back to 3Q19.

We expect a portion of these funds will be used for M&A…

In August 2021, DSE completed a A$20m capital raising, with the 'use of funds' at the time identified as:

- Accelerating strategic growth objectives;
- Strengthening the company's working capital and balance sheet position; and
- **Advancing M&A opportunities.**

However, in-line with the company's prudent approach to capital management, no M&A activity has occurred following the above placement – with management refusing to be drawn into overpaying for assets. Nevertheless, we understand the company continues to activity look for opportunities.

Note: DSE incurred $0.27m in 'due diligence' fees during for 1Q22 for a transaction which was never completed.

…this could add ~$5m to ARR

Working on the assumption that DSE would not allow its cash balance to fall under $10m, we estimate its current funding would be sufficient to add ~$5m of ARR to its top-line, at current market multiples (Figure 14). Of course, the use of scrip and/or debt would be further additive to this figure.

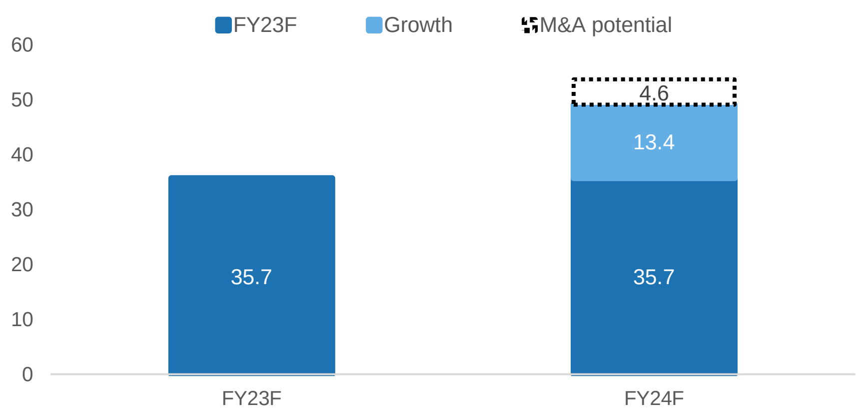
Figure 14: M&A optionality

Potential M&A uplift	
Available Cash, 4Q24F	28.4
Allocated to M&A (ie. $10m min)	18.4
Market EV / ARR multiple	4.0
Potential uplift (A$m)	**4.6**

Source: Company Reports, Ord Minnett Limited estimates

- The addition of ~$5m in ARR would see our FY24 estimates rise to $53.7m, from $49.1m – YoY growth would increase to 50%, from 38%.
- Further, DSE's valuation would further de-rate, when viewed on this basis; with its EV / revenue multiple falling to 2.8x.

Figure 15: Impact of potential M&A on FY24F growth



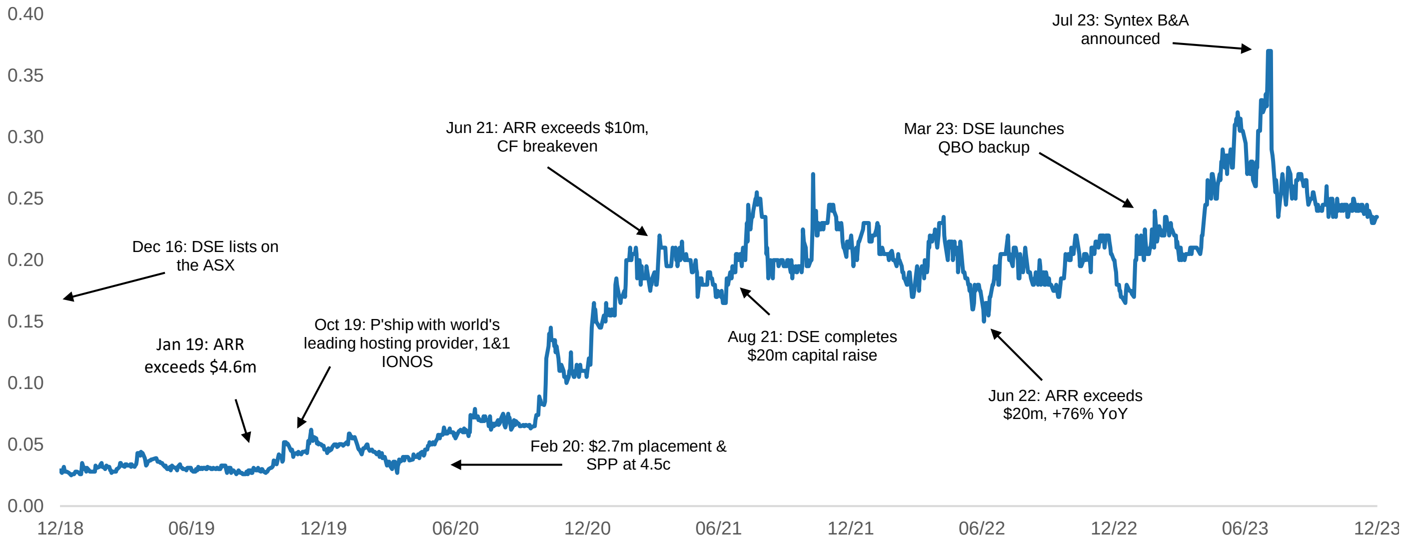
Source: Company Reports, Ord Minnett Limited estimates

Company Snapshot

History

- Founded in Singapore in 2011, Dropsuite is a cloud-based software platform offering backup, archiving, and recovery solutions for businesses.
- DSE was initially focused solely on backup services for websites – under the name Dropmysite – before rebranding to Dropsuite in 2016 and expanding its product focus, ultimately becoming an industry leader in M365 backup. The company also offers backup for Google Workspace, Quickbooks, and others.
- DSE sells its products via a network of ~4k IT reseller partners globally, including industry giants such as Ingram Micro and Pax8.
- **Dropsuite listed on the ASX in December 2016, at $0.10/sh.**

Figure 16: DSE 5-year price chart

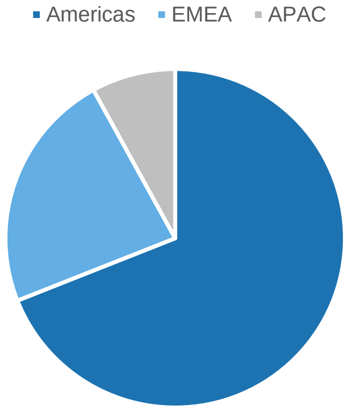


Source: Bloomberg

Footprint

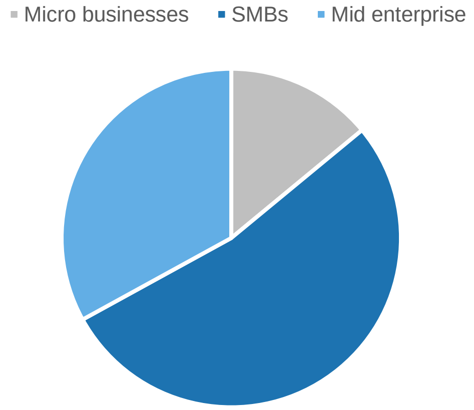
- Revenues primarily come from the Americas (69%), with EMEA (23%) and APAC (8%) also served.
- DSE primarily targets SMEs (~53% of revenues), with mid enterprise (~33%) and micro businesses (1-5 pax) comprising the balance of its revenues.

Figure 17: Revenue split by geography, FY23



Source: Company reports

Figure 18: Revenue split by customer segment, FY23



Source: Company reports

Revenue model

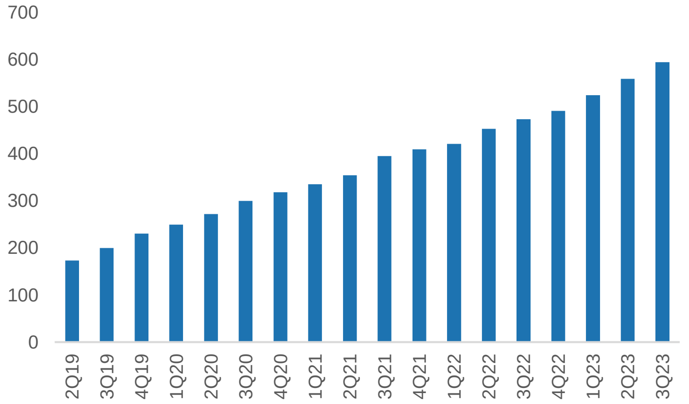
Users pay recurring monthly fees for the use of DSE's software, with payment either made directly to the company, or indirectly to MSPs depending on the sales channel used. In the latter case, DSE has no direct relationship with the end user, but rather invoices its partners on a monthly basis. DSE's business is heavily skewed toward this latter indirect sales channel.

Financial performance: prudent, profitable growth

Since listing in late-2016, DSE has delivered extremely consistent, and robust, growth across all of its KPIs. Additionally, the company has been a prudent capital allocator, with performance to-date delivered on just ~$18m of spent investment.

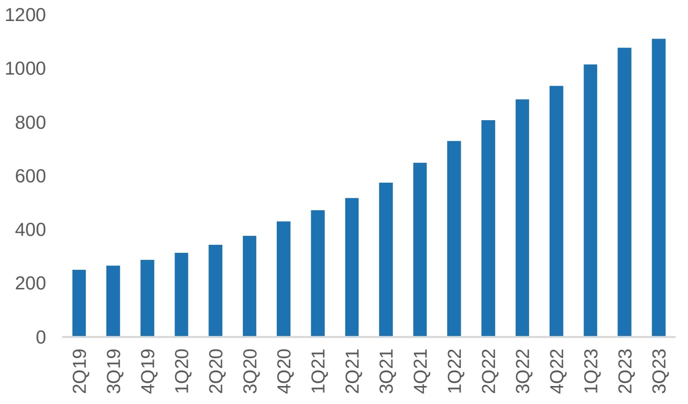
- **Partners.** IT reseller partners have risen to 594 (3Q23) from <200 as recently as 2019. These 'partners' include direct relationships only and do not extend to the company's ~4k indirect MSP relationships.
- **End users** now exceed 1.1m, from ~250k in 2019. Growth has moderated in recent quarters due to churn of a legacy, non-core partner. This churn event will cease beyond 4Q23 (discussed further below).

Figure 19: DSE's 594 partners do not include its ~4k indirect MSP relationships



Source: Company reports, Ord Minnett Limited estimates

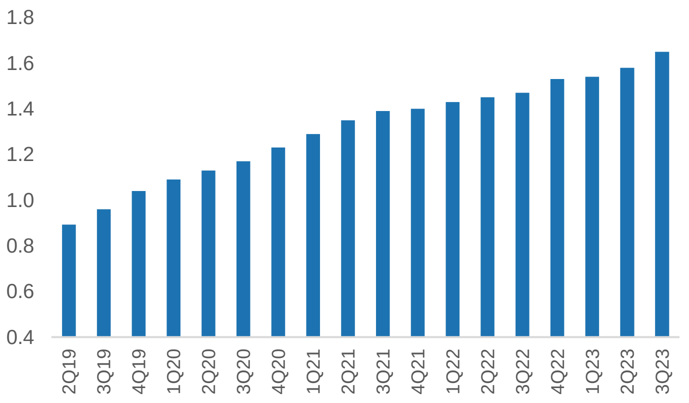
Figure 20: End users now exceed 1.1m



Source: Company reports, Ord Minnett Limited estimates

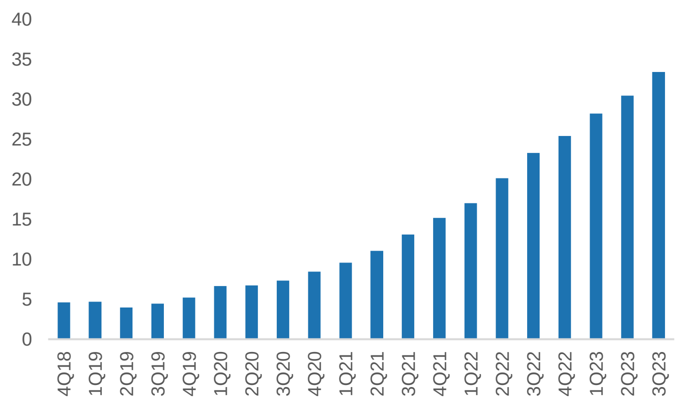
- **ARPUs.** Average Revenues Per User (ARPU) are US$1.65/m, ~double the US$0.90/m first disclosed in 1Q19. This growth has been driven by (1) positive mix, and (2) product cross / upsell.
- **ARR.** The combination of growth in the above KPIs has seen ARR explode from <$1m at the time of IPO to >$30m in FY23F (a >70% CAGR).

Figure 21: ARPUs continue to rise, driven by (1) mix, and (2) additional product launches



Source: Company reports, Ord Minnett Limited estimates

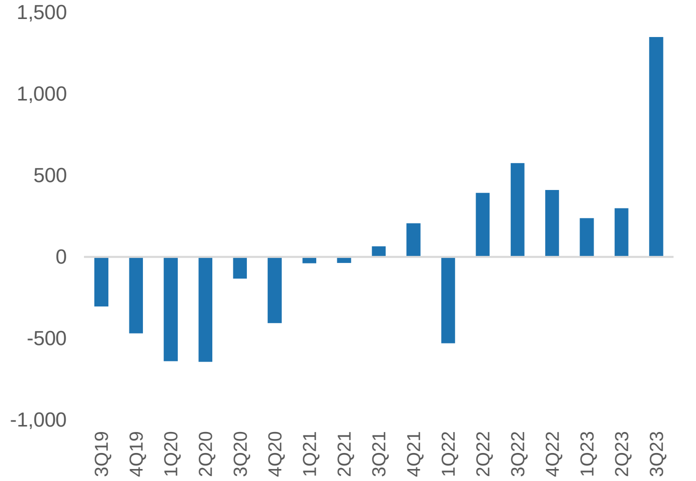
Figure 22: ARR has grown at a 7-year CAGR of >70%



Source: Company reports, Ord Minnett Limited estimates

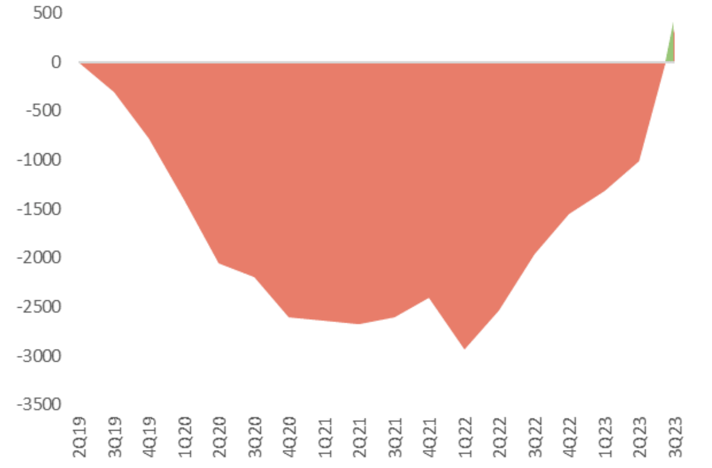
- **Profitable growth**. Not only has DSE grown with a 7-year CAGR of >70%, it has managed to do so profitably – delivering positive FCF in each of the past six quarters, while cumulative cash flows are positive dating back to 2Q19.

Figure 23: Quarterly FCF



Source: Company reports, Ord Minnett Limited estimates

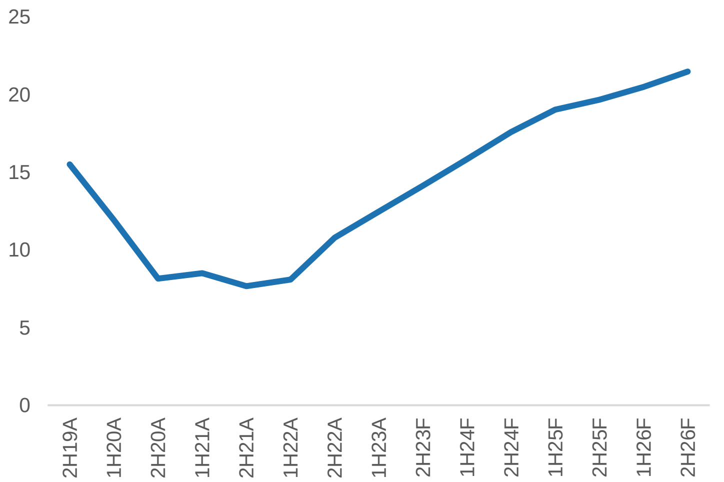
Figure 24: Cumulative FCF, since 2Q19



Source: Company reports, Ord Minnett Limited estimates

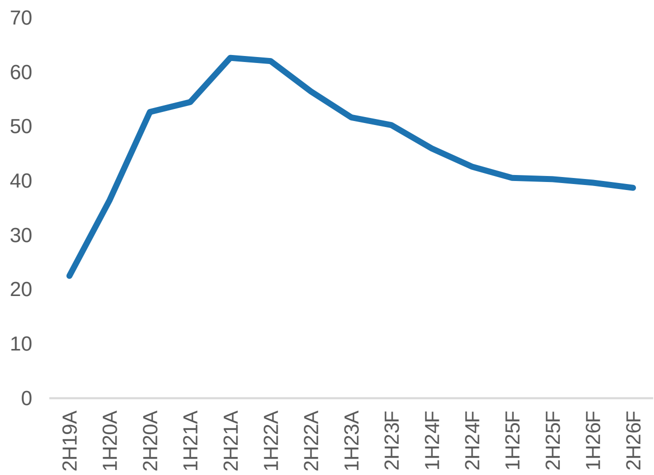
- **Attractive unit economics.** DSE's channel-first strategy allows for extremely attractive unit economics, with a CAC payback of just ~6 months (top quartile for ASX software names).
- **LTV: CAC.** We prefer CAC payback to LTV:CAC ratios, given issues inherent in calculating LTVs (i.e. long-term churn rates). Nevertheless, a back-of-the-envelope calculation implies LTV:CAC for DSE's business of >50x (Figure 26).

Figure 25: CAC over time (A$m), actual and forecast



Source: Company reports, Ord Minnett Limited estimates
Note: We use (1) marketing + (2) 25% of staff costs as our numerator

Figure 26: LTV:CAC over time (x), actual and forecast



Source: Company reports, Ord Minnett Limited estimates
Note: LTV calc = [ARPU x 12 x 3% churn / GP%]

- **Low churn.** DSE reports revenue churn of ~3% (or less) most quarters. This compares favourably with ASX peers, and once again highlights the benefit of its products and channel-first strategy (ie. MSPs / distributors relationships can take years to cultivate and are thus difficult to displace).
- **Prudent capital management.** Since inception, DSE has only raised ~$42m of external capital, of which just ~$18m has been invested. The company's enterprise value currently sits at ~$150m, for a cumulative ROIC of ~8x.

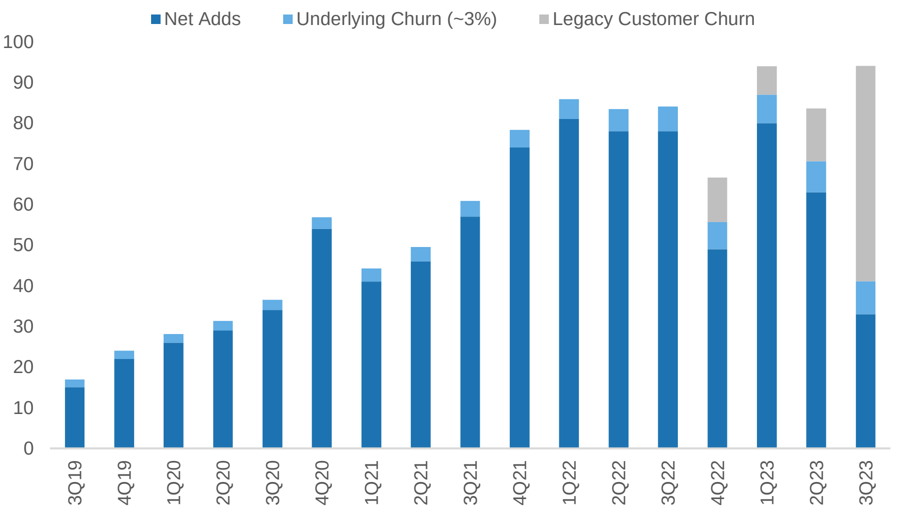
Recent performance is misleading

DSE's net user growth has slowed meaningfully over the past few quarters, from a consistent ~70-80k and >10% in absolute / QoQ growth terms, to ~30k / 3% in 3Q23.

However, per Figure 27, essentially all of this 'slow down' in **net adds** (blue bars) is explained by the churn of a single legacy, non-core, hosting partner (grey). Excluding this one-off event, we show that **gross adds** remain exceptionally steady at ~80-90k.

This customer churn has been well-flagged by the company and we expect 4Q23 will be the last quarter impacted by the event. From 1Q24, we model net user growth returning to historical levels, ie. >80k.

Figure 27: Paid user additions, QoQ (000s)



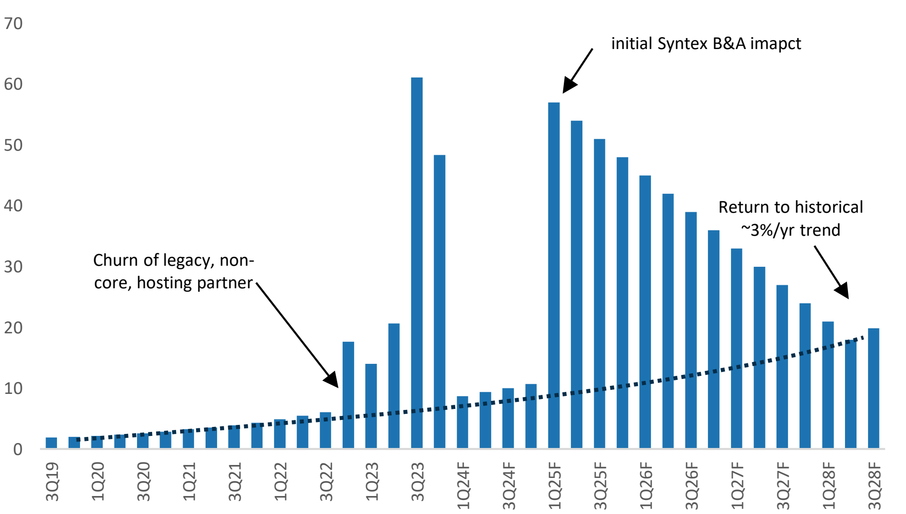
Source: Company Reports, Ord Minnett Limited estimates

Accounting for Microsoft's B&A launch

While we don't believe Microsoft's entry into the market will pose an existential threat for DSE, we are partial to the view that it could weigh on growth – noting, that even modest increases in churn can compound to have enormous impacts over time.

Accordingly, we model a 3% increase in quarterly user churn beginning 1Q25 (ie. our estimate for the first full quarter post-launch). Working on the assumption that churn will be most-pronounced immediately following launch, we then taper the QoQ impact progressively through FY28; where the company returns to its historic ~3%/yr trend.

Figure 28: Paid user churn assumptions, QoQ (000s)



Source: Company Reports, Ord Minnett Limited estimates

Product Overview

Why backup for M365 is essential

Millions of organisations rely on M365 for email communications, collaboration tools, and document management. This has seen the platform become the cornerstone of many business's operations and is true across industries.

However, many users mistakenly assume that Microsoft automatically backs up their data as part of its offering – this is not true and relates to the concept of a '**Shared Responsibility Model',** as discussed immediately below.

The Shared Responsibility Model

The Shared Responsibility Model (SRM) is a cloud security framework that separates the responsibilities of cloud service providers (ie. AWS, Azure) and their customers. The SRM states that while cloud providers are responsible for securing their service infrastructure, it is incumbent on customers to secure their data and applications within the cloud environment.

Accordingly, a dedicated M365 backup solution acts as a safety net, ensuring that businesses can recover their critical data swiftly and comprehensively. This is crucial for maintaining business continuity and preserving customer trust.

Different approaches, but ultimately all the same

While each cloud provider approaches the issue of 'Shared Responsibility' slightly differently, the key premise underlying each remains: customers are responsible for backing up their own data.

We provide exerts from the SRM terms and conditions of each of the 'big 3' cloud providers below and a summary of key responsibilities for each party within Figure 29.

- **Amazon Web Services.** 'Customers are responsible for managing their data (including encryption options), classifying their assets, and using IAM tools to apply the appropriate permissions'.
- **Microsoft Azure.** 'Regardless of the type of deployment, you always retain the following responsibilities – data, endpoints, account, access management'.
- **Google Cloud.** 'The cloud provider always remains responsible for underlying network infrastructure, and customers are always responsible for their access policies and data'.

Figure 29: The Shared Responsibility Model

	Amazon Web Services		Microsoft Azure		Google Cloud	
Responsibility	AWS	Customer	Microsoft	Customer	Google	Customer
Physical and infrastructure security	Yes	No	Yes	No	Yes	No
Platform security	Yes	No	Yes	No	Yes	No
Infrastructure management	Yes	No	Yes	No	Yes	No
Application security	No	Yes	No	Yes	No	Yes
Data security	No	Yes	No	Yes	No	Yes
Identity and access management	Yes	Yes	No	Yes	Yes	Yes
Endpoint security	No	Yes	No	Yes	No	Yes
Network security	Yes	Yes	Yes	Yes	Yes	Yes
Compliance	Yes	Yes	Yes	Yes	Yes	Yes

Source: Company T&Cs

Most cloud users are unaware of this fact…

This SRM concept remains broadly misunderstood, particularly amongst SME's; with a recent Arcserve Global study suggesting that 43% of IT decision-makers continue to believe cloud providers are responsible for data. These findings are in-line with research from the likes of IDC (>40% of companies do not backup M365) and Barracuda/Statista (only ~16% of companies' backup their SaaS applications).

The Dropsuite solution

DSE's products can be classified under Email Protection, Website Protection, and Accounting Data Protection.

Email Protection

Microsoft 365 (M365) Backup

DSE's M365 solution closes gaps in data protection users could encounter in the Microsoft 365 subscription service (Excel, Outlook, Teams, and more) environment.

As discussed above, the onus of data security, backup, and restoration is placed on the end user (before the announcement of Syntex B&A), with Microsoft taking no responsibility. This leads to gaps in security that are difficult to address and risks the integrity of user data. Examples where issues may arise include:

- **Accidental data deletion:** Human error, data sprawl, device usage that is not synced, equipment loss or theft, and employee turnover and administrative errors.
- **Recycle bin limitation**: M365 only saves deleted emails for up to 90 days.
- **Microsoft service limitation**: Microsoft will act as the infrastructure provider and does not guarantee the protection, storage or backup of a customer's data. Microsoft's Service Agreement (Sec.6b) outlines this and they further recommend using third-party solutions
- **Existing risks and vulnerabilities**: Categories include a) Exchange vulnerabilities; b) Print Spooler vulnerabilities; c) Sensitive Windows Registry database files vulnerabilities; d) Encrypting File System Remote Protocol (MS-EFSRPC) and Active Directory Certificate Services (AD CS) vulnerabilities; and e) Active X vulnerabilities

Figure 30: M365 Backup comprehensive solution works across multiple products

Outlook	Sharepoint	OneDrive	Contacts/ Calendars/ Tasks	Groups & Teams
View email without search	Restore site, document library, folder, files	Restore drive, folder, files	Restore calendar events, contacts, tasks	Download files
Migrate per user to other user or destination	Restore to other site	Restore to other drive	Download files	Channel Chat
Download (PST EML)	Restore all to one folder	Restore all to one folder	Email and Folders for Mailboxes and Public Folders	Tasks
Download Mailbox	Download files	Download drive, folder, files	Shared Mailboxes	Email
Shared Mailbox	Lists – items and columns for all permissions			Drive
Restore mailbox, folder, message	Document Libraries – content, views and content types for all permissions			Site
Migrate per mailbox to other user or destination	Sub-Sites – lists and document libraries			Calendar
Download PST, EML, mailbox				Files
				Conversations
				Notebook
				Planner

Source: DSE website, accessed 11 December 2023

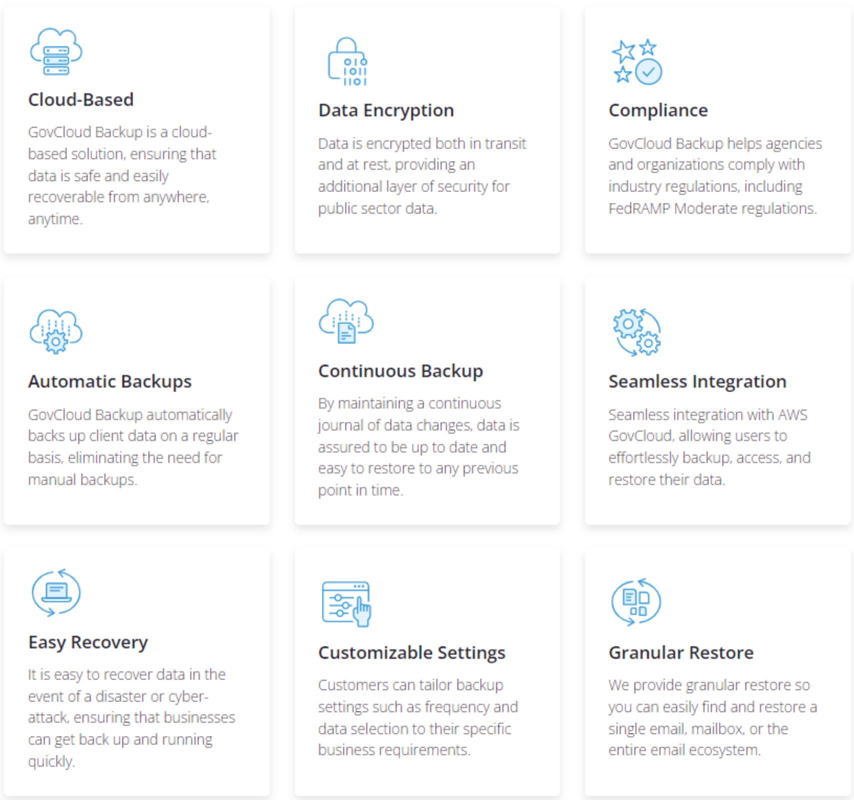
GovCloud Backup

A Microsoft 365 backup and restoration solution for US government agencies and other highly regulated industries dealing with classified and sensitive data stored in Amazon Web Services (AWS) GovCloud. The GovCloud Backup solution from DSE provides essential features for its userbase such as automated incremental backup, one-click data restore, and regulatory-compliant email archiving features.

DSE launched its GovCloud product in mid-2023.

Users of the AWS GovCloud require adherence to multiple compliance regimes including the FedRTFedRAMP High baseline; the DOJ's Criminal Justice Information Systems (CJIS) Security Policy; U.S. International Traffic in Arms Regulations (ITAR); Export Administration Regulations (EAR); Department of Defense (DoD) Cloud Computing Security Requirements Guide (SRG) for Impact Levels 2, 4 and 5; FIPS 140-2; IRS-1075; and more.

Figure 31: DSE's GovCloud solution encompasses M365 Backup and Archiving



Source: DSE website, accessed 11 December 2023

Google Workspace Backup

DSE provides a comprehensive backup solution for Google Workspace, including options for Gmail, My Drive, Shared Drive, Contacts, Calendars and Tasks. Similar to M365, Google Workspace has gaps in its security that DSE's solution caters for. Common issues include:

- **Accidental data deletion:** Human error, data sprawl, device usage that is not synced, equipment loss or theft, employee turnover and administrative errors
- **Trash bin limitation**: Google deletes end-user Drive files in the Trash folder after keeping them for 30 days. It allows admins to restore items deleted from a user's trash for up to 25 days after that. Emails are also kept in the Trash and Spam folders for 30 days.
- **Threat actor exploits**: Attacks led by hostile actors targeting Google Workspace vulnerabilities for business email compromise and spear phishing attacks.

Figure 32: Google Workspace Backup solution multiple applications, including Gmail

Gmail	Shared Drive	My Drive	Contacts / Calendars / Tasks
Restore mailbox, label, message Migrate per user/per mailbox to other user or destination Shared Mailbox Download PST, EML, mailbox Restore to original label, other label, new label Restore to original mailbox/user Restore/Migrate to other Workspace mailbox/user Restore/Migrate to other M365, Hex, Gmail and other mailbox/user	Restore all file types, including Google files Restore Shared Drive to a new folder Download Shared Drive file Advanced Search for Shared Drive	Restore drive, label, files Restore to other Drives Restore all to one folder Download drive, folder, files Restore all kinds of files including Google file type Download My Drive file Restore with conflict option (Append, create a copy, replace, skip)	Restore Contacts Restore Calendars Restore Tasks Download Contacts Download Calendars - Event, Meeting, etc. Download Tasks

Source: DSE website, accessed 11 December 2023

Email Backup for Data Protection and Compliance

Email backup, recovery and protection are important features due to the increased potential for accidental data deletion and enhanced compliance mandates and regulatory needs. DSE provides solutions for Workspace Gmail, Exchange Online, Hosted Exchange, IMAP/POP, and Open-Xchange.

Email Archiving

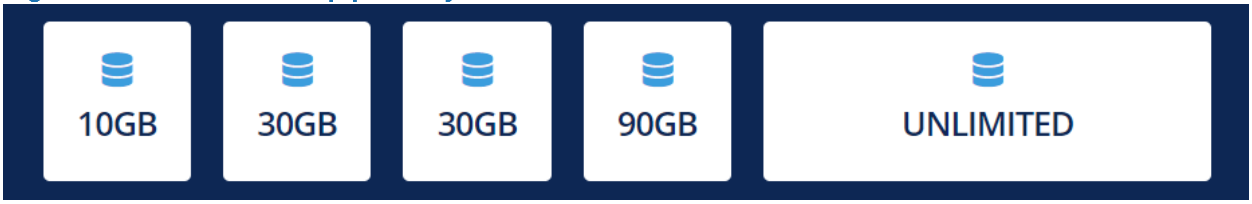
DSE provides a cloud-based solution for archiving of emails. This is provided across numerous systems including Microsoft Exchange Online, Hosted Exchange, and Workspace Gmail. Email archiving ensures all ‘assets’ are stored without fail and a business is compliant with relevant regulations. Beyond compliance, archiving can provide businesses with insights on data, assist in making more informed decisions, and analyse usage patterns, and corporate policy violations.

Website Protection

Website Backup is a cloud-based, database backup and monitoring service for websites to securely backup. Recover, monitor, and protect website data. The service is military-grade secure and easy to use. The solution further provides:

- **Website blacklist monitoring:** Easy to use blacklist monitoring tool that alerts customers if their website has been compromised and blacklisted by Google. The problem can be identified quickly, and a clean copy of the website restored in a single click. Google’s safe browsing tool is built into the DSE Website Backup tool, eliminating the worry of a customer’s website having visitors arrive on an infected site.
- **1-click restore:** Ability to simply and quickly restore a user’s website with 1-click, reducing downtime in the event of a website being hacked or tampered with. The feature works across the entire timeline of a website’s backups.

Figure 33: Website Backup plans by data size



Source: DSE website, accessed 11 December 2023

Accounting Data Protection

DSE provides an online backup solution for North America's leading cloud-based accounting software for SME's by Intuit (NSDQ: INTU), QuickBooks Online (QBO). The DSE QBO Backup offers a secure continuous and on-demand backup of "over 40 QBO objects", allowing for a quick and easy restore process. Customers can use a point-in-time restoration, download archived files for reporting, import into QBO, replicate record to other QBO accounts for testing and training, upgrade/downgrade subscription plans, auditing purposes, and entity changes.

DSE launched its QBO offering in early-2023. We understand this will be a premium-priced product.

Figure 34: DSE's QuickBooks Online Backup supports the back up of over 40 QBO items…

Transaction Data	List Data	Other Data
Invoice	Account	Attachable
Estimate	Budget	Company Info
Sales Receipt	Class	Entitlement
Payment/ Credit Card payments	Customer Type	Exchange Rate
Tax Payment	Department	Preferences
Deposits	Journal Code	
Bills/Bill Payment	Payment Method	
Refund Receipt	Tax Code	
Credit Memo	Tax Classification	
Vendor Credit	Tax Agency	
Journal Entry	Term Vendor	
Purchase		
Purchase Order		
Refund Receipt		
Time Activity		
Transfer		
Recurring Transaction		
Reimburse Charge		

Source: DSE website, accessed 11 December 2023

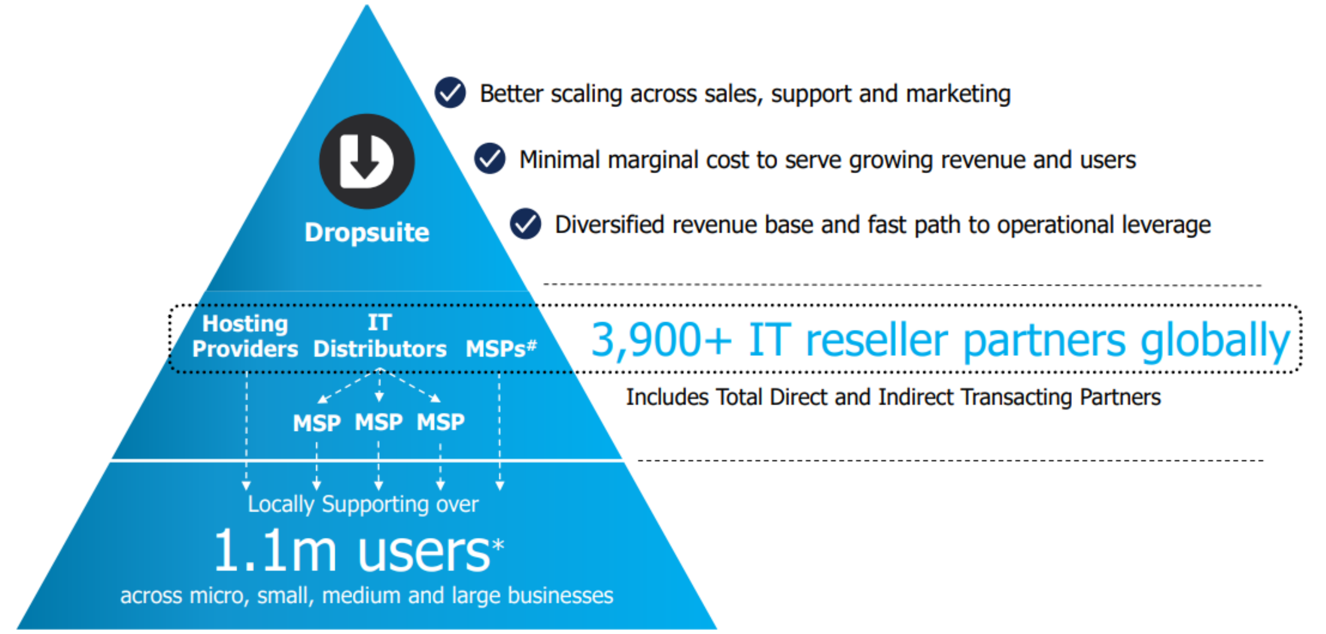
Resource-light G2M strategy

DSE runs a channel-first sales model

DSE distributes its products both directly and indirectly, by integrating them into the platforms of its network of distribution partners. The latter channel then on-sells DSE's products to MSPs, who in-turn sell to the end user. The majority of DSE's revenues and users come via the indirect channel.

In terms of its end user base; DSE's products are predominantly sold to SME's, although over time there has been an ongoing move up-market into Enterprise sales.

Figure 35: The DSE sales model



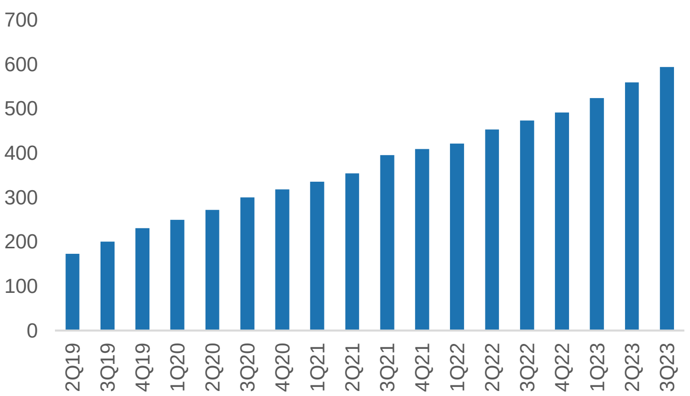
Source: Ord Minnett Limited estimates

DSE's relevance with IT resellers continues to grow

Growth in the number of IT reseller partners offering DSE's product has been a core tenet of the company's growth, with direct partner numbers rising from <200 in 2019 to ~600 at Sept 30 (Figure 36). This does not include the company's ~4k MSPs.

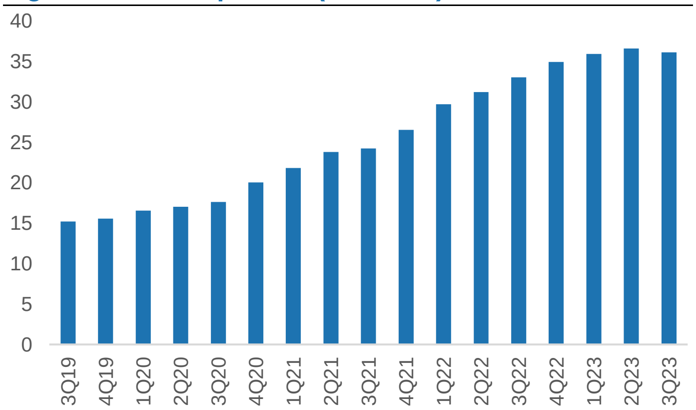
Additionally, the contribution from each of these partners has continued to improve (as measured by ARR/partner), which speaks to DSE's ability to grow and deepen these relationships over time. It also speaks to the high efficacy and low churn of the DSE product suite.

Figure 36: Number of partners



Source: Company reports, Ord Minnett Limited estimates

Figure 37: ARR / partner (US$000s)



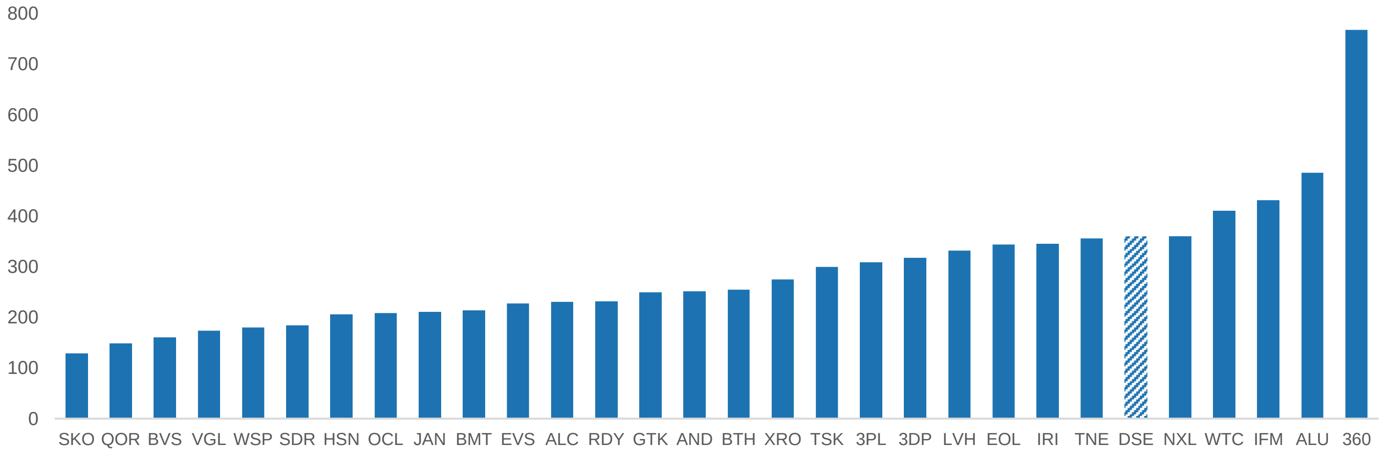
Source: Company reports, Ord Minnett Limited estimates

Benefits of the MSP approach

The MSP model benefits key stakeholders in the following ways:

- **Dropsuite**. The key benefit of its channel partner network is an ability to scale quickly in a labour and capital-efficient manner. Sales, marketing, customer support, billing and credit risk are all borne by channel partners. These benefits are clearly visible in measures of employee efficiency [i.e. rev / FTE], where DSE benchmarks toward the top of its peer group (Figure 38).

Figure 38: Revenues (A$m) / FTE for ASX-listed software names



Source: Ord Minnett Limited estimates, company reports
Note: Figures based on most-recent reporting period

- **Channel partners**. Benefits are two-fold, with MSPs able to increase revenues (and potentially margins), while providing a better customer experience; given the increased demand for cloud backup and archiving solutions.
- **End users**. The indirect sales model provides users with all the typical benefits of cloud storage (ie. minimal capital requirements), while being fully integrated into their MSPs infrastructure. This ensures billing, contracting and support all remain with existing service providers and eliminates the need for additional relationships and agreements.

Appeal of the SME market

DSE is built with an intuitive user experience that appeals to non-tech savvy users. Given the sheer nature of their size, many at the SME end of the market fall into this category and have an unsophisticated approach to data protection, where:

- 40% of SMEs worldwide report having lost essential data due to an attack.
- 47% of businesses with <50 employees do not allocate any funds toward cybersecurity (this is the opportunity).
- 59% of SME operators believe their company is too small to be targeted (an incorrect belief), and
- Only 14% of SME's surveyed say they are prepared for any form of attack.

Accordingly, this is fertile hunting ground for DSE given the segment's reliance on MSPs for advice and its general lack of penetration for cloud backup solutions. The market is also extremely large, with an estimated 333m SME's operating globally.

Competitor overview

Background

Key competitors include:

Figure 39: Competitor landscape

Company	Backup and Archive Services by Product/Environment/Deployment
Acronis Backup and Recovery Solution	Azure, Google Workspace, Hyper-V, M365,
AvePoint	Dynamics, Salesforce, M365
BackupAssist 365	M365
Barracuda Backup	Exchange, M365, Azure, AWS, Google Cloud, Hyper-V, VMware,
CloudAlly M365 Backup	Box, Dropbox, G Suite, Global Data Centres, M365, Salesforce, SharePoint
Commvault	M365, Dynamics 365, Salesforce, ThreatWise, GovCloud, File & Object
Datto	Endpoint backup for PCs and Servers, File level protection, Azure, SaaS
Microsoft Syntex	M365
Mimecast Sync & Recover	Exchange, Microsoft 365 (M365)
NovaBackup	M365, VMware, Hyper-V
TitanHQ Arc Titan	M365
Veeam Backup for M365	M365

Source: Company websites

DSE is the industry leader

We believe DSE has the strongest product in market, as evidenced by its consistent outperformance versus peers on both a qualitative (industry awards) and quantitative (market share) basis. Further, our discussions with industry participants also highlight DSE as a product leader in the space.

Qualitative: Consistently ranked as the product leader

Data Quadrant: #1 for product features, satisfaction, experience and capability

Each year the Info-Tech Research Group collects data from a range of software end users across to produce its *Data Quadrant Report* for a range of industries – including the Email Backup market.

Products are ranked on **features and satisfaction,** against v**endor experience and capabilities,** with each category comprising a range of fields including:

- Business value added
- Quality of features
- Usability and intuitiveness
- Vendor support
- Permission awareness
- Compliance
- And many others

In 2023, DSE ranked #1 amongst its peers for a 4th consecutive year (Figure 40).

Emotional Footprint: #1 for emotional connection and satisfaction

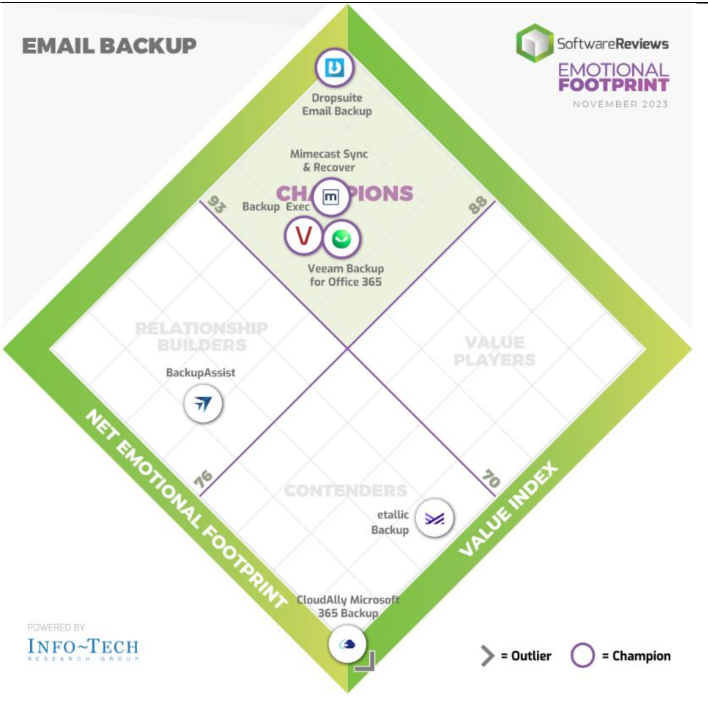
Separately, Info-Tech also releases an annual *Emotional Footprint Report* – which aggregates user's emotional responses across 25 'provocative' questions to create an indicator of user feeling toward a vendor and product.

The company then overlays this 'Net Emotional Footprint' with a 'Value Index' metric, capturing user satisfaction with their software given the costs they are paying. Here, once again DSE ranked a clear #1 amongst its peers (Figure 41).

Figure 40: SoftwareReviews – Data Quadrant

Source: Ord Minnett Limited estimates

Figure 41: SoftwareReviews – Emotional Footprint



Source: Ord Minnett Limited estimates

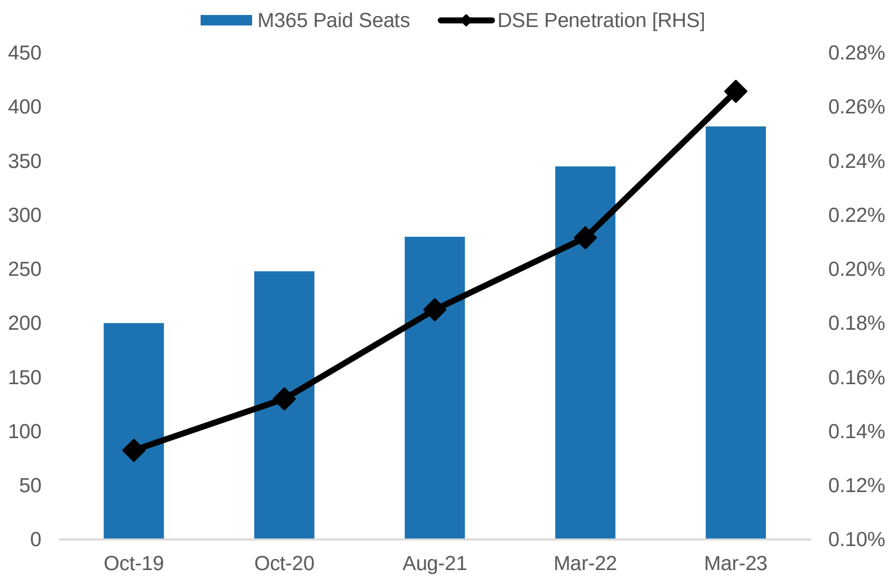
Quantitative: Continuing to take market share

In addition to the qualitative 'best in class' ratings discussed above, we also look at DSE's growth within its broader addressable market – where we would expect to see a correlation between product superiority and market share growth.

As per Figure 42, this appears to be the case, with DSE taking market share on a consistent (and rapid) basis since 2018. We define DSE's market share as paid users / total global M365 seats.

Note: this methodology does not account for the secondary markets served by DSE, i.e. Google Workspace, or Quickbooks.

Figure 42: Paid user additions, QoQ



Source: Company Reports, Ord Minnett Limited estimates

Microsoft 365 Backup & Archive

Background

At its Inspire Conference 2023, Microsoft provided a first look at its *365 Backup and Archive* (B&A) solutions, which will help companies protect and manage their data. The services will be included within the company's *Syntex* suite of products; which use AI to enrich and process large, unstructured data sets.

B&A will provide organisations with an ability to backup and recover data associated with OneDrive, SharePoint and Exchange services within a customer's existing M365 environment. The products will let organisations search and filter content for backups using metadata, while users can restore some or all files, sites and mailbox items.

At this stage B&A only allows site-level archiving, although the company expects to add file-level arching 'in the second half of 2024".

Figure 43: M365 core application range

Source: Microsoft website

Partnerships

Microsoft also noted B&A will include more extensive APIs available for partners to enhance their existing offerings. At this stage, the early named partners comprise of many DSE direct competitors, including AvePoint, Barracuda, CommVault, Burik, Veeam and Veritas.

We feel the threat is overblown…

While details remain scarce (public preview slated for 4Q23), Microsoft's services do appear to be in direct competition with DSE's existing products and seem well-suited for certain SME and enterprise customers.

However, based on our proprietary work and discussions with industry participants, we conclude that fears of any existential risk to DSE's business are overblow, given:

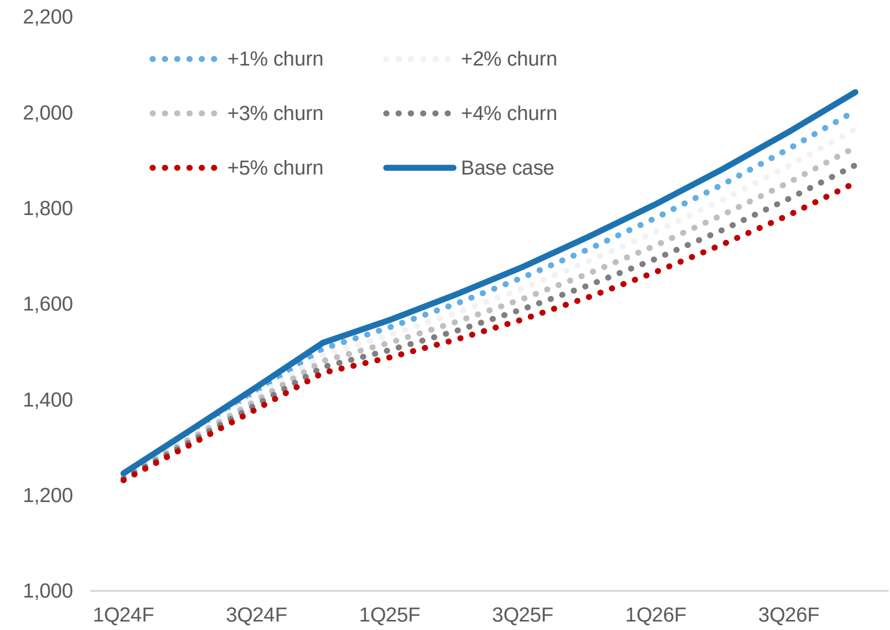
- MSPs will remain favourably disposed to DSE's product > Microsoft's, given the potentially higher margins / selling incentives attached to the former.
- The product is arguably not a true 'disaster recovery' solution, given Microsoft represents a single point of failure for Azure users.
- The markets for backup and archiving are large enough, and growing rapidly enough, to sustain both DSE and Microsoft.
- Microsoft's B&A product will not be suitable non-Azure users, nor multi-cloud operators.
- Microsoft's $/GB pricing model will not be suitable for all users.
- DSE still has superior features and user interface – both of which will take time for Microsoft to improve.
- Given the relative size of the SME backup and archiving market, Microsoft is likely to target enterprise customers (ie. not DSE's core target).

…although there is clearly some risk to growth

While we certainly don't see Microsoft's entry into the market as existential, we are partial to the view that it could weigh on growth. In particular, noting that even modest increases in churn can compound to have enormous impacts on growth over time.

Figure 44 shows that a ~5% increase in churn rates (ie. from 3% to 8%) would reduce net new user growth by >20% between FY24 – FY26. Accordingly, we will continue to watch developments over the coming year and have modelled some fairly material increases in churn rates beginning 1Q25, lasting through FY26.

Figure 44: Churn impact on net new user growth



Source: Ord Minnett Limited estimates

Structural Driver #1 – The rise of cybercrime

Background

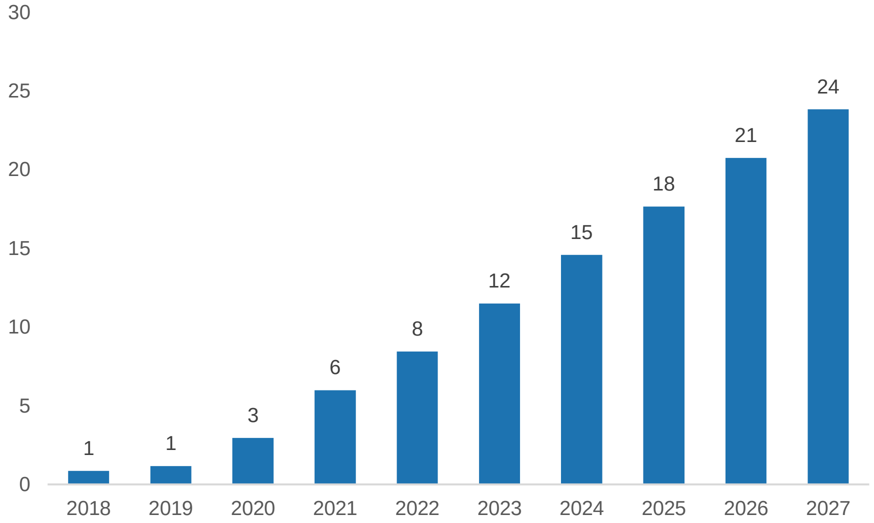
The rise of cybercrime is relentless, with increases in internet connectivity and the proliferation of smart devices providing cybercriminals with new avenues to exploit individuals.

In 2022, the average cost of a data breach was $4.4m, a 15% increase over the past 3 years (IBM), with this increase largely due to a rise in ransomware attacks, which are becoming increasingly sophisticated and costly.

- **Ransomware** is a form of malware that encrypts a victim's data, subsequently making it inaccessible unless a 'ransom' is paid to the attacker.
- The average downtime caused by a ransomware attack is 11 days, while **the average cost of downtime is US$5,600 per minute.**
- Of all cyber insurance claims, 34% were ransomware-related in 2022.
- IBM estimated an average ransom payment of $812k in 2022.

In addition to ransomware, businesses are also facing increased threats from other forms of malware, including phishing attacks, zero-day attacks, and/or supply chain attacks – the size and scope of which increase each year. In fact, the cost of all cybercrime is predicted to reach US$12tr in 2023, before rising further to US$24tr by 2027 (Figure 45).

Figure 45: The rising costs of cybercrime (US$tr)



Source: Statista, FBI, IMF

Migration to the cloud has only further exacerbated the issue

While offering myriad benefits (paradoxically, including improved security), the rise of cloud computing has actually contributed to the rise in cybercrime as businesses and individuals increasingly store sensitive data on cloud platforms – enticing cyber criminals to try and attack.

And while the aforementioned rise in cybercrime, malware, and other threats make it more important than ever for businesses to have backup and storage solutions in place to protect their data, <u>ultimately the cloud service providers cannot be relied upon to provide this service.</u>

This is due to the aforementioned concept of a **'Shared Responsibility Model'**.

All stakeholders are incentivised to address cloud security…

While companies are highly incentivised to implement cloud security measures given the potential for financial, regulatory and reputational impacts, it is equally the purview of all other stakeholders within the cloud computing ecosystem.

Cloud service providers

Security fears are cited as the biggest hesitation from customers evaluating a switch from legacy on-prem to the cloud. Accordingly, CSPs must maintain robust security measures if they wish to attract new customers. Moreover, and as with companies, issues of brand damage and regulatory compliance are front of mind for CSPs.

MSPs

In addition to standard regulatory and reputational considerations, MSPs are further incentivised to focus on cloud security sales, given:

- Provision of cloud backup and storage solutions can act as a differentiator when competing with peers.
- Backup and storage solutions may allow distributors or MSPs to expand their target market and customer base.
- Myriad benefits associated with improved customer satisfaction, for example increased retention and word-of-mouth referrals.

Distributors

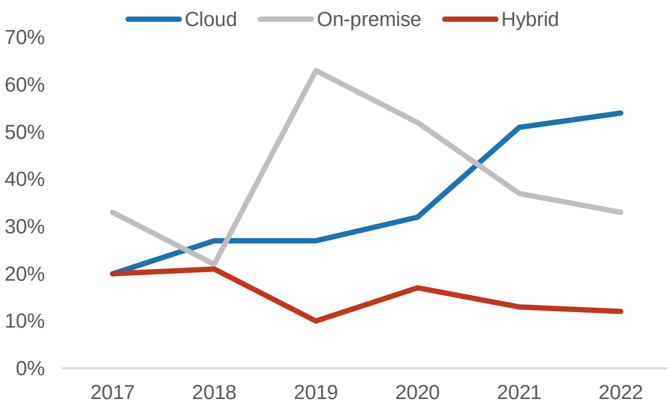
Distributors are incentivised by increased revenue and profitability associated with cloud backup provision. These products are typically (1) sold on a recurring revenue basis, and (2) attract higher margins than other IT products and services.

…although at this stage, behaviour looks broadly unchanged

Cloud backup has been rising is absolute terms (Figure 46), although we attribute this growth to the structural movement away from on-premise hosting. When looking at backup trends across all mediums, the findings suggest that backup habits remain broadly unchanged (in fact, there is a modest trend towards less-frequent backups), per Figure 47.

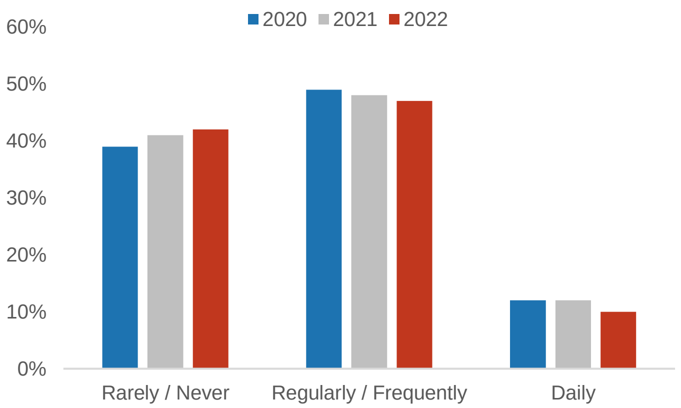
- Only 10% of organisation back up their data daily.
- Over half of IT users (56%) lost data at least once in 2021, 26% lost data multiple times.
- The percentage of businesses 'rarely' or 'never' backing up their data has stayed constant at ~40% for 3 consecutive years.

Figure 46: Backup by medium



Source: Acronis, 2022

Figure 47: Q: 'how often do you backup your data'



Source: Acronis, 2022

Given the above dynamics, we expect to see rates of cloud backup rise over time as data security breaches grow in regularity and scale, and the premise on which the SRM is based becomes more-widely appreciated.

Structural Driver #2 – Migration to the cloud

What is driving migration to the cloud?

Cloud migration encompasses the movement of data, applications and other digital assets, which were traditionally housed in on-premise data centres, to the cloud. This migration has been arguably the largest structural trend in technology over the past decade and is being driven by several factors, including.

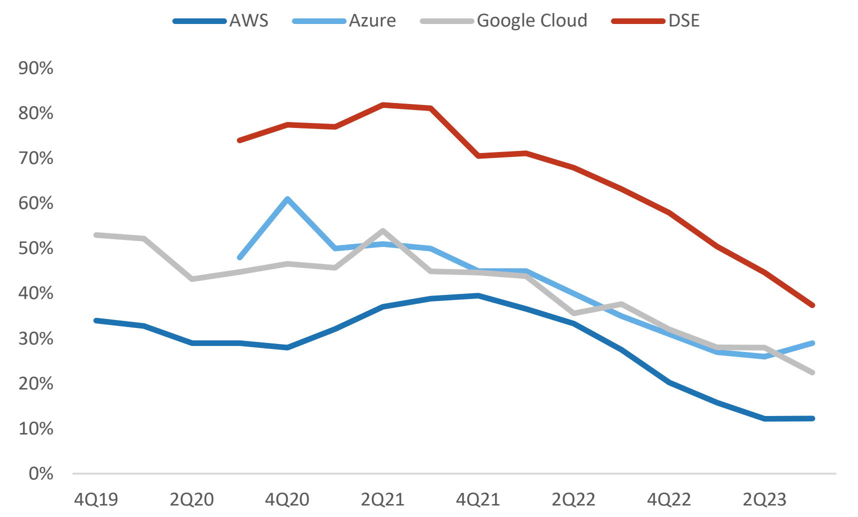
- **Cost efficiencies.** Businesses can significantly reduce capital expenditures on expensive hardware and software infrastructure items by paying on an 'as-a-service' basis.
- **Scalability.** Businesses can effortlessly scale their cloud usage up or down in-line with their demand requirements.
- **Reliability.** By relying on the cloud, businesses can reduce risks associated with on-premise hardware solutions failing or breaking down and interrupting business continuity.
- **Enhanced security and compliance.** Noted as the key reason organisations move to the cloud. Cloud service providers invest heavily in robust security measures, which often surpass what individual organisations could otherwise achieve.

DSE is highly correlated with growth in public cloud usage…

DSE exists to address the needs of businesses migrating to the cloud. Accordingly, it stands to reason that we should see a high level of correlation between its growth and general trends in cloud adoption, with the latter creating demand for its services.

Figure 48 compares growth rates for AWS, Azure and Google Cloud (the 'big 3') with those of DSE, demonstrating that (as expected) the two are inexorably linked.

Figure 48: DSE vs 'big 3' growth rates

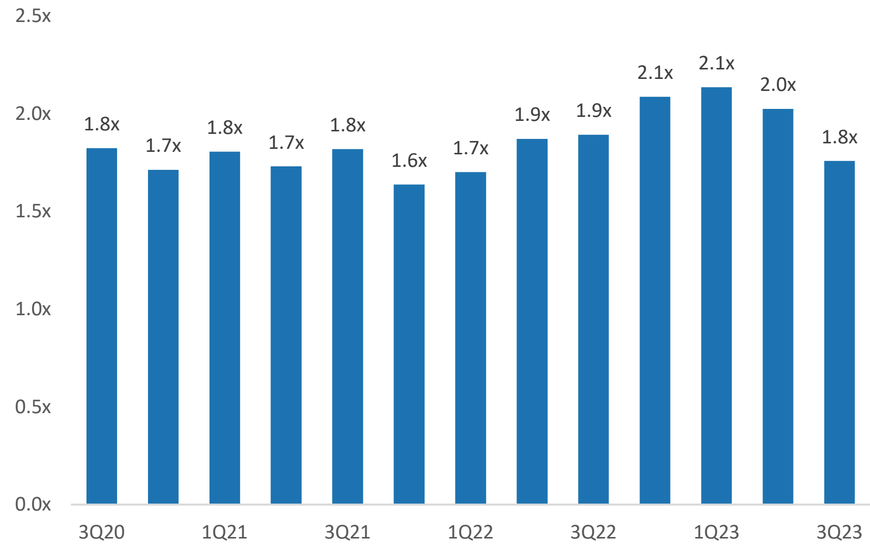


Source: Company reports, Ord Minnett Limited estimates

…and grows at ~2x the system average

DSE has historically grown at ~2x the system average, a trend which we expect to continue for the foreseeable future given the strengths discussed throughout this note, ie. its superior product offering, channel partner relationships, increased focus on security and growth of the MSP market etc.

Figure 49: DSE growth has been running at ~2x system



Source: Company Reports, Ord Minnett Limited estimates

Recent trends: Optimisations have weighed on cloud growth…

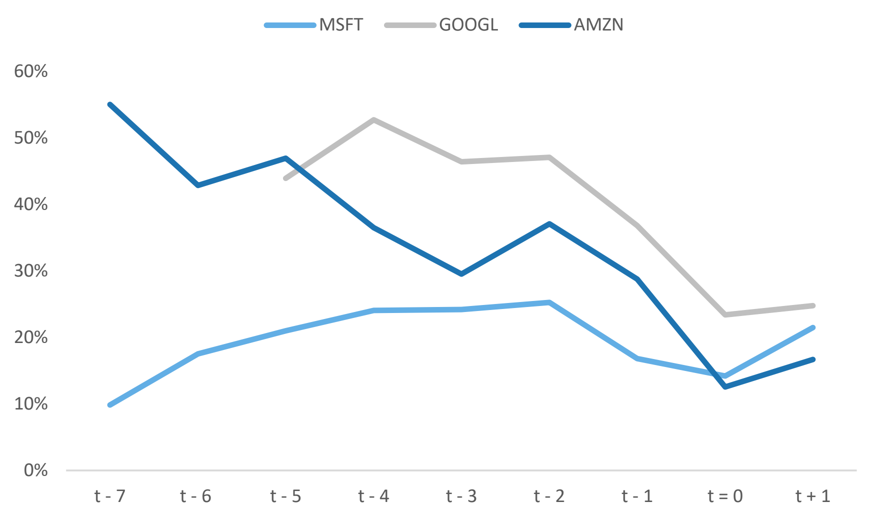
As per Figure 49 above, growth in cloud revenues across the major global providers has slowed markedly from >40% in 2021 to ~12-30% in the September quarter. And while some of this can be attributed to natural moderation that comes with extreme scale, the more-pronounced driver has been a slowing of consumption as cloud customers optimise their usage for leaner economic times. This is particularly true within the technology / software sectors.

…although a bottoming / re-acceleration appears to be forming…

We are beginning to see green shoots which suggest workloads are coming online at a more-rapid pace and the 'optimisation' thematic has played out. Accordingly, we suggest a re-acceleration in software revenues could be instore over 2024.

- Q3 results commentary as it related to AWS, Azure and Google Cloud was more upbeat in general.
- Bloomberg consensus estimates for each of these 'big 3' cloud providers show a bottoming / re-acceleration in cloud revenues over the coming year.

Figure 50: DSE vs 'big 3' growth rates

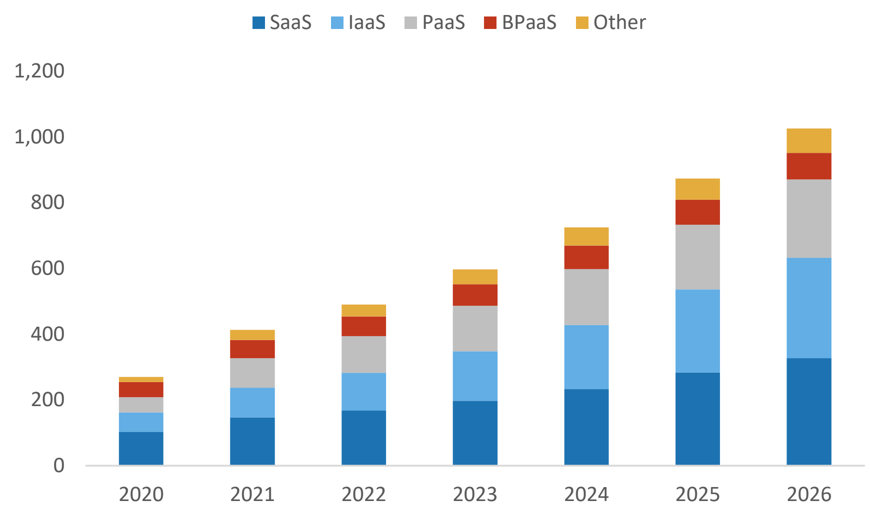


Source: Bloomberg
Note: MSFT = Sep year-end, consensus + / - XX years

Structural trends: Thematic shows no signs of stopping

We believe the abovementioned slowdown in cloud migrations is cyclical > structural and expect to see robust growth continue over the balance of the decade. This view is shared by leading industry consultants, Gartner, who continue to forecast the public cloud market growing to >US$1tr by 2026, or a 4-year CAGR of 20% (Figure 51).

Figure 51: Public cloud market forecasts (US$b)



Source: Gartner Research

Structural Driver #3 – Growth of the MSP industry

Background

The global managed services market was estimated at >US$250bn in 2022 and has been growing rapidly given an increasingly complex technology landscape. Against this backdrop, MSPs play a pivotal role as many organisations (particularly those at the smaller end of the market) simply do not possess the in-house resources to deal with all this complexity.

Benefits of MSPs

- **Expertise**. The employment of skilled IT professionals ensures businesses of all sizes have access to expertise in areas such as cybersecurity, cloud computing and network management.
- **Cost efficiency.** MSPs typically operate on a subscription model, eliminating the need for upfront investments.
- **Enhanced security.** As mentioned throughout this note, cybersecurity concerns are rising. MSPs offer robust security solutions to aid in addressing this problem.
- **Scalability and flexibility**. MSPs provide scalable solutions that can adapt (up or down) with growth in a business.
- **Support.** Typically, 24/7 support services are on offer. This can reduce business disruptions even if outside of standard operating hours.

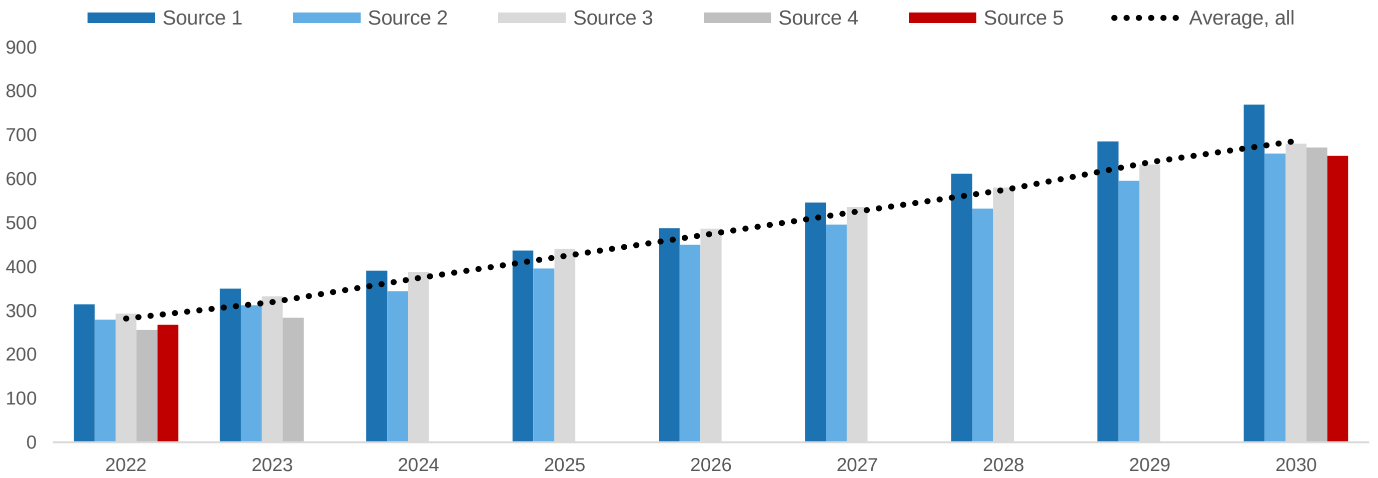
Ultimately, outsourcing IT management to MSPs allows organisation to concentrate on their core business functions.

Growth expected to run at ~3-4x the broader IT market

Going forward, the MSP industry is estimated to continue growing at an 8-14% CAGR through FY30 (depending on the source), well in excess of both GDP and the broader IT market (typically quoted as ~3-4x sector growth). Growth will be supported by:

- Ongoing **migration to the cloud** – with SMEs and enterprises leaning on MSPs to assist in transition.
- The **rise of remote work** and the complexities that brings for companies.
- The growing need for **cybersecurity** solutions.
- The **proliferation of mobile devices**, and
- **Future technologies** such as AI, robotics and quantum computing – all of which will only further complicate the global IT landscape.

Figure 52: Growth of the MSP industry (US$b)



Source: Grandview Research, market.us, Spherical Insights, Fortune Business, Precedence Research

Detailed Financials

Profit and Loss

Revenues

We expect top-line growth to moderate, from 52% in FY23F to a (still robust) 41% in FY24 and a 3-year CAGR of 30% through FY26F. Our estimates are predicated on:

- **Gross users:** Gross adds are expected to remain at the recent ~90k/qtr run-rate through FY24 and rise modestly thereafter.
- **Churn:** The recent churn of a legacy, non-core customer is expected to finish in 4Q23, when a further ~40k users come off. We then model a return to base-line ~3%/year in FY24, before a material step-up associated with the launch of Microsoft's B&A product beginning from 1Q25.
- **Net new users:** The above assumptions result in a re-acceleration of net user growth from 1Q24 and drive total users to 2.04m by the end of FY26, up ~900k vs 4Q23F – a 3-year CAGR of 21%.
- **ARPUs:** USD ARPUs rise to $1.90 by FY26F, +$0.23 vs FY23F, a very modest ~4% 3-year CAGR, as recent positive mix benefits (churn-related) subside.

Additional detail on our longer-term forecasts are contained within Figure 53.

Figure 53: Revenue drivers

Revenue Drivers	Units	FY20A	FY21A	FY22A	FY23F	FY24F	FY25F	FY26F	3YR
Revenue	**A$m**	**7.0**	**11.7**	**20.7**	**31.5**	**44.3**	**57.2**	**69.0**	**30%**
…growth	%		66%	77%	52%	41%	29%	21%	
Paying Users	000s	431	649	935	1158	1519	1741	2043	21%
…growth	%	50%	51%	44%	24%	31%	15%	17%	
Monthly ARPU	A$	1.64	1.95	2.26	2.57	2.69	2.81	2.92	4%
…growth	%	9%	19%	16%	14%	5%	4%	4%	
ARR	A$m	8.5	15.2	25.4	35.7	49.1	58.7	71.6	26%
…growth	%	0.6	80%	67%	40%	37%	20%	22%	

Source: Ord Minnett Limited estimates

Expenses

- **Gross profits.** Margins rise from 69% in FY23F to 71% in FY26F, driven by ongoing efficiencies and benefits of scale.
- **Cash opex:** Employee Benefits as a percentage of subscriptions fall to 37% (from 42% in FY23F) as a natural consequence of scale. SBP comes down in-line with this growth. All other line items increase broadly with revenue growth rates.
- **Statutory EBITDA:** rises from $2.2m to $10.5m over the same period. Margins rise from +7% to +15%.
- **Adj. EBITDA:** rises from $3.2m in FY23F, to $12.4m by FY26F (margins +10% to +18%). The sole different between statutory and adjusted EBITDA is share-based compensation.

Figure 54: Expense drivers

Expense Drivers		FY20A	FY21A	FY22A	FY23F	FY24F	FY25F	FY26F	3YR
Gross Profits	**A$m**	**4.6**	**7.5**	**13.6**	**21.7**	**30.9**	**40.5**	**49.3**	**31%**
Margins %		65%	64%	66%	69%	70%	71%	71%	
Marketing & Conference	A$m	-0.4	-0.6	-1.0	-1.6	-2.2	-2.9	-3.5	30%
Technology	A$m	-0.3	-0.3	-0.6	-0.9	-1.3	-1.7	-2.1	30%
Professional Fees	A$m	-0.3	-0.3	-0.3	-0.6	-0.9	-1.1	-1.4	30%
Employee Benefits	A$m	-4.5	-5.0	-8.1	-13.2	-17.9	-22.0	-25.2	24%
Stock-Based Compensation	A$m	-0.2	-0.2	-0.9	-1.0	-1.3	-1.7	-1.9	24%
Other	A$m	-0.7	-1.2	-1.5	-2.2	-3.1	-4.0	-4.8	30%
Operating Expenses	**A$m**	**-6.3**	**-7.5**	**-12.4**	**-19.6**	**-26.8**	**-33.4**	**-38.8**	**26%**
% of revenues									
Marketing & Conference	% of sales	-5%	-5%	-5%	-5%	-5%	-5%	-5%	
Technology	% of sales	-4%	-3%	-3%	-3%	-3%	-3%	-3%	
Professional Fees	% of sales	-4%	-2%	-1%	-2%	-2%	-2%	-2%	
Employee Benefits	% of sales	-63%	-42%	-39%	-42%	-40%	-38%	-36%	
Other	% of sales	-10%	-10%	-7%	-7%	-7%	-7%	-7%	
D&A	A$m	-0.5	0.0	-0.1	-0.1	-0.2	-0.3	-0.3	42%
Stock-based compensation	A$m	-0.2	-0.2	-0.9	-1.0	-1.3	-1.7	-1.9	24%
Adj. EBITDA	**A$m**	**-1.4**	**0.2**	**2.1**	**3.2**	**5.5**	**8.8**	**12.4**	**58%**
Margins %	%	-20%	1%	10%	10%	12%	15%	18%	

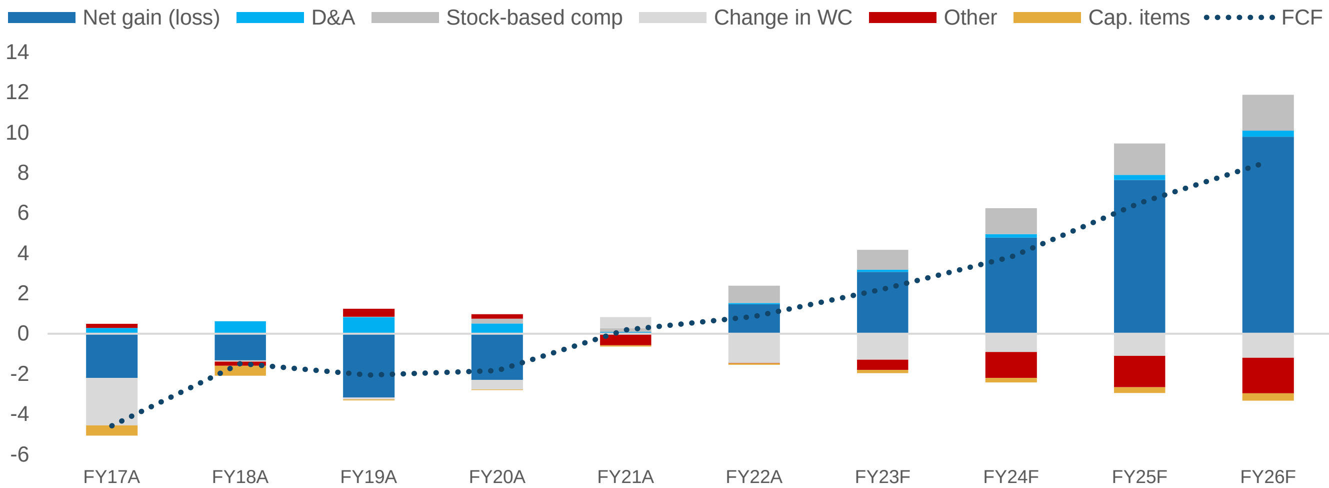
Source: Ord Minnett Limited estimates

Cash flow statement

We model FCF for FY23F of $2.2m, rising to $9.0m by FY26.

- Net profit / loss improves in-line with our expectations for the profitability of the wider business.
- We subtract any capitalised items, being just minor capex and ~$300k per year of capex.
- We do not model any material items below FCF, i.e. no placements, borrowing, or dividends before FY26F.

Figure 55: Free Cash Flow chart



Source: Ord Minnett Limited estimates

Balance sheet

DSE is a capital light business, with minimal capital expenditures and has a clean balance sheet. The company is debt free and carries zero intangibles. The company has accessed external equity capital twice in its history as a listed company.

- Cash balances rise from $23.0m at 1H23 to $44.2m by FY26. We expect cash to end FY23F at $24.6m.
- An alternative use of excess funds could include re-investing for growth and/or returning capital to shareholders. At this stage we forecast and expect neither.

Figure 56: Balance sheet

Balance Sheet (A$m)	FY20A	FY21A	FY22A	FY23F	FY24F	FY25F	FY26F
Current Assets							
Cash	2.5	21.6	22.3	24.6	28.4	35.2	44.2
Trade Receivables	1.4	2.2	4.1	6.3	8.7	10.8	13.1
Other	0.1	0.2	0.4	0.7	0.7	0.7	0.7
Current Assets	**4.0**	**24.0**	**26.8**	**31.6**	**37.8**	**46.8**	**58.0**
Non-Current Assets							
Investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0
PP&E	0.0	0.0	0.1	0.1	0.2	0.2	0.3
Other	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Non-Current Assets	**0.1**	**0.1**	**0.1**	**0.2**	**0.3**	**0.3**	**0.4**
Current Liabilities							
Trade Payables	0.7	2.0	2.5	3.5	4.7	5.7	6.6
Deferred Income/Contract Liability	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Income Tax Provision	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Employee Benefits	0.6	0.0	0.0	0.4	0.4	0.4	0.4
Borrowings	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current Liabilities	**1.4**	**2.2**	**2.6**	**4.0**	**5.2**	**6.2**	**7.2**
Non-Current Liabilities							
Other	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Non-Current Liabilities	**0.0**	**0.1**	**0.1**	**0.1**	**0.1**	**0.1**	**0.1**
Issued Capital	24.0	43.4	43.4	43.4	43.4	43.4	43.4
Reserves	0.2	0.1	1.0	1.7	1.7	1.7	1.7
Retained Earnings	-21.6	-21.6	-20.2	-17.4	-12.4	-4.3	6.0
Total Equity	**2.7**	**21.9**	**24.2**	**27.8**	**32.8**	**40.8**	**51.1**
Net Debt (Cash)	-2.5	-21.6	-22.3	-24.6	-28.4	-35.2	-44.2

Source: Ord Minnett Limited estimates

Risks / Catalysts

Key risks

- **Point solution.** DSE's revenues are reliant on its M365 backup and archiving products, which raises a concentration risk. Additional product launches and/or growth in secondary product lines (ie. QBO) will help moderate this risk.
- **Microsoft Syntex B&A**. As discussed throughout this report, Microsoft's B&A product is expected to launch 2H24. And while we don't believe this will pose an existential risk to DSE's business; developments will need to be monitored closely.
- **Key person risk**. The loss of key personnel, most-critically long-serving CEO Charif Elansari, is a key risk factor.
- **Technology risk.** The technology sector is fast-moving and as such, there is a risk that new (and superior) products come to market and usurp the market incumbents.
- **Security breaches**. A malicious attack on DSE's systems could place the integrity and privacy of client data (and its own reputation) at risk. As a security vendor, this is of particular importance. DSE follows industry best practices to minimise this risk.
- **Key business relationships.** DSE relies on relationships with key business partners including industry giants such as Ingram Micro and Pax8. A failure to maintain these relationships could impact business performance.

Catalysts

- **Re-acceleration of net user growth.** We believe essentially all of the recent 'slow down' in net adds is explained by the churn of a single legacy, non-core, hosting partner. This event will finish in 4Q23 which should see net adds re-accelerate from 1Q24. We feel this dynamic is underappreciated.
- **M&A**. We believe M&A has the potential to increase ARR by ~$5m (assuming an all-cash transaction at peer average ~4x multiples). A transaction of this nature would be well-received.
- **Lapping Syntex B&A launch**. Microsoft's B&A may act as an overhang, given its impact on DSE's business remains unknown until post launch. Accordingly, we see a re-rate opportunity once the product is in-market (and assuming its impact is negligible).
- **IR's → tech re-rate**. Global stock markets came under pressure beginning late-2021 and throughout 2022 as higher interest rates weighed on valuations. This was particularly true for longer-duration segments of the market, like software. Any reversal in inter rates is therefore likely to be positive for the broader sector and DSE within it.

ESG

Environmental

Data centres, required for cloud storage and computational power, consume a sizeable amount energy in their operation. As the shift to cloud continues globally, the associated carbon footprint is forecast to grow with it. Whilst DSE have not provided estimates on their emissions across Scopes 1, 2, or 3, we believe the company's largest contributor to its carbon footprint would be data hosting.

Social

DSE's *Diversity Policy* outlines the firm's objectives and strategies in order to achieve a diverse workforce.

Objectives to achieve include:

(a) diverse and skilled workforce, leading to continuous improvement in service delivery and achievement of corporate goals;

(b) a workplace culture characterised by inclusive practices and behaviours for the benefit of all staff;

(c) improved employment and career development opportunities for women;

(d) a work environment that values and utilises the contributions of employees with diverse backgrounds, experiences and perspectives through improved awareness of the benefits of workforce diversity and successful management of diversity; and

(e) awareness in all staff of their rights and responsibilities with regards to fairness, equity and respect for all aspects of diversity.

Measurable Objectives set by the Board are included in the annual KPIs for the CEO/MD and senior executives. These KPIs are not formally disclosed.

Women are currently underrepresented at both the Board and senior leadership levels. The board of directors comprises of zero women, whilst the leadership team has one woman out of the seven.

Governance

DSE is committed to ensuring the appropriate governance measures are undertaken with the appropriate frameworks in place. The company's policies and charters outlining these, including a) Corporate Governance Statement, b) Share Trading Policy, c) Anti-Corruption Policy, d) Board Charter, e) Continuous Disclosure Policy, f) Constitution, g) Diversity Policy, and the h) Whistleblower Policy.

Figure 57: Shareholdings - key management personnel (FY22)

	Shares	Performance Rights	Total
Theo Hnarakis	11,752,311	-	11,752,311
Charif El Ansari	33,685,439	400,000	34,085,439
Bruce Tonkin	1,514,123	-	1,514,123
Ridley Ruth^	15,594,468	200,000	15,794,468
Ron Hart*	9,494,667	200,000	9,694,667
Bill Kyriacou	1,454,444	240,000	1,694,444
Manoj Kalyanaraman	-	3,200,000	-
Kobe Li	120,000	80,000	200,000
Total	**73,615,452**	**4,320,000**	**74,735,452**

*Source: Ord Minnett Limited estimates, FY22 Annual Report, ^ Ridley Ruth resigned from DSE in late 2023, * Ron Hart no longer classified as key management personnel*

Figure 58: Remuneration - key management personnel (FY22)

	Fixed Remuneration			Variable Remuneration		
$AUD	Salary	Post-employment	Other	Cash STI	Equity Settled	Total Remuneration
Non-Executive Directors						
Theo Hnarakis	163,636	16,773	-	-	-	180,409
Bruce Tonkin	75,000	7,688	-	-	-	82,688
Executive Directors						
Charif El Ansari	341,291	-	1,193	107,972	62,972	513,428
Other Key Management Personnel						
Ridley Ruth^	253,174	-	65,730	124,761	6,490	450,155
Ron Hart*	30,206	-	888	-	6,490	37,584
Manoj Kalyanaraman**	248,110	-	1,937	-	191,114	441,161
Bill Kyriacou	137,800	7,350	3,000	-	11,677	159,827
Kobe Li	60,000	-	-	-	290	60,290
Total	**1,309,217**	**31,811**	**72,748**	**232,733**	**279,033**	**1,925,542**

*Source: Ord Minnett Limited estimates, FY22 Annual Report, ^ Ridley Ruth resigned from DSE in late 2023, * Ron Hart no longer classified as key management personnel, **remuneration from 16 Feb 2022 to 31 Dec 2022.*

Incentives

Cash bonus and incentive payments linked to certain individuals (not all) are measured on the outcome of defined EPS targets being met. These targets are undefined. The 'at-risk' short-term incentives of management are subject to annual performance reviews, undertaken by the Nomination and Remuneration Committee. No explicit KPIs or metrics determining incentive outcomes are outlined. We expect investors to prefer a greater level of disclosure. The issuance of various performance rights are subject to meeting a 30-day period VWAP from the date of grant.

Figure 59: Remuneration – Fixed and at risk

	Fixed remuneration		At risk - STI		At risk - LTI	
Name	2022	2021	2022	2021	2022	2021
Non-Executive Directors						
Theo Hnarakis	100%	100%	-	-	-	-
Bruce Tonkin	100%	100%	-	-	-	-
Executive Directors						
Charif El Ansari	67%	69%	21%	22%	12%	10%
Other KMP						
Ridley Ruth	71%	67%	28%	32%	1%	1%
Ron Hart	86%	84%	12%	16%	2%	-
Bill Kyriacou	93%	95%	-	-	5%	-
Manoj Kalyanaraman	57%	-	-	-	43%	-
Kobe Li	100%	100%	-	-	-	-

Source: DSE FY22 Annual Report

Investment Thesis, Valuation, and Risks

Dropsuite Limited *(Buy; Price Target: $0.33)*

Company Overview

Founded in Singapore in 2011, Dropsuite is a cloud-based software platform offering backup, archiving, and recovery solutions for businesses. The company specialises in protecting critical data from Microsoft 365, Google Workspace, QuickBooks, and others. Its products are distributed via a network of ~4k IT reseller partners globally.

DSE has delivered rapid top-line growth since its founding, with ARR rising at a 7-year CAGR of >70%, while growth has only fallen below 50% on one occasion. The company now serves >1m end users and is expected to generate >$30m in revenues for FY23F.

A profitable grower at the intersection of three mega-trends

As a leading provider of cloud-based backup and archiving for businesses, DSE operates at the intersection of three mega-trends, being (1) the rise of cybercrime, (2) the migration of on-premise hosting to the cloud, and (3) MSP industry growth. These themes have long runways and will continue to act as positive tailwinds for growth.

DSE has delivered extraordinary growth over the past 7-year (a CAGR of >70%) and has managed to do so profitably – delivering positive FCF in each of the past six quarters, while cumulative cash flows are now positive back to 2Q19. Additionally, management are prudent capital allocators, having built a ~$150m business on just ~$42m of outside capital (of which only ~$18m has been spent). We expect this performance to continue.

Microsoft concerns appear overblown

At its Inspire Conference 2023, Microsoft provided a first look at its 365 Backup and Archive solution (B&A) – DSE's price fell 22% on the day and has not recovered since. However, based on our work, and discussions with industry participants, we conclude that fears of existential risks to DSE's business are overblow. Accordingly, we believe the market's scepticism is providing an opportunity.

Valuation and Recommendation

We derive our 12-month forward A$0.33/Share Price Target via a 10-year DCF, which implies a FTM EV/revenue multiple of 4.0x. We believe this is appropriate given the considerable revenue growth we expect DSE to deliver in the medium-term (3-year CAGR = 30%), its solid gross margin (~70%) and strong FCF profile (FY23F = $2.2m, FY26F = $9.0m).

Our Price Target implies a 32% TSR, which underpins our BUY recommendation.

Risks to Rating and Price Target

Key risks to our core thesis, include:

- Point solution: M365 backup presents a concentration risk. Additional product launches and/or growth in secondary products moderates this risk.
- Increase competition from others within the cloud backup industry.
- Technology risk: new technologies / competitors enter the market and usurp DSE's products.
- Key person risk: DSE is run by a long-time CEO, Charif Elansari. His departure is a risk.
- Security breaches: A malicious attack on DSE's systems could result in client data loss and reputational damage.

Appendix 1 – Board of Directors

Charif El Ansari – Managing Director and Chief Executive Officer

Charif was DSE's first investor before taking over as CEO in October 2013. Prior to DSE, Charif was a founding member of Google Singapore (Asia Pacific HQ), first heading sales and operations then business development for Southeast Asia. In addition to building various regional teams at Google, he negotiated and launched key partnerships with top mobile operators, led the company's first Chrome web browser distribution partnership in Asia, built partnerships and alliances with media companies and led a team to launch the first localized advertising product in Indonesia winning Google Asia Pacific Innovation Award. Prior to Google he worked at Dell in a career that spanned the USA (Dell HQ) as well as China, Korea and Japan. At Dell, Charif took on various leadership roles covering supply chain operations, sales and marketing. He has a B.A. from the American University of Beirut and an MBA from Vanderbilt University (USA) and is member of Australian Institute of Company Directors (AICD).

Theo Hnarakis – Non-Executive Chairman

Theo Hnarakis brings a wealth of experience working in the media industry and scaling Australian ASX listed technology businesses. He graduated from the University of South Australia and held senior roles with News Corporation, Boral Group, the PMP Communications group and was the Managing Director and CEO of Melbourne IT until 2013. He has also held director roles with Neulevel a JV with US based listed company, Neustar, and with Advantate a JV with Fairfax Media.

Bruce Tonkin – Non-Executive Director

Dr Bruce Tonkin is currently Chief Operating Officer for the .au Domain Administration Limited, where he is responsible for operations of the .au (Australia) top level domain name. Prior to that he has been Chief Technology Officer and Chief Strategy Officer at Melbourne IT, where he was responsible for managing the development of the company's strategic and operating plans, strategic initiatives with major customers and suppliers, and managing evaluation of merger and acquisition opportunities. Bruce had been at Melbourne IT from 1999 until April 2017 and has gained more than 15 years of experience taking cloud-based services to global markets across the USA, Europe, and Asia for both SMEs and Enterprises. In that time annual revenue grew from $15m to a peak of $200m with offices in 10 countries, before the sale of its international business. Bruce also served on the Board of ICANN (Internet Corporation of Assigned Names and Numbers) for 9 years. ICANN manages the global domain name and IP addressing system for the Internet.

Eric Martorano – Independent Non-Executive Director

Eric is a highly qualified executive with a deep experience in driving global growth strategy and go-to market initiatives. He has worked for over 25 years with business customers and partners around the globe from small business through to enterprise customers. Eric is currently the Chief Revenue Officer (CRO) for Simplilearn, one of the world's leading online education providers, where he is responsible for sales, customer success, marketing, product, operations and delivery teams with full P&L responsibility for the company's global commercial business. Eric has previously held various leadership positions at Microsoft where he was ultimately General Manager of U.S. Channel Sales with responsibility for over $17 billion of revenue. Eric has also held a range of leadership positions, including CEO and CRO, across several fast-growing technology businesses. Eric holds an MBA from Pepperdine University and a bachelor's degree from California State University, Northridge and he has previously been nominated as CRN's 'Top 100 Executives' and '50 Most Influential Channel Chiefs'.

Eric joints the Dropsuite Board on 1 January 2024.

Appendix 2 - Management

Charif El Ansari – Managing Director and Chief Executive Officer

See Board of Directors.

Bill Kyriacou – Chief Finance Officer

Bill is the Chief Finance Officer of DSE and has been with the company since 2018. Bill brings more than 17 years' experience in building organisations and leading high performing finance teams. Bill's experience includes time across the telecommunications, Software-as-a-service, Agriculture, Media and Entertainment industries. Bill holds a Bachelor of Commerce (Accounting) from Swinburne University of Technology.

Frederique van de Poll – Global Head of Human Resources

Frederique is the Global Head of HR and has been with the company since early 2022. Frederique brings 14 years of experience within the Human Resources industry. Frederique has held senior positions previously with Gravity Supply Chain, Holland International School Limited Singapore, and the Dutch Ministry of Health. Frederique holds a Master of Science, Work and Organisational Psychology from Utrecht University.

Manoj Kalyanaraman – Chief Technology Officer

Manoj brings over 25 years' experience with recent previous roles including Vice President, Product and Engineering at BitTitan, Chief Technology Officer of Next Story Group, and Group Engineering Manager at Intuit. Manoj holds a Bachelor of Engineering (Mechanical Engineering) from the Bangalore University.

Eric Roach – SVP Global Channel Sales & Marketing

Eric joined as the Senior President of Global Channel Sales and Marketing in Oct 2022. Eric is responsible for the company's revenue growth, accountability for the development and execution of the overall go-to-market strategy globally, and the management of global revenue operations. Eric has held similar roles across Accordo Group, Intermedia, and Microsoft.

Mark Kirstein – Chief Product Officer

Mark joined as the Chief Product Officer of DSE in 2023. Mark has over 25 years' experience across product and software engineering. Mark was previously the Vice President of Product Management and Strategic Initiatives at Market Leader and prior to that, the Vice President of Product and Engineering at BitTitan. Mark holds a Bachelor's, Computer Science, from California Polytechnic State University-San Luis Obispo.

Appendix 3 – ASX Listed Software Comps

Figure 60: ASX Listed Comparable Peer Set – High Growth and Profitable

Australian Technology Companies

Australian Software Companies	Ticker	Price	Market Cap	EV	Revenue Growth (%)			Gross Margin (%)			EBITDA Margin (%)			EV/Revenue (x)			EV/Gross Profit (x)			EV/EBITDA (x)			Rule of 40 (%)		
		$/sh	A$m	A$m	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F
ASX Listed																									
WiseTech Global Ltd	WTC AU	73.33	24,442	24,555	25%	29%	62%	85%	86%	87%	61%	59%	48%	38.8x	30.1x	18.6x	45.6x	34.8x	21.5x	63.3x	51.3x	38.4x	86%	88%	110%
Xero Ltd	XRO AU	110.41	16,729	16,754	23%	23%	17%	88%	88%	88%	11%	28%	30%	13.1x	10.6x	9.1x	15.0x	12.1x	10.3x	n.m.	38.6x	29.9x	35%	51%	47%
Pro Medicus Ltd	PME AU	93.32	9,747	9,658	38%	34%	62%	99%	99%	99%	98%	96%	76%	n.m.	77.3x	47.6x	n.m	77.8x	47.9x	n.m.	80.6x	62.5x	136%	130%	139%
Altium Ltd	ALU AU	47.36	6,248	5,963	26%	29%	41%	92%	93%	93%	47%	44%	37%	19.6x	15.2x	10.8x	21.2x	16.5x	11.6x	41.8x	34.5x	28.8x	73%	73%	79%
Technology One Ltd	TNE AU	15.10	4,918	4,753	n.a.	34%	13%	87%	88%	88%	47%	43%	45%	12.9x	9.7x	8.5x	14.8x	11.0x	9.8x	27.4x	22.3x	19.1x	n.a.	77%	58%
Life360 Inc	360 AU	7.40	1,500	1,402	119%	67%	17%	74%	75%	76%	-36%	6%	10%	4.3x	2.6x	2.2x	5.7x	3.4x	2.9x	n.m.	42.6x	21.3x	83%	73%	27%
SiteMinder Ltd	SDR AU	4.95	1,371	1,333	15%	30%	60%	67%	66%	65%	-16%	3%	10%	11.5x	8.8x	5.5x	17.2x	13.4x	8.5x	n.m.	n.m.	53.9x	-1%	33%	70%
Gentrack Group Ltd	GTK AU	6.17	636	607	n.a.	35%	14%	n.a.	n.a.	n.a.	18%	15%	17%	5.2x	3.9x	3.4x	n.a.	n.a.	n.a.	28.4x	26.0x	20.2x	n.a.	49%	31%
Nuix Ltd	NXL AU	1.77	570	552	-13%	20%	13%	n.a.	n.a.	n.a.	23%	26%	28%	3.6x	3.0x	2.7x	n.a.	n.a.	n.a.	15.8x	11.8x	9.4x	9%	45%	42%
ReadyTech Holdings Ltd	RDY AU	3.49	408	439	56%	32%	32%	93%	94%	94%	34%	39%	35%	5.6x	4.3x	3.2x	6.0x	4.5x	3.4x	16.5x	11.0x	9.2x	90%	71%	67%
RPMGlobal Holdings Ltd	RUL AU	1.71	385	359	24%	18%	19%	50%	51%	53%	13%	21%	21%	4.3x	3.7x	3.1x	8.7x	7.2x	5.9x	33.9x	17.3x	15.1x	37%	39%	39%
Vista Group International Ltd	VGL AU	1.46	344	335	n.a.	17%	10%	7%	12%	17%	7%	12%	15%	2.7x	2.3x	2.1x	39.8x	19.4x	12.3x	36.6x	19.8x	13.9x	n.a.	29%	25%
3P Learning Ltd	3PL AU	1.21	331	312	69%	17%	9%	95%	95%	n.a.	14%	14%	16%	3.2x	2.7x	2.5x	3.4x	2.9x	n.a.	23.3x	19.5x	15.5x	83%	31%	25%
Volpara Health Technologies Ltd	VHT AU	1.10	279	269	n.a.	23%	18%	92%	92%	92%	-23%	1%	12%	8.4x	6.9x	5.8x	9.1x	7.4x	6.3x	n.m.	n.m.	48.6x	n.a.	24%	30%
Dropsuite Ltd	**DSE AU**	**0.25**	**174**	**152**	**n.a.**	**85%**	**24%**	**68%**	**68%**	**68%**	**7%**	**11%**	**12%**	**7.3x**	**4.0x**	**3.2x**	**10.7x**	**5.8x**	**4.7x**	**n.m.**	**37.6x**	**26.4x**	**n.a.**	**96%**	**36%**
TASK Group Holdings Ltd	TSK AU	0.42	148	128	93%	20%	13%	70%	67%	67%	10%	13%	17%	2.2x	1.8x	1.6x	3.1x	2.7x	2.4x	21.4x	14.3x	9.1x	103%	33%	31%
Energy One Ltd	EOL AU	4.05	122	145	16%	39%	27%	n.a.	n.a.	n.a.	34%	30%	27%	4.5x	3.2x	2.5x	n.a.	n.a.	n.a.	13.3x	11.0x	9.3x	50%	69%	54%
Alcidion Group Ltd	ALC AU	0.08	105	92	33%	18%	25%	87%	88%	89%	-4%	2%	6%	2.7x	2.3x	1.8x	3.1x	2.6x	2.1x	n.m.	n.m.	28.4x	28%	19%	31%
MedAdvisor Ltd	MDR AU	0.19	101	100	75%	45%	30%	33%	34%	35%	-5%	6%	7%	1.5x	1.0x	0.8x	4.5x	3.0x	2.3x	n.m.	17.6x	10.6x	70%	50%	38%
Mean			3,608	3,574	43%	32%	27%	74%	75%	74%	18%	25%	25%	8.4x	10.2x	7.1x	13.9x	14.0x	10.1x	29.2x	28.5x	24.7x	63%	57%	51%
Median			408	439	29%	29%	19%	86%	87%	87%	13%	15%	17%	4.9x	3.9x	3.2x	9.1x	7.3x	6.3x	27.4x	21.0x	20.2x	72%	50%	39%
High			24,442	24,555	119%	85%	62%	99%	99%	99%	98%	96%	76%	38.8x	77.3x	47.6x	45.6x	77.8x	47.9x	63.3x	80.6x	62.5x	136%	130%	139%
Low			21	17	-13%	17%	9%	7%	12%	17%	-36%	1%	6%	1.5x	1.0x	0.8x	3.1x	2.6x	2.1x	13.3x	11.0x	9.1x	-1%	19%	25%

Source: Bloomberg and IRESS as at 20 Dec 2023

NM – Negative EV multiples or multiples greater than 100x are not meaningful

NA – There is no consensus data for this metric e.g. gross margin is not a referenced metric

All figures adjusted to $AUD

Note: 1. Rule of 40 is calculated as EBITDA margin plus revenue growth

Glossary

- **ARR**: Annualised Recurring Revenue - is defined as the value of the contracted monthly recurring revenue multiplied by 12 months.
- **ARPU**: Average Revenue Per User
- **CAGR**: Compound Annual Growth Rate
- **Churn**: Partner Revenue Churn is defined as Lost Revenue in current period divided by previous period Revenue
- **M365:** Microsoft's cloud-based productivity suite, Microsoft 365. The suite includes productivity apps and services like Word, Excel, PowerPoint, Teams, OneDrive and others.
- **MSP**: Managed Service Provider is defined as an outsourced IT provider ensuring business availability and security for mostly small and medium businesses
- **QoQ**: Prior Quarter Comparative Period
- **PCP**: Prior Corresponding Period in Constant Currency % growth
- **SME**: Small to Medium enterprise
- **QBO**: QuickBooks Online

Dropsuite Limited

Buy

PROFIT & LOSS (A$m)	2021A	2022A	2023E	2024E	2025E
Revenue	11.7	20.7	31.5	44.3	57.2
Operating costs	(7.5)	(12.4)	(19.6)	(26.8)	(33.4)
Operating EBITDA	**0.0**	**1.3**	**2.2**	**4.1**	**7.1**
D&A	(0.0)	(0.1)	(0.1)	(0.2)	(0.3)
Non-operating items	-	-	-	-	-
EBIT	**(0.0)**	**1.2**	**2.1**	**3.9**	**6.9**
Net interest	0.0	0.3	0.8	1.0	1.2
Pre-tax profit	**(0.0)**	**1.5**	**2.8**	**5.0**	**8.0**
Net tax (expense) / benefit	-	-	-	-	-
Significant items/Adj.	-	-	-	-	-
Associate NPAT	0.1	1.5	3.1	5.0	8.0
Normalised NPAT	**0.1**	**1.5**	**3.1**	**5.0**	**8.0**
Reported NPAT	**0.1**	**1.5**	**3.1**	**5.0**	**8.0**
Normalised dil. EPS (cps)	0.0	0.2	0.4	0.7	1.1
Reported EPS (cps)	(0.0)	0.2	0.4	0.7	1.1
Effective tax rate (%)	-	-	-	-	-
DPS (cps)	-	-	-	-	-
DPS (cps)	-	-	-	-	-
Dividend yield (%)	-	-	-	-	-
Payout ratio (%)	-	-	-	-	-
Franking (%)	-	-	-	-	-
Diluted # of shares (m)	629.2	699.5	715.4	715.4	715.4

CASH FLOW (A$m)	2021A	2022A	2023E	2024E	2025E
Net Interest (paid)/received	0.0	0.2	0.8	1.0	1.2
Income tax paid	-	-	-	-	-
Other operating items	-	-	-	-	-
Operating Cash Flow	**0.3**	**0.9**	**2.4**	**4.0**	**7.1**
Capex	(0.1)	(0.1)	(0.2)	(0.2)	(0.3)
Acquisitions	-	-	-	-	-
Other investing items	-	-	-	-	-
Investing Cash Flow	**(0.1)**	**(0.1)**	**(0.2)**	**(0.2)**	**(0.3)**
Inc/(Dec) in equity	18.9	-	-	-	-
Inc/(Dec) in borrowings	-	-	-	-	-
Dividends paid	-	-	-	-	-
Other financing items	-	-	-	-	-
Financing Cash Flow	**18.9**	**-**	**-**	**-**	**-**
FX adjustment	-	(0.1)	0.1	-	-
Net Inc/(Dec) in Cash	19.1	0.9	2.2	3.8	6.8

BALANCE SHEET (A$m)	2021A	2022A	2023E	2024E	2025E
Cash	21.6	22.3	24.6	28.4	35.2
Receivables	2.2	4.1	6.3	8.7	10.8
Inventory	-	-	-	-	-
Other current assets	0.2	0.4	0.7	0.7	0.7
PP & E	0.0	0.1	0.1	0.2	0.2
Investments	0.0	0.0	0.0	0.0	0.0
Financial Assets	-	-	-	-	-
Intangibles	-	-	-	-	-
Other non-current assets	0.1	0.1	0.1	0.1	0.1
Total Assets	**24.1**	**26.9**	**31.9**	**38.1**	**47.1**
Short term debt	-	-	-	-	-
Payables	2.0	2.5	3.5	4.7	5.7
Other current liabilities	-	-	0.4	0.4	0.4
Long term debt	-	-	-	-	-
Other non-current liabilities	0.1	0.1	0.1	0.1	0.1
Total Liabilities	**2.2**	**2.7**	**4.1**	**5.3**	**6.3**
Total Equity	**21.9**	**24.2**	**27.8**	**32.8**	**40.8**
Net debt (cash)	(21.6)	(22.3)	(24.6)	(28.4)	(35.2)

DIVISIONS	2021A	2022A	2023E	2024E	2025E

KEY METRICS (%)	2021A	2022A	2023E	2024E	2025E
Revenue growth	66.3	77.0	52.2	40.6	29.2
EBITDA growth	-	49,740.6	73.9	89.8	72.4
EBIT growth	-	-	73.0	91.2	74.1
Normalised EPS growth	-	2,129.8	104.8	61.4	62.4
EBITDA margin	0.0	6.0	6.9	9.3	12.4
OCF /EBITDA	863,392.5	2,949.3	2,622.3	1,958.0	1,463.7
EBIT margin	-	5.8	6.5	8.9	12.0
Return on assets	-	4.7	7.0	11.3	16.1
Return on equity	0.5	6.4	11.8	16.4	21.9

VALUATION RATIOS (x)	2021A	2022A	2023E	2024E	2025E
Reported P/E	-	127.8	67.2	38.3	23.6
Normalised P/E	-	-	61.7	38.3	23.6
Price To Free Cash Flow	828.1	213.0	83.5	48.7	27.1
Price To NTA	6.7	6.7	5.8	4.8	3.9
EV / EBITDA	-	-	-	37.8	21.0
EV / EBIT	-	133.5	77.6	39.6	21.8

LEVERAGE	2021A	2022A	2023E	2024E	2025E
ND / (ND + Equity) (%)	(7,298.6)	(1,178.7)	(777.4)	(655.6)	(632.1)
Net Debt / EBITDA (%)	-	(1,785.5)	(1,132.3)	(688.4)	(494.9)
EBIT Interest Cover (x)	9.4	-	-	-	-
EBITDA Interest Cover (x)	-	-	-	-	-

SUBSTANTIAL HOLDERS	m	%
Topline Capital Management LLC	198.7	28.5%
John Fearon	37.4	5.4%
Charif El-Ansari	34.1	4.9%

VALUATION	
Cost of Equity (%)	10.5
Cost of debt (after tax) (%)	7.5
WACC (%)	**9.8**
Enterprise Value ($m)	181.8
Equity NPV Per Share ($)	**0.30**
Target Price Method	DCF
Target Price ($)	0.33
Valuation disc. / (prem.) to share price (%)	22.8

Institutional Research

Alastair Hunter	Head of Institutional Research	+61 3 9608 4168	ahunter@ords.com.au
Malcolm Wood	Macro Strategy Analyst	+61 2 8216 6777	mwood@ords.com.au
Lindsay Bettiol	Senior Research Analyst	+61 3 9608 4179	lbettiol@ords.com.au
Nicolas Burgess	Senior Research Analyst	+61 3 9602 9379	nburgess@ords.com.au
James Casey	Senior Research Analyst	+61 3 9602 9265	jamescasey@ords.com.au
Phillip Chippindale	Senior Research Analyst	+61 2 8216 6346	pchippindale@ords.com.au
Tom Godfrey	Senior Research Analyst	+61 7 3214 5587	tgodfrey@ords.com.au
Paul Kaner	Senior Research Analyst	+61 7 3214 5514	pkaner@ords.com.au
John Lawlor	Senior Research Analyst	+61 7 3214 5506	jlawlor@ords.com.au
Ian Munro	Senior Research Analyst	+61 3 9608 4127	ian.munro@ords.com.au
John O'Shea	Senior Research Analyst	+61 3 9608 4146	joshea@ords.com.au
Leanne Truong	Senior Research Analyst	+61 2 8216 6367	ltruong@ords.com.au
Rushil Paiva	Research Analyst	+61 3 9608 4155	rpaiva@ords.com.au
Oliver Burston	Research Associate	+61 3 9608 4166	oburston@ords.com.au
Tim Elder	Research Associate	+61 7 3214 5565	telder @ords.com.au
Milo Ferris	Research Associate	+61 2 8216 6691	mferris@ords.com.au
Dylan Jones	Research Associate	+61 3 9608 4104	djones@ords.com.au
William Thurlow	Research Associate	+61 2 8216 6623	wthurlow@ords.com.au
Benjamin Yun	Research Associate	+61 2 8216 6646	byun@ords.com.au

Institutional Sales (Australia)

Angus Esslemont	Head of Institutional Equities	+61 2 8216 6363	aesslemont@ords.com.au
Jim Bromley	Institutional Equities Sales	+61 2 8216 6343	jbromley@ords.com.au
Stephen Jolly	Institutional Equities Sales	+61 2 8216 6424	sjolly@ords.com.au
Isaac Morris	Institutional Equities Sales	+61 2 8216 6370	imorris@ords.com.au
Scott Ramsay	Institutional Equities Sales	+61 3 9608 4100	sramsay@ords.com.au
Matt White	Institutional Equities Sales	+61 3 9608 4133	mwhite@ords.com.au
Zac Whitehead	Institutional Equities Sales	+61 2 8216 6350	zwhitehead@ords.com.au
Trent Stewart	Institutional Derivatives Sales	+61 2 8216 6622	trent.stewart@ords.com.au
Brendan Sweeney	Operator	+61 2 8216 6781	bsweeney@ords.com.au

Institutional Sales (Hong Kong)

Chris Moore	Institutional Equities Sales	+61 2 8216 6362	cmoore@ords.com.hk

Ord Minnett Offices

Head Office
Sydney
Level 18, Grosvenor Place
225 George Street
Sydney NSW 2000
Tel: (02) 8216 6300
www.ords.com.au

Adelaide
Level 5
100 Pirie Street
Adelaide SA 5000
Tel: (08) 8203 2500

Bendigo
Level 1
103 Mitchell Street
Bendigo VIC 3550
Tel: (03) 4433 3400

Buderim (Sunshine Coast)
1/99 Burnett Street
Buderim QLD 4556
Tel: (07) 5430 4444

Brisbane
Level 34
71 Eagle Street
Brisbane QLD 4000
Tel: (07) 3214 5555

Canberra
101 Northbourne Avenue
Canberra ACT 2600
Tel: (02) 6206 1700

Geelong
Office 3, Suite 4
200 Malop Street
Geelong VIC 3220
Tel: (03) 4210 0200

Gold Coast
Level 7
50 Appel Street
Surfers Paradise QLD 4217
Tel: (07) 5557 3333

Hobart
Ground Floor
85 Macquarie Street
Hobart TAS 7000
Tel: (03) 6161 9300

Mackay
45 Gordon Street
Mackay QLD 4740
Tel: (07) 4969 4888

Mildura
128 Lime Avenue
Mildura VIC 3500
Tel: (03) 9608 4111

Melbourne
Level 22
35 Collins Street
Melbourne VIC 3000
Tel: (03) 9608 4111

Newcastle
426 King Street
Newcastle NSW 2300
Tel: (02) 4910 2400

Perth
Level 27
108 St Georges Terrace
Perth WA 6000
Tel: (02) 4910 2400

International
Hong Kong
1801 Ruttonjee House
11 Duddell Street
Central, Hong Kong
Tel: +852 2912 8980
www.ords.com.hk

Guide to Ord Minnett Recommendations

Our recommendations are based on the total return of a stock – nominal dividend yield plus capital appreciation – and have a 12-month time horizon.	
SPECULATIVE BUY	We expect the stock's total return (nominal yield plus capital appreciation) to exceed 20% over 12 months. The investment may have a strong capital appreciation but also has high degree of risk and there is a significant risk of capital loss.
BUY	The stock's total return (nominal dividend yield plus capital appreciation) is expected to exceed 15% over the next 12 months.
ACCUMULATE	We expect a total return of between 5% and 15%. Investors should consider adding to holdings or taking a position in the stock on share price weakness.
HOLD	We expect the stock to return between 0% and 5%, and believe the stock is fairly priced.
LIGHTEN	We expect the stock's return to be between 0% and negative 15%. Investors should consider decreasing their holdings.
SELL	We expect the total return to lose 15% or more.
RISK ASSESSMENT	Classified as Lower, Medium or Higher, the risk assessment denotes the relative assessment of an individual stock's risk based on an appraisal of its disclosed financial information, historical volatility of its share price, nature of its operations and other relevant quantitative and qualitative criteria. Risk is assessed by comparison with other Australian stocks, not across other asset classes such as Cash or Fixed Interest.