F5 Networks

El Nino Investments

Overview

F5 Networks (FFIV)

Application Software Industry

Headquarters: Seattle, WA

Market Cap: 6.86 B

PE: 19x Earnings

PEG: 1.07

Gross Margin: 83%

Net Margin: 19%

History & Acquisitions

1996 - F5 emerged (BIG-IP)

1999 - IPO (NASDAQ)

2003 - uRoam ($25M)

2004 - Magnifire WebSystems ($29M)

2005 - Swan Labs ($43M)

2007 - Acopia Networks ($210M)

2011 - Crescendo Networks' DPI Intellectual Property

2012 - Traffix Systems

2013 - LineRate Systems & Versafe

2014 - Defense.Net

Business

Leading developer & provider of software-defined application services

Application Delivery Networking (ADN)
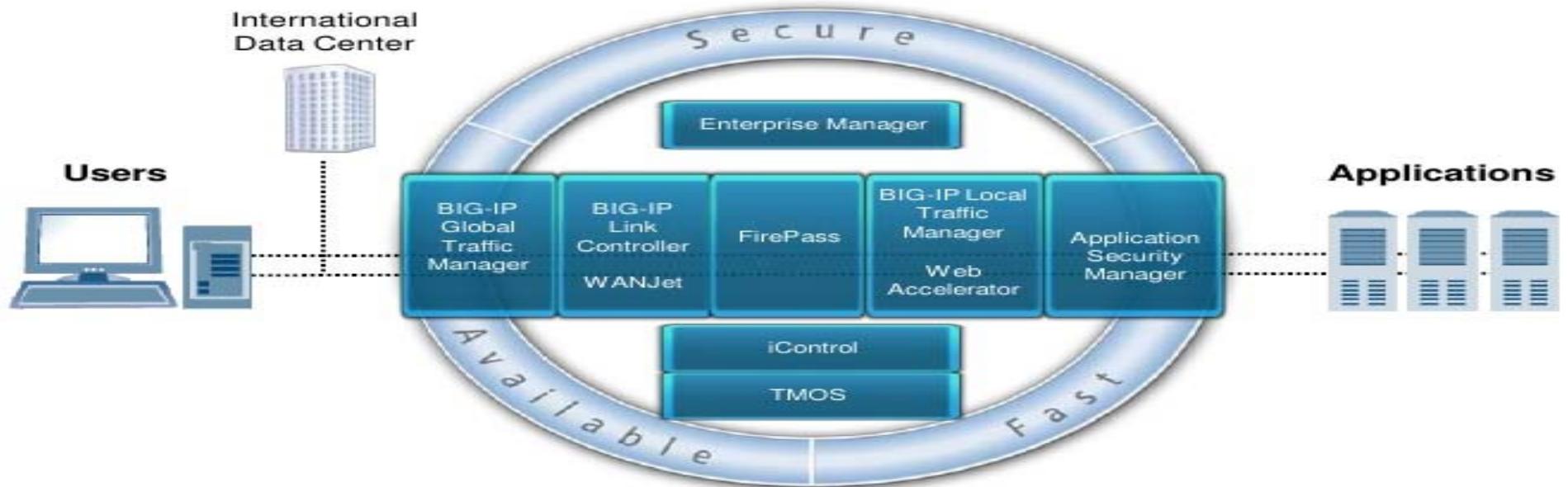
TMOS

**Full proxy software platform that supports industry's broadest array of application services**

Inspect and modify content of IP flows between users & apps

iControl – "the translator"

iRules – "the principal"

iCall – "the scientist"
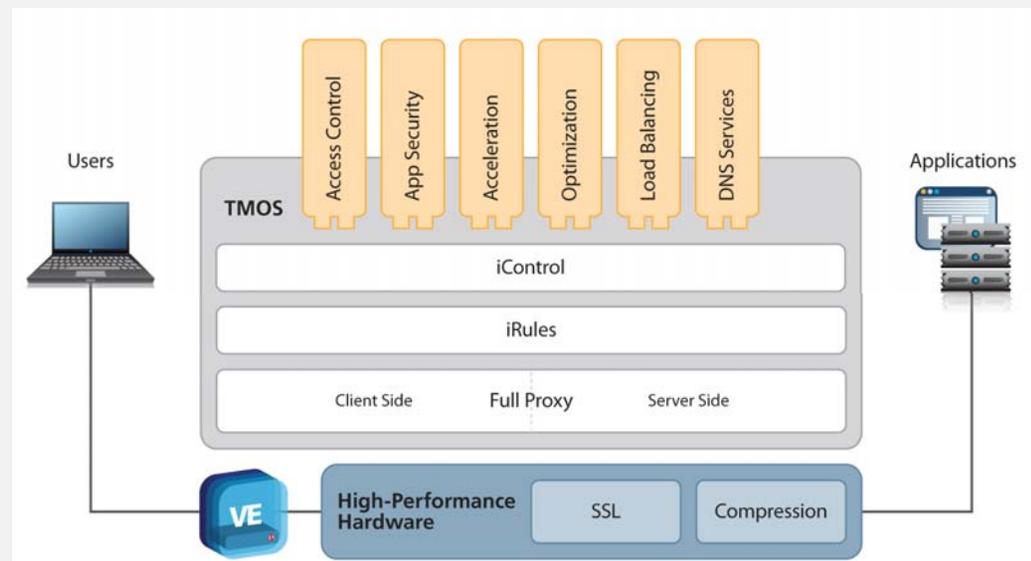
Suite of Application Services (Modules)

Legacy Products

Local Traffic Manager
BIG-IP DNS & Link Controller

Products through Acquisitions

Application Security Manager
Application Acceleration Manager
Access Policy Manager

New Products

Advanced Firewall Manager
Carrier Grade Network Address Translation
Policy Enforcement Manager

End-User Protection Products

WebSafe
MobileSafe

| LTM | GTM | AAM | AFM | APM | ASM | CGNAT | PEM |

The software modules deployed on the platform that deliver Software Defined Application Services

BIG-IP SOFTWARE (TMOS)

SOFTWARE
The brains that make the platform extensible and programmable.

Integrated Solutions (Hardware)

Purpose-built hardware servers designed to optimize performance of modules

> **BIG-IP appliances**
>
> **VIPRION products**

Massive performance and scalability to allow consolidation

Cost efficient

VIPRION Hardware Platform   BIG-IP Hardware Platform
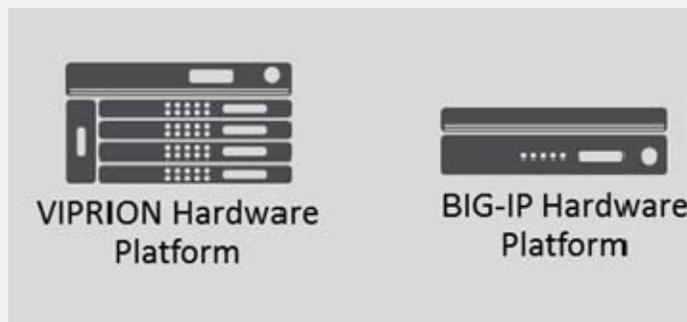
Virtual Editions (Software)

Software-only editions of modules

Industry's largest mix of software-only offerings

Greater flexibility to deploy a mix of integrated app services

Tend to have lower performance than hardware

Common Attributes between H & S

Deployed in Hybrid Infrastructures

    Data Center and Private

    Multiple Data Centers

    Data Center and Public

Modules can be sold individually in both forms

Support all modules

Subscription Services

'14 Cloud-Based (Silverline) – SaaS platform

> DDoS protection
>
> Web Application Firewall
>
> Very Customizable

End-User Protection Modules

> WebSafe
>
> MobileSafe

Cloud
Servers
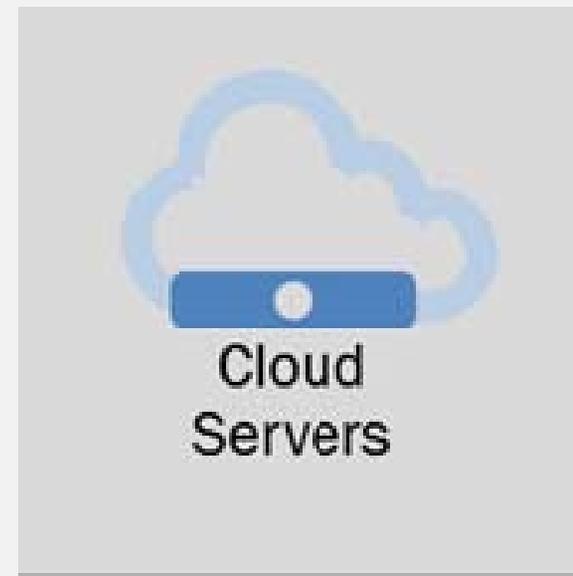
Diameter Signaling and Routing

Acquired Traffix in 2012

Consolidates signals for service providers from legacy infrastructures to 4G/LTE

"Helps upgrade signals" more efficiently with little lag time

CGNAT module

PEM module

Services for our Services

Consulting

Training

Installation

Maintenance

Other technical support
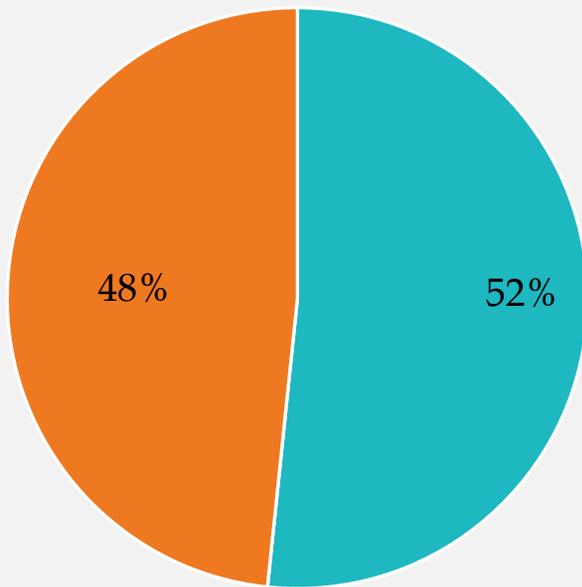
Revenues

Total Revenues increased
10.8% in 2015
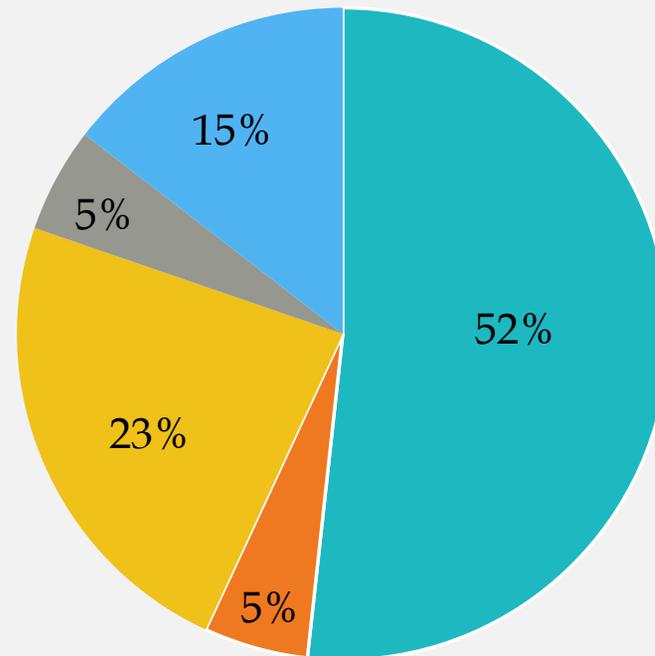
Sales by Distributors
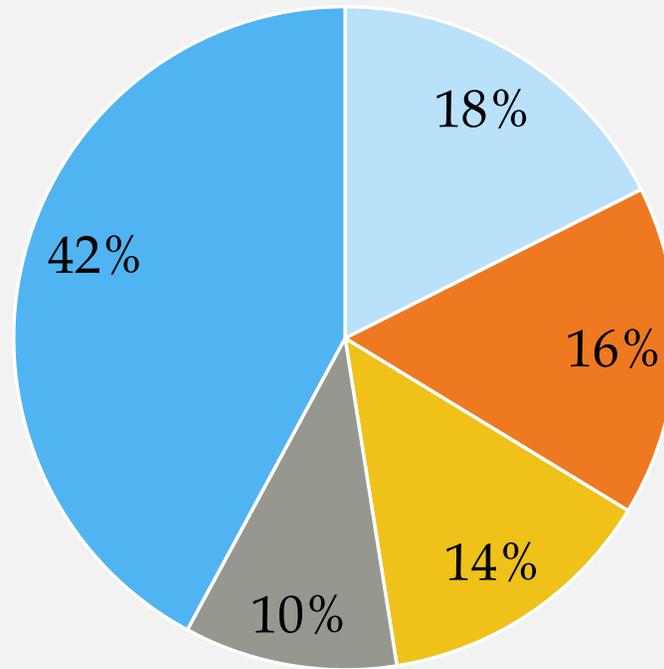
Westcon Group 18% · Ingram Micro 16% · Avnet Tech Solutions 14% · Arrow ECS 10% · Others 42%

Employees
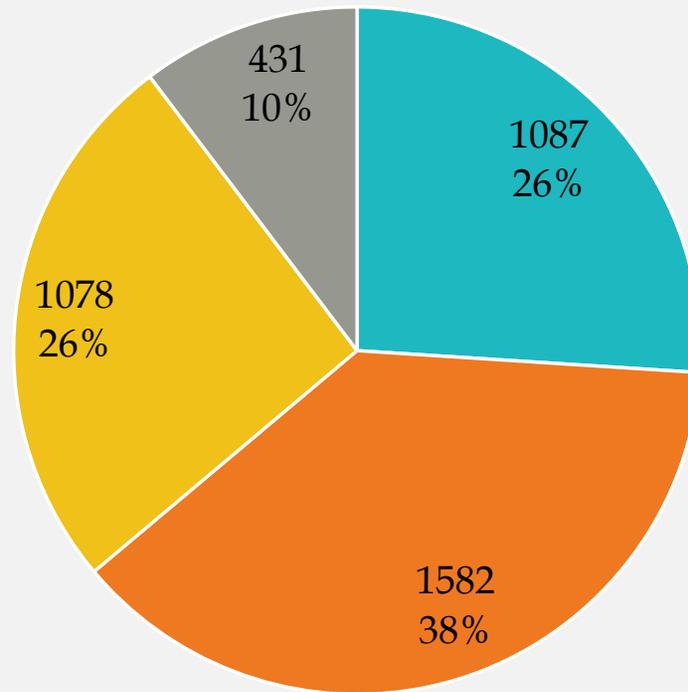
- Product Development
- Sales
- Professional Services & Tech Support
- Adminstration

	Value	Percentage
	1087	26%
	1582	38%
	1078	26%
	431	10%

Partners

Customers

- **49** of the **Fortune 50** companies

- **20** of the **top 20** U.S. commercial banks

- **15** of the **15** executive departments of the U.S. cabinet

- **10** of the **top 10** largest global insurance companies

- **10** of the **top 10** U.S. telecommunications companies

- **10** of the **top 10** "best" U.S. retail companies

- **10** of the **top 10** "best" global brands

- **10** of the **top 10** global Telecom operators

- **10** of the **top 10** global automotive companies

- **10** of the **top 10** world's "most admired" companies

- **9** of the **Fortune 10** companies

- **7** of the **top 10** global oil and gas companies

- **10** of the **10** largest mobile operators

- **6** of the **top 6** U.S. securities companies

Risks

Growing competition

Failure to precisely research & develop

Continuing innovation

Reliant on Supplier & Distributor relationships for products and sales

Competitive Advantage

Network Effect

Switching Costs

Brand Recognition

Product Mix

Buffettology

Qualitative Review

Qualitative Analysis	
What type of business is this: commodity or sustained competitive advantage?	Competitive Advantage
Can you easily explain what the business does?	Yes
Is it heavily unionized?	No
Does it require heavy capital infusion?	No
Does it require lots of research and development?	Yes
Can inventory become obsolete?	Yes
Are there chronic "one time" write-offs?	No
Is the company able to raise its price to offset inflation?	Yes
Will the company be able to sell more in the future?	Yes
If I gave you $1 billion could you develop a competitor? If the answer is "no" your business has a sustained competitive advantage.	No

Interpretation of Financial Statements

TTM	Value	Low Threshold	Pass?
Gross Profit Margin	82.61%	≥ 20%	Yes
% SGA	46.58%	≤ 80%	Yes
% R&D	19.15%	≤ 10%	No
% Depreciation	3.30%	≤ 10%	Yes
Interest % of OP	0%	≤ 15%	Yes
Net Profit Margin	18.79%	≥ 10%	Yes
Current Ratio	1.5	≥ 1	Yes
Obligation Ratio	-1.67 years	< 5 years	Yes
Adj. Debt to Shareholder Equity	0.83	< 0.8	No
Return on Equity	28.98%	≥ 15%	Yes
Return on Capital	28.98%	≥ 15%	Yes
Dividend Payout Ratio	0%	≤ 60%	Yes
Preferred Stock	None	None	Yes
Capital Expenditures	19.67%	≤ 25%	Yes
Net Earning Trend	Stable	Up	Yes
Retained Earnings Trend	Up	Up	Yes

Revenues

Gross Profit Margin

|	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	TTM
Gross Profit Margin (%)	77.66%	77.38%	77.08%	78.10%	80.50%	81.94%	82.86%	82.92%	82.10%	82.71%	82.59%
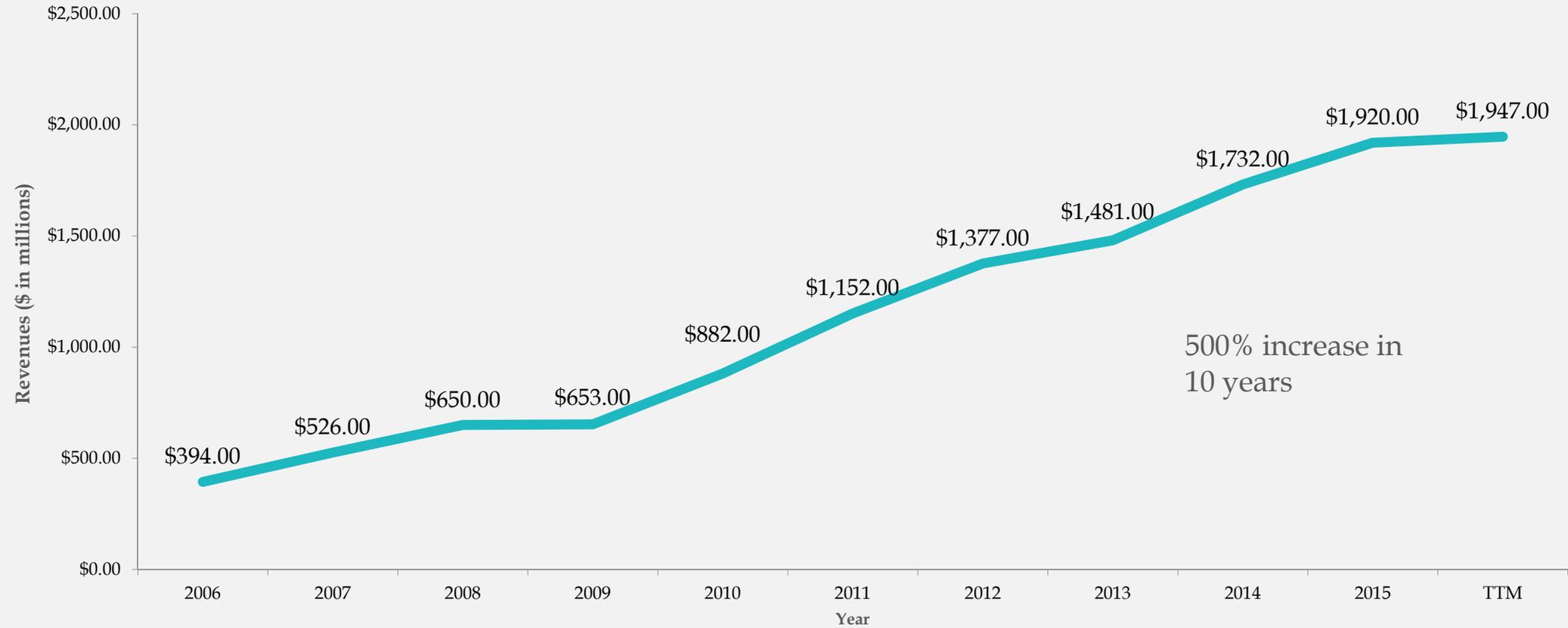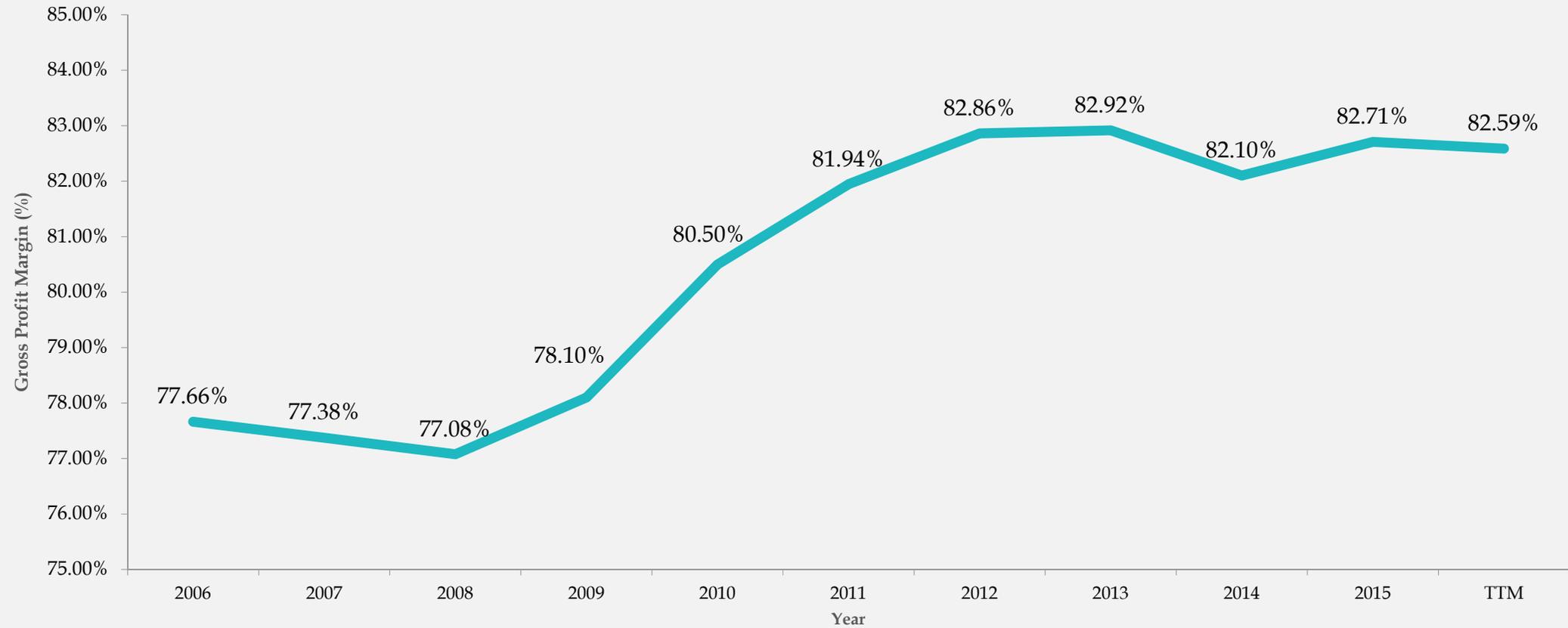
Net Profit Margin
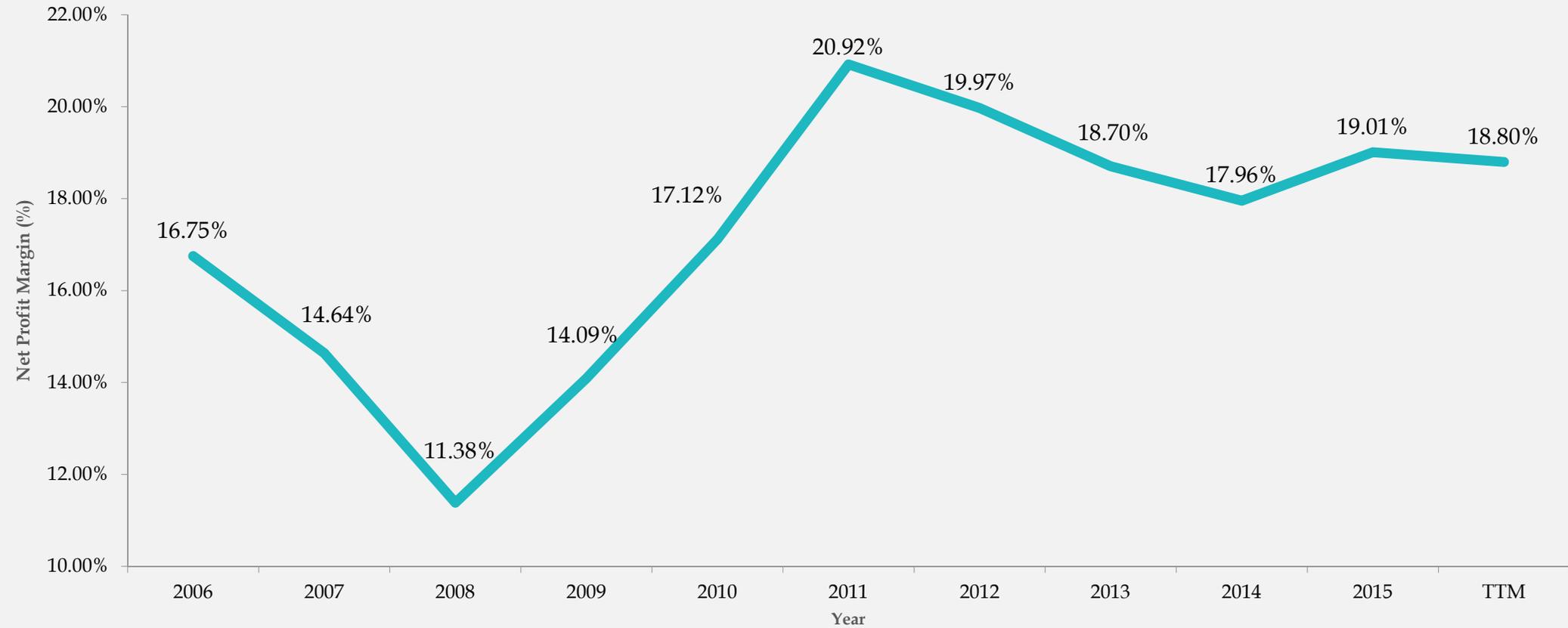
Return on Equity
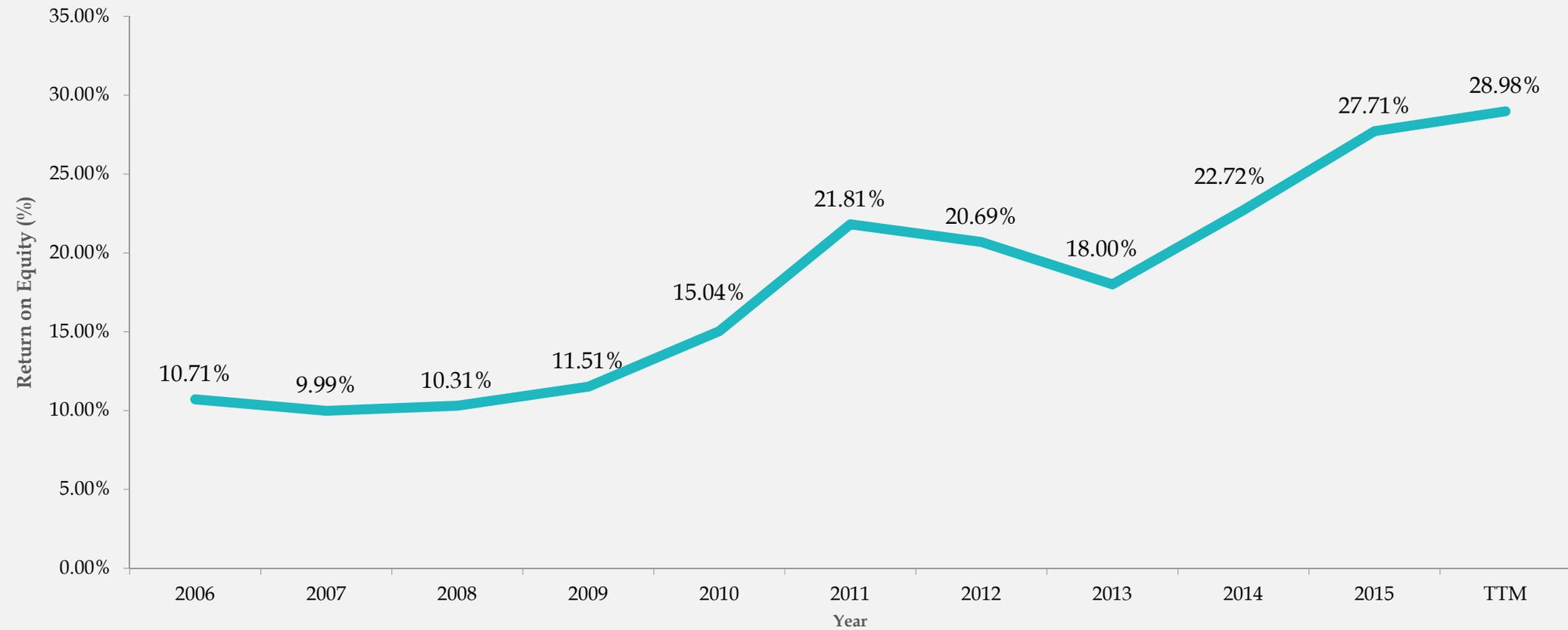
Return on Capital
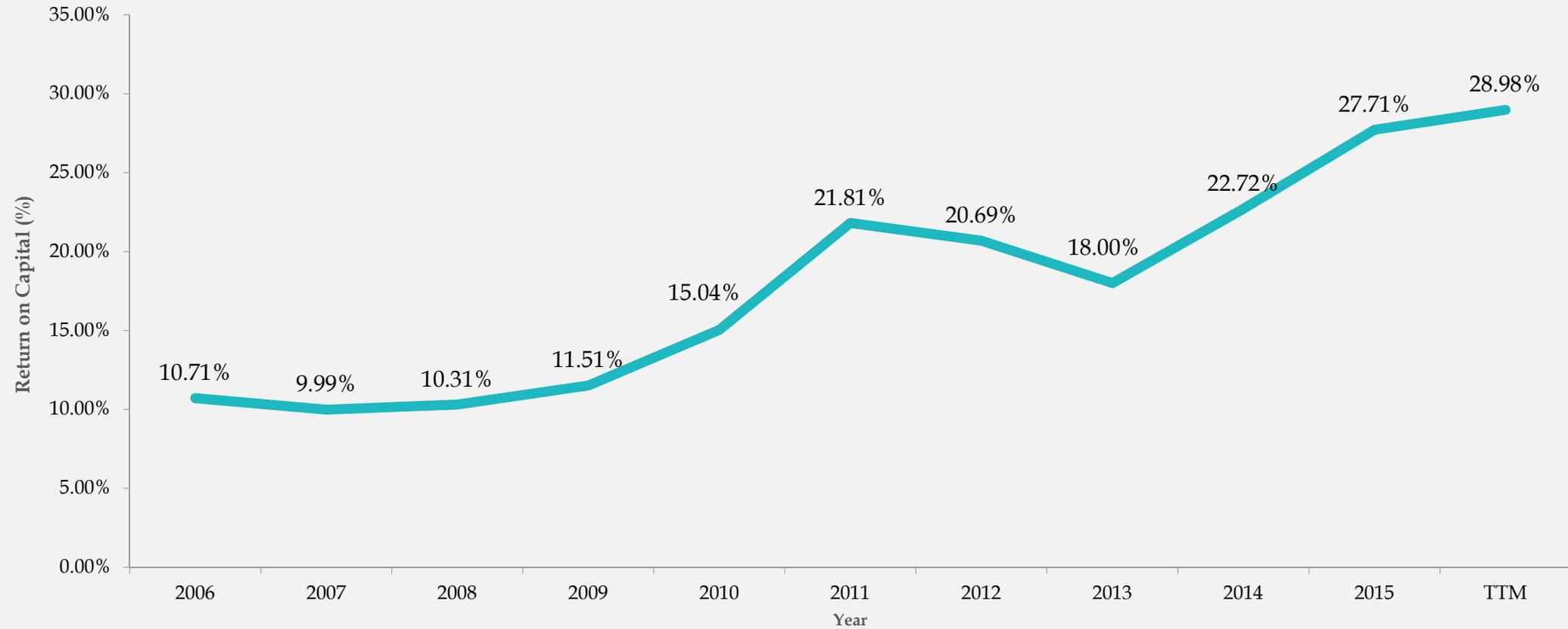
Working Capital

Total Shares Outstanding

Bought back 16% of shares at an average price of $82.41 per share
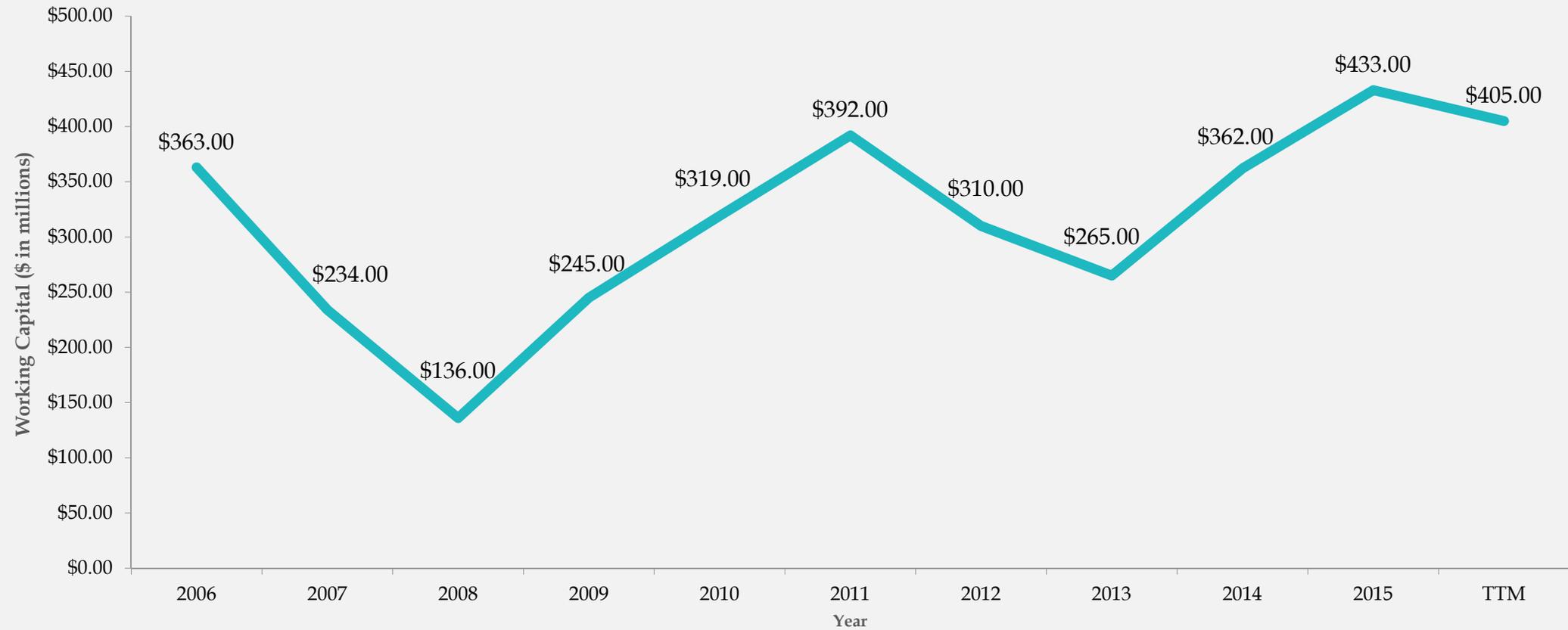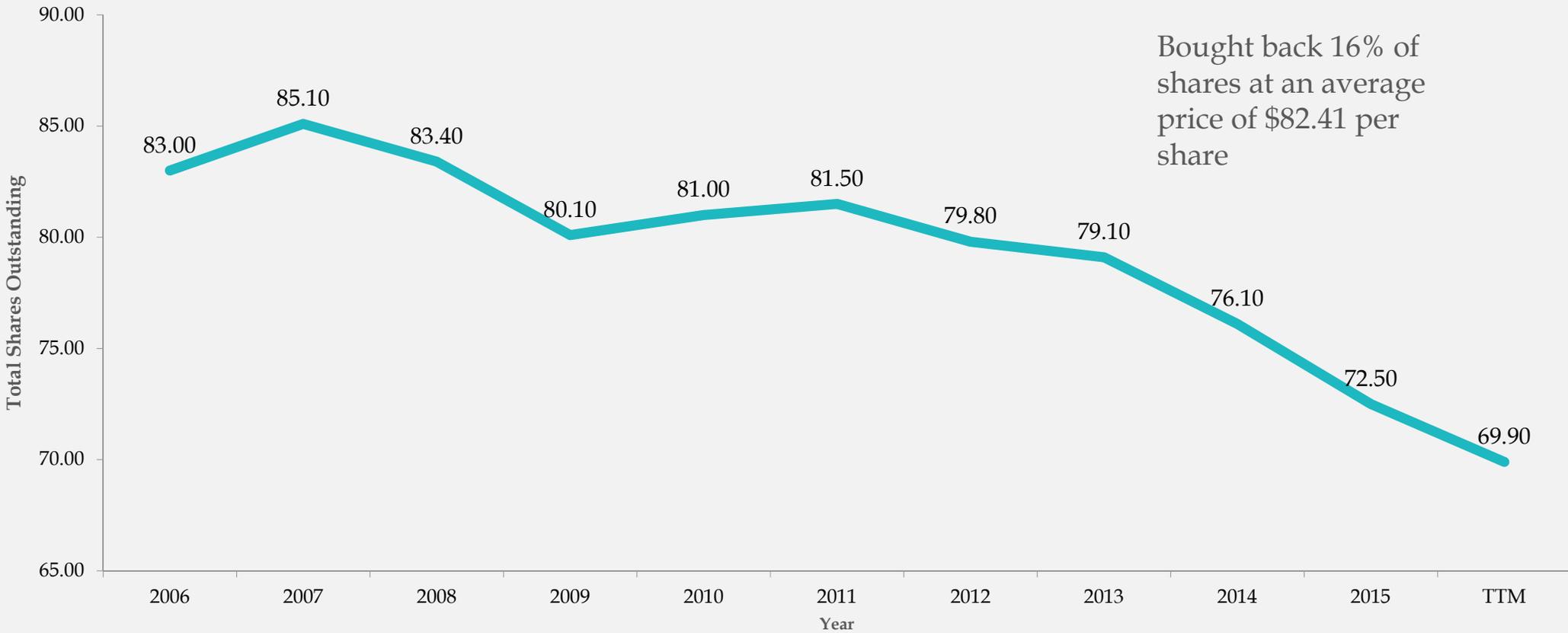
Quantitative Review

| Increasing trends?	
Sales per share	Increasing
Cashflow per share	Increasing
Earnings per share	Increasing
Dividends declared per share	N/A
Capital Spending per share	Increasing
Book Value per share	Increasing
Revenues (Sales)	Increasing
Gross Profit Margin	Increasing
Operating Profit Margin	Increasing
Net Profit	Increasing
Net Profit Margin	Increasing
Working Capital	Increasing
Shareholder's Equity	Increasing
Return on Total Capital	Increasing
Return on Shareholder's Equity	Increasing
Common Shares Outstanding	Decreasing
Long-Term Debt	N/A

Value Bands

Price/Sales

P/S	3.71
Rank	11%
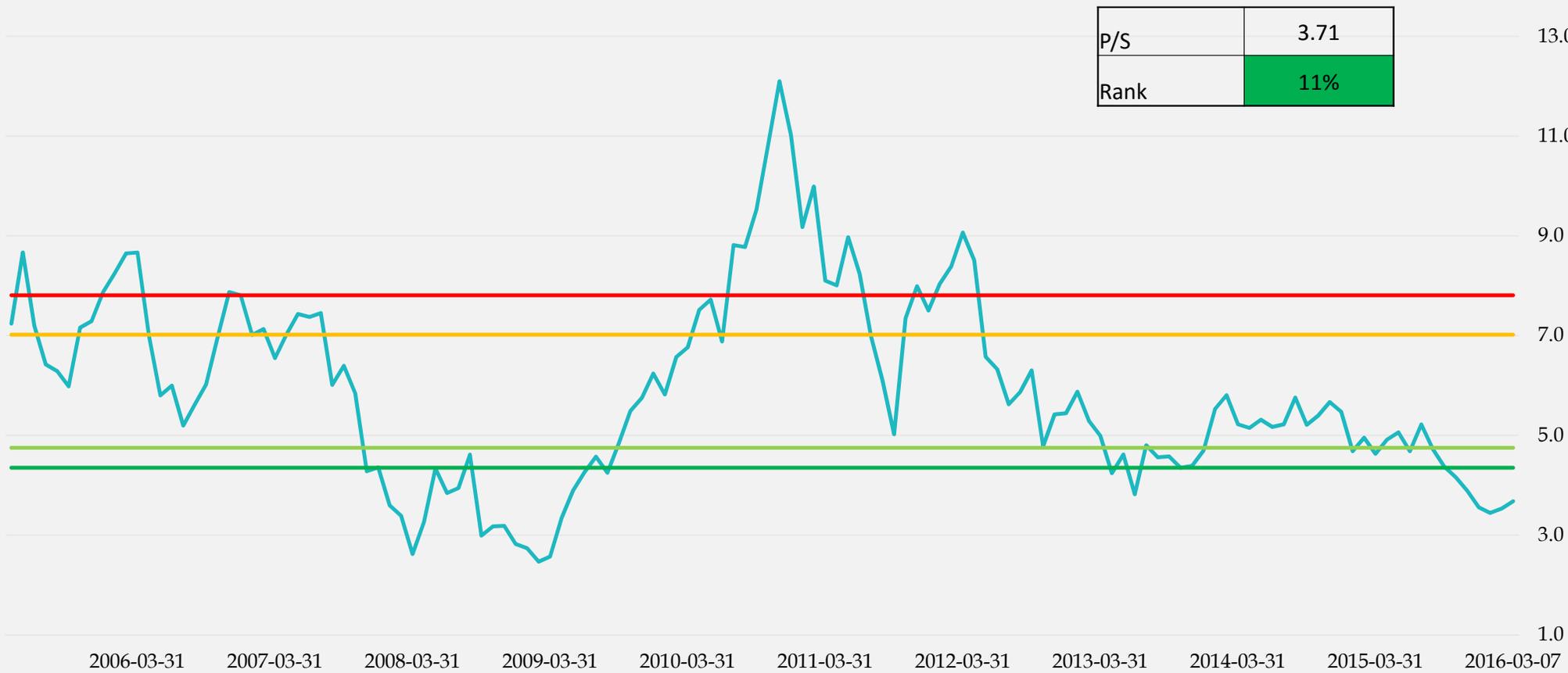
Price/Earnings

P/E	19.75
Rank	2%
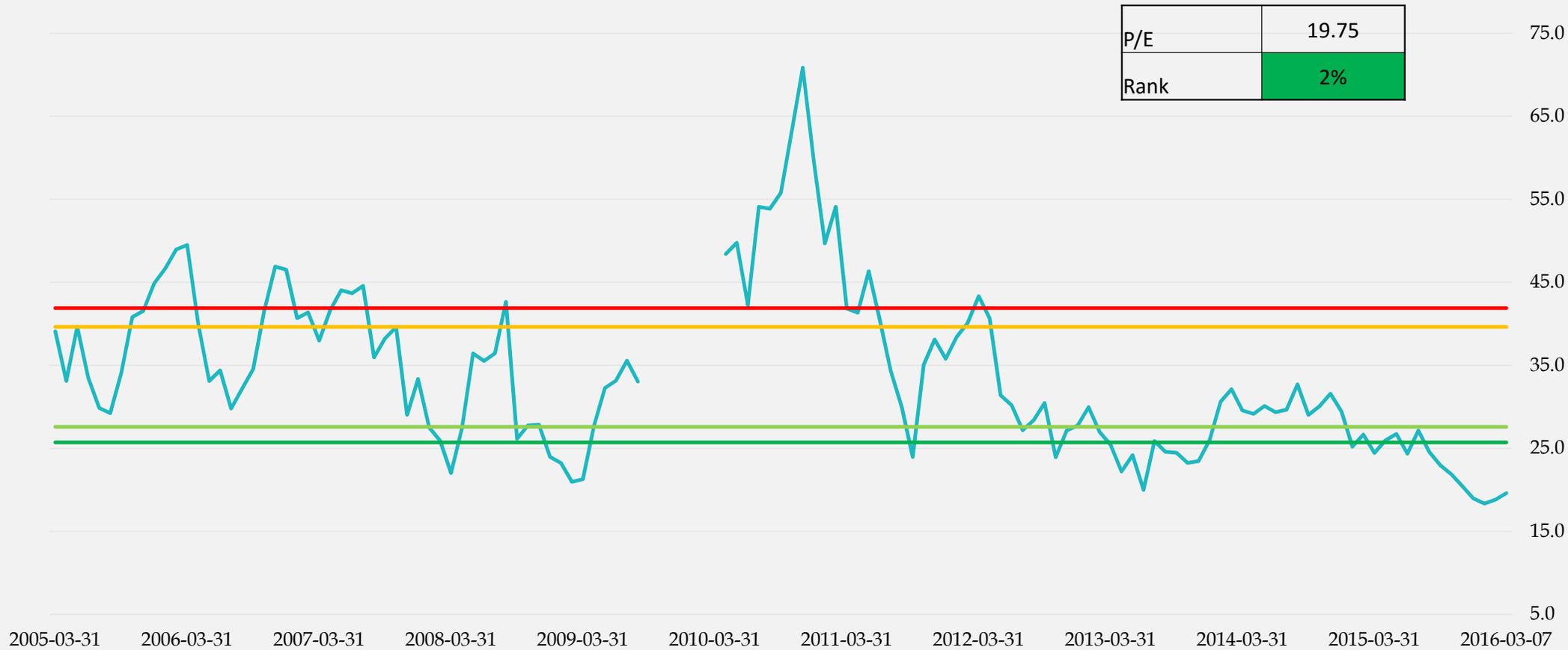
Price/Earnings Less Cash

PE Less Cash	17.27
Rank	2%
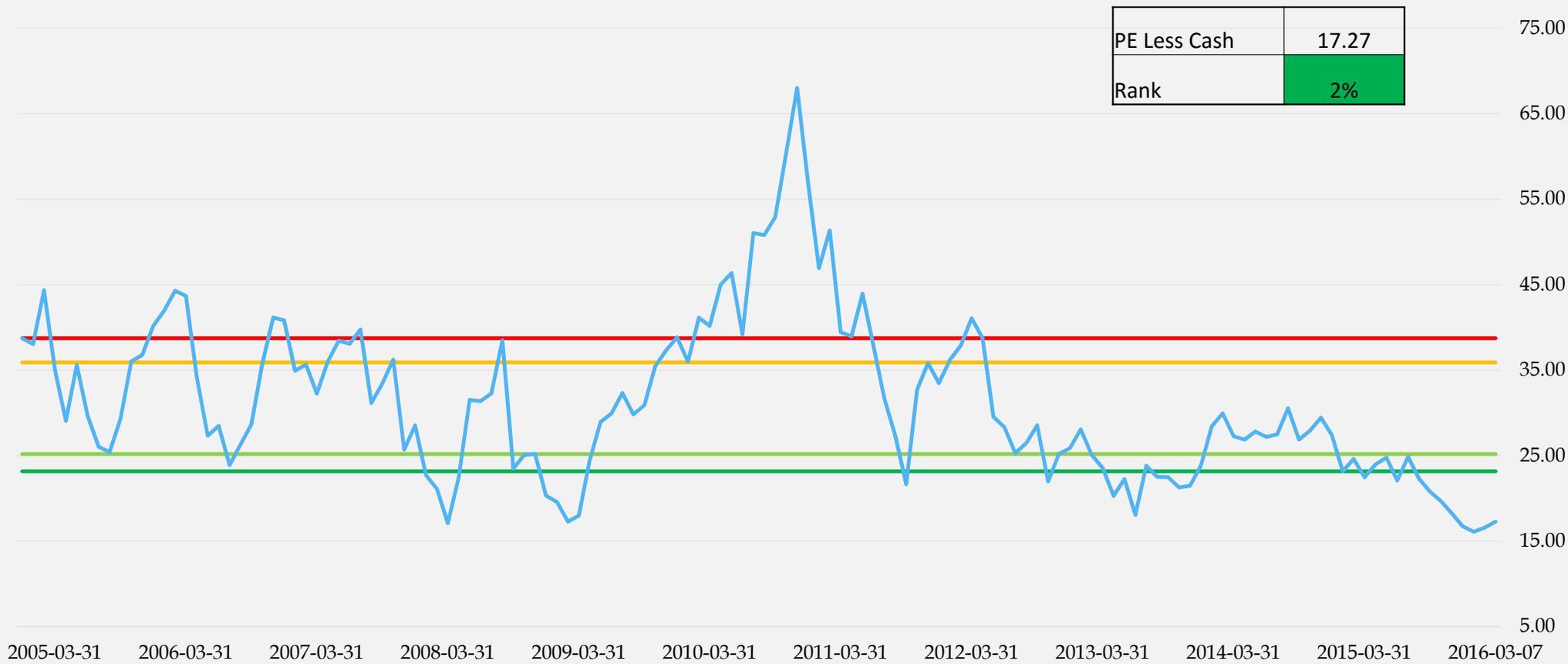
Price/Book

P/B	5.49
Rank	58%
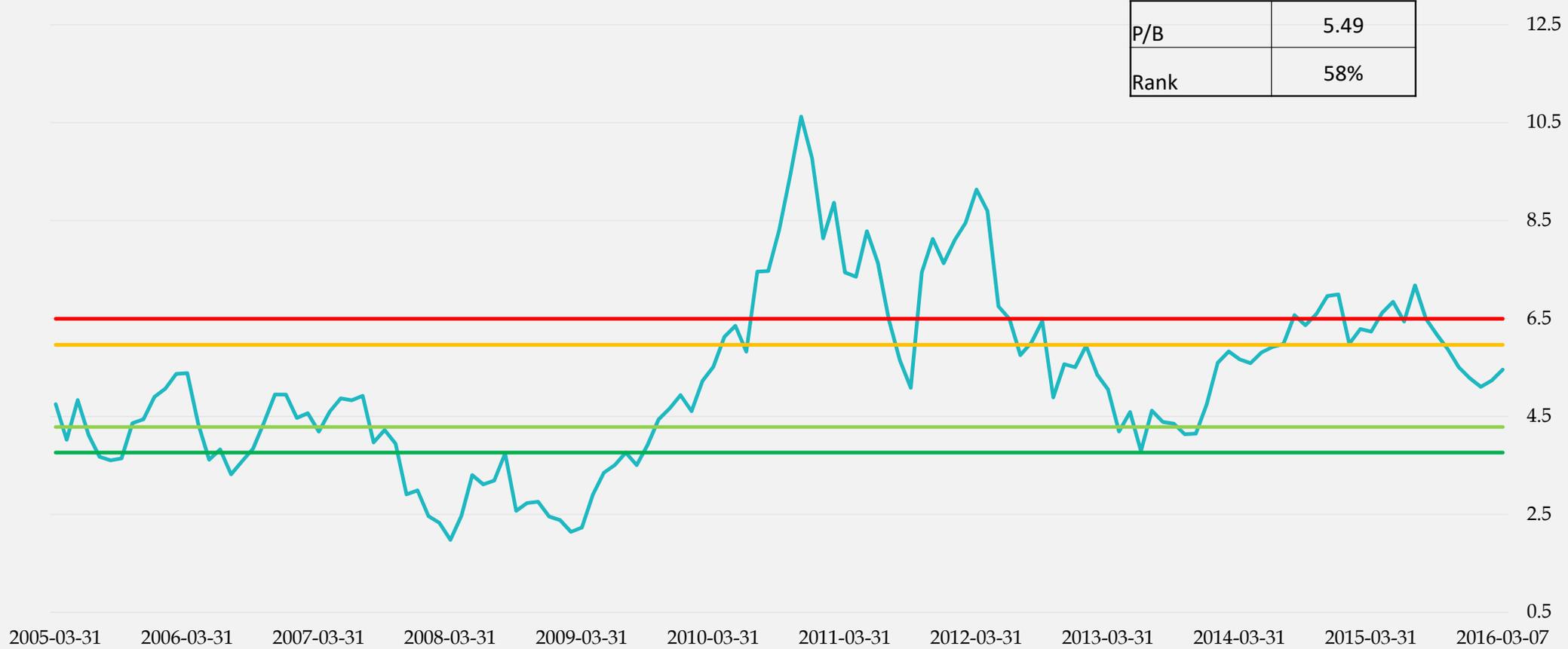
Price/Cashflow
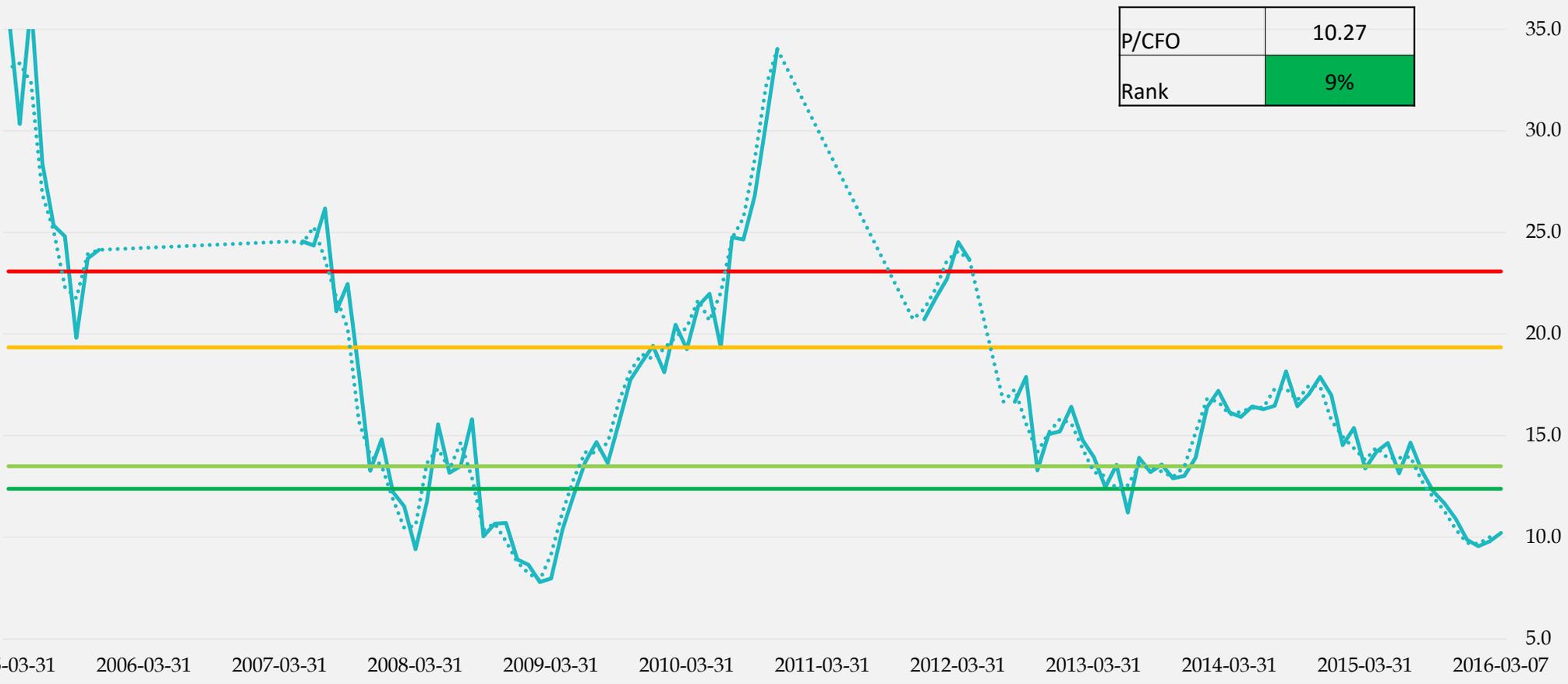
Price/Free Cashflow

P/FCF	11.45
Rank	6%
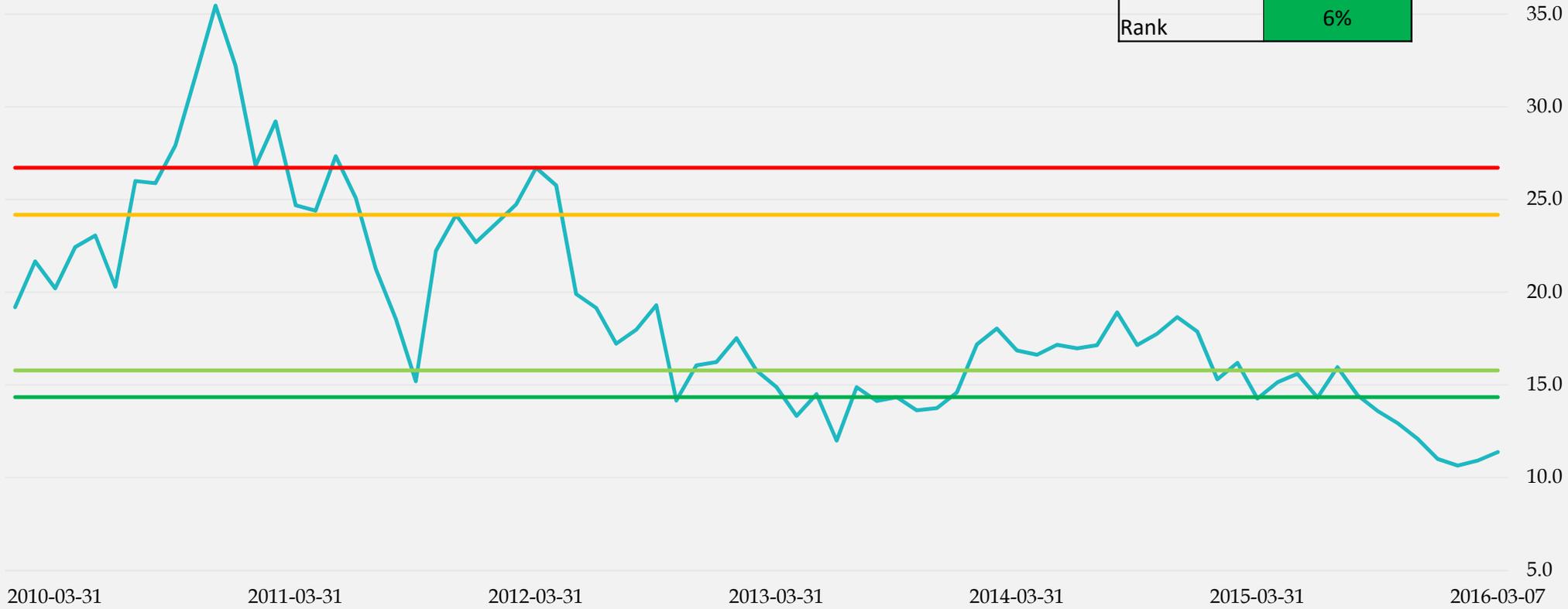
Enterprise Value/Revenue

EV/Rev	3.12
Rank	11%
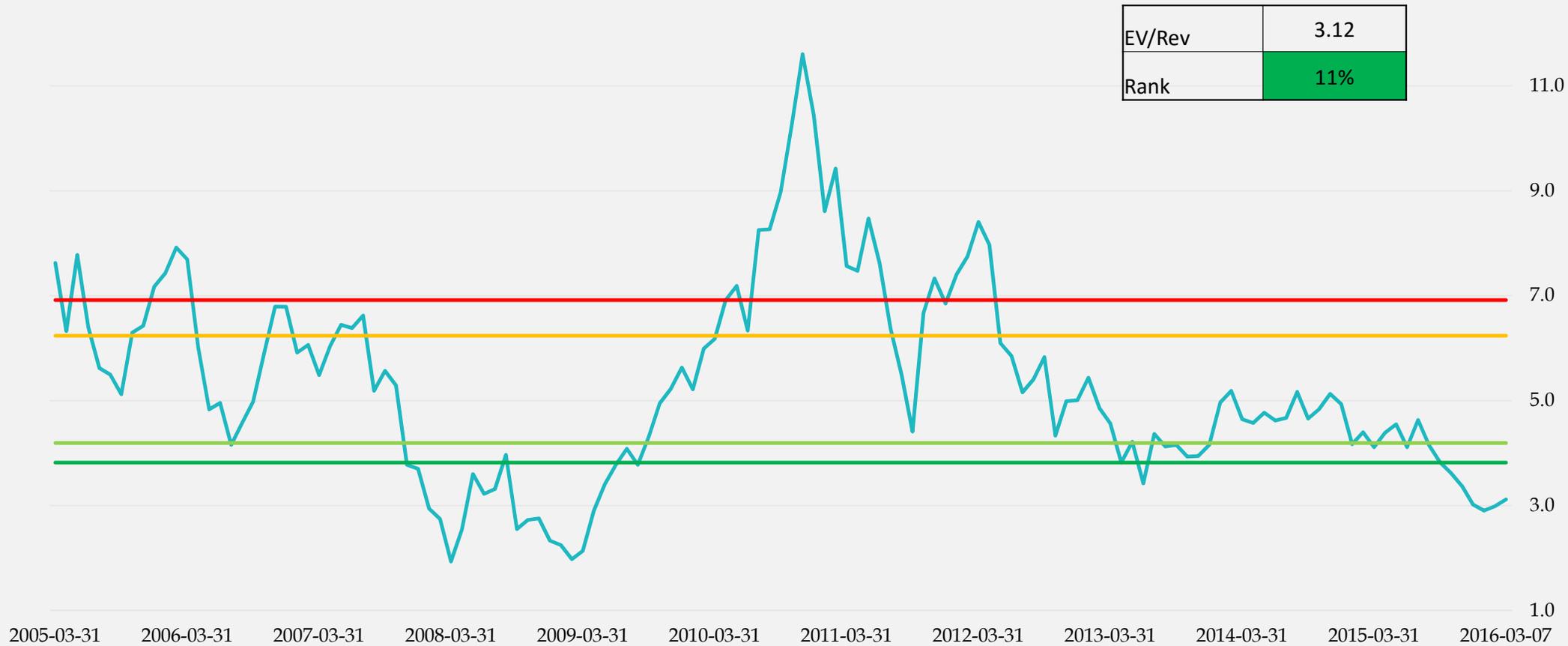
Enterprise Value/EBITDA

EV/EBITDA	10.03
Rank	2%
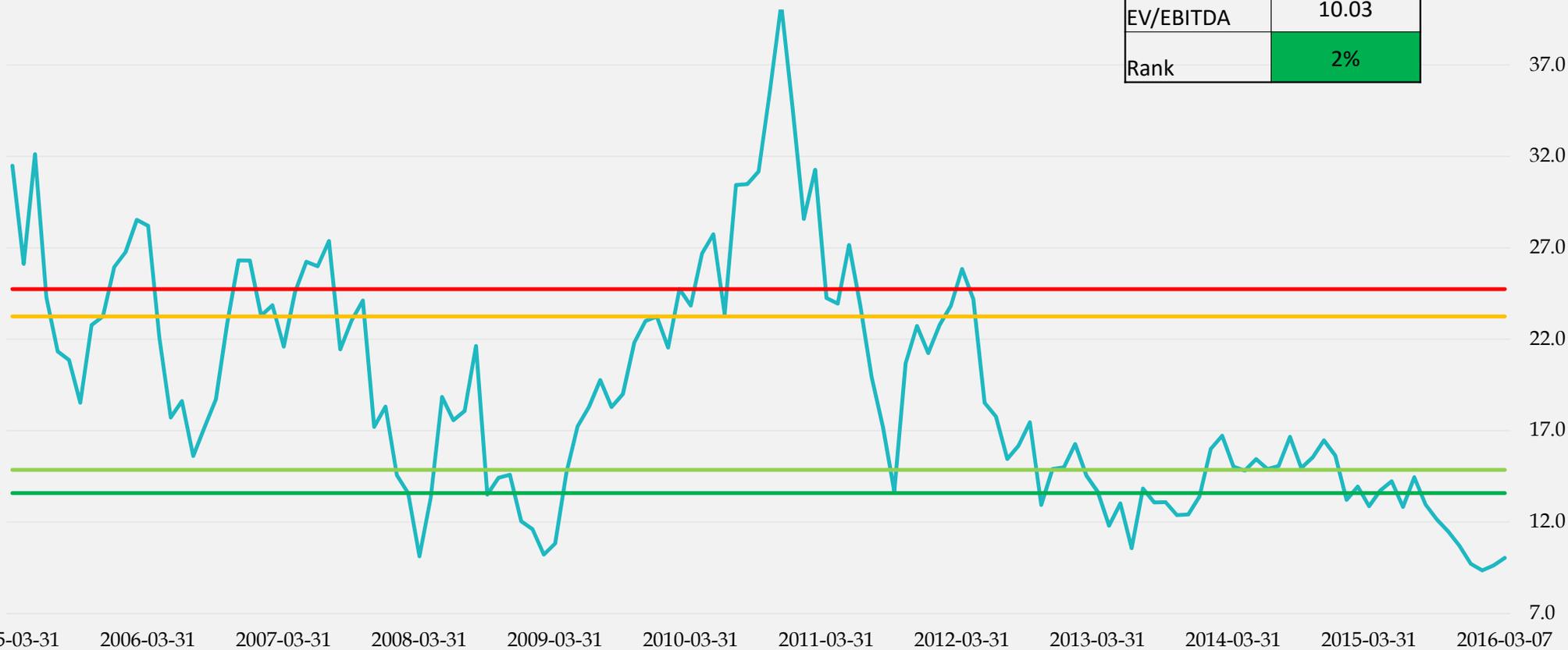
Enterprise Value/EBIT

EV/EBIT	11.00
Rank	2%
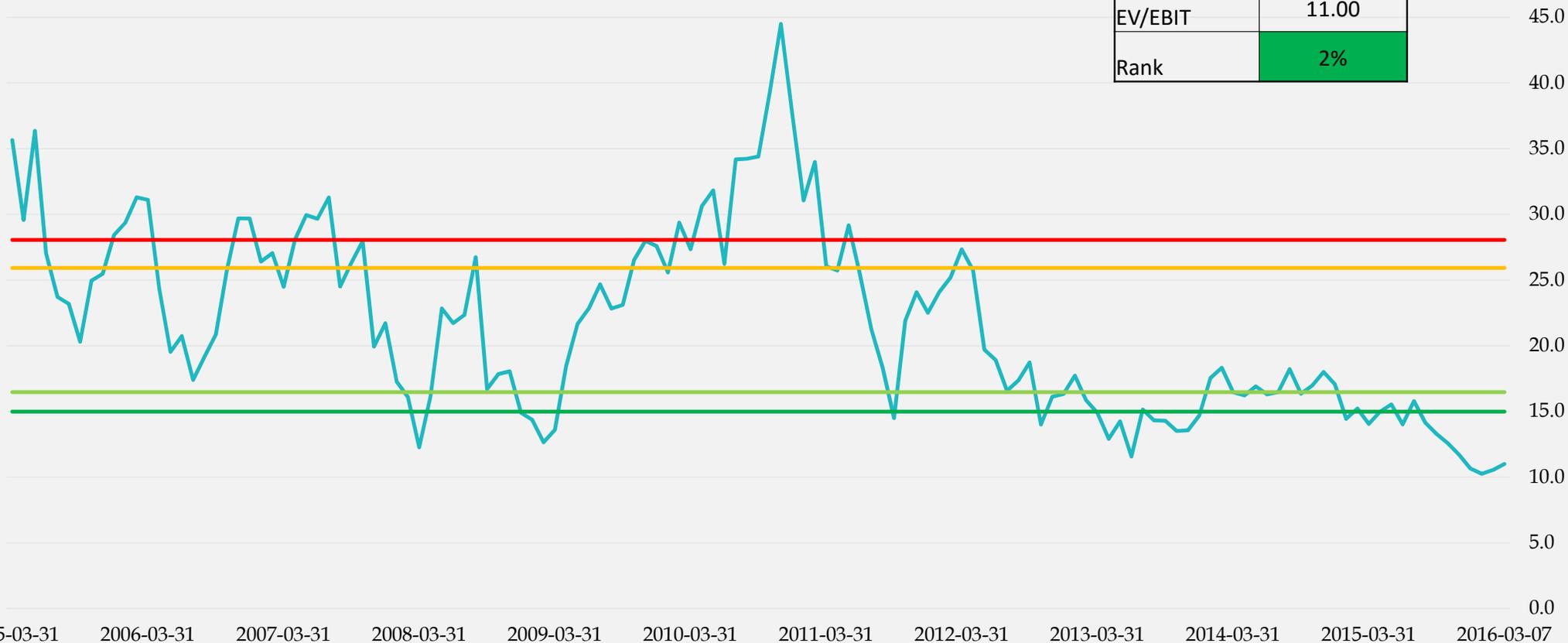
Intra-Portfolio Evaluations

Intra-Portfolio Evaluations – Current

Ticker	Price / Sales
WMT	0.5
BBBY	0.7
CHRW	0.8
WBA	0.8
AIG	1.2
BRK.B	1.6
IBM	1.7
PEP	2.4
NSRGY	2.5
UNP	3.1
QCOM	3.5
FFIV	3.7
ORCL	4.5
MSFT	4.8

Ticker	Price / Earnings
BBBY	10.1
IBM	10.2
BRK.B	14.1
WMT	14.2
UNP	14.3
QCOM	17.5
ORCL	18.4
FFIV	19.5
WBA	19.6
CHRW	20.4
NSRGY	23.7
PEP	27.2
AIG	31.5
MSFT	36.8

Ticker	P/E Adjusted
BBBY	11.7
IBM	13.4
BRK.B	14.8
QCOM	16.6
ORCL	17.3
FFIV	17.7
WMT	17.9
UNP	18.2
CHRW	22.1
WBA	22.3
NSRGY	25.1
PEP	31.7
MSFT	31.8
AIG	44.4

Ticker	Price / Book
AIG	0.7
BRK.B	1.3
QCOM	2.6
WMT	2.8
WBA	2.8
UNP	3.2
BBBY	3.3
ORCL	3.5
NSRGY	3.8
MSFT	5.3
FFIV	5.4
CHRW	8.9
IBM	9.4
PEP	12.1

Ticker	Price / Free Cash Flow
BBBY	10.5
IBM	10.6
FFIV	11.3
ORCL	14.9
WMT	15.0
CHRW	15.5
QCOM	16.7
MSFT	17.5
PEP	18.9
WBA	21.3
BRK.B	22.0
AIG	24.1
NSRGY	24.3
UNP	25.3

Ticker	52-wk Range
AIG	$50.20 — $64.93
UNP	$67.06 — $118.66
BBBY	$41.26 — $78.10
FFIV	$86.03 — $135.20
NSRGY	$68.00 — $79.99
QCOM	$42.24 — $74.09
WBA	$71.50 — $97.30
IBM	$116.90 — $176.30
ORCL	$33.13 — $45.24
WMT	$56.30 — $83.90
BRK.B	$123.55 — $148.57
MSFT	$39.72 — $56.85
CHRW	$59.71 — $76.18
PEP	$76.48 — $103.44

Ticker	PEG Forward
BRK.B	-
AIG	0.7
QCOM	1.1
WBA	1.3
FFIV	1.3
IBM	1.4
UNP	1.6
ORCL	1.8
MSFT	2.0
CHRW	2.4
BBBY	2.4
PEP	3.3
NSRGY	4.6
WMT	70.5

Intra-Portfolio Evaluations – 5 Year Historical

Ticker	▲ 5-Year Price / Sales Range		
NSRGY			
FFIV	3.2		9.4
BBBY	0.6		1.9
QCOM	2.9		8.1
CHRW	0.6		1.4
IBM	1.4		2.4
WMT	0.4		0.6
UNP	2.1		4.9
ORCL	3.6		5.4
BRK.B	1.1		2.0
WBA	0.4		1.2
MSFT	2.9		5.1
PEP	1.5		2.4
AIG	0.1		1.4

Ticker	▲ 5-Year Price / Earnings Range		
NSRGY			
FFIV	17.0		50.8
UNP	12.5		24.0
BRK.B	12.7		19.9
BBBY	8.3		18.7
IBM	8.7		16.0
WMT	11.0		19.0
QCOM	12.4		26.5
CHRW	13.9		33.5
ORCL	13.3		24.1
WBA	10.0		43.6
AIG	2.1		-
MSFT	8.8		39.5
PEP	15.1		27.4

Ticker	▲ 5-Year Price / Book Range		
NSRGY			
IBM	7.9		14.5
QCOM	2.1		4.1
BBBY	2.7		5.0
ORCL	2.9		5.0
WMT	2.3		3.8
FFIV	3.8		9.1
UNP	2.1		5.1
WBA	1.7		4.9
BRK.B	1.0		1.6
CHRW	5.7		11.2
AIG	0.4		0.8
MSFT	3.1		5.7
PEP	4.0		12.3

Ticker	▲ 5-Year Price / Cash Flow Range		
NSRGY			
FFIV	8.9		26.3
CHRW	12.5		35.5
QCOM	11.7		32.9
BBBY	6.1		15.0
IBM	6.8		12.8
WMT	6.8		12.3
UNP	6.9		16.6
ORCL	9.6		18.7
BRK.B	7.8		14.1
PEP	11.1		16.6
MSFT	7.1		16.1
WBA	6.4		19.5
AIG	0.3		-

Ticker	▲ 5-Year Price Range		
IBM	$116.90		$215.90
BBBY	$41.26		$80.82
QCOM	$42.24		$81.97
FFIV	$67.53		$139.46
UNP	$38.87		$124.52
WMT	$48.31		$90.97
ORCL	$24.72		$46.71
CHRW	$50.21		$82.61
NSRGY	$52.72		$80.65
AIG	$19.18		$64.93
WBA	$28.53		$97.30
BRK.B	$65.35		$152.94
MSFT	$23.65		$56.85
PEP	$58.50		$103.44

Industry Breakdown

Industry Breakdown

Information from FFIV 10-K	F5 Networks	Juniper	Cisco*	Checkpoint	Imperva	Citrix	Allot	Riverbed	Oracle*	IBM*	Akamai	Blue Coat
Network Firewall	Y	Y	Y	Y								
Web Application Firewall	Y		Y		Y	Y						
Carrier Grade NAT	Y	Y	Y									
Deep Packet Inspection	Y						Y					
Wide Area Network	Y							Y				
Diameter Signaling	Y								Y			
End-User Protection	Y									Y		
Cloud-Based Protection	Y										Y	
Malware Protection	Y											Y

Industry Breakdown

TTM	F5	Juniper	Checkpoint	Brocade	Citrix	Riverbed
Market Cap	6.86 B	9.66 B	15.40 B	4.16 B	11.56 B	3.31 B
Gross Profit Margin	83%	63%	88%	68%	81%	74%
Net Profit Margin	19%	13%	42%	15%	10%	7%
Obligation Ratio	0	0	0	0	1.03	N/A
Return on Equity	28%	14%	19%	14%	15%	9%
Return on Capital	28%	10%	19%	11%	10%	4%
Return on Assets	16%	7%	14%	9%	6%	4%
Patents	231	2,480	39	56	N/A	195

DuPont Analysis – 5 year

F 5 Networks	Total Asset Turnover	Financial Leverage Multiplier	Net Profit Margin	Return on Equity
TTM	0.84	1.83	18.79%	28.89%
2015	0.83	1.76	19.01%	27.77%
2014	0.79	1.59	17.97%	22.57%
2013	0.66	1.44	18.72%	17.80%
2012	0.72	1.43	19.98%	20.57%

Competitor DuPont Analysis

Using TTM Data	Total Asset Turnover	Financial Leverage Multiplier	Net Profit Margin	Return on Equity
F5 Networks	0.84	1.83	18.79%	28.89%
Juniper Networks	0.56	1.88	13.05%	13.72%
Checkpoint Software	0.32	1.44	42.08%	19.39%
Brocade	0.57	1.56	15.33%	13.63%
Citrix	0.59	2.77	9.75%	15.94%
Riverbed	0.56	2.29	6.54%	8.38%

Total Returns since Inception

Discounted Cash Flows

Discounted Cash Flows – Default

Discounted Cash Flows – Kill it

Discounted Cash Flows – Valueline Estimates

Conscious Investor

Conscious Investor – 3 years

	9/06	9/07	9/08	9/09	9/10	9/11	9/12	9/13	9/14	9/15	EPSttm	Years	HGROWTH	STAEGR®
EPS ($)	0.795	0.904	0.891	1.143	1.865	2.963	3.449	3.504	4.090	5.031	$5.110	3	19.82%	99.24%
SPS ($)	4.832	6.230	8.220	8.257	10.976	14.553	17.497	18.969	23.601	27.372		3	20.12%	98.93%

	Price	EPSttm	P/E Ratio	HGrowth	Payout	STRET®	Req Return	TARG®
Default	100.87	$5.110	25.32	19.82%	0.0%	20.51%	-10.00%	$4.24K
Safety	100.87	$5.110	16.37	14.13%	0.0%	10.39%	-10.00%	$1.68K

Conscious Investor – 6 years

	9/06	9/07	9/08	9/09	9/10	9/11	9/12	9/13	9/14	9/15	EPSttm	Years	HGROWTH	STAEGR®
EPS ($)	0.795	0.904	0.891	1.143	1.865	2.963	3.449	3.504	4.090	5.031	$5.110	6	17.98%	90.50%
SPS ($)	4.832	6.230	8.220	8.257	10.976	14.553	17.497	18.969	23.601	27.372		6	18.91%	96.48%

	Price	EPSttm	P/E Ratio	HGrowth	Payout	STRET®	Req Return	TARG®
Default	100.87	$5.110	25.32	17.98%	0.0%	18.72%	-10.00%	$3.63K
Safety	100.87	$5.110	16.37	13.28%	0.0%	9.63%	-10.00%	$1.56K

Conscious Investor – 10 years

	9/06	9/07	9/08	9/09	9/10	9/11	9/12	9/13	9/14	9/15	EPSttm	Years	HGROWTH	STAEGR®
EPS ($)	0.795	0.904	0.891	1.143	1.865	2.963	3.449	3.504	4.090	5.031	$5.110	10	25.70%	83.35%
SPS ($)	4.832	6.230	8.220	8.257	10.976	14.553	17.497	18.969	23.601	27.372		10	21.12%	94.38%

	Price	EPSttm	P/E Ratio	HGrowth	Payout	STRET®	Req Return	TARG®
Default	100.87	$5.110	25.32	25.70%	0.0%	26.27%	-10.00%	$6.85K
Safety	100.87	$5.110	16.37	14.71%	0.0%	10.91%	-10.00%	$1.77K

Conscious Investor – Safety & Kill It

	Price	EPSttm	P/E Ratio	HGrowth	Payout	STRET®
Default	100.87	$5.110	25.32	25.70%	0.0%	26.27%
Safety	100.87	$5.110	16.37	14.71%	0.0%	10.91%
⟳ Saved	99.77	$5.110	16.37	11.50%	0.0%	8.16%

Cut growth rate by 21.82%

	Price	EPSttm	P/E Ratio	HGrowth	Payout	STRET®
Default	100.87	$5.110	25.32	25.70%	0.0%	26.27%
Safety	100.87	$5.110	16.37	14.71%	0.0%	10.91%
⟳ Saved	99.77	$5.110	13.50	10.00%	0.0%	5.04%

Cut P/E by 17.5%
Cut growth rate by 32%

Conscious Investor – Kill It Again

	Price	EPSttm	P/E Ratio	HGrowth	Payout	STRET®
Default	100.87	$5.110	25.32	25.70%	0.0%	26.27%
Safety	100.87	$5.110	16.37	14.71%	0.0%	10.91%
↻ **Saved**	99.77	$5.110	10.00	7.00%	0.0%	0.06%

Cut P/E by 39%
Cut growth rate by 52.4%

Conclusion

Strong Financials

    No Long-Term Debt

    High Margins

Moaty-Business

    Product Mix

    Customers & Partners

Undervalued & Predictable

    Comfortable Margin of Safety

Recommendation

Limit Order at $95.50