

Allianz

Cyber Security

Invest to protect your everyday life



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For fund distributors
and professional
investors only

How is the significant and increasing prevalence of cyberattacks impacting governments, businesses and individuals alike?

The number and severity of attacks has certainly increased in the past few years, as hackers have become more sophisticated. The digital transformation that is going on globally is creating more efficiencies and improving productivity and convenience, but the risk of cyberattacks is much greater. With more data stored and transmitted to and from the cloud sources such as corporations, governments, smartphones, connected vehicles and devices, sharing apps or e-commerce, the risks will continue to increase. The need for security is critical now more than ever and this will be a long-term and evolving trend.

What does this mean for companies providing cyber security services?

Cyber security companies need to continue developing more innovative products and services to protect against sophisticated cyber criminals who easily and quickly find new ways to steal sensitive data. Traditional firewall protection is no longer adequate security in the cloud environment, so legacy security companies are developing new technologies or acquiring smaller companies to offset their mature traditional security business. Newer, smaller companies are growing very rapidly because their solutions are specifically designed to protect data in the cloud environments.

The cyber security companies with the best products/services and efficient business models should generate greater revenue growth and profitability over time. In the digital world, cyber security must remain a top budget priority so revenue and profitability should not be as cyclical as it was in the past for this industry.

Describe the competitive environment in the cyber security industry.

The cyber security industry is competitive, but it is not a "winner take all" industry. We find this industry very attractive as an investment opportunity because there are many companies that provide security for different use cases and applications. With the shift to technologies such as cloud, connected devices, Artificial Intelligence (AI), 5G and remote work, new security needs are arising and companies need multiple security services to adequately protect networks and data. Therefore, we believe many cyber security companies can achieve very attractive growth over the next several years.

What is the competitive advantage and uniqueness of your strategy and team?

We believe our team's approach is truly distinctive. Each member contributes to the management of client portfolios, thereby leveraging the collective experience and judgment of the entire investment management team to the benefit of each



Walter Price
Senior Portfolio Manager

Value. Shared.

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client. There is a strong bond and vision within the team which is reflected in the low team turnover. Walter Price and Huachen Chen lead the team, both being experienced and successful stock pickers with a combined over 70+ years of industry experience. Together they have built a competitive track record – in terms of both absolute and relative performance.

The team is well set to evolve with the marketplace and broader investment landscape, utilising AllianzGI's global resources to maximise client outcomes over the long term.

What are the key aspects of this strategy?

The strategy is a global equity strategy aiming to provide investors with capital appreciation over the long term through investing in innovative companies operating in the cyber security space.

Exposure to a major growth theme (long- and short-term)

The megatrend "digitalisation" makes our digital lives more vulnerable, which increases the need for cyber security. This necessity has been exacerbated by the COVID-19 pandemic, as the importance of digitalisation has increased much faster than originally expected.

Pure play exposure in cyber security companies with mid-cap bias

The fund seeks to identify secular winners that benefit from long-term growth tailwinds. It invests in about 30-60 security stocks, which are mostly pure play stocks, offering a concentrated, high conviction portfolio. Although the fund has a broad industry exposure, by following an all-cap approach, the fund management has an emphasis on higher-growth mid-cap companies.

One of the longest track records in the cyber security space

At 20 years, the fund management team has one of the longest track records in engaging with cyber security stocks.

A similar strategy has been managed for clients in Japan since 2017, with great success. The European version will additionally adopt an explicit sustainability approach.

Regarding the investment universe, do you have any criteria such as the ratio of sales revenue in cyber security business?

We do not have a specific target ratio of sales revenue in a company's cyber security business. We seek companies where security is becoming or already is an important part of their businesses. We hold a variety of companies in the portfolio where some companies are "pure plays" in cyber security, some have significant revenue from cyber security (about 20%-50%), while others generate a very small portion of overall revenue from cyber security. Some large companies that generate a very small percentage of overall revenue from cyber security are securing the future client infrastructure (the cloud) by building in best security practices and hiring hundreds or thousands of security professionals to secure the data and data centers from attack. Eventually, sales from cyber security should become a much larger portion of overall revenue for these companies. We believe this approach allows us to capture more growth in cyber security revenues, rather than waiting for a company to reach a specific target percentage of revenue before adding it to the portfolio.

What do you think about valuation for cyber security companies?

We assess valuation from multiple perspectives and the method can be different for different types of companies. For high growth software companies that make up most of the Cyber Security Fund, we must have high conviction that the company's future earnings growth justifies the higher valuations. We estimate earnings growth over a period of years based on our fundamental research, and discount back

Investment process

We run the portfolio as a team, where everyone has a voice. If there is a strong divergence of opinion among the team, the stock will not be included in the portfolio. The team will do more work until there is agreement to own or avoid the stock.



Our portfolio management team identify major growth trends within the cyber security sector.



We invest in companies across the major segments of the cyber security industry, including endpoint security, network security, perimeter security, data security, and application security.



We employ a bottom-up investment approach that relies on deep fundamental research to identify cyber security companies with attractive earnings growth potential, quality management, strong competitive advantages, and reasonable valuation relative to growth.



We build an intimate knowledge of and relationship with companies via regular meetings with management teams.



We aim to invest in companies that possess one or more of the following:

- Sustained earnings growth
- Market leadership
- Barriers to entry
- High quality management
- Strong balance sheet
- Reasonable valuation relative to growth rates and industry peers

to the present period. If we believe a company can reasonably grow into its valuation by delivering earnings growth ahead of consensus over our time horizon, we are comfortable with owning a stock with a high valuation.

We do not believe cyber security valuations are extreme because earnings growth has improved, and we think this is sustainable due to multiple tailwinds related to the digital transformation.

Do you envisage any headwinds/risks? In what type of market environments do you expect to outperform/underperform?

We are excited about the investment opportunities presented by this industry. We expect to see a dramatic increase in the volume of data stored in the cloud, accessed through mobile devices, and transmitted to and from connected devices. As a result, we believe security spending will be an ongoing requirement and should remain a top priority for companies and governments of all sizes.

Our goal is to outperform the benchmark and the competition every year. We aim to add value across different market environments, particularly when equity prices are driven by the underlying strength of company fundamentals. We believe high quality stocks notably outperform the market over the long term.

Throughout the course of an investment cycle, there are times when equity prices do not accurately reflect the underlying strength of company fundamentals and our emphasis on high quality growth companies can be a short-term headwind. When investors focus heavily on macroeconomic events, geopolitical issues, monetary policy, etc., rather than company fundamentals, our process may not be immediately rewarded. While this may be a headwind, we believe through strong stock selection we can navigate through these short-term market swings and continue to deliver added value for our clients without compromising our investment discipline.

Opportunities

- + High return potential of stocks in the long run
- + Investments specifically in the cyber security area
- + Broad diversification across numerous securities
- + Possible extra returns through single security analysis and active management
- + Currency gains against investor currency possible in unhedged unit classes

Risks

- High volatility of stocks, losses possible. The volatility of fund unit prices may be strongly increased.
- Underperformance of the investment theme possible
- Limited participation in the yield potential of single securities
- Success of single security analysis and active management not guaranteed
- Currency losses against investor currency possible in unhedged unit classes

For more information, please contact your local AllianzGI representative or visit updates.allianzgi.com



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