

# EQUITY RESEARCH

February 2, 2022

Initiating Coverage

## MAGNET FORENSICS, INC.

Investigating A High Growth Market – Initiating At Outperformer

### Our Conclusion

As of February 2, we are initiating coverage on Magnet Forensics, Inc. with an Outperformer rating and C\$33 price target based on a 2023E EV/Sales multiple of 8.0x. Magnet is a leading provider of digital investigation tools for public safety and corporate clients. We see multiple avenues for potential future growth, including user and product extension within the existing customer base, continued expansion into the enterprise market, and M&A.

### Key Points

**Growth In Digital Evidence Driving Market Expansion:** Magnet provides public safety organizations with tools to recover, manage and analyze digital evidence. These organizations have seen a rapid rise in the amount of digital evidence, which is now present in 85% of all criminal investigations. Magnet uses a land-and-expand strategy within public sector organizations, with its +120% net revenue retention highlighting the stickiness of its solutions. Recent case analytics and intelligence offerings have broadened Magnet's user base within public safety clients to non-technical users. Magnet's annual recurring revenue per account has grown by 86% over the past two years as clients add users and additional functionality.

**Private Sector A Relatively Untapped Opportunity:** Magnet's private sector business has grown quickly as public sector users migrate to the private sector and digital threats against corporations rise exponentially. Magnet launched a dedicated private sector offering in 2020 and the private sector now comprises over 30% of sales. We see strong growth opportunities within the private sector for Magnet, with the average selling price of its corporate offering almost double that of its traditional public sector solution.

**A Capital-efficient Growth Story:** Magnet has been bootstrapped since inception, with insiders owning ~75% of the business post-IPO. We do see lack of liquidity as a potential concern for larger institutional fund managers. Magnet had a 49% CAGR in annual recurring revenue between 2018-2020, while maintaining market-leading gross margins (mid-90% range). Post-IPO, we expect Magnet to focus on executing on the growth opportunity, and forecast adjusted EBITDA margins in the mid-teens through 2023E.

**M&A Is Upside:** Pre-IPO, Magnet focused predominantly on organic growth. Post-IPO, the company has a new focus on M&A, acquiring DME Forensics in September 2021 for ~\$9 million. We believe that Magnet is looking for tuck-in opportunities that fill out the product suite. The company had \$110 million in net cash at the end of Q3 and we see the potential for ~\$2/share-\$11/share upside from capital deployment on M&A.

**Valuation:** Our C\$33 price target values Magnet at 8.0x EV/2023E sales, in line with the peer average. We regard Magnet as attractive at these levels. The company scores well on a Rule-of-40 basis (68%), but trades well below similar-scoring peers. Our upside scenario of C\$42.50 values the company in line with Rule-of-40 peers at 10x 2023E sales.

All figures in US dollars unless otherwise stated (C\$1.268:US\$1.00).

Please see "Price Target Calculation and Key Risks to Price Target" information on page 17. For required regulatory disclosures please refer to "Important Disclosures" beginning on page 18.

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### Outperformer

MAGT-TSX, Sector: Information Technology

Current Price (2/1/22): C\$24.60

Price Target (12-18 mos.): C\$33.00

### CIBC Estimates and Valuation

(Dec. 31)	2020	2021	2022	2023
Revenue(mln)	51.23A	67.60E	88.35E	116.56E
Adj. EPS	0.64A	0.56E	0.82E	0.88E
Adj. EBITDA(mln)	15.4A	15.9E	14.1E	17.8E

Revenue(mln)	Q1	Q2	Q3	Q4
2021	14.66A	16.46A	17.77A	18.70E
2022	18.50E	21.40E	23.50E	24.95E

Adj. EPS	Q1	Q2	Q3	Q4
2021	0.06A	0.23A	0.09A	0.20E
2022	0.12E	0.26E	0.15E	0.29E

Adj. EBITDA(mln)	Q1	Q2	Q3	Q4
2021	4.8A	4.4A	4.7A	3.6E
2022	3.0E	3.5E	3.7E	3.9E

Valuation	2020	2021	2022	2023
P/Sales	16.2x	12.3x	9.4x	7.1x
P/E	30.2x	34.5x	23.7x	22.0x
EV/EBITDA	43.3x	41.9x	47.1x	37.4x
FCF Yield		1.7%	1.5%	1.8%

### Stock Performance and Key Indicators

Enterprise Value:	C\$844M	Shares O/S:	42.9M
Market Cap.:	C\$1,055M	Float:	34.9M
52-wk Range:	C\$22.08 - C\$64.90	Div. / Yield:	C\$0.00/0.00%

### TSX Composite Index vs. MAGT-TSX



(Source: FactSet)

**Magnet Forensics, Inc. (MAGT-TSX) — Outperformer**Price (2/1/22) C\$24.60 12-18 mo. Price Target **C\$33.00**

Sector: Information Technology

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Peer Comparison	2020	2021E	2022E	2023E
EV/Sales - Canadian Software Pee	-	10.2x	7.5x	5.7x
EV/Sales - Magnet	-	10.8x	8.3x	6.3x
Key Financial Metrics	2020	2021E	2022E	2023E
Net Debt	(11)	(108)	(120)	(135)
Total Debt	10	9	9	9
Net Debt/EBITDA	(1.2x)	(6.1x)	(8.5x)	(8.5x)
Free Cash Flow	21	15	12	15
Sales Growth	32.5%	32.0%	30.7%	31.9%
Per Share Data	2020	2021E	2022E	2023E
FCFPS	-	0.34	0.28	0.35
Adj. EPS Dil.	0.64	0.56	0.82	0.88
Wgt Avg # of Shares	0.0	38.1	40.4	40.4
FD Number of Shares	0.0	39.8	42.6	42.6
Income Statement	2020	2021E	2022E	2023E
<b>Revenue</b>	<b>51</b>	<b>68</b>	<b>88</b>	<b>117</b>
Cost of Goods Sold	3	4	7	8
<b>Gross Profit</b>	<b>49</b>	<b>63</b>	<b>82</b>	<b>108</b>
Gross Margin %	94.90%	93.43%	92.50%	93.00%
Tot Operating Exp	36	50	70	93
<b>Adj. EBITDA</b>	<b>15</b>	<b>16</b>	<b>14</b>	<b>18</b>
Adj EBITDA Margin	30.0%	23.5%	16.0%	15.3%
D&A	2	2	2	3
Interest Expense	0	0	1	1
<b>Pretax profit</b>	<b>13</b>	<b>12</b>	<b>11</b>	<b>14</b>
Tax Expense	2	3	3	4
<b>Adjusted Net Income</b>	<b>11</b>	<b>9</b>	<b>8</b>	<b>10</b>
Adjusted Net Margin	20.7%	12.9%	9.0%	8.7%
Cash Flow Statement	2020	2021E	2022E	2023E
<b>Net CFO</b>	<b>23</b>	<b>16</b>	<b>14</b>	<b>17</b>
Capex	(2)	(1)	(2)	(2)
<b>Free Cash Flow</b>	<b>21</b>	<b>15</b>	<b>12</b>	<b>15</b>
Balance Sheet	2020	2021E	2022E	2023E
Cash & ST Investment	21	117	129	144
Goodwill	1	7	6	6
<b>Total Assets</b>	<b>45</b>	<b>151</b>	<b>177</b>	<b>203</b>
LT Int-Bearing Debt	8	7	7	7
<b>Total Liabilities</b>	<b>55</b>	<b>62</b>	<b>77</b>	<b>93</b>
<b>Shareholders' Equity</b>	<b>(10)</b>	<b>90</b>	<b>100</b>	<b>110</b>

Source: FactSet, Company Reports &amp; CIBC World Markets Inc.

**Company Profile**

Magnet is a developer of data analytics software used for digital forensics investigations. Magnet AXIOM is used to preserve, identify, extract, analyze and document digital forensic artifacts.

**Investment Thesis**

1) Leading global digital forensics investigation solutions provider; 2) Well positioned in growing public and private end-markets; 3) Unified product platform is a competitive advantage.

**Price Target (Base Case): C\$33.00**

Our price target is based on 8x EV/2023E sales, in line with the peer average. The peer set includes similar-growth Rule-of-40 peers, digital forensics peers, end-point security providers and Canadian SaaS peers.

**Upside Scenario: C\$42.50**

Our upside scenario is calculated using 40% growth in 2023E and a 10.0x EV/Sales multiple. We assume 10% revenue growth from M&A and an EV/Sales multiple in line with similar-growth Rule-of-40 peers.

**Downside Scenario: C\$17.00**

Our downside scenario is calculated using 20% growth in 2023E and a 4.0x EV/Sales multiple. We assume no revenue growth from M&A and a multiple in line with slower-growth digital forensics peers.

## Investment Thesis

We are initiating coverage of Magnet Forensics, Inc. (Magnet) with an Outperformer rating and C\$33 price target based on an 8.0x EV/2023E sales multiple. Magnet provides a comprehensive digital investigation software platform for public and private sector organizations. The company has been bootstrapped since inception, with management owning ~75% of the business post-IPO. The company is profitable, with market-leading gross margins (mid-90%).

**Well Positioned In A Growing Market:** The digital investigations and intelligence market is expected to grow at a 10% CAGR between 2021 and 2026E to reach \$10.2 billion, according to IDC. Magnet is well positioned to benefit from increased spending on digital investigation software, with 85% of criminal investigations now including some form of digital evidence. Magnet is growing its annual recurring revenue (ARR) well above market rates as the company displaces legacy providers and expands in the private sector. The company has a land-and-expand model within the public sector, and its +120% net dollar retention rate underscores its success in adding further seats/cross-selling additional solutions into its customer base.

**Expect +30% Revenue Growth Through Our Forecast:** Magnet has an established position within the public sector. From here, we believe that Magnet will work to add seats at existing customers and cross-sell its suite (case analytics and discovery) to expand the solution more broadly to non-technical users within organizations. The company has reaped early successes with this strategy, with ARR from the London Metropolitan Police increasing by 10x when the organization purchased additional solutions. Magnet unveiled a dedicated private sector solution in 2020 and has seen strong growth in this market, which now represents roughly 35% of revenue. We expect strong growth from this segment through our forecast, with the average selling price of the private sector solution almost double that of the traditional public sector offering.

**M&A Is Upside:** Magnet has historically focused on organic growth. However, post-IPO we believe that M&A will be a higher priority. We expect Magnet will look for tuck-ins (\$10 million-\$20 million in size) to fill out the product suite and for more transformational acquisitions to move into new areas. Acquisition criteria include strategic fit with the platform and profitability. We consider DME Forensics, acquired in September 2021 for \$9 million (3x revenue), as a good example of an acquisition that satisfies Magnet's M&A criteria. The acquisition of DME allowed Magnet to build out video forensic capabilities much more quickly than if it had chosen to develop the solution internally. With \$110 million in net cash at the end of Q3, we estimate ~10% upside to our price target from Magnet deploying the capital.

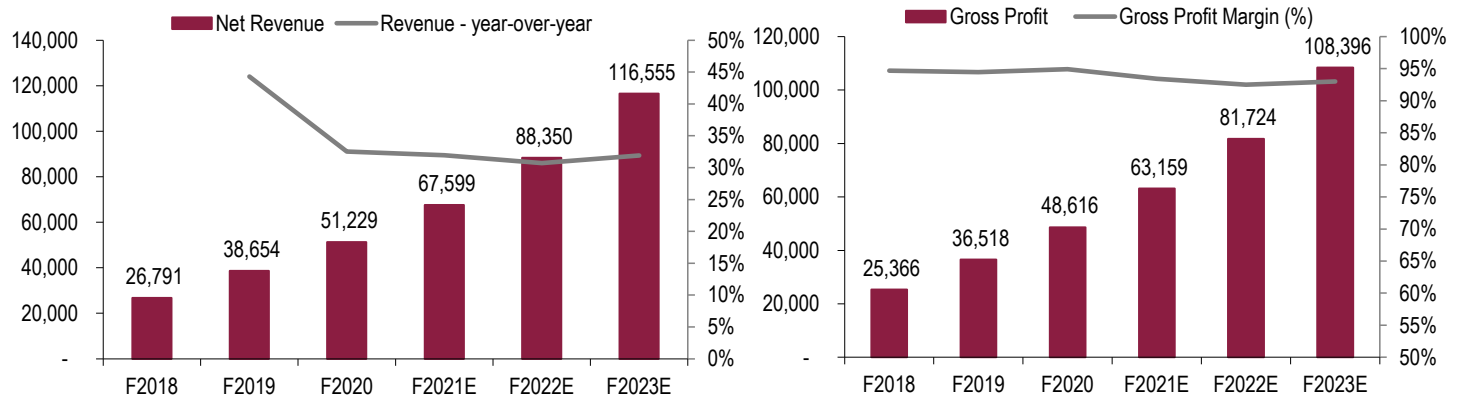
**Valuation:** Our C\$33 price target values Magnet at 8.0x EV/2023E sales, in line with the peer average. We regard Magnet as attractive at these levels. The company scores well on a Rule-of-40 basis (68%), but trades well below similar-growth peers. Our upside scenario of C\$42.50 values the company in line with Rule-of-40 peers.

## Well Positioned In A Growing Market

Founded in 2010, Magnet Forensics is a developer of data analytics software used for digital forensics investigations. Its flagship product, Magnet AXIOM, is used globally by digital forensics investigators to preserve, identify, extract, analyze and document digital forensic evidence (“artifacts”). While Magnet’s products were initially designed for use by law enforcement and public safety organizations, the business has expanded to serve private enterprise customers as cybercrime within organizations has become a growing threat. After establishing its position as a key player in the digital forensics market, Magnet now offers a full suite of digital forensics, case analytics, and electronic discovery solutions to serve the evolving needs of the public and private sectors.

Magnet has seen strong organic revenue growth and cash flow to date, growing annual recurring revenue at a 49% CAGR between 2018-2020, while maintaining gross profit margins in the 95% range. Today, the company has over 4,000 customers in 93 countries.

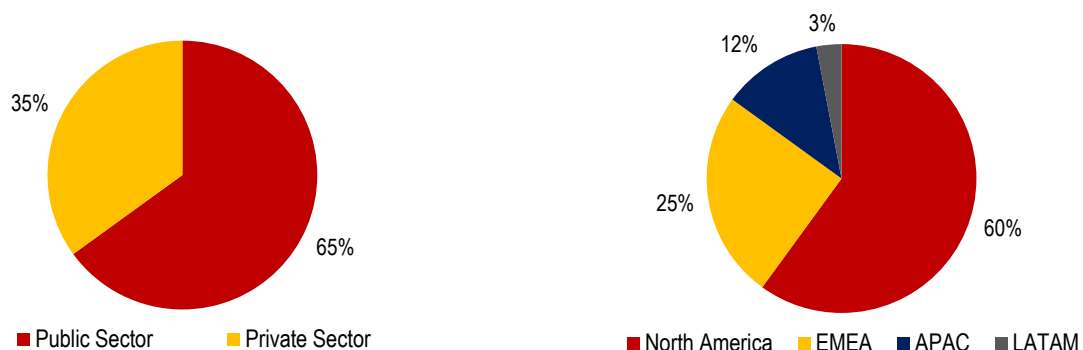
**Exhibit 1: Magnet Forensics – Revenue (left) And Gross Profit (right) Growth, 2018 - 2023E (\$000)**



Source: Company reports and CIBC World Markets Inc.

The company is well positioned to benefit from increased spending on digital investigation software, with 85% of criminal investigations now including some form of digital evidence. The company has been expanding the scope of its offering and 35% of revenue now comes from the private sector. Magnet has a +120% net dollar retention rate, underscoring its success in adding further seats/cross-selling additional solutions into its customer base.

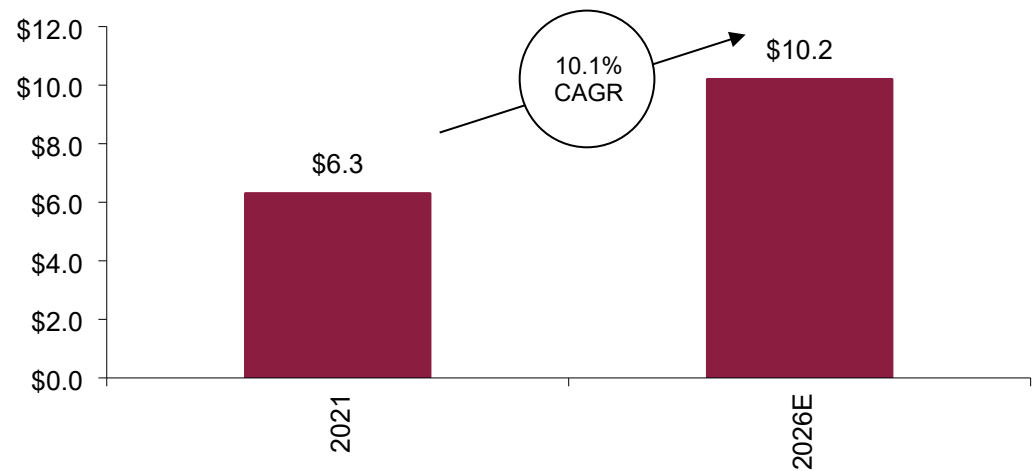
**Exhibit 2: Magnet Forensics – Revenue Breakdown, April 2021**



Source: Company reports and CIBC World Markets Inc.

According to IDC, the digital investigations and intelligence market is large and expanding rapidly. It is expected to grow at a 10% CAGR between 2021 and 2026E, reaching \$10.2 billion. Magnet has been growing at three to four times this rate, with the company displacing legacy providers.

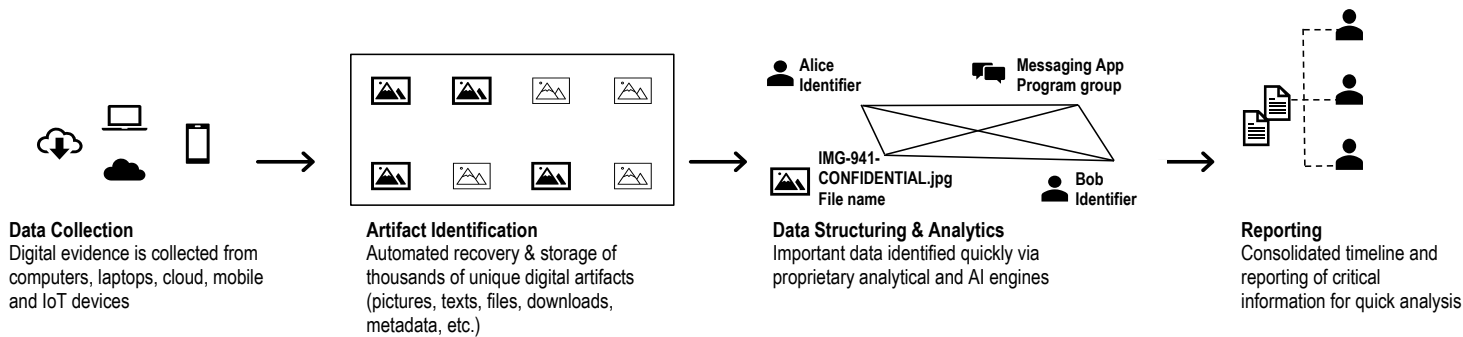
Exhibit 3: Market Opportunity – Digital Investigation & Intelligence Market, 2021 - 2026E (\$B)



Source: Company reports, Mordor Intelligence, Homeland Security Research Corp., IDC, and CIBC World Markets Inc.

We see Magnet’s competitive advantage as being the unified nature of its platform, providing one window into all of the digital evidence (“artifacts”) recovered across a number of different devices. In contrast to competitors’ siloed offerings, Magnet’s solutions build connections, flag possible evidence, and create a timeline of events using artifacts from nearly any device.

Exhibit 4: Magnet Forensics – Unified Digital Investigation Platform & Product Journey, January 2022



Source: Company reports and CIBC World Markets Inc.

The company’s case intelligence and analytics offerings help it to reach a broader audience within an organization, moving beyond the specific technologists tasked with handling digital forensics. This wider scope allows the company to increase the number of paid seats or licenses, providing a clear path to growing average revenue per account (ARPA).

Exhibit 5: Magnet Forensics – Solution Suites Span The Digital Evidence Lifecycle, January 2022

→ Expanding The Potential User Base		
Digital Forensics	Case Analytics & Intelligence	Private Sector
Magnet AXIOM	Magnet REVIEW	Magnet AXIOM Cyber
Magnet AXIOM Cyber	Magnet AUTOMATE	Magnet AUTOMATE Enterprise
Magnet OUTRIDER	Magnet ATLAS	

Source: Company reports, Modor Intelligence, Homeland Security Research Corp., IDC, and CIBC World Markets Inc.

A competitive dynamic unique to the digital forensics market is the need for many public sector law enforcement agencies to rely on multiple digital forensics tools to corroborate extracted artifacts. This requirement leads to public sector clients relying on more than one digital forensics provider. This dynamic drives Magnet's land-and-expand strategy, as customers with multiple providers can easily compare and contrast the capabilities, functionality and effectiveness of the tools as they use them, with the better-performing tool likely to gain a stronger foothold within an organization. Ideally, this generates an expansion in the number of paid seats and licenses.

Magnet's competitors range from point solution providers that focus on individual devices or investigation types to more holistic providers. We view Cellebrite as Magnet's closest competitor, with a suite of cloud and on-premise tools that can extract data artifacts from a variety of devices and provide analytics and insights similar to those from Magnet. The primary difference between the two companies is Magnet's heavier weighting towards the private sector, with 35% of its customers in the private sector compared to Cellebrite generating 10% of its revenue from that sphere.

Other digital forensics competitors are more focused on artifact extraction from an individual device type or subset of devices. Oxygen Forensics and MSAB are two competitors that specifically specialize in data extraction from mobile devices and cloud platforms. These providers also provide analytics tools and services to work with the extracted data.

Some of Magnet's competitors (e.g., Nuix) have their legacies in e-discovery tools that help organizations prepare for litigation or regulatory response by identifying, collecting and producing electronically stored information and have started to look to the digital forensics market as an extension of their own products. While there is a natural overlap in the tools used for digital forensics and e-discovery, Nuix and other providers with a history in e-discovery typically specialize in investigations where large numbers of emails comprise the bulk of evidence.

Magnet has much stronger sales growth than digital services peers, with most growing closer to market rates. We believe Magnet's outperformance is created by a combination of land-and-expand strategies within existing public sector customers and the company's expansion into cyber security offerings for corporate customers. Magnet also has very strong gross margins, highlighting the capital-efficient nature of its business.

#### Exhibit 6: Digital Forensics Peers – Financial Comparison, 2021E - 2023E

	(C\$MM)		Sales Growth			EBITDA Growth			Gross Margin			EBITDA Margin		
	Market Cap	C21E Sales	C21E	C22E	C23E	C21E	C22E	C23E	C21E	C22E	C23E	C21E	C22E	C23E
Magnet	\$1,113	\$86	33.1%	29.6%	30.3%	46%	-7%	44%	94.0%	93.4%	93.1%	22.3%	16.0%	17.7%
Cellebrite	\$1,597	\$307	NA	17.3%	18.3%	NA	-11%	23%	82.4%	80.0%	80.7%	19.2%	14.6%	15.3%
MSAB	\$90	\$43	-0.9%	15.0%	12.0%	22%	28%	21%	91.6%	91.4%	91.5%	16.3%	18.2%	19.7%
Nuix Ltd.	\$608	\$161	2.2%	6.1%	12.6%	4%	7%	29%	70.8%	70.8%	70.8%	35.2%	35.6%	40.6%
<b>Average</b>	<b>\$852</b>	<b>\$149</b>	<b>11.4%</b>	<b>17.0%</b>	<b>18.3%</b>	<b>24.3%</b>	<b>4.5%</b>	<b>29.3%</b>	<b>84.7%</b>	<b>83.9%</b>	<b>84.0%</b>	<b>23.3%</b>	<b>21.1%</b>	<b>23.3%</b>

Source: Company reports and CIBC World Markets Inc.



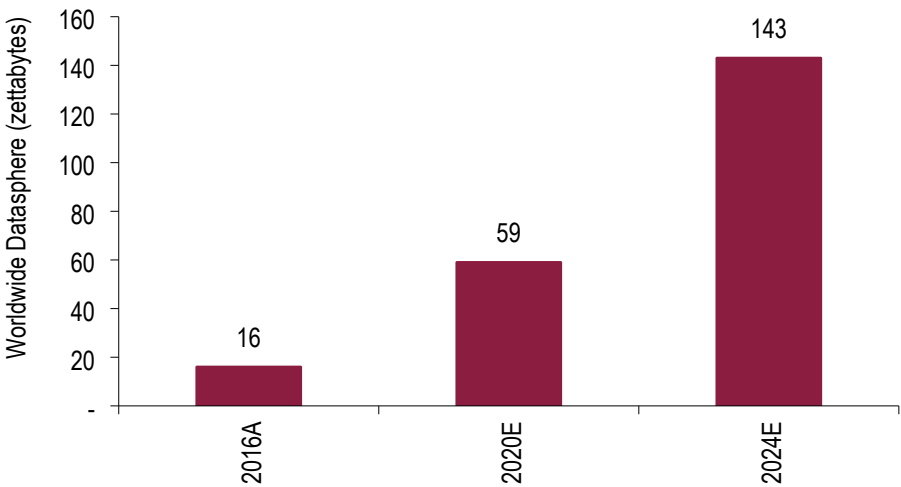
Expect +30% Revenue Growth

Public Sector Base Creates Upsell Opportunities

Magnet was initially developed to be sold into the public sector, with founder Jad Saliba developing the solution based on his experience as a police officer in a digital forensics unit. Today, Magnet’s public sector base includes police forces as well as customers in the defense and intelligence sectors. The company also offers broader public sector solutions geared towards regulatory and compliance enforcement. From here, we foresee the opportunity to add further licenses to existing customers and to cross-sell additional solutions into the base.

The investigative challenges facing the public sector are growing rapidly, with many organizations overwhelmed by the amount of digital evidence being collected. Today, roughly 85% of criminal investigations include some form of digital evidence.

Exhibit 7: IDC Research – Exponential Increase In Digital Evidence, April 2017



Source: IDC, “Global Datasphere Forecast” and “Data Age 2025: The Evolution of Data To Life-Critical.”

Public safety organizations have struggled to modernize antiquated workflows and keep pace with the increase in digital evidence. Magnet has a strong install base using its AXIOM digital evidence offering and we view digital evidence as a jumping-off point from which Magnet can sell additional solutions into public safety organizations, creating an integrated platform.

**AXIOM:** Magnet’s flagship product is AXIOM, which allows digital investigators to preserve, identify, extract, analyze, and document digital forensic artifacts. With every computer program, file system, operating system and other application generating different traces of data, digital investigators must consider how to access potentially thousands of types of digital forensic artifacts from a wide range of data sources, including their various versions and formats.

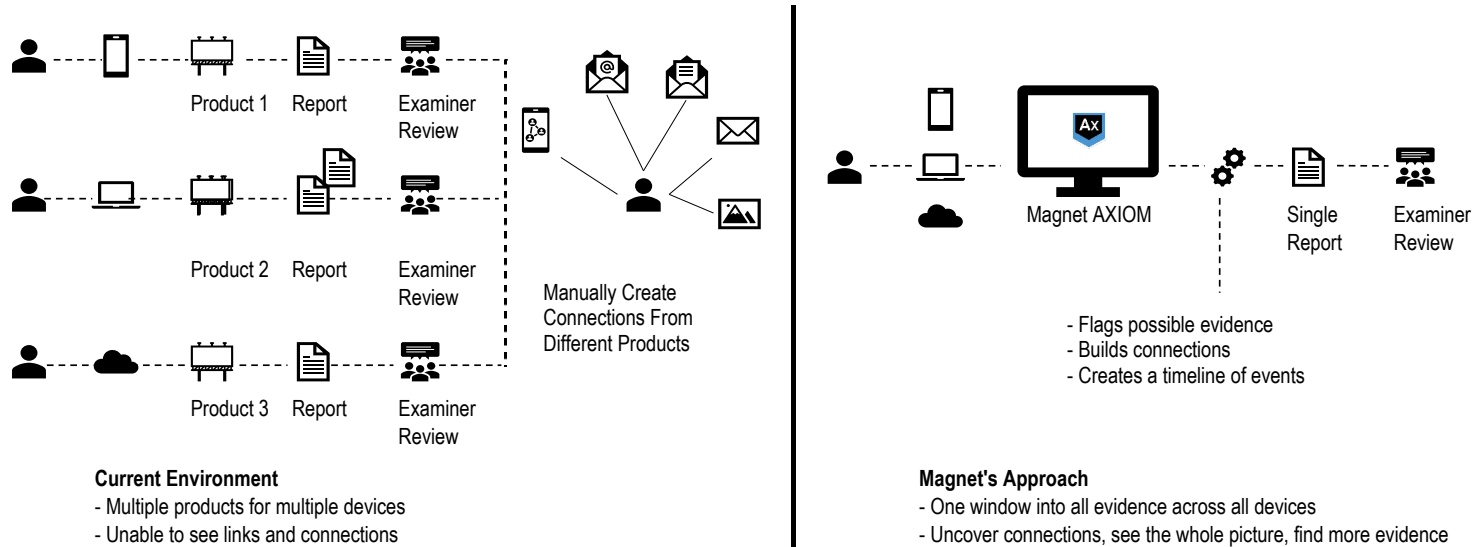
Exhibit 8: Magnet Forensics – Types Of Digital Forensic Artifacts, April 2021

Types Of Digital Forensic Artifacts					
Browser History	Email	Texts	Files	Videos	Documents
Social Networking Apps	Images	App Records	Meta Data	Access History	Location Data

Source: Company reports and CIBC World Markets Inc.

AXIOM's competitive advantage lies in its ability to provide a unified view of evidence and artifacts across all devices. The solution flags possible evidence and creates a timeline of events, in contrast to other solutions, which offer multiple products for multiple devices.

### Exhibit 9: Magnet Forensics – Product Offering Improves Data Visualization & Analytics For Users, January 2022



Source: Company reports and CIBC World Markets Inc.

### Cross-selling Case Analytics & Intelligence

From Axiom, Magnet has expanded its services to include case analytics and intelligence. Case analytics products allow Magnet to reach a broader user audience beyond the digital forensics unit. Magnet's digital forensics solutions typically serve 1%-2% of a public sector organization, but case analytics solutions can help reach deeper into an organization, targeting general (non-forensic and non-technical) investigators. Once a customer is using case analytics & intelligence tools, Magnet becomes more entrenched within the organization and a per-user/seat pricing model drives ARPA growth. The company's case analytics and intelligence solutions include AUTOMATE, REVIEW and ATLAS.

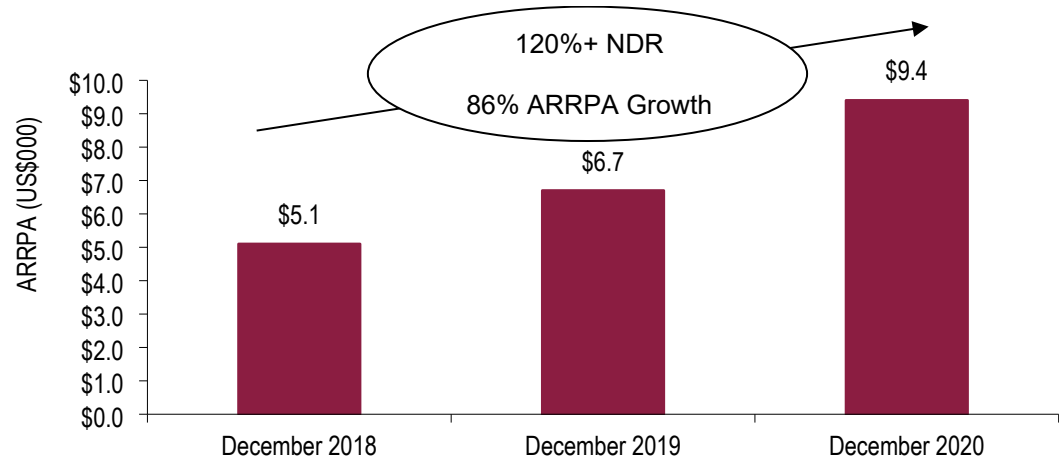
**AUTOMATE:** Magnet AUTOMATE helps public sector organizations automate mobile and computer workflows, improving efficiency and allowing lab technicians to focus on higher-value tasks. The solution is sold based on processing capacity/nodes. Magnet has seen ARR increase roughly 6x in customers that have adopted AUTOMATE, and those ARR increases continue as customers look to build out more workflows with the solution. We see AUTOMATE as well positioned amid current tight labour markets.

**REVIEW:** Magnet REVIEW allows non-technical users to review digital evidence within a secure, agency-wide collaboration platform. The solution was purpose-built to empower non-technical users to review case information and was rolled out in 2021. The London Metropolitan Police has been the largest win to date, with ARR from the agency increasing tenfold when REVIEW was adopted.

**ATLAS:** Magnet ATLAS provides digital forensics case management, allowing stakeholders agency-wide to manage, collaborate on, analyze and report on all aspects of digital investigations. The solution allows organizations to securely store, track and manage cases while upholding the chain of custody.

Magnet has seen solid client retention, with a 120%+ net retention rate and 86% ARRPA growth over the past two years as clients add users and extra functionality.



**Exhibit 10: Magnet Forensics – ARRPA Historical Growth, December 2018 - December 2020**

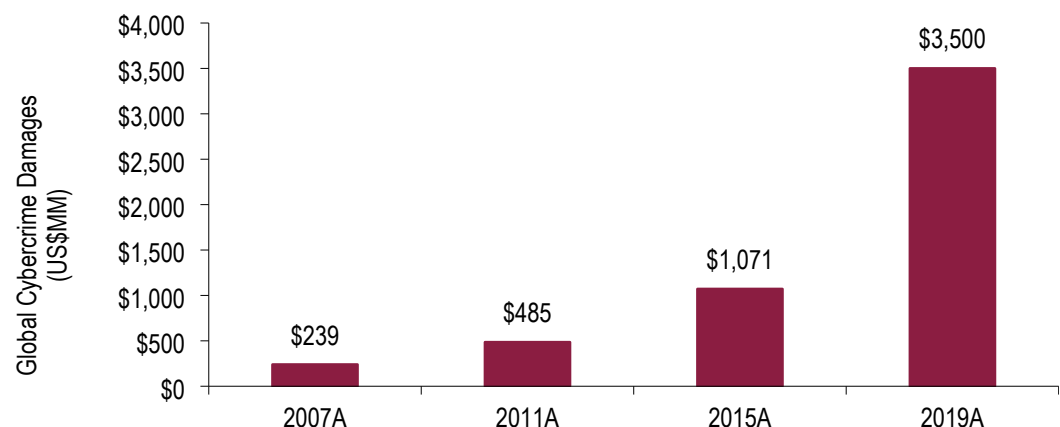
Source: IDC, "Global Datasphere Forecast" and "Data Age 2025: The Evolution of Data To Life-Critical."

**Case Study – London Metropolitan Police:** The London Metropolitan Police (Met) is a long-time Magnet customer and one of the 10 largest law enforcement agencies in the world. The Met announced in August 2021 that it would be expanding its use of the solution to include Magnet REVIEW case analytics solutions. REVIEW was developed in collaboration with the Met to bring together technical and non-technical investigators to collaborate while maintaining the forensic integrity of the evidence. With the additional case analytics and intelligence services, Magnet increased ARR from the customer by roughly 10x.

We see a number of future expansion areas for the AXIOM platform, including e-discovery, vertical-specific software (i.e., major crimes) and records management. We expect that Magnet will use a combination of organic growth, M&A, and partnerships to continue to build AXIOM into an end-to-end solution.

### Private Sector Demand Expanded The Solution

Following the introduction of AXIOM in 2016, Magnet saw significant demand from private sector organizations given a surge in cyber events. The FBI Internet Crime Report suggests that global cybercrime damage has increased exponentially over the past several years from \$239 million in 2007 to \$3.5 billion in 2019.

**Exhibit 11: FBI: Internet Crime Report – Escalating Global Cybercrime Damage, 2007 - 2019**

Source: FBI: Internet Crime Report, company reports, and CIBC World Markets Inc.

As a result of this increased interest, Magnet extended its offering into the private sector. In 2020, the company launched AXIOM CYBER, a version of AXIOM purpose-built for the private sector. The solution allows organizations to perform remote investigations and gives them the ability to collect and analyze evidence gathered from multiple sources. The company's public sector customer base provides credibility when selling into the private sector as police officers move into the private sector and bring Magnet's solutions with them. Magnet has seen strong growth in its AXIOM CYBER offering, with the private sector growing from 25% of revenue in 2020 to ~35% of revenue in 2021E. The company is able to charge nearly double the average selling price for AXIOM CYBER versus the traditional AXIOM product.

Magnet has made significant strides in its private sector business in a short period of time, signing 150 of the Fortune 1000 as customers, including Amazon, Chevron and Allstate. The company also counts consulting firms as private sector customers, with these firms currently using Magnet for specific engagements. We foresee the potential for consulting firms to become channel partners for Magnet as they become more reliant on the tools. Magnet has traditionally focused on a land-and-expand strategy within the public sector, and the company is developing a "hunter" sales team to focus on new logo acquisition within the private sector.

## M&A Is Upside

Pre-IPO, Magnet focused predominantly on organic growth, completing three opportunistic tuck-ins over a 10-year period. Post-IPO, the company has hired a VP of Corporate Development to focus on M&A and we believe that M&A will be a larger priority moving forward. We expect Magnet to focus on tuck-ins (\$10 million-\$20 million in size) to fill out the product suite and on more transformational acquisitions to move into new areas. Acquisition criteria include a strong strategic fit with the platform and profitability. We believe that Magnet will continue to selectively look at acquisitions, focusing on opportunities that:

1. **Add Complementary Products/Accelerate Product Roadmap:** The market is very fragmented, with a number of point solutions (e.g., recovering data from a vehicle) that could be combined with AXIOM to strengthen the core platform and make it stickier.
2. **Expand Into Adjacencies With A Focus On The Enterprise Market:** We expect that Magnet could seek larger acquisitions to add adjacent solutions, especially into the enterprise market. We foresee opportunities in areas such as incident response, ransomware and e-discovery.

In September 2021 Magnet acquired DME Forensics, a video and multimedia evidence solution, for ~3x revenue or \$9 million (including a \$2.25 million earn out). Magnet had \$110 million in net cash at the end of Q3 and we foresee the potential for \$2/share-\$11/share upside from the company deploying the capital at reasonable multiples.

**Exhibit 12: Magnet Forensics – M&A Scenario (US\$MM) & Upside To Price Target (C\$), January 2022**

	M&A Spend				
	\$ 40	\$ 50	\$ 60	\$ 70	\$ 80
<b>6.0x</b>	1.89	2.36	2.83	3.31	3.78
<b>5.0x</b>	2.27	2.83	3.40	3.97	4.53
<b>4.0x</b>	2.83	3.54	<b>4.25</b>	4.96	5.67
<b>3.0x</b>	3.78	4.72	5.67	6.61	7.56
<b>2.0x</b>	5.67	7.09	8.50	9.92	11.34

Source: CIBC World Markets Inc.

## Valuation

### EV/Sales Is Our Primary Valuation Metric

We initiate coverage with an Outperformer rating and a C\$33 price target. Our target is based on 8.0x EV/2023E sales of \$117 million, inclusive of net cash (post-IPO) and (fully diluted) shares outstanding of 39.8 million. Our EV/Sales multiple of 8.0x is in line with the peer average. Our peer set comprises similar-growth Rule-of-40 peers, digital forensics peers, end-point security providers and Canadian SaaS peers.

### EV/Gross Profit Is Our Secondary Valuation Metric

EV/Gross profit is our secondary valuation metric. We value the 2023E gross profit of \$108 million at an 11x multiple, in line with the peer average. Given Magnet's best-in-class gross margins, this valuation yields a C\$41/share value.

**Exhibit 13: Magnet Forensics – Comp Table, February 1, 2022**

	Enterprise Value	2023E Gross Margins	EV/S			EV/GP			EV/EBITDA		
	(\$mlns.)		C21E	C22E	C23E	C21E	C22E	C23E	C21E	C22E	C23E
U.S. Enterprise SaaS Peers (Tier 1 SaaS - Rule of 40 > 50)											
Zoom Video Communications, Inc.	40,142	77.0%	10.1x	8.6x	7.3x	13.6x	11.4x	9.5x	24.3x	22.5x	19.4x
Lightspeed Commerce Inc*	3,965	48.1%	8.7x	5.9x	4.4x	17.1x	12.2x	9.1x	NEG	NEG	NEG
Nuvei Corporation*	9,111	79.7%	12.6x	9.6x	7.5x	15.7x	12.1x	9.4x	28.9x	22.0x	16.8x
CrowdStrike Holdings, Inc. Class A	40,150	77.8%	29.0x	20.6x	15.4x	37.9x	26.7x	19.8x	>50	>50	>50
Zscaler, Inc.	35,661	78.9%	43.8x	31.0x	23.4x	>50	38.9x	29.7x	>50	>50	>50
Shopify, Inc. Class A	114,606	51.6%	25.0x	18.8x	13.9x	45.8x	35.5x	27.0x	>50	>50	>50
DocuSign, Inc.	24,923	84.5%	12.3x	9.7x	7.8x	14.8x	11.7x	9.3x	>50	46.0x	37.1x
Veeva Systems Inc Class A	33,799	74.5%	18.6x	15.8x	13.5x	24.9x	21.2x	18.1x	44.4x	40.1x	34.1x
Magnet Forensics, Inc.*	732	93.0%	10.8x	8.3x	6.3x	11.6x	9.0x	6.8x	46.1x	>50	41.2x
Twilio, Inc. Class A	32,782	54.9%	11.8x	9.0x	6.9x	21.9x	16.5x	12.6x	>50	>50	>50
HubSpot, Inc.	22,544	82.2%	17.5x	13.5x	10.8x	21.7x	16.6x	13.2x	>50	>50	>50
ServiceNow, Inc.	115,946	81.8%	19.7x	15.6x	12.5x	24.3x	19.2x	15.3x	>50	49.0x	38.7x
U.S. Enterprise SaaS Peers (Tier 1 SaaS - Rule of 40 > 50) Average		73.7%	18.3x	13.9x	10.8x	22.6x	19.3x	15.0x	36.0x	35.9x	31.2x
Digital Forensics Peers											
Cellebrite DI Ltd.	927	80.7%	3.8x	3.3x	2.8x	4.6x	4.1x	3.4x	19.9x	22.3x	18.1x
Micro Systemation AB Class B	883	90.9%	2.7x	2.3x	2.1x	3.0x	2.5x	2.3x	15.6x	10.7x	9.2x
Nuix Ltd.	421	70.8%	2.4x	2.3x	2.0x	3.4x	3.2x	2.8x	6.8x	6.3x	4.9x
Open Text Corporation	15,183	75.7%	4.4x	4.3x	4.1x	5.9x	5.7x	5.5x	11.9x	11.3x	10.9x
Palantir Technologies Inc. Class A	25,886	80.3%	17.0x	13.1x	10.1x	20.7x	16.2x	12.6x	>50	48.7x	33.3x
Digital Forensics Peers Average		79.7%	6.0x	5.0x	4.2x	7.5x	6.3x	5.3x	13.6x	19.9x	15.3x
Endpoint Security Providers											
CrowdStrike Holdings, Inc. Class A	40,150	77.8%	29.0x	20.6x	15.4x	37.9x	26.7x	19.8x	>50	>50	>50
BlackBerry Limited*	4,735	62.4%	5.0x	4.8x	4.4x	7.6x	7.3x	7.0x	NEG	NEG	NEG
SentinelOne, Inc. Class A	10,354	68.0%	NA	31.0x	18.9x	NA	48.5x	27.8x	NA	NEG	NEG
McAfee Corp. Class A	13,446	81.7%	7.0x	6.4x	5.8x	8.6x	7.9x	7.1x	15.8x	14.0x	11.7x
Check Point Software Technologies	14,272	89.6%	6.6x	6.4x	6.2x	7.4x	7.2x	6.9x	13.2x	13.0x	12.9x
Fortinet, Inc.	46,603	76.9%	14.0x	11.8x	9.9x	18.1x	15.2x	12.9x	49.2x	41.8x	34.3x
Endpoint Security Providers Average		76.1%	12.3x	13.5x	10.1x	15.9x	18.8x	13.6x	26.1x	22.9x	19.6x
Canadian Software Peers											
Magnet Forensics, Inc.*	732	93.0%	10.8x	8.3x	6.3x	11.6x	9.0x	6.8x	46.1x	>50	41.2x
Thinkific Labs, Inc.*	249	72.1%	6.6x	4.1x	2.7x	8.5x	5.7x	3.8x	NEG	NEG	NEG
Docebo, Inc.*	1,631	82.5%	15.6x	10.7x	7.7x	19.5x	13.2x	9.3x	NEG	NEG	NEG
Lightspeed Commerce Inc*	3,965	48.1%	8.7x	5.9x	4.4x	17.1x	12.2x	9.1x	NEG	NEG	NEG
E Automotive, Inc.*	463	49.8%	6.2x	4.8x	3.4x	13.2x	9.8x	6.9x	NEG	NEG	NEG
Kinaxis, Inc.*	3,380	72.0%	13.6x	10.9x	9.4x	21.1x	15.6x	13.1x	>50	>50	42.4x
Canadian Software Peers Average		69.6%	10.2x	7.5x	5.7x	15.2x	10.9x	8.2x	NA	NA	41.8x
Magnet Forensics, Inc.*	732	93.0%	10.8x	8.3x	6.3x	11.6x	9.0x	6.8x	46.1x	>50	41.2x
Overall Average		74.3%	13.3x	10.3x	8.0x	17.2x	14.3x	11.1x	27.1x	27.9x	26.7x

\*Share Prices Converted to USD

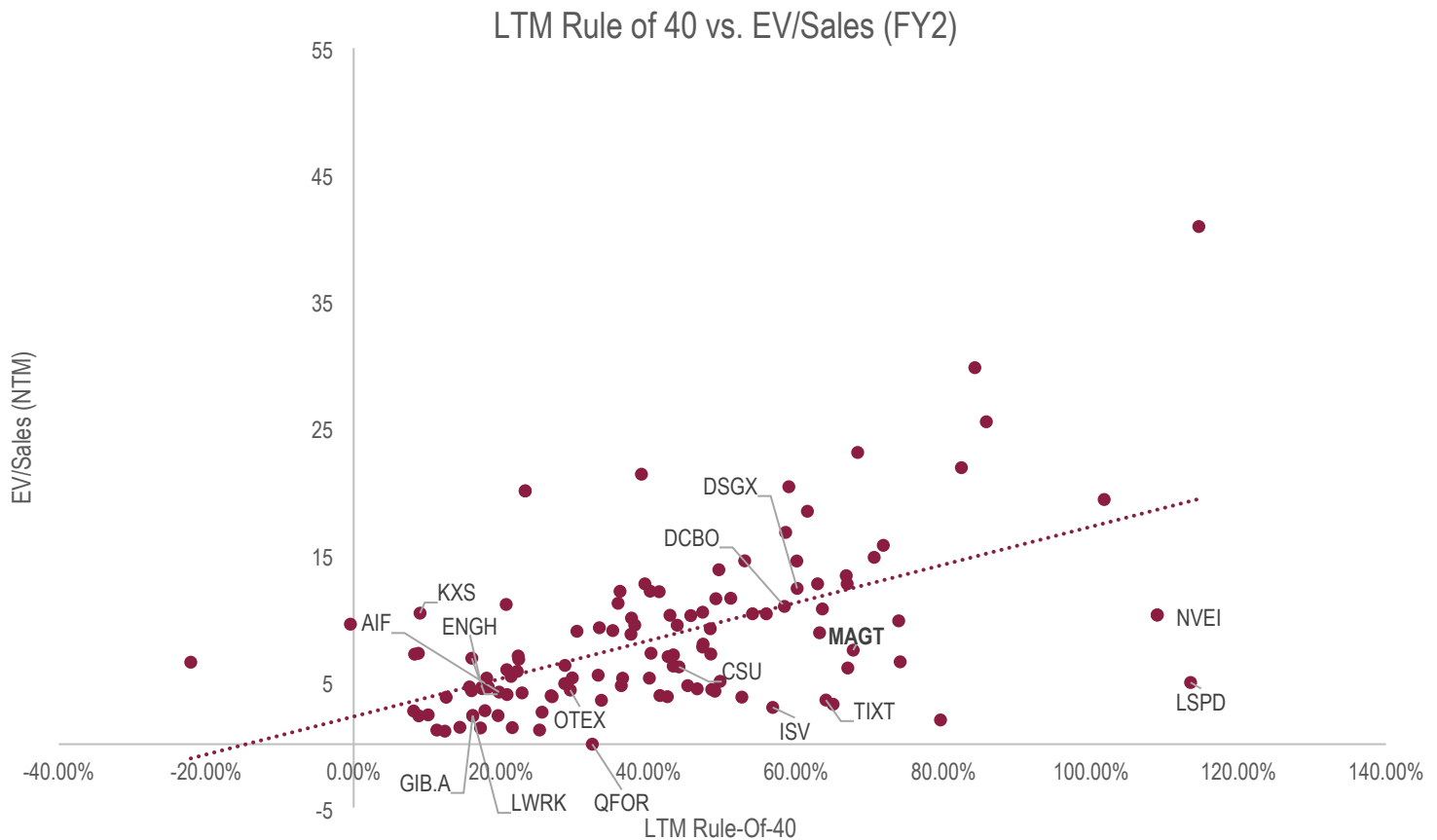
Bolded names are covered by CIBC; consensus estimates for all names except Magnet, Docebo and Kinaxis, which are our estimates.

Source: Company reports, FactSet and CIBC World Markets Inc.

## Rule Of 40

With strong revenue growth and solid free cash flow (FCF) margins, Magnet scores well on a Rule-of-40 basis at over 65%. Compared to software peers, Magnet's EV/Sales valuation relative to its Rule-of-40 score is below the group's trendline, highlighting a reasonable opportunity for multiple expansion given that sustainable free cash flow margins should help Magnet maintain its Rule-of-40 strength moving forward.

**Exhibit 14: Technology Equities – Rule-of-40 Vs. EV/Sales, January 2022**



Source: Company reports, FactSet and CIBC World Markets Inc.

## Base Case And Upside/Downside Scenarios

In the table in Exhibit 15, we summarize our base case and upside/downside scenarios for Magnet.

Our base case assumes 30% revenue growth and an 8.0x EV/Sales multiple on 2023E revenue.

Our upside scenario is based on 40% revenue growth in 2023E and a 10.0x EV/Sales multiple. In this scenario we incorporate 10% revenue growth from M&A and an EV/Sales multiple that is in line with similar-growth Rule-of-40 peers.

Our downside scenario is based on 20% revenue growth in 2023E and a 4.0x EV/Sales multiple. In this scenario we assume no M&A, organic growth slowing to the 20% range, and a multiple in line with slower-growth, less-capital-efficient digital forensics peers.

**Exhibit 15: Magnet Forensics – Upside/Downside Scenarios, January 2022**

	Base Case	Upside Scenario	Downside Scenario
2023E Revenue Growth	30%	40%	20%
Target Multiple (EV/S)	8.0x	10.0x	4.0x
Scenario Value	C\$33.00	C\$42.50	C\$17.00

Source: CIBC World Markets Inc.

**Key Potential Catalysts And Risks****Exhibit 16: Magnet Forensics – Key Potential Catalysts And Risks**

Catalysts	Risks
<b>Enterprise Demand Accelerates:</b> Magnet has capitalized on the rise in cyberattacks and cybercrime by tailoring its products for enterprise customers. While our forecast does factor in an acceleration of enterprise demand, faster-than-anticipated demand growth would be a catalyst for growth.	<b>Competitive Threats Erode Market Share:</b> There are a number of competitive providers of digital forensics tools. Were Magnet to cede market share to existing or new competitors, our growth assumptions would be at risk. Competitive pressure may come in the form of improved technology, pricing pressure, sales team ineffectiveness and other issues.
<b>Investor Demand Tilts Further Towards Profitable Technology:</b> In an investing environment that we expect to feature rising interest rates, profitable technology companies may attract more attention than unprofitable ones. With very strong gross margins, Magnet would benefit from a market that favors technology companies showing strong profitability.	<b>Data/Security Concerns:</b> Magnet's technology extracts protected data to aid investigators in their work. Were Magnet found to be the cause of a data breach or privacy violation, there would likely be negative ramifications for Magnet's brand. Poor public perception would challenge our growth forecast.
<b>Acquisitions Add Capabilities, Fuel Growth:</b> After growing the business without relying on external capital, Magnet now has significant cash reserves to pursue inorganic growth. Magnet has already completed one acquisition post-IPO and we expect management to remain active on M&A. Successful acquisitions could have a permanent impact on growth rates by expanding the total addressable market and increasing cross-sell opportunities.	<b>Regulation:</b> Given Magnet's products give investigators' access to protected data, there is a risk that regional governments may look to introduce legislation that limits the use of digital forensics tools. Increased regulation over digital forensics tools would have a clear negative impact on Magnet's ability to attract new customers and retain existing ones.
<b>Magnet Is Acquired:</b> As Magnet moves further into the enterprise market, it may become a more attractive acquisition target to a larger enterprise provider. While it is unlikely that management and insider owners would be willing to pursue a sale in the short term, it may be a long-term catalyst for the business.	<b>Multiple Voting Shares:</b> Adam Belsher, Jad Saliba and Jim Balsillie hold multiple voting shares, granting them voting control of the company. Under this structure, holders of common shares have little influence over the strategic direction of the firm or input in potential changes to the corporate structure. However, we note that voting control also allows the company to maintain its long-term strategy despite short-term headwinds.
<b>Generalist Investigator Demand Accelerates:</b> Magnet has sought to broaden its public sector market by offering products to investigators who aren't trained specifically on digital forensics tools. Expanding the market could lead to a material increase in the demand for overall seat licenses, a subsequent increase in the addressable market, and an acceleration in public sector revenue growth.	<b>Valuation Environment Worsens:</b> At the time of publishing, technology stocks and other growth equities are suffering broadly as interest rates appear poised to rise. As a pure-play technology firm, Magnet's share price is likely to continue to suffer in a challenging environment for technology companies.

Source: CIBC World Markets Inc.

**Financial Outlook**

Our summary financial forecast for Magnet is detailed in the table in Exhibit 17. We estimate 2023 revenue of \$117 million and adjusted EBITDA of \$18 million. Our forecast does not include the impact of future M&A.

**Exhibit 17: Magnet Forensics – Financial Summary, 2020 - 2023E**

	2020A	2021E	% Growth	2022E	% Growth	2023E	% Growth
Revenue	\$51.2	\$67.6	32.0%	\$88.4	30.7%	\$116.6	31.9%
Operating Expenses							
Sales And Marketing	\$15.7	\$21.2	35.3%	\$30.9	45.8%	\$42.0	35.7%
Research And Development	\$13.8	\$18.2	32.4%	\$24.7	35.6%	\$32.6	31.9%
General And Admin	\$6.1	\$11.0	80.0%	\$14.1	28.1%	\$18.6	31.9%
<b>Total Operating Expenses</b>	<b>\$35.6</b>	<b>\$50.5</b>	<b>41.9%</b>	<b>\$69.8</b>	<b>38.2%</b>	<b>\$93.2</b>	<b>33.6%</b>
Opex As % Of Revenue	69.5%	74.7%		79.0%		80.0%	
Adjusted EBITDA	\$15.4	\$15.9	3.2%	\$14.1	(11.0%)	\$17.8	25.9%
Adjusted EBITDA Margin %	30.0%	23.7%	-	16.6%	-	15.8%	

Source: Company reports and CIBC World Markets Inc.

**Revenue**

We expect organic revenue growth in the 30% range over our forecast period. Our forecast does not include future M&A, which we consider as upside to our model.

Magnet's products are sold through two licensing alternatives: term license subscription contracts and perpetual license contracts. Term licenses have a typical duration of one to three years and are available for product and solution offerings, while perpetual licenses are designed primarily to meet the needs of public sector clients and give customers the right to use the software in perpetuity.

Perpetual license customers are also required to purchase a separate term subscription (one to three years) to receive maintenance and support. Of total software license revenue in 2020, 60% was from perpetual licenses, although that percentage is falling as Magnet looks to grow recurring revenue by emphasizing term license subscriptions. A breakdown of revenue from licenses and from maintenance and professional services contracts is included in the table in Exhibit 18.

**Exhibit 18: Magnet Forensics – Revenue Breakdown, 2019 - 2020**

	2020 (C\$000)	2019 (C\$000)	% Change
License – Perpetual	9,634	8,917	8%
License – Term	6,560	3,436	91%
<b>Total License Revenue</b>	<b>16,194</b>	<b>12,353</b>	<b>31%</b>
Software Maintenance & Support	29,221	22,038	33%
Professional Services	5,814	4,263	36%
<b>Total Revenue</b>	<b>51,229</b>	<b>38,654</b>	<b>33%</b>

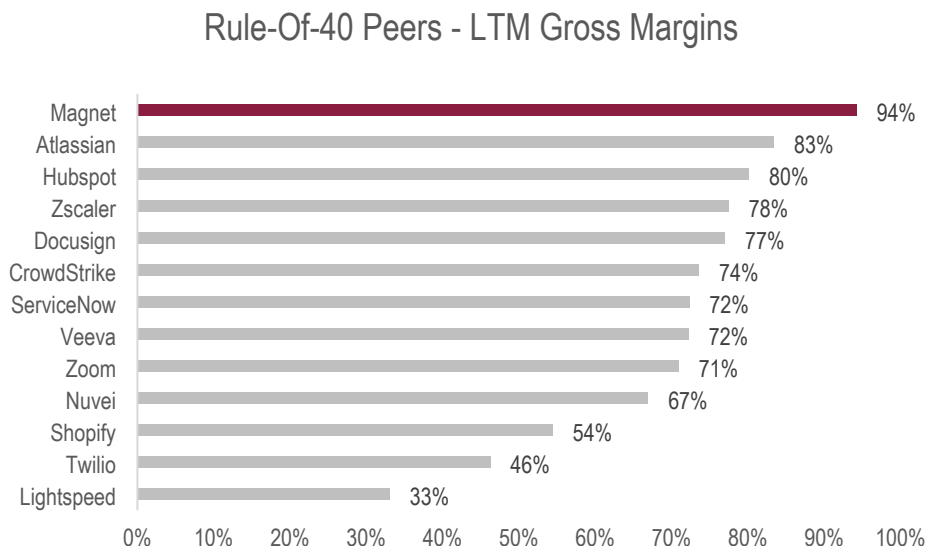
Source: Company reports and CIBC World Markets Inc.



## Gross Margin

Magnet has market-leading gross margins of mid-90%. We believe solid gross margins set a clear path to maintaining profitability as the company scales. As illustrated in the bar chart in Exhibit 19, Magnet's gross margins are best-in-class compared to other SaaS peers with similar-growth, LTM rule-of-40 scores.

**Exhibit 19: Rule-of-40 Peers – Gross Margins, January 2022**



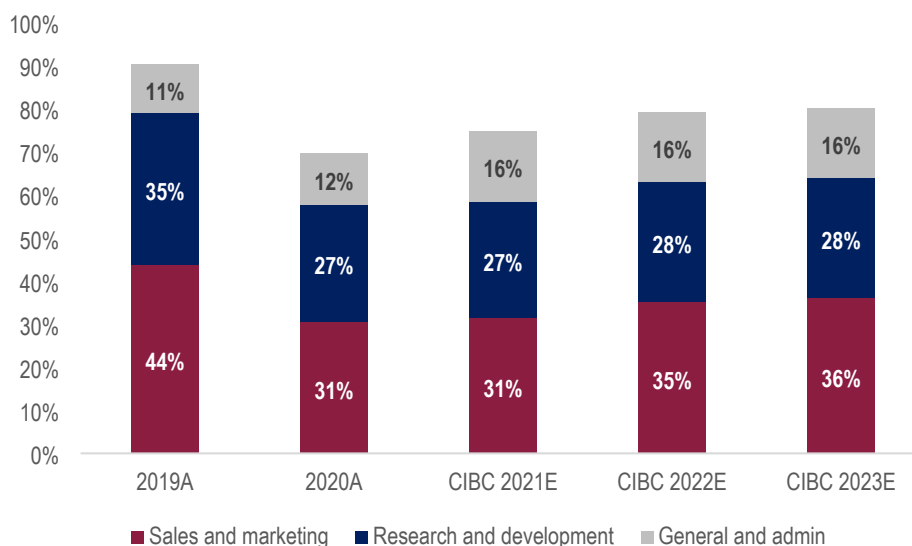
Source: Company reports, FactSet and CIBC World Markets Inc.

## EBITDA Margin

Magnet had 30% EBITDA margins in 2020, driven by a number of pandemic-related factors, including: 1) wage subsidies in Canada, the U.S. and Singapore; 2) a slower rate of hiring in the early stages of the pandemic; and, 3) operating savings from sales and marketing.

We see margins in the mid- to high teens as more sustainable, with the company continuing to invest in sales and marketing and R&D while still maintaining solid profitability levels.

**Exhibit 20: Magnet Forensics – Expense Profile, 2019 - 2023E**

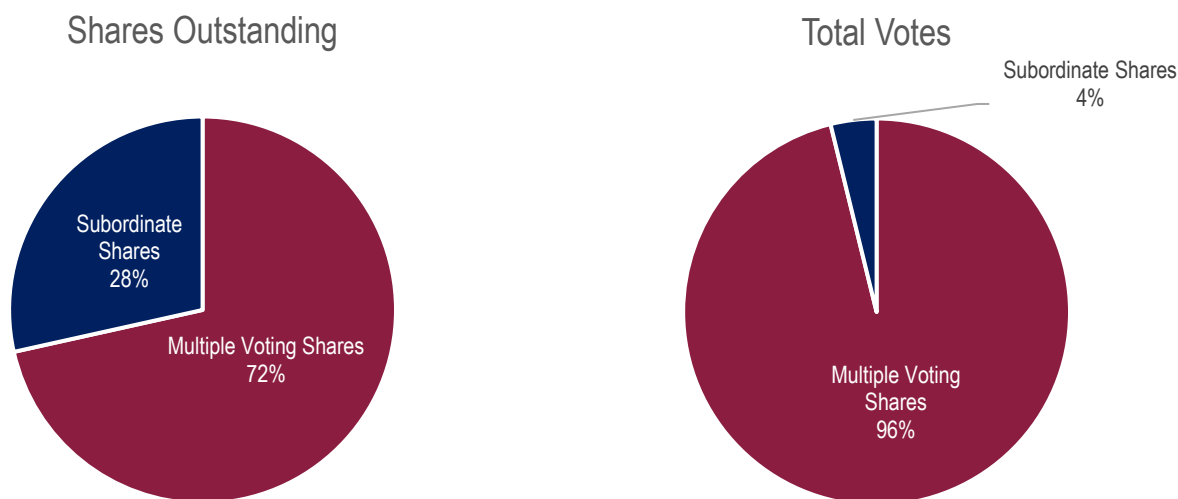


Source: Company reports and CIBC World Markets Inc.

## Management Ownership & Share Structure

Magnet has two share classes: subordinate voting shares and multiple voting shares. Each multiple voting share entitles the holder to 10 votes, while the subordinate shares entitle holders to one vote. Other than the difference in voting rights, the two classes have equal rights in all other respects (dividends, return of capital, distributions on liquidation). Following Magnet's bought deal equity raise in December 2021, 100% of the multiple voting shares in the company are owned by Adam Belsher, Jad Saliba and Jim Balsillie, and those shares represent 96% of total company votes. The voting structure of the shares leads to the three owners of the multiple voting shares retaining full control over company decision-making.

**Exhibit 21: Magnet Forensics – Shares Outstanding & Associated Voting Rights, December 2021**



Source: Company reports and CIBC World Markets Inc.

We expect management will slowly reduce its stake in the company, with insiders executing a \$74.4 million bought deal secondary offering in December 2021. The secondary sellers included Jad Saliba, Adam Belsher and certain other members of management and In-Q-Tel. Through the secondary offering, the selling shareholders sold 2.457 million shares at a price of C\$30.30/share. Post the secondary offering and excluding the impact of the multiple voting shares, our estimate of the current ownership of the company is outlined in the table in Exhibit 22.

**Exhibit 22: Magnet Forensics – Ownership Structure, 2021**

	Ownership (000)	Ownership %
Jad Saliba	11,811	29%
Adam Belsher	11,262	28%
Jim Balsillie	6,199	15%
Angelo Loberto	1,110	3%
IPO & Bought Deal Shareholders	8,347	21%
Other	1,709	4%
<b>Total</b>	<b>40,438</b>	<b>100%</b>

Source: Company reports and CIBC World Markets Inc.

**Exhibit 23: Magnet Forensics – Management Biographies, 2022**

Name	Position	Tenure	Biography
Adam Belsher	Director & Chief Executive Officer	10 years	Mr. Belsher brings more than 15 years of experience as a marketing and sales executive in the technology sector. He previously served as Vice President of the Verizon Business Unit for Research in Motion (RIM). He holds an Honours Bachelor of Commerce degree from Carleton University.
Jad Saliba	Founder & Chief Technology Officer	10 years	Mr. Saliba founded Magnet in 2010 after years of experience serving as a police officer and digital forensics investigator.
Angelo Loberto	Chief Operating Officer	7 years	Mr. Loberto joined Magnet with 16 years of experience in finance and corporate operations in the technology sector. He previously held senior executive roles at BlackBerry and KPMG. Mr. Loberto is a Chartered Accountant and has a Chartered Director designation from the DeGroote School of Business.
Peter Vreeswyk	Chief Financial Officer	3 years	Mr. Vreeswyk was promoted from VP Finance, a role he held for three years while executing the company's financial and operational strategies. He previously worked at KPMG and Coca-Cola Company.
Scott Williams	Chief Strategy Officer	3 years	Mr. Williams is a seasoned executive with experience in leading fast-paced, high-growth businesses. He held a variety of senior-level positions with Research In Motion (BlackBerry), SiriusXM and FreshBooks.
Craig McLennan	Chief Revenue Officer	1 year	Mr. McLennan joined Magnet in April 2021, and is responsible for sales and marketing activities. Prior to joining Magnet, he helped build Microsoft's Customer Success business in Canada. Mr. McLennan previously held leadership roles at Samsung Canada and BlackBerry. He holds a Bachelor of Arts degree from the University of Waterloo and an MBA from the University of Toronto's Rotman School of Management.
Ben Schommer	Chief Information Security Officer	0 year	Mr. Schommer brings more than two decades of international cybersecurity experience. He worked for the United States Marine Corps and SAIC in network engineering and held deputy CISO and CISO positions at Tata Communications, FBR Capital Markets and Proxios.

Source: Company reports.

**Environmental, Social, And Governance**

Magnet does not publish an annual sustainability report, leading to limited disclosure around its ESG metrics.

- Magnet has one female on its board of directors and two on the executive leadership team, representing 20% of its board and 12% of its senior management team, respectively. Two of Magnet's five board members are independent. Board Chair Jim Balsillie is not an independent director.
- The company's insiders have voting control of the company. Please refer to Exhibit 21 for further details.
- Due to the nature of Magnet's business, the handling of data privacy is a key risk factor for the company. On the other hand, the business' primary business model in helping to combat cybersecurity events should be a positive for ESG-focused investors.
- With the company's recent IPO, we expect Magnet will begin to provide additional disclosures on its ESG performance. We view this as an opportunity for Magnet to differentiate itself from smaller-cap peers.

**Price Target Calculation**

We derive our price target of C\$33 by applying an 8x EV/Sales multiple to our 2023 estimate based on the current capital structure. The 8x multiple is in line with Rule-of-40 peers, digital forensics peers, end-point security providers and Canadian SaaS peers.

**Key Risks To Price Target**

The primary risks to our price target include the following: 1) competitive threats erode market share; 2) data/security concerns relating to data breach or privacy violation; 3) potential regulation on use of digital forensics tools; 4) acquisitions lead to margin pressure; and, 5) valuation environment worsens as interest rate outlook changes.

## Important Disclosures

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Stock Ratings	Abbreviation	Description
Outperformer	OP	Stock is expected to outperform similar stocks in the coverage universe during the next 12-18 months.
Neutral	NT	Stock is expected to perform in line with similar stocks in the coverage universe during the next 12-18 months.
Underperformer	UN	Stock is expected to underperform similar stocks in the coverage universe during the next 12-18 months.
Tender	TR	Shareholders are advised to tender shares to a specific offer as we do not believe a superior offer will materialize.
Not Rated	NR	CIBC World Markets does not maintain an investment recommendation on the stock.
Restricted	R	CIBC World Markets is restricted (due to potential conflict of interest) from rating the stock.

Sector Ratings	Abbreviation	Description
Overweight	O	Sector is expected to outperform the broader market averages.
Marketweight	M	Sector is expected to equal the performance of the broader market averages.
Underweight	U	Sector is expected to underperform the broader market averages.
None	NA	Sector rating is not applicable.

Note: Broader market averages refer to S&P 500 in the U.S. and S&P/TSX Composite in Canada.

## CIBC World Markets Inc. Price Chart

For price and performance charts, please visit CIBC on the web at <https://researchcentral.cibccm.com/#/disclaimer-central-new> or write to CIBC World Markets Inc., 161 Bay Street, 4th Floor, Toronto, ON M5H 2S8, Attn: Research Disclosure Chart Request.

## Important Disclosure Footnotes for Magnet Forensics, Inc. (MAGT.TO)

- 2a These companies are clients for which a CIBC World Markets company has performed investment banking services in the past 12 months: Magnet Forensics, Inc.
- 2c CIBC World Markets Inc. has managed or co-managed a public offering of securities for these companies in the past 12 months: Magnet Forensics, Inc.
- 2e CIBC World Markets Inc. has received compensation for investment banking services from these companies in the past 12 months: Magnet Forensics, Inc.
- 2g CIBC World Markets Inc. expects to receive or intends to seek compensation for investment banking services from these companies in the next 3 months: Magnet Forensics, Inc.
- 7 CIBC World Markets Corp., CIBC World Markets Inc., and their affiliates, in the aggregate, beneficially own 1% or more of a class of equity securities issued by these companies: Magnet Forensics, Inc.
- 12 The equity securities of these companies are subordinate voting shares: Magnet Forensics, Inc.

For important disclosure footnotes for companies mentioned in this report that are covered by CIBC World Markets Inc., click here: [CIBC Disclaimers & Disclosures](#)

Companies mentioned in the report but not listed are not covered by fundamental research at CIBC.

### Ratings Distribution\*: CIBC World Markets Inc. Coverage Universe

(as of 02 Feb 2022)	Count	Percent	Inv. Banking Relationships	Count	Percent
Outperformer	176	58.5%	Outperformer	176	100.0%
Neutral	116	38.5%	Neutral	115	99.1%
Underperformer	9	3.0%	Underperformer	9	100.0%
Tender	0	0.0%	Tender	0	0.0%
Restricted	7	2.3%	Restricted	7	100.0%

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