

# Cloudflare

## What it does

Cloudflare's mission is to help build a better Internet. The company operates a global network which provides faster, more secure, websites and apps. Cloudflare is the foundation for anything connected to the internet.

## Why we own it

- The move from on-premise IT to the Cloud continues at pace. Cloudflare helps when enterprises replace their network appliances with cloud-based services.
- Market leadership in reverse proxy services such as content delivery networks (CDN's) and distributed denial of service (DDoS) protection. Currently protecting 26 million websites, however the market is vast.
- Three additional opportunities in virtual private networks (VPN), multiprotocol label switching (MPLS) and other enterprise networking solutions.
- Beyond the above, there is also an expansion in their Workers product into 'edge compute' or so-called distributed datacentre. This new business largely leverages the infrastructure that supports the enterprise networking business.

## How it could be worth many times more

- One pillar of the upside case lies in Cloudflare's networking and Software-as-a-Service (SaaS) core business. It doesn't feel unreasonable to think that within the next decade it could capture around 20% of a \$60bn market, with 30% net margins.
- A second pillar of the investment thesis is Cloudflare's 'Workers' product, which makes it possible to run applications at the 'edge' for less latency, lower cost and greater control. This could be a potentially massive market, eating into what would otherwise be done in the cloud. Exceptional reputation as best-of-breed in this space could be conducive to outlier returns.

## Where we might be wrong

- The shift from legacy enterprise solutions proves difficult and not as rapid as we might hope.
- Opportunities in serverless computing becomes dominated by Amazon and Microsoft.

## Short 10 questions

### Can sales double in the next five years?

1

Comfortably, based on additional market penetration into existing products and the move into enterprise and notably cross-selling.

### Ten years and beyond?

2

The edge computing segment (its Workers product) is what potentially takes Cloudflare's business into the next phase of its growth.

### Competitive advantage?

3

Fundamentally better product as a function of better design and an innovative and unencumbered culture.

### Is the business culture different?

4

Mission driven to build a better internet. Innovation outsourced to decentralised hubs to foster experimentation.

### Customers like you? Contribute to society?

5

Security more important as the online transition continues. Democratisation of technical resources that were only available to platform giants.

### Are returns worthwhile?

6

A software business with 60+% incremental contribution margins.

### Will they rise or fall?

7

Will rise meaningfully over time. 20% operating margin seems unduly conservative. 50% or more in the core business seems plausible.

### How is capital allocated?

8

Growing server network and R&D.

### Could it be worth 5x as much?

9

Addressable markets are massive and opportunities are widening.

### What doesn't the market understand?

10

Breadth of capability makes it hard to analyse.

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**Registered Office:**  
**Calton Square, 1 Greenside Row, Edinburgh EH1 3AN, Scotland**  
**Telephone +44 (0)131 275 2000 [bailliegifford.com](http://bailliegifford.com)**

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**BGI Principal Office: Calton Square, 1 Greenside Row, Edinburgh EH1 3AN, Scotland.**

**Telephone: +44 (0)131 275 2000**

**780 Third Avenue, 43rd Floor, New York, NY 10017.**

**Telephone: (212) 319 4633**

**BGE Head Office: 4/5 School House Lane East, Dublin 2 D02 N279, Ireland.**

**Telephone: +35 315 294 150**

**BGE Frankfurt Branch: WINX Tower, Neue Mainzer Str. 6-10, 60311 Frankfurt, Germany**

**BGE Amsterdam Branch: Atrium Building, Strawinskylaan 3051, 4th Floor,  
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