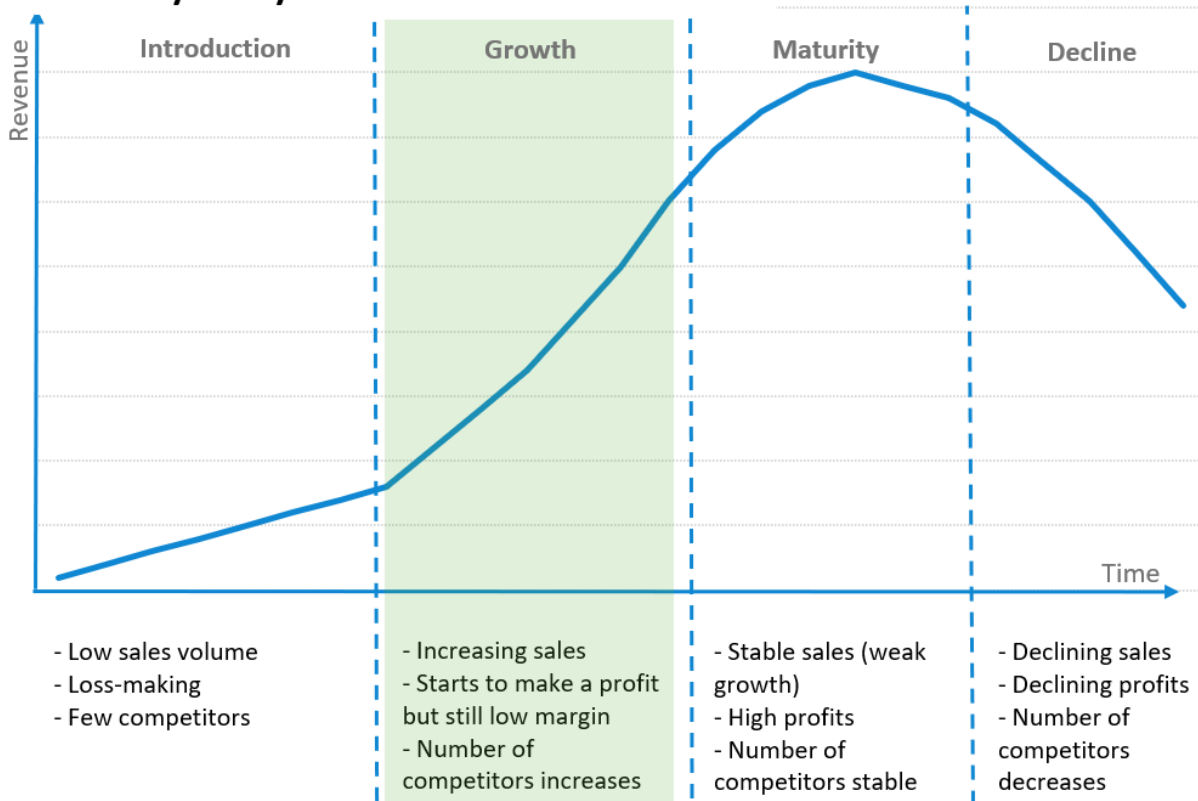


Market Snapshot

The cybersecurity industry is an attractive investment target, offering the potential for profit from the technological transformation processes surrounding us and the consequences of growing geopolitical tensions ([increased NATO defence budgets](#)). However, in order to make informed investment decisions, it is advisable to familiarise yourself with the characteristics of the industry that may affect companies' pricing power, profitability, valuation, and long-term strategy.

In terms of industry life cycle, cybersecurity is in its early growth stage. It is an emerging field: the total age of publicly traded cybersecurity companies with revenues exceeding \$1 billion (Palo Alto Networks, Fortinet, Gen Digital, CrowdStrike, Check Point, Okta, Zscaler, and Trend Micro) was only 197 years at the end of last year. In summary, the average age of the largest companies in the sector is approximately 25 years. Consequently, companies reinvest a substantial portion of their profits and cash flow back into operations to achieve rapid growth, and dividend payments are not common in the industry.

Industry life cycles and their characteristics



Source: OTP Multi-Asset Research

Due to the low profitability typical of this phase, P/E-based valuations are very high in the industry, with multiples of around 40-50 being common. However, low and volatile EPS figures render these valuations inconsistent. It is therefore more appropriate to use EV/S-based valuations for companies in this industry.

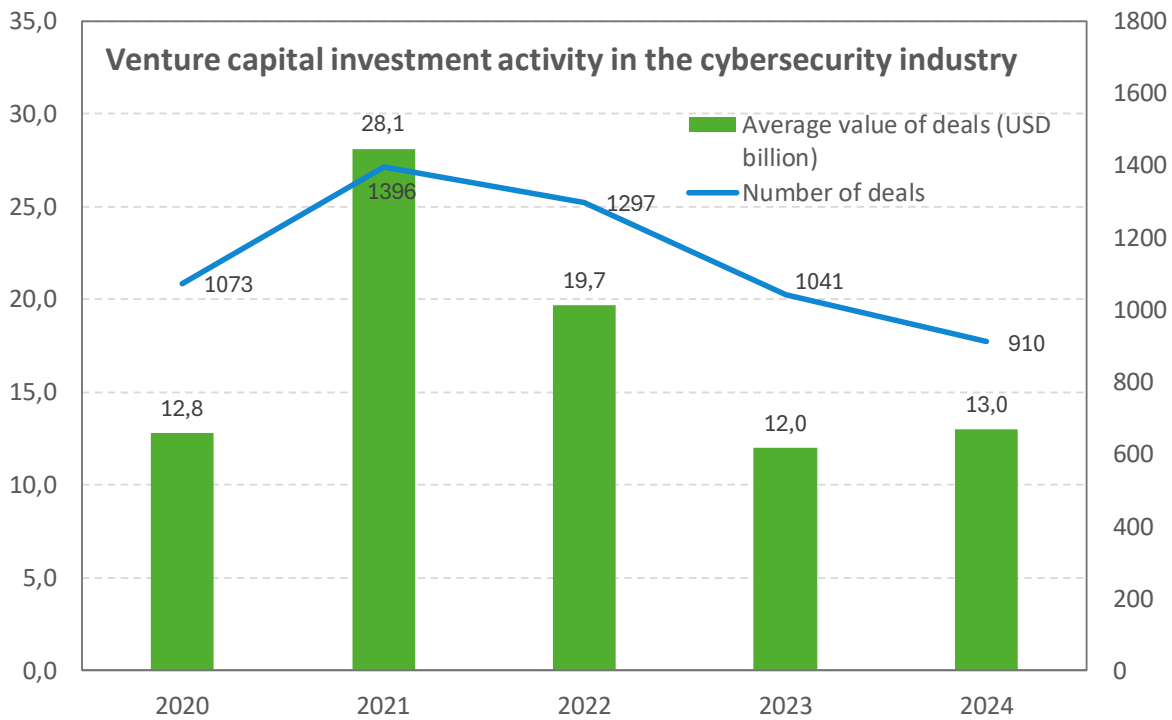
Market Snapshot

With regard to its sensitivity to economic cycles, the technology sector is becoming increasingly cyclical. However, within this sector, cybersecurity is one of the more defensive areas, with companies characterised by lower betas (systematic risk of shares). Furthermore, it is one of the most fragmented segments within the technology sector. Consequently, there is intense price competition among the many smaller players in the industry, which encourages companies to innovate continuously.

Furthermore, the rapid development of AI technology is compelling cybersecurity companies to adapt by expanding and updating their product and service portfolios at an accelerated pace in order to gain a competitive advantage and increase their market share. While the solutions created through innovation can be differentiated to a certain extent, competitive dynamics are constantly changing as a result of rapid development. Consequently, no player has yet succeeded in establishing a lasting dominant position, thereby limiting their pricing power.

Cybersecurity is a popular industry among venture capitalists due to its growth potential. This facilitates early-stage financing for start-ups, thereby enabling easier market entry and ultimately reducing barriers to entry for the industry as a whole. Furthermore, in recent years, they have required an average of 10-15% less financing to enter the market than other venture capital investments. The only barrier to entry is the lack of skilled professionals, which is a serious problem: there is a global shortage of nearly 3.5 million skilled workers in this field (~39% of positions are unfilled). The low capital requirements and attractive growth prospects are appealing to new entrants, but this puts pressure on the margins of existing players.

Market Snapshot



Source: PitchBook Data, OTP Multi-Asset Research

In this sector, suppliers' bargaining power is relatively limited due to the availability of alternative suppliers and the tendency to establish diversified supplier networks. This is of particular relevance to on-premise network and firewall service providers that also sell products. In contrast, buyers enjoy a strong bargaining position, given the presence of numerous companies offering substitute products or services in this multi-player market.

Switching costs are higher in the corporate segment due to the costs of integrating new systems and training employees, although these are not insurmountable for companies. However, in the consumer segment, switching between cyber security companies' services is possible at virtually no cost, which gives them weaker pricing power compared to their corporate counterparts.

Recent changes in the regulatory environment are supportive for the industry. Violations of the stricter data protection guidelines may result in penalties of up to 7% of sales in the EU. Furthermore, regulations require greater transparency from companies regarding data protection incidents, exposing market players to increased reputational risk if they are unable to prevent cyber-attacks. This could ultimately prove to be more damaging than the fines for most companies, as it threatens to undermine consumer confidence. This will encourage companies to invest more resources in prevention, which will help increase orders for cyber security companies. In addition, based on the actions of the first Trump

Market Snapshot










administration, a looser regulatory environment is likely to emerge in the US in the coming years in terms of industry acquisitions, which could help consolidate the industry.




Overall, the cybersecurity industry is known for its intense competition and high level of innovation, which are typical of industries in a growth phase. At present, the primary objective of most companies is to increase their market share, and they are offering lower prices, which results in lower operating margins. Furthermore, the ease with which new companies can enter the market, coupled with the stronger bargaining position of buyers, does not increase the pricing power of cybersecurity companies.

The regulatory environment is conducive to dynamic revenue growth, which is also supported by reinvestment in operations. Consequently, shareholder payouts, in the form of dividends or share buybacks, are not a frequent occurrence. Consolidation processes are expected to take place in the cybersecurity segment in the coming period, with a high number of M&A transactions, profit margins likely to improve and cash flow generation also likely to pick up.

As an investor, you may be concerned by the high valuation levels seen in the industry, but these are common in the growth cycle. The technology sector has followed a similar development path in the past. When making investment decisions, it may be advisable to focus on growth indicators, particularly revenue growth, given that increasing market share is currently the most significant factor for companies in the industry. If an investor also wishes to take valuation considerations into account, it is recommended to use EV/S instead of P/E multiples, as this leads to more consistent results.

Market Snapshot

Cybersecurity industry characteristics		
Industry life cycle	Growth phase	
Cyclicalit	Technology is cyclical but cybersecurity is more defensible	
Entry and exit barriers	Rather low	
Suppliers' bargaining position	Weak (a large number of available alternatives)	
Industry concentration	One of the most fragmented segments within technology	
Differentiation opportunity - pricing power - industry competition	Innovation is important -> differentiated products, intense pricing competition	
Switching cost for consumers	Higher but not insurmountable in the corporate segment, low in the retail segment	
Consumers' bargaining position	Rather strong (high number of available substitutes)	
Regulation	Stricter data protection regulations, greater transparency required (reputational risk for companies) -> supportive environment, more orders for cybersecurity companies	

 : Positive
  : Neutral
  : Negative

Source: OTP Multi-Asset Research

In a subsequent analysis, we will examine the supply and demand dynamics and other characteristics driving growth in the cybersecurity industry.

Market Snapshot

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2025.07.23.