

IAR SYSTEMS

Dent in turnaround trajectory

IAR Systems' Q4 report was a slight hiccup in its accelerated profitable growth turnaround, but we still expect it to see 45%+ EBIT growth YOY in 2023e with relative insulation from support and updates at ~40% of net sales, and durable design activity as developers choose IAR's tools to boost productivity and the cost of ownership. We reiterate our SEK140–250 fair value.

Q4 sales in line with our forecast but operating leverage declined to 7%. IAR reported Q4 organic sales growth of 7% YOY (from 11% YOY in Q3 and 14% in Q2), which led to net sales 1% above our forecasts. We expected SEK2.1m of security sales, which were SEK0.2m, while IAR had also categorised ~SEK2.3m of security sales incorrectly in Q3, denting our short-term expectations. Adj. EBIT was 28% below our forecast (15.2% margin, down 1.4%-points YOY), resulting in a poor 7% incremental margin from ~25–50% seen in recent quarters. Adjusting for higher depreciation related to new office leases (~SEK3m) and an incentive programme (~SEK1m), we believe the underlying EBIT margin would have been 19.2% (up 2.6%-points YOY). Cash flows were soft in Q4 (cash flow from operations declined 36% YOY) to set up an LTM cash conversion of 90%. IAR proposed a 2022 SEK1.5 DPS (our estimate: SEK1.64) after two years of no dividends, which should take its net cash to SEK143m by end-2023e.

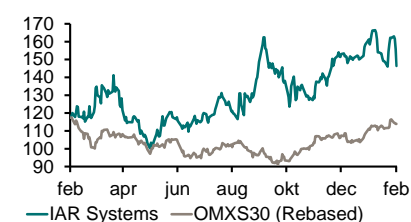
We have cut 2023e EBITDA by 2%, EBIT by 8%, and EPS by 10%, to factor in: 1) softer ramp-up assumptions for security sales; 2) higher investment in modernising internal processes, systems, and the UX/UI of the Embedded Workbench; 3) higher D&A from new office leases; and 4) higher interest costs. For 2023, we forecast 8% organic net sales growth YOY (split 5% YOY development tools and SEK15m in security solutions (3% of group net sale).

Fair value of SEK140–250 reiterated, corresponding to a 2023e EV/EBIT of 15–28x. IAR Systems is trading at 16x 2023e EV/EBIT (or 14x EV/EBIT and 6.5% FCF yield excluding Secure Thingz). We believe management's ambitious ramp-up of security sales for 2023e could be twice as high as our forecasts, but should it not materialise, we believe there is industrial interest in Secure Thingz's IoT security technology, with either outcome potentially acting as a catalyst for the business over the coming years.

Year-end Dec	2019	2020	2021	2022	2023e	2024e	2025e
Revenue (SEKm)	406	372	358	423	476	527	572
EBITDA adj (SEKm)	146	133	238	132	180	213	246
EBIT adj (SEKm)	108	84	66	79	116	146	174
PTP (SEKm)	107	77	-69	73	110	141	170
EPS rep (SEK)	5.96	4.36	-4.94	4.04	6.22	7.99	9.64
EPS adj (SEK)	5.96	4.36	4.90	4.48	6.22	7.99	9.64
DPS (SEK)	3.00	0.00	0.00	1.50	2.18	2.80	3.37
Revenue growth (%)	5.3	-8.3	-3.8	18.1	12.6	10.7	8.5
EBITDA growth adj (%)	1.7	-9.0	79.4	-44.4	36.2	18.2	15.6
EPS growth adj (%)	-10.6	-26.8	12.5	-8.6	38.9	28.3	20.7
EBITDA margin adj (%)	35.9	35.7	66.5	31.3	37.9	40.4	43.1
EV/Sales adj (x)	6.30	5.12	4.32	4.67	3.90	3.36	2.98
EV/EBITDA adj (x)	17.5	14.3	6.5	14.9	10.3	8.3	6.9
EV/EBIT adj (x)	23.6	22.7	23.6	25.0	16.1	12.2	9.8
P/E adj (x)	31.2	32.1	24.0	33.6	23.5	18.3	15.2
P/Book (x)	4.28	3.11	2.74	3.08	2.73	2.47	2.21
ROE (%)	14.2	9.9	nm	9.2	12.2	14.1	15.3
ROCE (%)	17.7	12.4	9.9	11.5	15.1	17.6	19.2
Dividend yield (%)	1.6	0.0	0.0	1.0	1.5	1.9	2.3
FCF yield (%)	0.9	1.9	3.6	3.3	4.2	5.6	5.5

Source: Company (historical figures), DNB Markets (estimates)

IARB versus OMXS30 (12m)



Source: Factset

SUMMARY

Share price (SEK)	146
Tickers	IARB SS

CAPITAL STRUCTURE

No. of shares (m)	13.7
No. of shares fully dil. (m)	13.7
Market cap. (SEKm)	1,998
NIBD adj end-2023e (SEKm)	-143
Enterprise value adj (SEKm)	1,855
Net debt/EBITDA adj (x)	-0.79
Free float (%)	100

Source: Company, DNB Markets (estimates)

NEXT EVENT

Q1 2023	26/04/2023
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ESTIMATE CHANGES (SEK)

Year-end Dec	2023e	2024e	2025e
Sales (old)	481.0	525.9	
Sales (new)	476.1	527.0	571.9
Change (%)	-1.0	0.2	nm
EPS adj (old)	6.91	8.60	
EPS adj (new)	6.22	7.99	9.64
Change (%)	-9.9	-7.1	nm

Source: DNB Markets,

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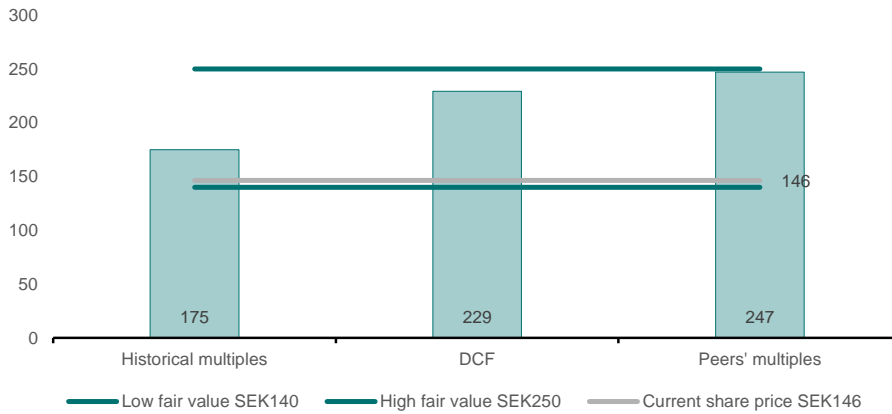
ANALYSTS

Joachim Gunell

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Overview

Valuation (SEK)



Source: DNB Markets

Valuation methodology

- We continue to base our fair value on a DCF, IAR Systems' historical valuation multiples, and a peers' multiple regression analysis (methodology unchanged).
- On our estimates, IAR Systems is trading at a 2024e P/E of 18x, EV/EBIT of 12x, and EV/sales of 3x.

Source: DNB Markets

Downside risks to our fair value

- Weakening of the embedded systems developer community (C/C++ language difficulty, cultural shifts in the workforce, low-level code abstraction, etc.).
- Competitive advantages disrupted by open-source alternatives or stronger commercial technologies.
- New product developments are too costly and might not translate into sales, which could make investors lose trust in the company's ability to resurrect its organic growth profile.
- IAR Systems is highly sensitive to a strengthening of the SEK (particularly against the USD, EUR, and JPY).

Source: DNB Markets

DNB Markets estimates

- We view IAR Systems as a market leader in a niche industry (ensuring high code quality in embedded software and programming secure devices for the Internet of tomorrow) with the potential to accelerate organic growth to above its targeted 10–15% from new product launches (for which SEK500m+ of R&D investment has already been taken).
- Our assessed medium-term value-creation potential remains high, but so is the burden of execution at this stage after the negative EPS revision trend since 2019, where we believe IAR is one year into its turnaround.

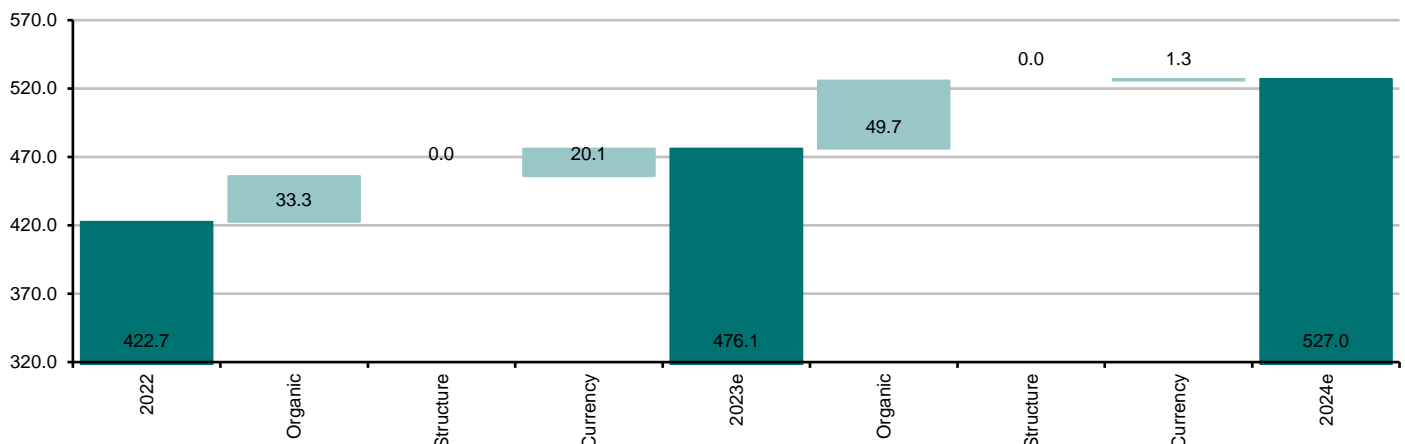
Source: DNB Markets

Upside risks to our fair value

- The company over-achieving on its financial targets (particularly 10–15% organic growth).
- Successful traction of its new offerings (IoT security, RISC-V, 64-bit, etc.) could offer potential shareholder value creation beyond our fair value.
- IoT security legislation that requires identity to be built into microcontrollers.
- SaaS transition would support the revenue mix, lessen the cyclicality, and enhance the investment profile.
- Participation in industry consolidation owing to the strategic importance of development tools.

Source: DNB Markets

Sales bridge 2022–2024e (SEKm)



Source: DNB Markets (forecasts), company (historical data)

ESG overview

Sustainability assessment

	Positive	Negative
Conclusions	<ul style="list-style-type: none"> ■ IAR Systems’ software-development tools are market-leading in terms of code quality, analysis, functional safety, and security. Its software ensures that the code is in line with industry standards, thereby guaranteeing its reliability when applied. ■ Increased IoT security legislation drives demand for its products, as its OEM customers must comply with new security design requirements. 	<ul style="list-style-type: none"> ■ Data loss or security bugs in the software code could trigger regulatory scrutiny as well as legal costs and reputational damage, hampering its growth prospects. ■ IAR Systems’ competitiveness relies greatly on its ability to continuously innovate. For this, its highly skilled workforce is a key resource. Failure to attract and retain such professionals could lead to delays in innovation and a loss of market share.
Actions being taken by company	<ul style="list-style-type: none"> ■ Embedded programmers need to protect their code from IP theft and illegal copying, as IoT security issues are becoming increasingly prevalent. Following the acquisition of Secure Thingz, IAR Systems’ tools are increasingly linked to sustainability, as they help developers take control of security from inception in the IP throughout the lifecycle of a digital product. 	<ul style="list-style-type: none"> ■ IAR Systems’ development tools are the most used in the embedded industry, owing to its leading optimisation technology, comprehensive debugger quality, and renowned technical support. This is confirmed by its loyal customer base (~5% annual customer churn). It has 46,000+ OEM customers and 150,000+ technology users, 95% of which are recurring customers, we believe.

Key ESG drivers

Short-term

- IAR Systems’ security offering (Secure Desktop Provisioner, Embedded Trust, and C-Trust) ensures that its customers’ intellectual property is protected against IP theft, overproduction, and piracy, and that software updates can be managed in a secure fashion. In other words, it creates a secure infrastructure and protects its customers’ digital products from sabotage programmes and data intrusion.
- Examples of customer use cases have included: a leading vending-machine provider, whose IP was stolen (stolen credit card and transaction details); a global white-goods company, whose stolen IP led to twice as many products being manufactured; and a leading door-sensor provider, whose IP was stolen internally, which led to direct revenue loss.
- To stay ahead of the competition, IAR Systems relies heavily on its employees in the development and innovation of new technologies.
- Following the integration of Secure Thingz, IAR Systems’ addressable market has expanded from application development into manufacturing and update management (the entire lifecycle of embedded systems). To keep pace with competition in a larger market, it needs to retain highly skilled software engineers, which could come at a higher cost than its traditional business.
- An increasingly larger part of IAR Systems could revolve around Cambridge-based Secure Thingz. This could create some corporate cultural challenges versus the Uppsala-based legacy business.

Long-term

- Regulators are likely to play an active role in the long-term uptake of secure development tools. This should have an impact on programmers’ designs, as applications need to remain secure across the entire lifecycle to comply with new legislation. We note legislative initiatives in Europe (UK government, ETSI, ENISA) and the US (California and Oregon IoT Security law, IoT Cybersecurity Improvement Act), and government initiatives across Singapore, Japan, South Korea, China, etc.
- Considering its offering of software development tools to over 150,000+ technology users as well as the sensitive nature of the data it handles, IAR Systems is exposed to possible hacking attempts and misappropriation of technological data.

10 February 2023

Q4 results

Figure 1: Q4 results versus expectations

Key highlights (SEKm, except per share data)	Q4 2022		Deviation	Deviation	Q4 2021	DNBe
	Actual	DNB	(%)	Absolute	Actual	2023e
Net sales	108.8	107.8	1%	1	91.6	476.1
Gross profit	105.0	104.3	1%	1	88.6	461.9
Gross margin	96.5%	96.8%	-0.2pp		96.7%	97.0%
One-offs	0.0	0		0	-134	0
EBITDA adj.	32.4	35.1	-8%	-3	13.2	180.3
EBITDA adj. margin	29.8%	32.5%	-2.8pp		14.4%	37.9%
EBIT	16.5	23.0	-28%	-6	15.2	115.5
EBIT margin	15.2%	21.3%	-6.1pp		16.6%	24.3%
EBIT adj.	16.5	23.0	-28%	-6	15.2	115.5
EBIT adj. margin	15.2%	21.3%	-6.1pp		16.6%	24.3%
EPS adj.	1.07	1.26	-15%	-0.19	2.11	6.22
Adj. FCF (CFO - capex)	3.3	14.5	-77%	-11	23.4	84.6
Cash conversion	20%	63%	-43.2pp		154%	73%
Rule of 40 (EBIT)	33.9%	39.1%	-5.1pp		17.6%	36.9%
Revenue growth YOY	18.8%	17.7%	1pp		1.0%	12.6%
Organic	6.9%	6.2%	0.7pp		2.0%	7.9%
Structural	0.0%	0.0%	0pp		0.0%	0.0%
FX	11.9%	11.5%	0.4pp		-1.0%	4.7%
Segment	Q4 2022		Deviation	Deviation	Q4 2021	DNBe
(SEKm)	Actual	DNB	(%)	Absolute	Actual	2023e
Net sales						
Development tools	108.6	105.7	3%	3	91.5	461.3
Security solutions	0.2	2.1	-91%	-2	0.1	14.8
Other	0.0	0.0	n.a.	0	0.0	0.0
Total	108.8	107.8	1%	1	91.6	476.1
Net sales growth						
Development tools	18.7%	15.6%	3.1pp		2.2%	10.2%
Security solutions	100.0%	2011.5%	-1911.5pp		-91.7%	885.1%
Other						
Total	18.8%	17.7%	1pp		1.0%	12.6%
Net sales						
License-based	57.0	62.1	-8%	-5	49.4	275.3
Support and softw are updates	45.4	41.3	10%	4	36.1	180.7
Other	6.4	4.5	42%	2	6.1	20.0
Total	108.8	107.8	1%	1	91.6	476.1

Source: Company (historical figures), DNB Markets (estimates)

Estimate revisions

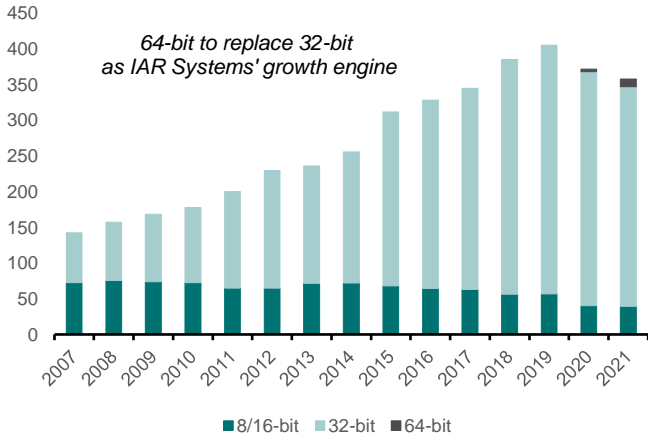
Figure 2: Estimate changes

(SEKm, except per share data)	Old			New			Change		
	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
Net sales	481	526		476	527	572	-1%	0%	
Growth YOY, of which	14.6%	9.3%		12.6%	10.7%	8.5%	-194bp	137bp	
Organic	11.6%	9.3%		7.9%	10.4%	8.5%	-372bp	111bp	
Structural	0.0%	0.0%		0.0%	0.0%	0.0%	0bp	0bp	
FX	3.0%	0.0%		4.7%	0.3%	0.0%	178bp	27bp	
Gross profit	469	514		462	513	558	-1%	0%	
<i>Gross margin</i>	97.5%	97.7%		97.0%	97.3%	97.5%	-46bp	-39bp	
EBITDA	183	217		180	213	246	-1%	-2%	
IAC	0	0		0	0	0			
Adj. EBITDA	183	217		180	213	246	-1%	-2%	
Depreciation and amortisation	-58	-63		-65	-67	-72	12%	7%	
EBIT	125	154		116	146	174	-8%	-6%	
Adj. EBIT	125	154		116	146	174	-8%	-6%	
<i>Adj. EBIT margin</i>	26.0%	29.4%		24.3%	27.6%	30.4%	-170bp	-173bp	
Capitalised development costs (CDC)	51	55		56	56	59	9%	1%	
EBIT excl. CDC	15.3%	18.9%		12.5%	17.1%	20.1%	-280bp	-185bp	
Adj. Net profit	94	117		85	109	132	-10%	-7%	
Adj. EPS (diluted)	6.91	8.60		6.22	7.99	9.64	-10%	-7%	
DPS	2.42	3.01		2.18	2.80	3.37	-10%	-7%	
Net sales by segment									
Development tools	462	486		461	492	517	0%	1%	
Security solutions	19	40		15	35	55	-23%	-13%	
Other	0	0		0	0	0			
Total	481	526		476	527	572	-1%	0%	
Net sales by product type									
License-based	286	322		275	321	357	-4%	0%	
Support and software updates	177	185		181	185	193	2%	0%	
Other	18	19		20	21	22	10%	9%	
Total	481	526		476	527	572	-1%	0%	
Balance sheet and cash flow									
Adj. FCF	85	113		85	112	109	-1%	-1%	
Cash	228	308		204	279	342	-10%	-10%	
Net cash (-) / net debt (+)	-208	-289		-143	-225	-297	-31%	-22%	

Source: DNB Markets

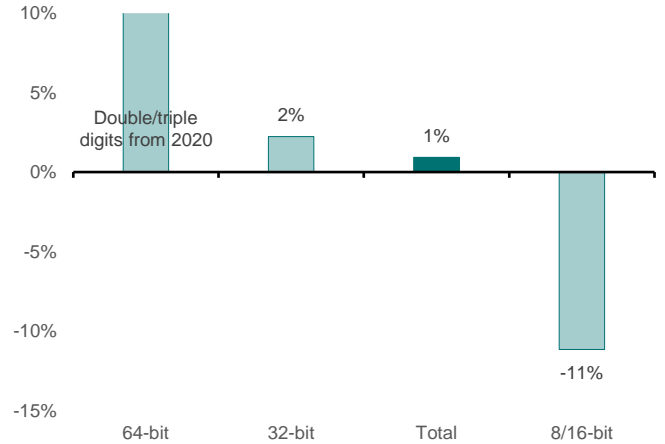
Key charts

Figure 3: Net sales mix by processor type (2007–2021)



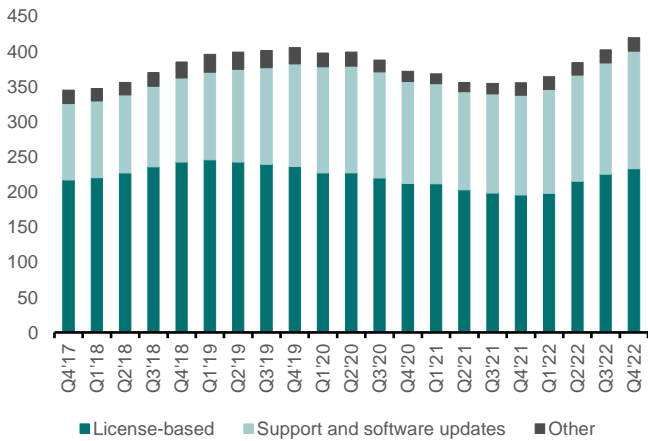
Source: Company (historical data), DNB Markets (further calculations)

Figure 4: Net sales CAGR by processor type (2017–2021)



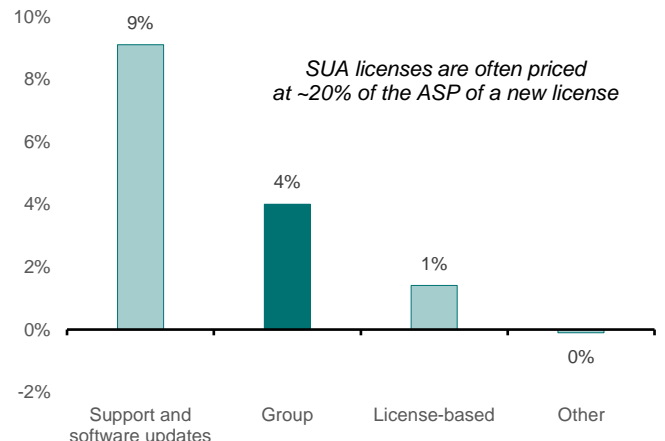
Source: Company (historical data), DNB Markets (further calculations)

Figure 5: Net sales mix by product type (LTM, 2017–2022)



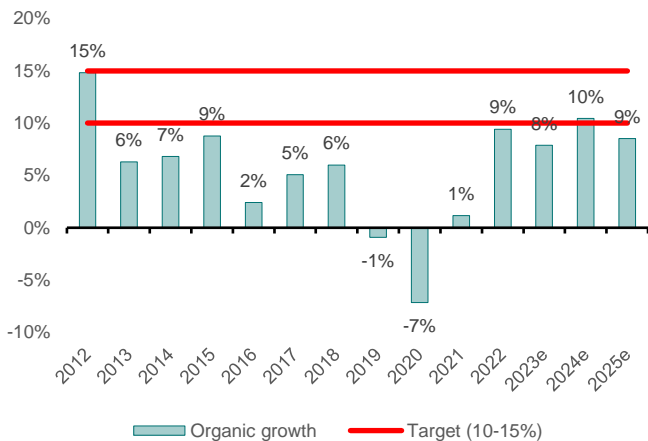
Source: Company (historical data), DNB Markets (further calculations)

Figure 6: Net sales CAGR by processor type (2016–2022)



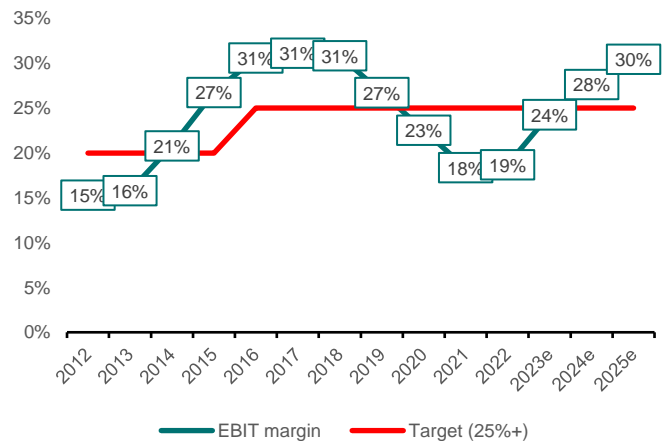
Source: Company (historical data), DNB Markets (further calculations)

Figure 7: Financial goal 1 – organic sales growth of 10–15%



Source: DNB Markets (forecasts), company (historical data)

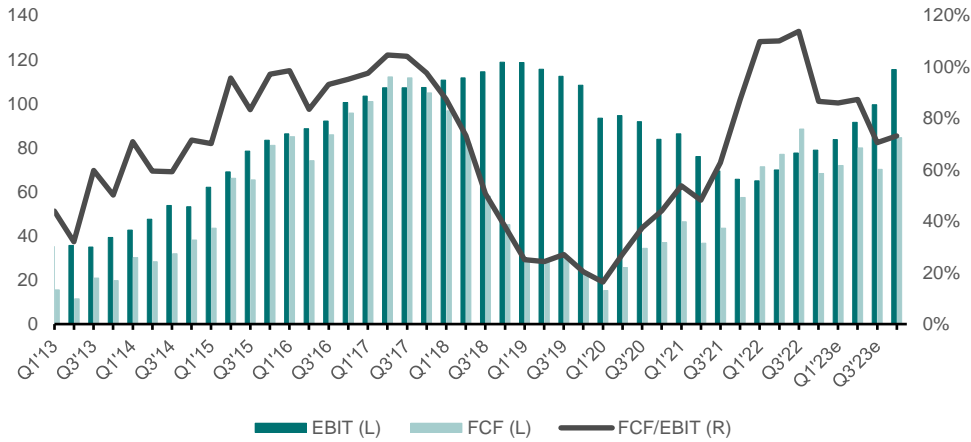
Figure 8: Financial goal 2 – EBIT margin >25%



Source: DNB Markets (forecasts), company (historical data)

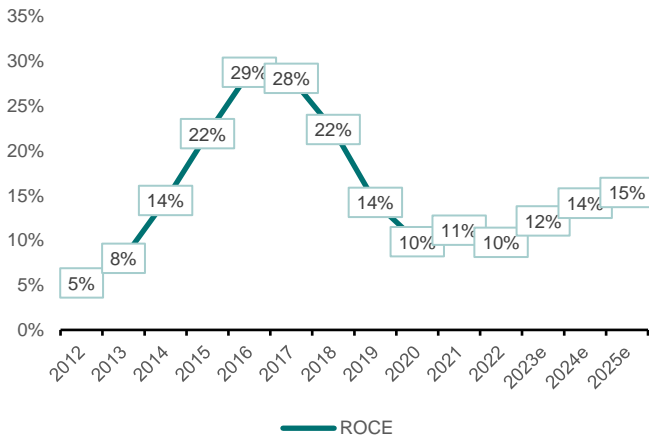
10 February 2023

Figure 9: LTM FCF versus LTM EBIT (2012–2023e) – coming out of an intense investment period to accelerate organic growth since 2018



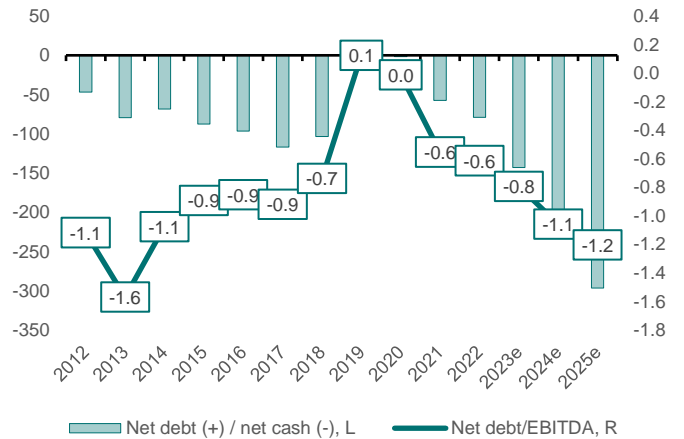
Source: DNB Markets (forecasts), company (historical data)

Figure 10: Return on capital employed (2012–2025e)



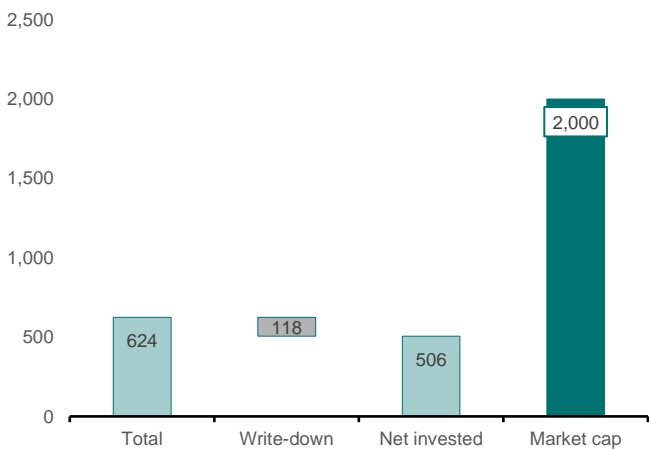
Source: DNB Markets (forecasts), company (historical data)

Figure 11: Net debt to EBITDA (x, SEKm)



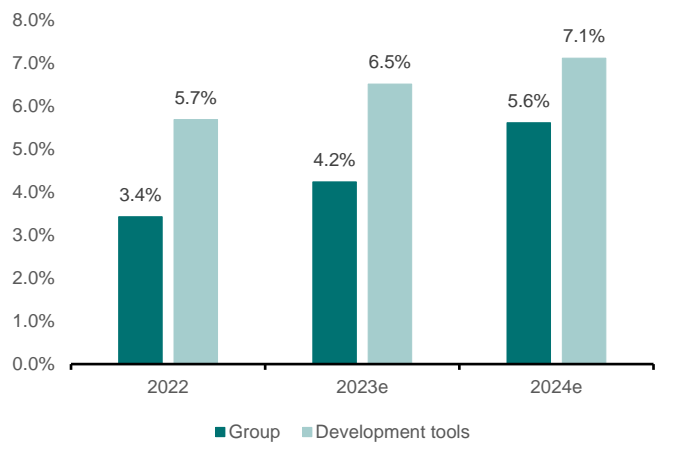
Source: DNB Markets (forecasts), company (historical data)

Figure 12: Investments (SEKm, 2016–2023e)



Source: Company (historical data), DNB Markets (forecasts and further calculations)

Figure 13: FCF yield (2022–2024e)



Source: Company (historical data), DNB Markets (forecasts and further calculations)

Forecasts

Figure 14: Annual income statement and key items (SEKm, 2017–2025e)

(SEKm)	2018	2019	2020	2021	2022	2023e	2024e	2025e	22-25e CAGR
Net sales	385.2	405.6	372.0	355.8	419.9	476.1	527.0	571.9	11%
Growth YOY, of which	10%	5%	-8%	-4%	19%	13%	11%	9%	
Organic	6%	-1%	-7%	1%	9%	8%	10%	9%	
Structural	0%	0%	0%	0%	0%	0%	0%	0%	
FX	4%	6%	-1%	-6%	9%	5%	0%	0%	
COGS	-9.0	-10.8	-14.1	-12.0	-12.8	-14.2	-14.2	-14.2	
Gross profit	376.2	394.8	357.9	346.0	409.9	461.9	512.8	557.7	
Capitalised work	0.0	0.0	0.0	0.0	50.2	56.1	55.6	59.3	
Other external expenses	-68.2	-63.7	-37.7	-38.3	-58.3	-61.7	-67.0	-71.3	
Personnel costs	-167.9	-185.3	-187.5	-203.8	-273.1	-276.0	-288.4	-299.4	
EBITDA	140.1	145.8	132.7	103.9	128.7	180.3	213.0	246.3	
IAC	-3.2	0.0	0.0	-134.2	-3.6	0.0	0.0	0.0	
Adj. EBITDA	143.3	145.8	132.7	238.1	132.3	180.3	213.0	246.3	
Depreciation and amortisation	-24.5	-37.4	-48.9	-172.4	-53.3	-64.7	-67.3	-72.1	
EBIT	115.6	108.4	83.8	-68.5	75.4	115.5	145.7	174.1	
Adj. EBIT	118.8	108.4	83.8	65.7	79.0	115.5	145.7	174.1	30%
Financial items	-1.8	-1.4	-7.0	-0.1	-2.2	-5.9	-5.0	-4.4	
Profit before tax	117.0	107.0	76.8	-68.6	73.2	109.6	140.7	169.7	
Taxes paid	-26.2	-25.8	-17.4	1.2	-15.6	-24.7	-31.7	-38.2	
Adj. Net profit	94.0	81.2	59.4	66.8	61.2	85.0	109.0	131.5	29%
EPS	6.67	5.96	4.36	-4.94	4.04	6.22	7.99	9.64	
Adj. EPS (diluted)	6.67	5.96	4.36	4.90	4.48	6.22	7.99	9.64	
DPS	5.00	3.00	0.00	0.00	1.50	2.18	2.80	3.37	
Margins									
Gross	97.7%	97.3%	96.2%	96.6%	97.0%	97.0%	97.3%	97.5%	
EBITDA	36.4%	35.9%	35.7%	29.0%	30.4%	37.9%	40.4%	43.1%	
Adj. EBITDA	37.2%	35.9%	35.7%	66.5%	31.3%	37.9%	40.4%	43.1%	
EBIT	30.0%	26.7%	22.5%	-19.1%	17.8%	24.3%	27.6%	30.4%	
Adj. EBIT	30.8%	26.7%	22.5%	18.4%	18.7%	24.3%	27.6%	30.4%	
FCF margin	11.9%	5.4%	9.9%	16.1%	16.2%	17.8%	21.3%	19.1%	
Rule of 40 (EBIT)	42.5%	32.0%	14.2%	14.6%	36.8%	36.9%	38.3%	39.0%	
ROCE	28.1%	17.7%	12.4%	9.9%	11.5%	15.1%	17.6%	19.2%	
Cash flow									
Cash flow from operating activities	92.6	105.7	118.4	131.6	128.0	157.9	189.8	192.8	
Capex	-46.8	-83.6	-81.4	-74.1	-59.6	-73.3	-77.8	-83.3	
Adj. FCF	45.8	22.1	37.0	57.5	68.4	84.6	112.1	109.4	17%
Cash conversion (FCF/EBIT)	39%	20%	44%	88%	87%	73%	77%	63%	
Balance sheet									
Cash	106.1	60.7	67.8	113.4	148.2	204.3	278.6	341.9	
Net cash (-) / net debt (+)	-103.3	18.4	-1.5	-57.4	-78.9	-143.0	-225.3	-296.6	
Net debt/EBITDA	-0.7x	0.1x	0.0x	-0.6x	-0.6x	-0.8x	-1.1x	-1.2x	

Source: Company (historical data), DNB Markets (estimates)

Figure 15: Annual segment overview (SEKm, 2017–2025e)

(SEKm)	2018	2019	2020	2021	2022	2023e	2024e	2025e	22-25e CAGR
Net sales by segment									
Development tools	380.2	403.9	367.0	355.1	418.4	461.3	492.2	516.6	7%
Security solutions	5.0	1.7	5.0	0.7	1.5	14.8	34.8	55.3	233%
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Total	385.2	405.6	372.0	355.8	422.7	476.1	527.0	571.9	11%
Net sales growth by segment									
Development tools	10%	6%	-9%	-3%	18%	10%	7%	5%	
Security solutions		-66%	194%	-86%	114%	885%	135%	59%	
Other									
Total	10%	5%	-8%	-4%	19%	13%	11%	9%	
Net sales by product									
License-based	242.9	236.3	212.4	196.1	233.0	275.3	321.1	357.1	15%
Support and softw are updates	119.4	146.3	145.2	141.6	167.9	180.7	185.2	193.2	5%
Other	22.9	23.0	14.4	18.1	19.0	20.0	20.7	21.6	4%
Total	385.2	405.6	372.0	355.8	422.7	476.1	527.0	571.9	11%
Net sales growth by product									
License-based	12%	-3%	-10%	-8%	19%	18%	17%	11%	
Support and softw are updates	10%	23%	-1%	-2%	19%	8%	2%	4%	
Other	20%	0%	-37%	26%	5%	5%	4%	4%	
Total	10%	5%	-8%	-4%	19%	13%	11%	9%	

Source: Company (historical data), DNB Markets (estimates)

Figure 16: Quarterly segment overview (SEKm, 2020–2023e)

(SEKm)	Q3'21	Q4'21	Q1'22	Q2'22	Q3'22	Q4'22	Q1'23e	Q2'23e	Q3'23e	Q4'23e
Net sales by segment										
Development tools	87.8	91.5	97.0	107.2	105.6	108.6	111.3	119.3	114.3	116.5
Security solutions	0.1	0.1	0.4	0.4	0.5	0.2	0.6	2.9	4.5	6.7
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	90.0	91.6	98.3	107.6	106.1	110.7	111.9	122.2	118.8	123.2
Net sales growth by segment										
Development tools	-1%	2%	9%	23%	20%	19%	15%	11%	8%	7%
Security solutions	-75%	-92%	33%	100%	400%	100%	56%	632%	804%	3252%
Other										
Total	-1%	1%	10%	23%	20%	19%	15%	14%	12%	13%
Net sales by product										
License-based	46.2	49.4	52.0	67.8	56.2	57.0	63.4	75.5	68.3	68.2
Support and softw are updates	36.9	36.1	41.2	36.9	44.4	45.4	43.9	42.4	46.0	48.4
Other	4.8	6.1	4.2	2.9	5.5	6.4	4.7	4.3	4.5	6.5
Total	90.0	91.6	98.3	107.6	106.1	110.7	111.9	122.2	118.8	123.2
Net sales growth by product										
License-based	-9%	-5%	4%	35%	22%	15%	22%	11%	21%	20%
Support and softw are updates	4%	2%	19%	9%	20%	26%	6%	15%	4%	7%
Other	85%	79%	2%	-6%	15%	5%	11%	48%	-18%	2%
Total	-1%	1%	10%	23%	20%	19%	15%	14%	12%	13%

Source: Company (historical data), DNB Markets (estimates)

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Figure 17: Quarterly income statement and key items (SEKm, 2020–2023e)

(SEKm)	Q3'21	Q4'21	Q1'22	Q2'22	Q3'22	Q4'22	Q1'23e	Q2'23e	Q3'23e	Q4'23e
Net sales	90.0	91.6	98.3	107.6	106.1	110.7	111.9	122.2	118.8	123.2
Grow th YOY , of w hich	-1%	1%	10%	23%	20%	19%	15%	14%	12%	13%
Organic	-1%	2%	3%	14%	11%	7%	8%	7%	8%	11%
Structural	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
FX	0%	-1%	7%	9%	9%	12%	6%	7%	4%	2%
COGS	-2.8	-3.0	-2.8	-3.1	-3.1	-3.8	-3.4	-3.5	-3.5	-3.8
Gross profit	87.2	88.6	95.5	104.5	103.0	106.9	108.5	118.7	115.3	119.4
Capitalised w ork	13.7	14.1	12.2	10.5	11.3	16.2	13.6	14.0	14.0	14.4
Other external expenses	-10.3	-14.1	-11.5	-11.9	-18.8	-16.1	-15.0	-15.0	-15.7	-16.0
Personnel costs	-55.6	-75.4	-66.0	-71.2	-61.3	-74.6	-70.0	-74.0	-63.0	-69.0
EBITDA	35.0	13.2	30.2	31.9	34.2	32.4	37.1	43.7	50.6	48.8
IAC	2.1	-134.2	0.9	0.0	-4.5	0.0	0.0	0.0	0.0	0.0
Adj. EBITDA	32.9	147.4	29.3	31.9	38.7	32.4	37.1	43.7	50.6	48.8
Depreciation and amortisation	-14.1	-132.2	-13.0	-12.3	-12.1	-15.9	-16.1	-16.3	-16.1	-16.3
EBIT	20.9	-119.0	17.2	19.6	22.1	16.5	21.0	27.4	34.6	32.5
Adj. EBIT	18.8	15.2	16.3	19.6	26.6	16.5	21.0	27.4	34.6	32.5
Financial items	-0.3	1.8	-0.9	-0.5	1.1	-1.9	-1.5	-1.5	-1.5	-1.4
Profit before tax	20.6	-117.2	16.3	19.1	23.2	14.6	19.5	25.9	33.1	31.1
Taxes paid	-4.7	11.8	-4.4	-4.8	-6.4	0.0	-4.4	-5.8	-7.4	-7.0
Adj. Net profit	13.8	28.8	11.0	14.3	21.3	14.6	15.1	20.1	25.6	24.1
EPS	1.17	-7.72	0.88	1.05	1.04	1.07	1.11	1.47	1.88	1.77
Adj. EPS (diluted)	1.01	2.11	0.81	1.05	1.56	1.07	1.11	1.47	1.88	1.77
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00
				33%	41%	9%				
Margins										
Gross	96.9%	96.7%	97.2%	97.1%	97.1%	96.6%	97.0%	97.1%	97.1%	96.9%
EBITDA	38.9%	14.4%	30.7%	29.6%	32.2%	29.3%	33.1%	35.8%	42.6%	39.6%
Adj. EBITDA	36.6%	160.9%	29.8%	29.6%	36.5%	29.3%	33.1%	35.8%	42.6%	39.6%
EBIT	23.2%	-129.9%	17.5%	18.2%	20.8%	14.9%	18.7%	22.5%	29.1%	26.4%
Adj. EBIT	20.9%	16.6%	16.6%	18.2%	25.1%	14.9%	18.7%	22.5%	29.1%	26.4%
FCF margin	24.1%	25.5%	15.7%	15.3%	31.3%	3.0%	17.0%	20.0%	19.8%	14.3%
Rule of 40 (EBIT)	22.1%	17.6%	27.2%	41.3%	43.0%	35.8%	32.6%	36.0%	41.1%	37.7%
ROCE	9.7%	9.3%	9.5%	10.4%	11.8%	11.6%	11.9%	12.6%	13.3%	15.1%
Cash flow										
Cash flow from operating activities	41.4	40.5	28.8	26.0	47.4	25.8	36.7	43.1	41.7	36.4
Capex	-19.7	-17.1	-13.4	-9.5	-14.2	-22.5	-17.7	-18.7	-18.2	-18.8
Adj. FCF	21.7	23.4	15.4	16.5	33.2	3.3	19.0	24.4	23.5	17.6
Cash conversion (FCF/EBIT)	115%	154%	94%	84%	125%	20%	91%	89%	68%	54%
Balance sheet										
Cash	91.3	113.4	125.0	117.9	158.8	148.2	165.2	167.1	188.7	204.3
Net cash (-) / net debt (+)	-36.4	-57.4	-72.0	-85.9	-131.1	-78.9	-97.9	-101.8	-125.4	-143.0
Net debt/EBITDA	-0.3x	-0.6x	-0.7x	-0.8x	-1.2x	-0.6x	-0.7x	-0.7x	-0.8x	-0.8x

Source: Company (historical data), DNB Markets (estimates)

Valuation

Figure 18: Valuation approaches (SEKm, %)

	Peers regression	DCF	Historical average
Net sales (2023e)			476
Adj. EBIT (2023e)			116
Adj. EPS (2023e)			6.22
Sales CAGR (2022–2024e)	12.5		11.7
Adj. EBIT margin (2023e)	23.0		24.3
RO40 (2023e)	47.0		35.9
Target multiple	RO40, P/B, EV/S	10% WACC	20x EV/EBIT
Enterprise value	3,294	3,050	2,310
Net debt (+)/cash (-)	-79	-79	-79
Equity value	3,373	3,129	2,389
Shares outstanding	13.7	13.7	13.7
Implied price/share	247	229	175
Implied potential	69%	57%	20%

2024e valuation multiples

Implied EV/sales	6.2	5.8	4.4
Implied EV/EBIT	22.6	20.9	15.9
Implied P/E	30.9	28.7	21.9

Source: DNB Markets

Figure 19: Implied valuation multiples based on current share price

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
Net sales	328	345	385	406	372	356	420	476	527	572
Growth YOY	5.4%	5.1%	10.2%	5.2%	-8.3%	-4.4%	18.8%	12.6%	10.7%	8.5%
Gross profit	316	337	376	395	358	346	410	462	513	558
Gross margin	96.3%	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	97.0%	97.3%	97.5%
Adj. EBITDA	117	127	140	146	133	104	129	180	213	246
EBITDA margin	36.9%	36.9%	37.2%	35.9%	35.7%	66.5%	31.3%	37.9%	40.4%	43.1%
Adj. EBIT	101	107	119	108	84	66	79	116	146	174
EBIT margin	30.6%	31.1%	30.8%	26.7%	22.5%	18.4%	18.7%	24.3%	27.6%	30.4%
Adj. Net profit	82	80	94	81	59	67	61	85	109	132
Adj. FCF	95	105	46	22	37	58	68	85	112	109
FCF margin	29.0%	30.4%	11.9%	5.4%	9.9%	16.2%	16.3%	17.8%	21.3%	19.1%
Cash conversion	95%	98%	39%	20%	44%	88%	87%	73%	77%	63%
Rule of 40 (EBIT)	36.0%	36.2%	41.0%	31.9%	14.2%	14.0%	37.5%	36.9%	38.3%	39.0%
ROCE	35.0%	37.4%	28.1%	17.7%	12.4%	9.9%	11.5%	15.1%	17.6%	19.2%
ROIC	27.4%	28.5%	21.9%	13.8%	10.1%	10.4%	9.3%	11.9%	13.8%	15.0%
Market cap	2,602	2,387	3,310	2,535	1,905	1,606	1,998	1,998	1,998	1,998
Net debt	-97	-117	-103	18	-1	-57	-79	-143	-225	-297
Enterprise value	2,505	2,270	3,206	2,554	1,904	1,548	1,919	1,855	1,773	1,702
EV/Sales	7.6x	6.6x	8.3x	6.3x	5.1x	4.4x	4.6x	3.9x	3.4x	3.0x
EV/EBIT	24.9x	21.1x	27.0x	23.6x	22.7x	23.6x	24.3x	16.1x	12.2x	9.8x
P/E	31.7x	29.8x	35.2x	31.2x	32.1x	24.0x	32.7x	23.5x	18.3x	15.2x
FCF yield	3.7%	4.4%	1.4%	0.9%	1.9%	3.6%	3.4%	4.2%	5.6%	5.5%

Source: Company (historical figures), DNB Markets (estimates)

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Figure 20: EV/sales 12-month forward IAR Systems (2018–2023)



Source: Bloomberg

Figure 21: EV/EBITDA 12-month forward IAR Systems (2018–2023)



Source: Bloomberg

Figure 22: EV/EBIT 12-month forward IAR Systems (2018–2023)



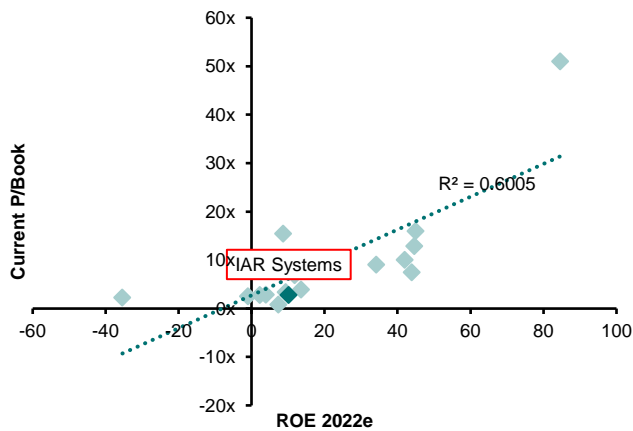
Source: Bloomberg

Figure 23: P/E 12-month forward IAR Systems (2018–2023)



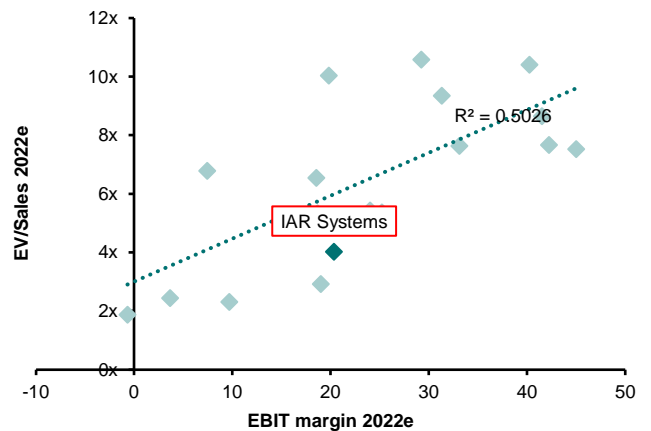
Source: Bloomberg

Figure 24: Current P/book versus ROE 2023e



Source: Bloomberg (underlying data), DNB Markets (further calculations)

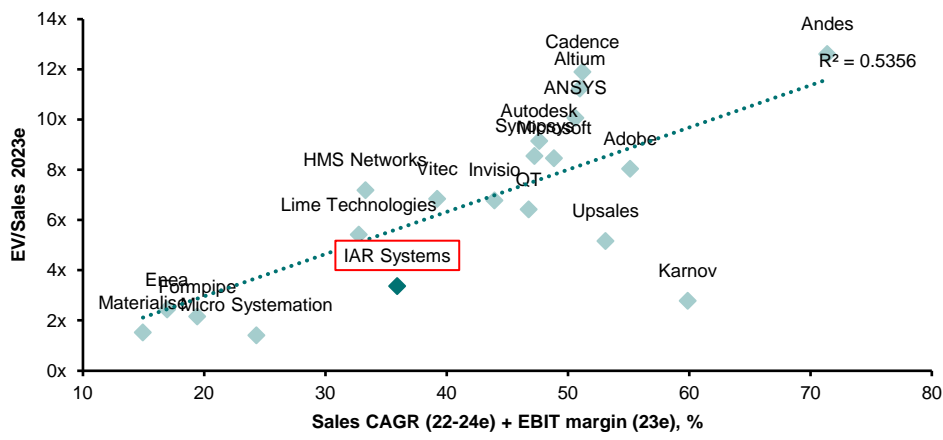
Figure 25: EV/sales versus EBIT margin (2023e)



Source: Bloomberg (underlying data), DNB Markets (further calculations)

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Figure 26: EV/sales 2023e versus sales CAGR + EBIT margin



Source: Bloomberg (underlying data), DNB Markets (further calculations)

Figure 27: IAR Systems' valuation versus listed peers

	Mkt. cap.	P/E (x)			EV/EBIT (x)			EV/EBITDA (x)			EV/Sales (x)			2023 yield (%)		ROE (%)		EBIT margin		CAGR 2022-2024e (%)			
	(SEKbn)	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e	DPS	FCF	2023e	2024e	2023e	2024e	Sales	EBIT	EPS	
IAR Systems (DNBe)	2.0	24	18	15	16	12	10	10	8	7	4	3	3	1.5	4.2	12	14	24.3	27.6	12	36	38	
Premium/discount		-42%	-38%	-50%	-49%	-47%	-55%	-52%	-62%	-56%	-48%	-48%	-46%										
IAR Systems (Cons.)	2.0	21	17		14	11		10	8		4	4		1.7	4.2			26.3	29.7	12	33	37	
Premium/discount		-48%	-43%	n.a.	-54%	-52%	n.a.	-55%	-65%	n.a.	-49%	-45%	n.a.										
Nordic software																							
Enea	2.2	24	19	13	18	14	11	7	7	5	3	2	2		7.6	4	5	12.8	14.3	4	20	-6	
Formpipe	1.3	35	23	17	28	18	13	13	10	8	2	2	2	3.0	2.7	8	13	9.0	12.6	10	128	132	
HMS Networks	20.2	39	37	35	30	28	27	26	25	24	8	7	7	1.0	2.9	29	25	24.7	24.7	9	8	10	
Invisio	8.1	63	42	31	48	31	24	37	27	21	8	7	6	0.7	1.4	28	33	16.7	21.1	27	134	157	
Karnov	6.4	21	17	54	31	23	26	13	11	10	3	3	3	1.6	6.3	4	7	10.8	13.7	49	50	30	
Lime Technologies	3.2	34	29		31	25		19	17		6	5		1.2	3.4	42	39	19.1	20.0	14	18	17	
Micro Systemation	0.7	17	13	11	12	9	7	9	8	6	2	1	1	5.3	6.7	35	40	13.2	15.3	11	21	17	
QT	16.6	42	29	23	34	22	15	28	19	14	8	6	5	0.0	2.6	34	37	23.1	27.1	24	35	24	
Upsales	1.2	38	29		29	22		23	18		7	5	4	1.6	1.5	67	62	22.8	23.3	30	37	40	
Vitec	18.2	46	39	35	39	33	29	21	18	16	8	7	6	0.7	1.3	10	11	19.4	20.4	20	27	31	
WithSecure	3.1			88			59		91	16	1	1	1	0.0		-8	-2	-13.7	-5.0	12	-53	-54	
Engineering software																							
Adobe	1,797.4	25	22	20	20	18	15	18	16	14	9	8	7	0.0	4.6	44	40	44.7	44.1	10	9	13	
Altium	37.3	55	44	36	41	32	26	36	29	24	13	11	10	1.8	1.3	23	28	32.2	34.4	19	29	29	
Andes	10.4	56	36								19	13		1.7		20	15	25.0	39.0	46	339	17	
ANSYS	246.1	33	29	26	26	24	22	24	23	24	11	10	9	0.0	2.7	14	13	42.0	42.6	9	10	10	
Autodesk	502.7	34	31	26	27	25	21	25	23	20	10	9	8	0.0	4.0	149	123	35.9	36.2	12	20	21	
Cadence	532.1	40	35	31	32	28	25	29	26	23	13	12	11	0.0	2.4	36	23	40.9	40.7	10	11	12	
Materialise	5.7	103	32	21	69	21	11	14	9	7	2	2	1	0.0	0.8	2	5	2.4	6.8	13		164	
Microsoft	20,584.1	29	25	22	23	20	17	19	17	15	9	8	8	1.0	3.1	36	34	40.6	42.0	8	8	6	
Synopsys	580.4	36	31	29	27	24	20	25	28	19	10	9	8		2.8	25	23	34.4	34.8	13	16	16	
Average	1,218.9	40	30	30	31	23	22	22	22	16	8	6	5	1.1	3.2	30	29	22.8	25.4	18	46	34	
Median	13.5	36	29	26	29	23	21	22	18	16	8	7	6	0.8	2.7	26	24	23.0	24.0	13	20	17	

Source: Bloomberg (underlying data), DNB Markets (further calculations)

Summary of positives

Attractive position in a structural growth niche

Sweden-based IAR Systems is a world-leading provider of commercial software tools and services for programming processors in embedded systems (computer hardware and software designed for a specific function) that enable the development and ensure the code quality of digital products. Its professional customers are mainly developers (150,000+ technology users) at OEMs (46,000+) building these systems for products going into fields such as industrial automation, medical technology, telecommunication, consumer electronics, and the automotive industry. Although the niche for IAR Systems' addressable market is largely undefined, it has said it captures a ~40% market share for commercial tools. We note several prospects for the market to show a mid-to-high single-digit CAGR over the medium term: 1) a continued increase in the number (and complexity) of embedded systems driven by the growth of IoT; 2) demand for reliable and advanced software tools that offer faster time-to-market and a complete development platform; and 3) a lack of software developers, which increases demand for more powerful software-development tools.

Market dynamics benefiting the market leader

In our view, IAR Systems' key competitive advantages stem from: 1) its complete toolchain for product developers across 8-, 16-, 32-, and 64-bit processors; 2) its independence, which enables it to support a wide range of design architecture – customers can choose the programming environment and tools according to their own needs, regardless of processor or project, which avoids locking customers into one technical platform (a factor amplified by the global semiconductor shortage); and 3) superior industrial-quality, as its commercial customers cannot compromise on tools' code performance, reliability, user-friendliness, or time-to-market by using inferior technologies, such as open-source alternatives. IAR Systems' solutions create codes that are compact, fast, and stable.

96%+ gross margins ensure high level of scalability

Although IAR Systems' organic growth has averaged 1% in the past five years, we believe the company has a diversified set of growth opportunities that could support its 10–15%+ organic sales growth target in the medium term and an acceleration of its most promising new product launches: 1) migrating its existing 32-bit customers (~80% of 2021 sales) to 64-bit; 2) broader RISC-V adoption; and 3) IoT security taking off. With ~95% customer retention, we believe it could scale up with its existing customer base, which, in combination with 96%+ gross margins, could provide a highly scalable cost structure over the coming years that could add a tailwind to significant margin expansion with high cash conversion.

Early leader in two of the embedded industry's most prominent themes

In 2018, IAR Systems acquired Cambridge-based start-up Secure Thingz, which offers advanced security solutions focusing on IoT. Although we share the company's view about the potential to emerge as an early leader in the embedded systems security market, it has taken IAR Systems several years to find a way to commercially package its award-winning security technology (which led to a SEK116m write-down of intangible assets in 2021). We expect broader adoption in the coming years from secure IP being seen as a business imperative and increasingly stringent security legislation. We are cautiously optimistic about recent customer agreements to provide secure coding in the manufacturing of IoT devices for Secure Thingz. Moreover, the RISC-V ecosystem is maturing (RISC-V foundation members have expanded fivefold since IAR Systems joined in 2018), setting the scene for a potential breakout. Semico and Tractica forecast a ~100% CAGR of RISC-V cores, reaching an estimated 62bn units in 2025 and a ~USD70m–80m RISC-V tools market for a 40%+ CAGR to 2025, of which IAR should gain a sizeable share.

Summary of negatives

Possible shift in the competitive landscape

IAR Systems holds leading positions across most processor types, but it still faces a highly competitive environment, particularly from the independent supplier Green Hills Software and Arm's development tool, Kiel, we believe. In addition, the increasingly strategic nature of development tools for many industries could attract competition from disruptive innovators or free, open-source-based alternatives, which are gaining popularity, as younger generations of developers could be unwilling to pay for licences or be restricted to a single technology from one vendor.

Potential weakening of the Embedded Workbench community

According to Slashdata, there were 7.5m active software developers writing in the C/C++ language of the ~27m active developers globally in 2021. However, C++ is relatively hard to master. As developers often understand all aspects of a programming language, the difficulty of the language may affect the future number of C++ developers. We view this as a challenge, especially if we see a wider push from processor manufacturers and OEMs to provide developers with high-level tools that can abstract out the lower-level hardware and software in product development.

Product development might prove too costly and not materialise in sales growth

We believe IAR Systems was underinvested from 2015, which drove a considerable EBIT margin and ROCE expansion up to 30%+ given the inherent scalability of the business model. However, as organic growth abated, IAR Systems underwent the most comprehensive investment phase in its nearly 40-year history, investing SEK500m+ over the past five years in its security offering, 64-bit support, and RISC-V tools. We believe these investments have been the appropriate approach to provide building blocks to take the company to the next level. The pandemic has delayed project designs and, thus, customers committing to new investment decisions, but we have still seen few proof-points indicating that IAR Systems stands to reap the fruit of these investments. Its new management team made a SEK116m impairment of intangible development assets in Q4 2021.

One of the most FX-sensitive stocks on the OMX Stockholm exchange

Although >98% of sales are from markets outside Sweden, we estimate ~40% of the fixed cost base is denominated in SEK; thus, the company is fairly sensitive to fluctuations in this currency. If the SEK were to strengthen by ~10% against its most important currencies (USD, EUR, JPY) as well as the GBP and KRW, we estimate a ~10% FX headwind for sales and a ~40% headwind for 2022 EBIT.

SaaS transition still ahead for IAR Systems

We prefer subscription-based revenue models to traditional on-premises perpetual licence delivery models, as the SaaS models generates more predictable near-term revenue and cash flow, with, we believe, the potential to become more profitable longer-term. We believe it would make sense for IAR Systems to undergo such a transition in revenue mix to add visibility while potentially opening up for new customers that would not typically pay for its high-end licence products. However, such a transition would probably come at the expense of a short-term moderation in revenue growth and profitability (cloud revenue recognised over time versus perpetual upfront, in combination with increased investments to support cloud infrastructure).

Continued market consolidation among processor vendors

The ongoing consolidation trend among processor vendors could last longer than IAR Systems expects, which could continue to create market uncertainty and disrupt IAR Systems' partner network. We believe that a certain level of market fragmentation has been central to IAR Systems' competitiveness, as it has the broadest support in the market for different processor vendors and design architectures.

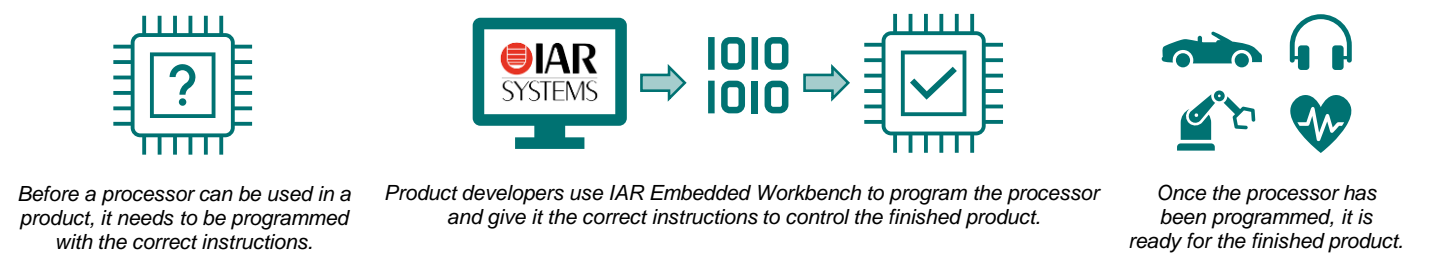
Business overview

IAR Systems was founded in 1983 by engineer Anders Rundgren and provides world-leading software for programming processors in embedded systems (computer systems designed to perform a dedicated function in a mechanical or electrical system). Its leading software tool chain – the IAR Embedded Workbench – facilitates, quality-assures, and improves the time-to-market of programming instructions in 8-, 16-, 32-, and 64-bit processors.

World-leading provider of software for programming processors in embedded systems, which enable the development of digital products

According to IAR, individuals interact 30+ times a day with a product that is programmed by one of its loyal 46,000+ OEM customers (~95% recurring customers), or 150,000+ technology users found mainly in the automotive, industrial automation, medical technology, and consumer electronics industries such as Denso, Bosch, ABB, Continental, or Miele.

Figure 28: IAR Embedded Workbench in the customer’s product development



Source: Company (underlying data), DNB Markets (graph structuring)

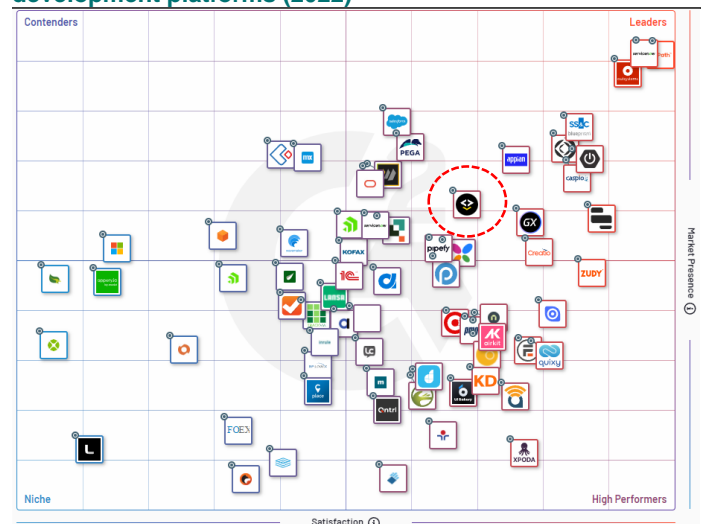
Headquartered in Uppsala, Sweden, IAR Systems has 200+ employees in 15 offices on three continents with technical support teams in its customers’ local time zones in 10+ languages. Its independent software supports more than 14,000 different processors from more than 70 processor vendors, which is more than any other supplier in the market, meaning customers can choose the programming environment and tools according to their own needs regardless of processor or project. This avoids locking customers into one technical platform. Moreover, it can re-use 70–80% of previously developed code instead of rewriting it (saving time and resources).

Figure 29: Example of customers



Source: Company

Figure 30: Users view IAR Systems as a leader for low-code development platforms (2022)



Source: G2 Grid
 Note: G2 scores products and sellers based on reviews gathered from its user community, as well as data aggregated from online sources and social networks; score is based on market presence and user satisfaction

With almost 40 years’ experience in the embedded industry, IAR Systems has built long-standing relationships and an extensive partner network, including: 1) suppliers of processors and architectures (Arm, RISC-V, Renesas, STMicroelectronics, etc.); 2) industry organisations for coding standards, certification, security compliance (TÜV SÜD, CERT C, MISRA, IoT Security Foundation, etc.); 3) services vendors (cloud services vendors, programming

Long-standing embedded industry partnerships

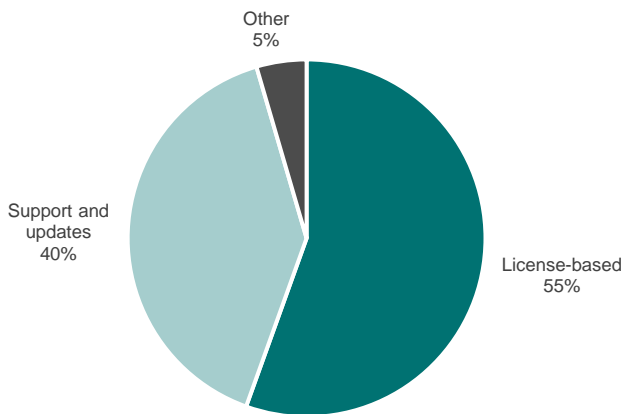
companies, etc.); and 4) suppliers of integrated programmes (real-time operating systems, graphics development, etc.).

IAR Systems' business model is primarily licence- and transaction-based, where customers (users, developers) pay upfront for a right-to-use licences (perpetual software keys) to access the software, while the customer can add support and updates for an annual cost of ~20% of the licence price. This means IAR Systems depends on selling new licences to facilitate growing net sales, we believe.

Perpetual licence-based business model with ~40% recurring revenues

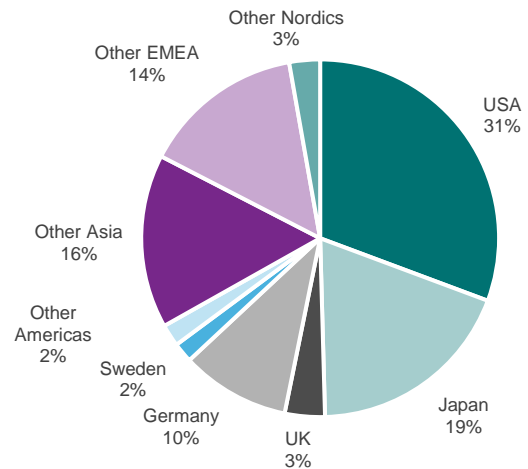
- **Development tools (~99% of net sales)** consist of IAR Embedded Workbench (8- to 64-bit) with world-leading code-optimisation technology, compiler, debugger probes and analysis tools (ensuring code quality and coding standards), functional safety certifications (pre-certified build tools), RISV-V architecture, and a Linux offering for continuous integration.
- **Security solutions (~1%)** consist of: 1) Embedded Trust, which enables the security specialist in an organisation to set security guidelines in accordance with company policy; 2) C-Trust, which makes it possible for developers to prepare encrypted code that automatically follows the prevailing security guidelines; and 3) Secure Desktop Provisioner, which helps OEM customers to securely programme products by giving each device a unique identity. The medium-term embedded security market opportunity with an 'out of the box' solution for mainstream MCUs appears likely to be beneficial for IAR, especially in device production as opposed to product development (royalty-based instead of licences). However, it will probably take time for security regulations and standards to significantly affect the marketplace.

Figure 31: Net sales by revenue stream (2022)



Source: Company

Figure 32: Geographical net sales split (2021)



Source: Company

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Forecast changes – P&L

(SEKm)	New			Old			Change		
	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
Revenues	476	527	572	481	526		-5	1	
Cost of sales	-14	-14	-14	-12	-12		-2	-2	
Gross profit	462	513	558	469	514		-7	-1	
Operating expenses	-338	-355	-371	-337	-351		0	-4	
EBITDA	180	213	246	183	217		-3	-4	
EBITDA adj	180	213	246	183	217		-3	-4	
EBITDA margin (%)	37.9	40.4	43.1	38.0	41.3	nm	-0.2	-0.9	nm
Depreciation	-35	-35	-36	-20	-21		-15	-14	
Amortisation	-30	-32	-36	-38	-42		8	10	
EBIT	116	146	174	125	154		-9	-9	
EBIT adj	116	146	174	125	154		-9	-9	
Net financial items	-6	-5	-4	-3	-3		-3	-2	
PBT	110	141	170	122	151		-12	-11	
Taxes	-25	-32	-38	-27	-34		3	2	
Minorities	0	0	0		0			0	
Net profit	85	109	132	94	117		-9	-8	
Adjustments to net profit	0	0	0	0	0		0	0	
Net profit adj	85	109	132	94	117		-9	-8	
<i>Per share data (SEK)</i>									
EPS	6.22	7.99	9.64	6.91	8.60		-0.69	-0.61	
EPS adj	6.22	7.99	9.64	6.91	8.60		-0.69	-0.61	
DPS ordinary	2.18	2.80	3.37	2.42	3.01		-0.24	-0.21	
DPS	2.18	2.80	3.37	2.42	3.01		-0.24	-0.21	
<i>Other key metrics (%)</i>									
Revenue growth	12.6	10.7	8.5	14.6	9.3	nm	-1.9	1.4	nm
EBIT adj growth	46.2	26.1	19.5	46.1	23.7	nm	0.1	2.4	nm
EPS adj growth	38.9	28.3	20.7	47.7	24.5	nm	-8.9	3.9	nm
Avg. number of shares (m)	14	14	14	14	14		0	0	
Capex	-73	-78	-83	-67	-72		-6	-6	
OpFCF	107	135	163	115	145		-8	-10	
Working capital	-51	-64	-54	-55	-60		4	-4	
NIBD adj	-143	-225	-297	-208	-289		65	63	

Source: DNB Markets

Forecast changes – By segment and assumptions

(SEKm)	New			Old			Change		
	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
Assumptions									
Revenue org. % YOY	7.87	10.44	8.52	11.60	9.33		-3.72	1.11	
Structure impact % YOY	0.00	0.00	0.00		0.00			0.00	
Currency impact % YOY	4.75	0.27	0.00	2.97	0.00		1.78	0.27	

Source: DNB Markets

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Quarterly numbers

(SEKm)	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023e	Q2 2023e	Q3 2023e	Q4 2023e	Q1 2024e
Revenues	90	92	98	108	106	111	112	122	119	123	126
Cost of sales	-3	-3	-3	-3	-3	-4	-3	-4	-4	-4	-3
Gross profit	87	89	96	105	103	107	108	119	115	119	123
Operating expenses	-66	-90	-78	-83	-80	-91	-85	-89	-79	-85	-89
EBITDA	35	13	30	32	34	32	37	44	51	49	48
Depreciation	-5	-5	-6	-6	-5	-9	-9	-9	-9	-9	-9
Amortisation	-9	-127	-7	-7	-7	-7	-7	-7	-7	-8	-8
EBIT	21	-119	17	20	22	17	21	27	35	33	31
Net financial items	0	2	-1	-1	1	-2	-2	-2	-2	-1	-1
PBT	21	-117	16	19	23	15	19	26	33	31	30
Taxes	-5	12	-4	-5	-6	0	-4	-6	-7	-7	-7
Minorities	0	0	0	0	0	0	0	0	0	0	0
Net profit	16	-105	12	14	17	15	15	20	26	24	23
Adjustments to net profit	-2	134	-1	0	5	0	0	0	0	0	0
Net profit adj	14	29	11	14	21	15	15	20	26	24	23
Dividend paid	0	0	0	0	0	0	0	-20	0	0	0
Avg. number of shares (m)	14	14	14	14	14	14	14	14	14	14	14
<i>Per share data (SEK)</i>											
EPS	1.17	-7.72	0.88	1.05	1.04	1.07	1.11	1.47	1.88	1.77	1.70
EPS adj	1.01	2.11	0.81	1.05	1.56	1.07	1.11	1.47	1.88	1.77	1.70
DPS ordinary	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00	0.00
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00	0.00
<i>Growth and margins (%)</i>											
Revenues, QOQ growth	3.0	1.8	7.3	9.5	-1.4	4.3	1.1	9.2	-2.8	3.7	2.5
Revenues, YOY growth	1.2	1.0	10.6	23.1	17.9	20.9	13.8	13.6	12.0	11.3	12.8
EPS adj, YOY growth	-26.2	140.0	-14.1	26.6	54.3	-49.3	37.3	40.6	20.4	65.3	54.0
Gross margin	96.9	96.7	97.2	97.1	97.1	96.6	97.0	97.1	97.1	96.9	97.3
EBITDA adj margin	36.6	160.9	29.8	29.6	36.5	29.3	33.1	35.8	42.6	39.6	38.0
Depreciation/revenues	-5.7	-5.7	-5.8	-5.3	-5.1	-7.9	-7.9	-7.3	-7.3	-7.1	-6.9
EBIT adj margin	20.9	16.6	16.6	18.2	25.1	14.9	18.7	22.5	29.1	26.4	24.8
Net profit margin	17.7	nm	12.1	13.3	15.8	13.2	13.5	16.4	21.6	19.6	18.4

Source: Company (historical figures), DNB Markets (estimates)

Adjustments to quarterly numbers

(SEKm)	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023e	Q2 2023e	Q3 2023e	Q4 2023e	Q1 2024e
EBITDA	35	13	30	32	34	32	37	44	51	49	48
EBITDA adj	33	147	29	32	39	32	37	44	51	49	48
EBIT	21	-119	17	20	22	17	21	27	35	33	31
Other EBIT adjustments	2	-134	1	0	-5	0	0	0	0	0	0
EBIT adj	19	15	16	20	27	17	21	27	35	33	31
Net profit	16	-105	12	14	17	15	15	20	26	24	23
Other EBIT adjustments	2	-134	1	0	-5	0	0	0	0	0	0
Net profit adj	14	29	11	14	21	15	15	20	26	24	23

Source: Company (historical figures), DNB Markets (estimates)

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Quarterly numbers by segment and assumptions

(SEKm)	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023e	Q2 2023e	Q3 2023e	Q4 2023e	Q1 2024e
Assumptions											
Revenue org. % YOY	-0.67	1.98	3.04	13.84	10.89	6.88	8.33	6.69	8.29	10.84	11.71
Structure impact % YOY	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Currency impact % YOY	-0.45	-0.99	6.52	9.27	9.33	11.90	6.41	6.90	3.67	2.14	1.14

Source: Company (historical figures), DNB Markets (estimates)

Annual P&L

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e	
Revenues	328	345	385	406	372	358	423	476	527	572	
Cost of sales	-12	-9	-9	-11	-14	-12	-13	-14	-14	-14	
Gross profit	316	337	376	395	358	346	410	462	513	558	
Operating expenses	-203	-209	-236	-249	-225	-242	-331	-338	-355	-371	
EBITDA	113	127	140	146	133	104	129	180	213	246	
Depreciation	-3	-2	-3	-13	-20	-20	-26	-35	-35	-36	
Amortisation	-14	-17	-22	-25	-29	-152	-28	-30	-32	-36	
EBIT	97	107	116	108	84	-69	75	116	146	174	
Net financial items	0	-2	-2	-1	-7	0	-2	-6	-5	-4	
PBT	100	106	117	107	77	-69	73	110	141	170	
Taxes	-22	-26	-26	-26	-17	1	-16	-25	-32	-38	
Effective tax rate (%)	22	24	22	24	23	2	21	23	23	23	
Minorities	0	0	0	0	0	0	0	0	0	0	
Net profit	78	80	91	81	59	-67	58	85	109	132	
Adjustments to net profit	4	0	3	0	0	134	4	0	0	0	
Net profit adj	82	80	94	81	59	67	61	85	109	132	
Dividend paid	-88	-63	-68	-68	0	0	0	-20	-30	-38	
Avg. number of shares	13	13	14	14	14	14	14	14	14	14	
<i>Per share data (SEK)</i>											
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.04	6.22	7.99	9.64	
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.48	6.22	7.99	9.64	
DPS ordinary	7.00	5.00	5.00	3.00	0.00	0.00	1.50	2.18	2.80	3.37	
DPS	7.00	5.00	5.00	3.00	0.00	0.00	1.50	2.18	2.80	3.37	
<i>Growth and margins (%)</i>											
Revenue growth	5.4	5.1	11.7	5.3	-8.3	-3.8	18.1	12.6	10.7	8.5	
EPS adj growth	23.0	2.6	5.3	-10.6	-26.8	12.5	-8.6	38.9	28.3	20.7	
Gross margin	96.3	97.5	97.7	97.3	96.2	96.6	97.0	97.0	97.3	97.5	
EBITDA margin	34.5	36.9	36.4	35.9	35.7	29.0	30.4	37.9	40.4	43.1	
EBITDA adj margin	35.7	36.9	37.2	35.9	35.7	66.5	31.3	37.9	40.4	43.1	
Depreciation/revenues	-0.8	-0.7	-0.7	-3.2	-5.5	-5.7	-6.0	-7.4	-6.7	-6.3	
EBIT margin	29.4	31.1	30.0	26.7	22.5	nm	17.8	24.3	27.6	30.4	
EBIT adj margin	30.6	31.1	30.8	26.7	22.5	18.4	18.7	24.3	27.6	30.4	
PBT margin	30.5	30.6	30.4	26.4	20.6	nm	17.3	23.0	26.7	29.7	
Net profit margin	23.8	23.2	23.6	20.0	16.0	nm	13.6	17.8	20.7	23.0	

Source: Company (historical figures), DNB Markets (estimates)

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Adjustments to annual P&L

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
EBITDA	113	127	140	146	133	104	129	180	213	246
EBITDA adj	117	127	143	146	133	238	132	180	213	246
EBIT	97	107	116	108	84	-69	75	116	146	174
Other EBIT adjustments	-4	0	-3	0	0	-134	-4	0	0	0
EBIT adj	101	107	119	108	84	66	79	116	146	174
Net profit	78	80	91	81	59	-67	58	85	109	132
Other EBIT adjustments	-4	0	-3	0	0	-134	-4	0	0	0
Net profit adj	82	80	94	81	59	67	61	85	109	132
<i>Per share data (SEK)</i>										
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.04	6.22	7.99	9.64
Recommended adjustment	0.00	0.00	0.00	0.00	0.00	9.85	0.44	0.00	0.00	0.00
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.48	6.22	7.99	9.64

Source: Company (historical figures), DNB Markets (estimates)

Cash flow

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
Net profit	78	80	91	81	59	-67	58	85	109	132
Depreciation and amortisation	17	20	25	37	49	172	53	65	67	72
Cash flow from operations (CFO)	114	124	93	106	118	132	128	158	190	193
Capital expenditure	-19	-19	-47	-84	-81	-74	-60	-73	-78	-83
Acquisitions/Investments	0	0	-171	-19	0	0	0	0	0	0
Divestments	0	0	0	0	0	0	0	0	0	0
Cash flow from investing (CFI)	-19	-38	-218	-102	-81	-74	-60	-73	-78	-83
Free cash flow (FCF)	95	86	-125	4	37	58	68	85	112	109
Net change in debt	0	0	0	30	6	1	1	0	0	0
Dividends paid	-88	-63	-68	-68	0	0	0	-20	-30	-38
Share issue (repurchase)	0	0	172	0	0	0	0	0	0	0
Other	0	0	4	-14	-30	-16	-40	-8	-8	-8
Cash flow from financing (CFF)	-88	-63	108	-52	-25	-15	-40	-28	-38	-46
Total cash flow (CFO+CFI+CFF)	7	23	-17	-49	12	42	29	56	74	63
<i>FCFF calculation</i>										
Free cash flow	95	86	-125	4	37	58	68	85	112	109
Less: tax shields/other	0	0	0	0	0	0	0	0	0	0
Less: acquisitions	0	0	171	19	0	0	0	0	0	0
Less: divestments	0	0	0	0	0	0	0	0	0	0
Growth (%)										
CFO	15.7	8.5	-25.3	14.1	12.0	11.1	-2.7	23.3	20.2	1.5
CFI	-3.3	-98.9	-478.5	53.0	20.4	9.0	19.6	-23.0	-6.1	-7.2
FCF	18.5	-9.4	-244.7	102.8	957.1	55.4	19.0	23.7	32.5	-2.3
CFF	-39.0	28.5	270.4	-148.3	52.7	38.6	-162.3	28.1	-32.5	-22.3
FCFF	nm	nm	nm	nm	nm	nm	nm	nm	nm	nm

Source: Company (historical figures), DNB Markets (estimates)

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Balance sheet

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
Assets	396	410	722	825	834	813	922	983	1,060	1,127
Inventories	6	5	7	7	6	10	11	10	10	9
Trade receivables	48	51	63	67	59	59	67	65	61	56
Other receivables	19	12	38	52	64	44	34	33	30	27
Current financial assets	0	0	0	0	0	0	0	0	0	0
Cash and cash equivalents	99	120	106	61	68	113	148	204	279	342
Current assets	172	187	214	186	196	226	260	312	379	434
Property, plant and equipment	6	6	9	7	8	15	17	18	19	21
Other intangible assets	197	194	484	624	624	567	639	646	655	665
Deferred tax assets	16	3	13	5	4	3	3	3	3	3
Non-current financial assets	5	20	2	2	3	3	4	4	4	4
Non-current assets	224	223	508	639	638	587	663	671	682	693
Total assets	396	410	722	825	834	813	922	983	1,060	1,127
Equity and liabilities	396	410	722	825	834	813	922	983	1,060	1,127
Total equity	280	290	550	592	613	585	667	731	811	904
Trade payables	5	6	7	9	5	9	8	7	7	6
Other payables and accruals	92	86	131	117	111	133	146	151	158	140
Short-term debt	1	1	0	25	18	18	0	0	0	0
Total current liabilities	99	102	140	164	150	179	173	178	183	165
Long-term debt	2	2	1	41	32	20	50	42	34	26
Deferred tax liabilities	15	14	30	27	37	28	30	30	30	30
Other non-current liabilities	1	2	2	1	1	1	2	2	2	2
Total non-current liabilities	18	17	32	69	70	49	82	74	66	58
Total liabilities	116	120	172	233	220	228	255	252	250	223
Total equity and liabilities	396	410	722	825	834	813	922	983	1,060	1,127
<i>Key metrics</i>										
Net interest bearing debt	-97	-117	-103	18	-2	-57	-79	-143	-225	-297

Source: Company (historical figures), DNB Markets (estimates)

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Valuation ratios

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
<i>Enterprise value</i>										
Share price (SEK)	206.00	189.00	243.00	186.00	139.80	117.80	150.40	146.40	146.40	146.40
Number of shares (m)	12.63	12.63	13.62	13.63	13.63	13.63	13.65	13.65	13.65	13.65
Market capitalisation	2,602	2,387	3,310	2,535	1,905	1,606	2,053	1,998	1,998	1,998
Net interest bearing debt	-97	-117	-103	18	-2	-57	-79	-143	-225	-297
Adjustments to NIBD	0	0	0	0	0	0	0	0	0	0
Net interest bearing debt adj	-97	-117	-103	18	-2	-57	-79	-143	-225	-297
EV	2,505	2,270	3,206	2,554	1,904	1,548	1,974	1,855	1,773	1,702
EV adj	2,505	2,270	3,206	2,554	1,904	1,548	1,974	1,855	1,773	1,702
<i>Valuation</i>										
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.04	6.22	7.99	9.64
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.48	6.22	7.99	9.64
DPS ordinary	7.00	5.00	5.00	3.00	0.00	0.00	1.50	2.18	2.80	3.37
DPS	7.00	5.00	5.00	3.00	0.00	0.00	1.50	2.18	2.80	3.37
P/E	33.4	29.8	36.4	31.2	32.1	-23.8	37.2	23.5	18.3	15.2
P/E adj	33.4	29.8	36.4	31.2	32.1	24.0	33.6	23.5	18.3	15.2
P/B	9.31	8.22	6.02	4.28	3.11	2.74	3.08	2.73	2.47	2.21
Average ROE	27.3%	28.1%	21.6%	14.2%	9.9%	-11.2%	9.2%	12.2%	14.1%	15.3%
Earnings yield adj	3.0%	3.4%	2.7%	3.2%	3.1%	4.2%	3.0%	4.3%	5.5%	6.6%
Dividend yield	3.4%	2.6%	2.1%	1.6%	0.0%	0.0%	1.0%	1.5%	1.9%	2.3%
Free cash flow yield	3.7%	3.6%	-3.8%	0.1%	1.9%	3.6%	3.3%	4.2%	5.6%	5.5%
EV/SALES	7.63	6.58	8.32	6.30	5.12	4.32	4.67	3.90	3.36	2.98
EV/SALES adj	7.63	6.58	8.32	6.30	5.12	4.32	4.67	3.90	3.36	2.98
EV/EBITDA	22.1	17.8	22.9	17.5	14.3	14.9	15.3	10.3	8.3	6.9
EV/EBITDA adj	21.4	17.8	22.4	17.5	14.3	6.5	14.9	10.3	8.3	6.9
EV/EBIT	26.0	21.1	27.7	23.6	22.7	-22.6	26.2	16.1	12.2	9.8
EV/EBIT adj	24.9	21.1	27.0	23.6	22.7	23.6	25.0	16.1	12.2	9.8
EV/capital employed	8.9	7.8	5.8	3.8	2.8	2.4	2.7	2.3	2.1	1.8
EV/NOPLAT	33.3	27.1	35.6	30.2	29.1	-29.0	33.6	20.6	15.6	12.5
EV/OpFCF (taxed)	32.8	26.8	45.6	66.6	57.9	10.4	35.7	22.8	17.2	13.7

Source: Company (historical figures), DNB Markets (estimates)

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Key accounting ratios

	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
<i>Profitability (%)</i>										
ROA	19.6	19.9	16.0	10.5	7.2	-8.2	6.6	8.9	10.7	12.0
ROCE	35.0	37.4	28.1	17.7	12.4	9.9	11.5	15.1	17.6	19.2
ROCE after tax	27.3	29.1	21.9	13.8	9.7	7.8	8.9	11.8	13.7	15.0
<i>Return on invested capital (%)</i>										
Net PPE/revenues	1.9	1.8	2.3	1.8	2.0	4.1	4.0	3.8	3.7	3.6
Working capital/revenues	-7.5	-6.9	-7.8	-0.2	3.4	-8.3	-10.1	-10.7	-12.2	-9.4
<i>Cash flow ratios (%)</i>										
FCF/revenues	29.0	25.0	-32.4	0.9	9.9	16.1	16.2	17.8	21.3	19.1
FCF yield (%)	3.7	3.6	1.4	0.9	1.9	3.6	3.3	4.2	5.6	5.5
CFO/revenues	34.8	35.9	24.0	26.1	31.8	36.8	30.3	33.2	36.0	33.7
CFO/market capitalisation	4.4	5.2	2.8	4.2	6.2	8.2	6.2	7.9	9.5	9.6
CFO/capex	614.0	652.1	197.9	126.4	145.5	177.6	214.8	215.4	244.1	231.3
CFO/current liabilities	115.8	121.1	66.2	64.4	78.9	73.7	73.9	88.8	103.5	116.8
Cash conversion ratio	122.2	107.9	-137.6	4.3	62.3	-85.3	118.8	99.6	102.8	83.2
Capex/revenues	5.7	5.5	12.1	20.6	21.9	20.7	14.1	15.4	14.8	14.6
Capex/depreciation	744.0	791.7	1800.0	648.1	401.0	363.2	233.7	208.6	220.2	230.7
OpFCF margin	30.0	31.4	25.1	15.3	13.8	45.8	17.2	22.5	25.7	28.5
Total payout ratio	113.3	78.9	75.0	50.4	0.0	0.0	37.1	35.0	35.0	35.0
<i>Leverage and solvency (x)</i>										
Net debt/EBITDA	-0.85	-0.92	-0.74	0.13	-0.01	-0.55	-0.61	-0.79	-1.06	-1.20
Total debt/total capital (BV)	0.01	0.01	0.00	0.08	0.06	0.05	0.05	0.04	0.03	0.02
LTD / (LTD + equity (MV))	0.00	0.00	0.00	0.02	0.02	0.01	0.02	0.02	0.02	0.01
<i>Cash conversion cycle</i>										
Inventory turnover days	167.5	223.3	267.7	223.1	147.6	289.0	322.2	246.9	253.6	234.6
Receivables turnover days	74.7	66.2	96.1	106.8	120.2	104.7	86.5	75.3	62.4	53.2
Credit period	158.6	244.8	296.1	310.9	129.4	279.8	239.5	189.9	169.0	156.4
Cash conversion cycle	83.7	44.8	67.7	18.9	138.3	113.8	169.2	132.3	146.9	131.4

Source: Company (historical figures), DNB Markets (estimates)

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Important Information

Company: IAR Systems
 Coverage by Analyst: Joachim Gunell
 Date: 09-2-2023

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