

IAR SYSTEMS

The worst appears over

IAR Systems is gradually taking the necessary steps to turn around the soft operating momentum, which is likely to continue over the coming quarters. Having rebuilt our model to capture its revenue streams better, we have lowered our 2022–2023e net sales and EPS by ~3–8%, given the high drop-through from its 96%+ gross margins. We expect no overnight success but highlight that IAR Systems has invested 5+ years of profits in new products over the past five years that have yet to translate into tangible net sales growth. We reiterate our SEK130–220 fair value.

Ahead of Q1 results (due on April 26), we expect: organic net sales growth of 2% YOY with slight project delays while support and updates sales is still growing at a faster pace to set up sales of SEK96m. We forecast a 20.0% adj. EBIT margin (up 0.9%-points YOY), corresponding to a 'rule of 40' of 27.6% with 60% cash conversion.

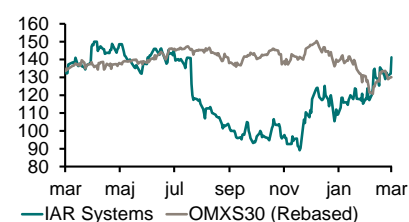
We have reduced our 2022–2023e net sales by ~3% and EPS by ~8% to reflect: 1) our rebuilt model, which includes new segments; 2) slightly slower acceleration of organic growth 2022; 3) reduced security expectations in 2023; and 4) slight worse FX than mid-February. Given IAR Systems' 96%+ gross margins, such net sales changes have a high drop-through on EPS. We now expect IAR to show 6% YOY organic net sales growth 2022 (11% total) and 26% adj. EBIT growth YOY, which, after flat organic growth over the past three years, should mark a trough.

SEK130–220 fair value reiterated, which at the mid-point corresponds to a 2023e EV/EBIT of 21x. We believe the worst is over and we are encouraged by the new management teams' swift actions (new management team, impairments, new revenue models and license systems, shifted compensation models for sales employees, etc.), although it will probably take a few quarters to complete the turnaround. We see additional potential growth if its RISC-V or security offering gain a commercial breakthrough. Its core development tools offering is trading at a 2023e FCF yield of 6%.

Year-end Dec	2018	2019	2020	2021	2022e	2023e	2024e
Revenue (SEKm)	385	406	372	358	395	448	498
EBITDA adj (SEKm)	143	146	133	238	145	176	212
EBIT adj (SEKm)	119	108	84	66	82	109	142
PTP (SEKm)	117	107	77	-69	79	106	139
EPS rep (SEK)	6.67	5.96	4.36	-4.94	4.48	6.03	7.89
EPS adj (SEK)	6.67	5.96	4.36	4.90	4.48	6.03	7.89
DPS (SEK)	5.00	3.00	0.00	0.00	1.57	2.11	2.76
Revenue growth (%)	11.7	5.3	-8.3	-3.8	10.4	13.3	11.4
EBITDA growth adj (%)	12.7	1.7	-9.0	79.4	-39.0	21.5	20.0
EPS growth adj (%)	5.3	-10.6	-26.8	12.5	-8.6	34.7	30.8
EBITDA margin adj (%)	37.2	35.9	35.7	66.5	36.7	39.4	42.5
EV/Sales adj (x)	8.32	6.30	5.12	4.32	4.61	3.96	3.43
EV/EBITDA adj (x)	22.4	17.5	14.3	6.5	12.5	10.1	8.1
EV/EBIT adj (x)	27.0	23.6	22.7	23.6	22.1	16.2	12.1
P/E adj (x)	36.4	31.2	32.1	24.0	31.5	23.4	17.9
P/Book (x)	6.02	4.28	3.11	2.74	2.98	2.72	2.45
ROE (%)	21.6	14.2	9.9	nm	9.9	12.2	14.4
ROCE (%)	28.1	17.7	12.4	9.9	12.4	15.3	18.0
Dividend yield (%)	2.1	1.6	0.0	0.0	1.1	1.5	2.0
FCF yield (%)	1.4	0.9	1.9	3.6	2.5	3.6	4.7

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

IARB versus OMXS30 (12m)



Source: Factset

SUMMARY

Share price (SEK)	141
Tickers	IARB SS

CAPITAL STRUCTURE

No. of shares (m)	13.7
No. of shares fully dil. (m)	13.7
Market cap. (SEKm)	1,927
NIBD adj end-2022e (SEKm)	-105
Enterprise value adj (SEKm)	1,822
Net debt/EBITDA adj (x)	-0.72
Free float (%)	100

Source: Company, DNB Markets (estimates)

NEXT EVENT

Q1 2022	26/04/2022
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ESTIMATE CHANGES (SEK)

Year-end Dec	2022e	2023e	2024e
Sales (old)	406.5	460.2	513.8
Sales (new)	395.2	447.6	498.4
Change (%)	-2.8	-2.7	-3.0
EPS (old)	4.97	6.43	8.43
EPS (new)	4.48	6.03	7.89
Change (%)	-10.0	-6.2	-6.4

Source: DNB Markets,

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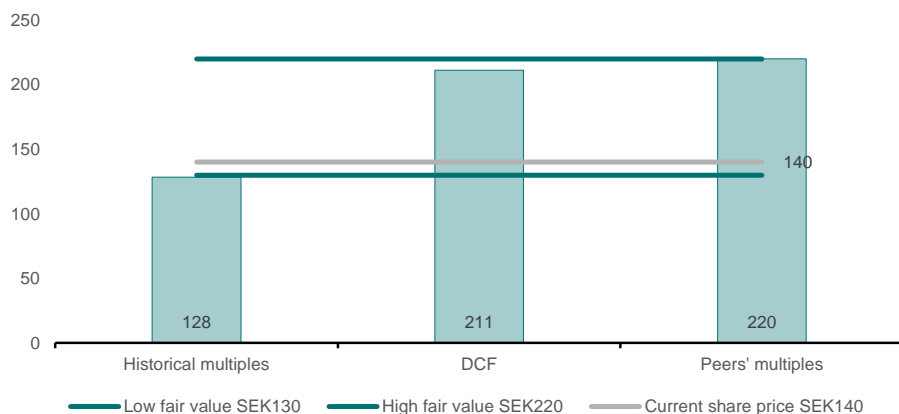
ANALYSTS

Joachim Gunell

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Overview

Valuation (SEK)



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 may 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.

Source: DNB Markets

Valuation methodology

- We continue to base our SEK130–220 fair value on our DCF, IAR Systems' historical valuation multiples, and peers' multiple regression analysis (methodology unchanged).
- On our estimates, IAR Systems is trading at 2024e P/E of 18x, EV/EBIT of 12x, and EV/sales of 3x.

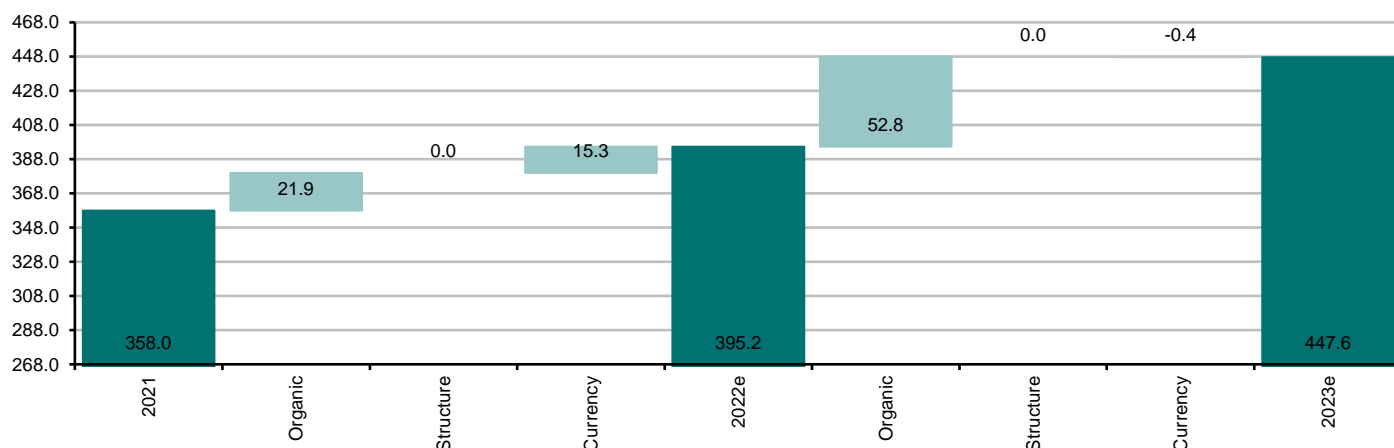
Source: DNB Markets

Upside risks to our fair value

- The company over-delivering 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 in microcontrollers.
- SaaS transition would support the revenue mix, lessen the cyclicity, and enhance investment profile.
- Participation in industry consolidation owing to the strategic importance of development tools.

Source: DNB Markets

Sales bridge 2021–2023e (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; a leading door-sensor provider, whose IP was stolen internally, which led to direct revenue loss, etc.
- 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.

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Q1 2022 preview

Figure 1: Q1 expectations

Key highlights (SEKm, except per share data)	Q1 2022e		Deviation	Deviation	Q1 2021	DNBe
	Actual	DNB	(%)	Absolute	Actual	2022e
Net sales		95.7			88.9	395.2
Gross profit		92.3			85.5	381.5
Gross margin		96.4%			96.2%	96.5%
One-offs		0			0	0
EBITDA adj.		34.3			29.8	145.2
EBITDA adj. margin		35.8%			33.5%	36.7%
EBIT		19.1			17.0	82.5
EBIT margin		20.0%			19.1%	20.9%
EBIT adj.		19.1			17.0	82.5
EBIT adj. margin		20.0%			19.1%	20.9%
EPS adj.		1.04			0.94	4.48
Adj. FCF (CFO - capex)		11.9			1.4	47.6
Cash conversion		62%			8%	58%
Rule of 40 (EBIT)		27.6%			15.4%	31.3%
Revenue growth YOY		7.6%			-3.7%	11.1%
Organic		1.6%			6.0%	6.1%
Structural		0.0%			0.0%	0.0%
FX		6.0%			-9.6%	5.0%
Segment (SEKm)		Q1 2022e	Deviation	Deviation	Q1 2021	DNBe
		Actual	(%)	Absolute	Actual	2022e
Net sales						
Development tools		95.5			88.6	393.8
Security solutions		0.2			0.3	1.4
Other		0.0			0.0	0.0
Total		95.7			88.9	395.2
Net sales growth						
Development tools		7.7%				344.5%
Security solutions		-27.4%				362.6%
Other						
Total		7.6%				344.5%
Net sales						
License-based		53.1			50.1	222.3
Support and software updates		38.1			34.7	154.9
Other		4.5			4.1	18.0
Total		95.7			88.9	395.2

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

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Estimate revisions

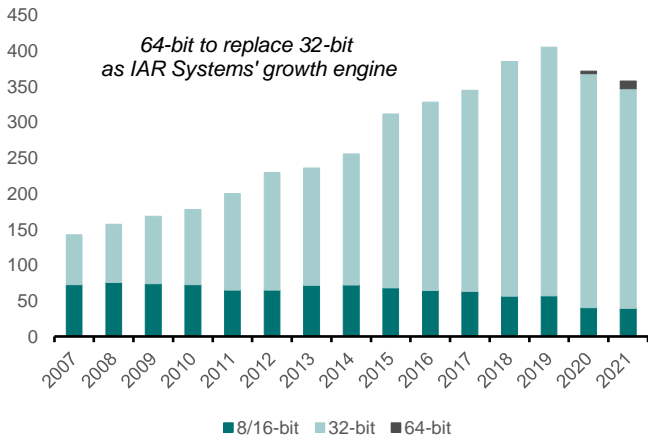
Figure 2: Forecast changes

(SEKm, except per share data)	Old			New			Change		
	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e
Net sales	406	460	514	395	448	498	-3%	-3%	-3%
Growth YOY, of which	14.2%	13.2%	11.7%	11.1%	13.3%	11.3%	-315bp	4bp	-31bp
Organic	8.4%	12.8%	11.7%	6.1%	13.4%	11.3%	-232bp	58bp	-31bp
Structural	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0bp	0bp	0bp
FX	5.8%	0.4%	0.0%	5.0%	-0.1%	0.0%	-82bp	-54bp	0bp
Gross profit	394	448	501	381	435	485	-3%	-3%	-3%
Gross margin	97.0%	97.3%	97.4%	96.5%	97.2%	97.4%	-43bp	-9bp	-5bp
EBITDA	160	187	225	145	176	212	-9%	-6%	-6%
IAC	0	0	0	0	0	0			
Adj. EBITDA	160	187	225	145	176	212	-9%	-6%	-6%
Depreciation and amortisation	-68	-68	-71	-63	-67	-70	-7%	-1%	-2%
EBIT	92	119	153	82	109	142	-10%	-8%	-7%
Adj. EBIT	92	119	153	82	109	142	-10%	-8%	-7%
Adj. EBIT margin	22.6%	25.8%	29.9%	20.9%	24.4%	28.5%	-170bp	-139bp	-137bp
Capitalised development costs (CDC)	n.a.	n.a.	n.a.	61	63	62			
EBIT excl. CDC	n.a.	n.a.	n.a.	5.4%	10.5%	16.0%			
Adj. Net profit	68	88	115	61	82	108	-10%	-6%	-6%
Adj. EPS (diluted)	4.97	6.43	8.43	4.48	6.03	7.89	-10%	-6%	-6%
DPS	1.74	2.25	2.95	1.57	2.11	2.76	-10%	-6%	-6%
Net sales by segment									
Development tools	405	443	474	394	436	465	-3%	-2%	-2%
Security solutions	1	17	40	1	11	33	-6%	-32%	-16%
Other	0	0	0	0	0	0			
Total	406	460	514	395	448	498	-3%	-3%	-3%
Net sales by product type									
License-based	n.a.	n.a.	n.a.	222	265	305			
Support and software updates	n.a.	n.a.	n.a.	155	164	174			
Other	n.a.	n.a.	n.a.	18	19	20			
Total	406	460	514	395	448	498	-3%	-3%	-3%
Balance sheet and cash flow									
Adj. FCF	57	74	104	48	69	92	-17%	-6%	-12%
Cash	161	211	284	145	193	256	-10%	-8%	-10%
Net cash (-) / net debt (+)	-133	-183	-256	-105	-153	-216	-21%	-16%	-16%

Source: DNB Markets

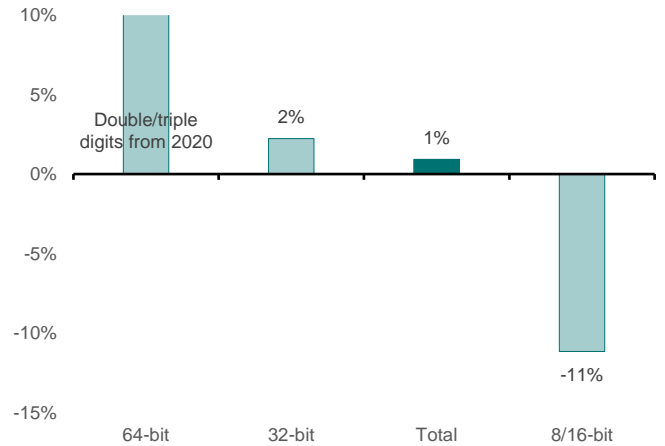
Key charts

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



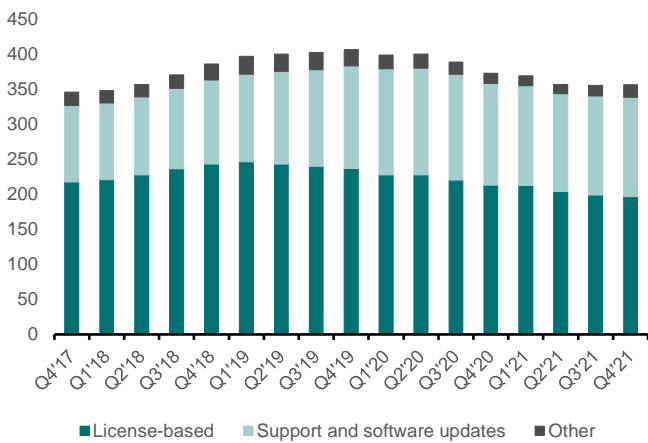
Source: Company (historical data), DNB Markets (further calculations)

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



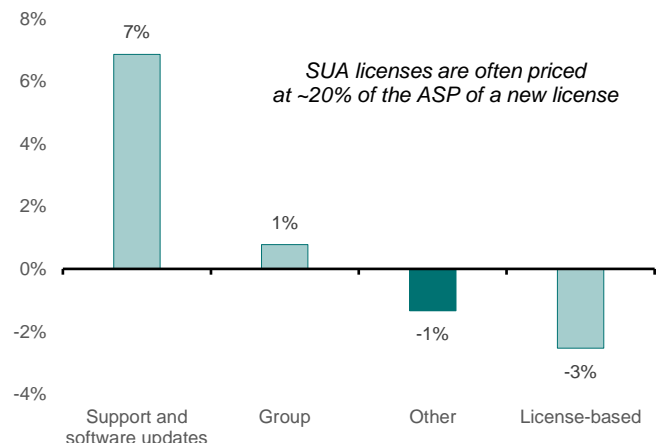
Source: Company (historical data), DNB Markets (further calculations)

Figure 5: Net sales mix by product type (LTM, 2017–2021)



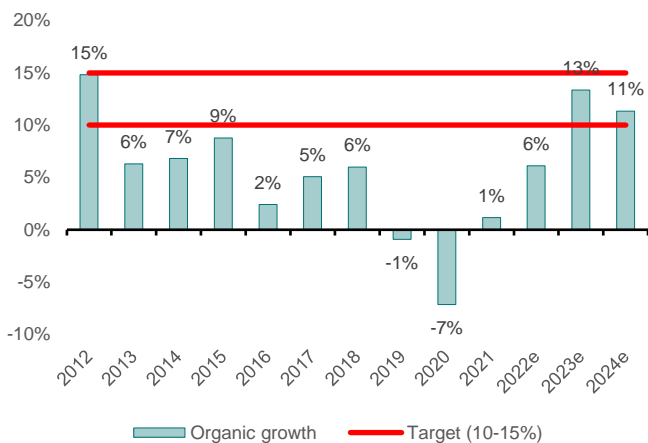
Source: Company (historical data), DNB Markets (further calculations)

Figure 6: Net sales CAGR by processor type (2016–2021)



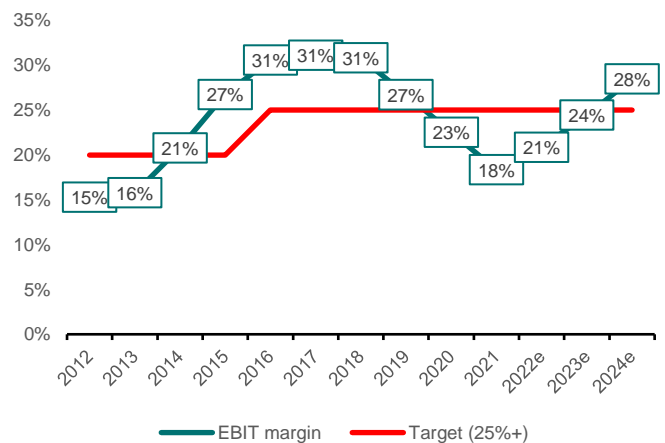
Source: Company (historical data), DNB Markets (further calculations)

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



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

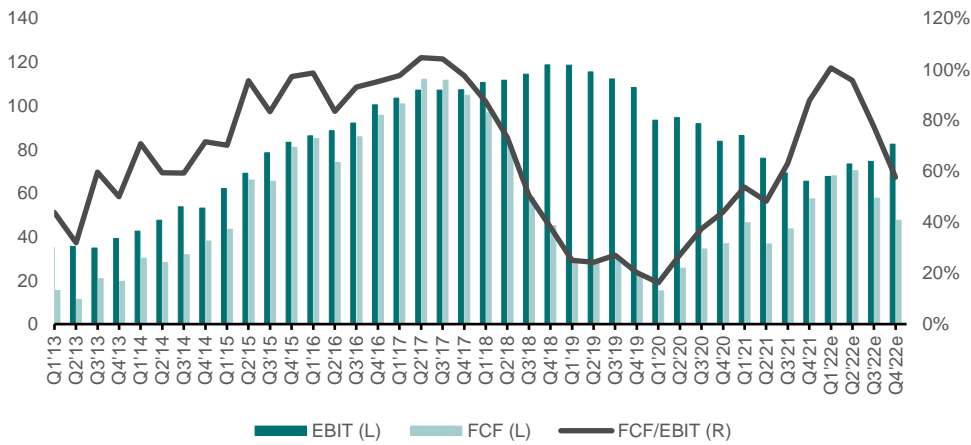
Figure 8: Financial goal 2 – EBIT margin >25%



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

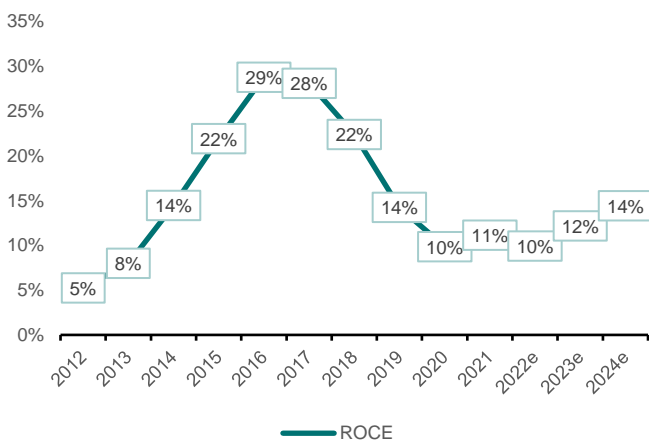
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Figure 9: LTM FCF versus LTM EBIT (2012-2022e) – coming out of an intense investment period to accelerate organic growth since 2018



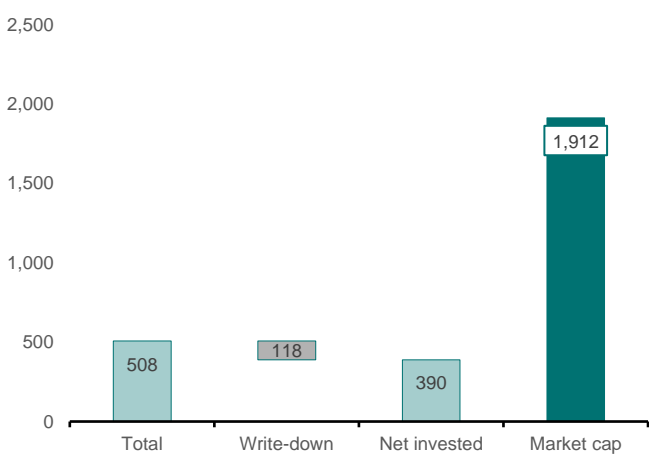
Source: DNB Markets (forecasts), company (historical data)

Figure 10: Return on capital employed (2012–2024e)



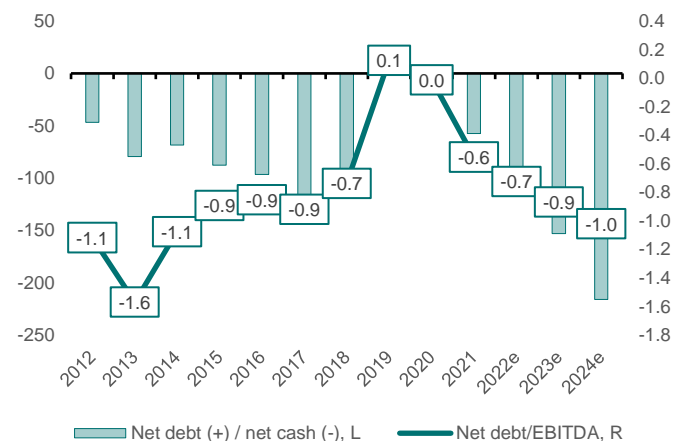
Source: DNB Markets (forecasts), company (historical data)

Figure 12: Investments (SEKm, 2016–2021)



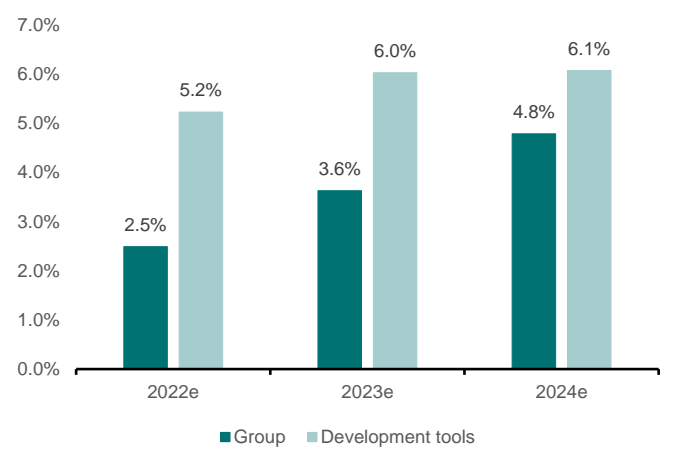
Source: Company (historical data), DNB Markets (forecasts and further calculations)

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



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

Figure 13: FCF yield (2022–2024e)



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

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Forecasts

Figure 14: Annual income statement and key items (SEKm, 2017–2024e)

(SEKm)	2017	2018	2019	2020	2021	2022e	2023e	2024e	21-24e CAGR
Net sales	345.0	385.2	405.6	372.0	355.8	395.2	447.6	498.4	12%
Growth YOY, of which	5%	10%	5%	-8%	-4%	11%	13%	11%	
Organic	5%	6%	-1%	-7%	1%	6%	13%	11%	
Structural	0%	0%	0%	0%	0%	0%	0%	0%	
FX	0%	4%	6%	-1%	-6%	5%	0%	0%	
COGS	-8.5	-9.0	-10.8	-14.1	-12.0	-13.7	-12.7	-13.2	
Gross profit	336.5	376.2	394.8	357.9	346.0	381.5	434.9	485.2	
Other external expenses	-49.2	-68.2	-63.7	-37.7	-38.3	-41.7	-45.5	-49.4	
Personnel costs	-160.1	-167.9	-185.3	-187.5	-203.8	-194.6	-213.0	-224.0	
EBITDA	127.2	140.1	145.8	132.7	103.9	145.2	176.4	211.8	
IAC	0.0	-3.2	0.0	0.0	-134.2	0.0	0.0	0.0	
Adj. EBITDA	127.2	143.3	145.8	132.7	238.1	145.2	176.4	211.8	
Depreciation and amortisation	-19.8	-24.5	-37.4	-48.9	-172.4	-62.8	-67.0	-69.8	
EBIT	107.4	115.6	108.4	83.8	-68.5	82.5	109.4	141.9	
Adj. EBIT	107.4	118.8	108.4	83.8	65.7	82.5	109.4	141.9	29%
Financial items	-1.7	-1.8	-1.4	-7.0	-0.1	-3.6	-3.2	-3.0	
Profit before tax	105.7	117.0	107.0	76.8	-68.6	78.9	106.2	138.9	
Taxes paid	-25.7	-26.2	-25.8	-17.4	1.2	-17.8	-23.9	-31.3	
Adj. Net profit	80.0	94.0	81.2	59.4	66.8	61.1	82.3	107.7	
EPS	6.33	6.67	5.96	4.36	-4.94	4.48	6.03	7.89	
Adj. EPS (diluted)	6.33	6.67	5.96	4.36	4.90	4.48	6.03	7.89	17%
DPS	5.00	5.00	3.00	0.00	0.00	1.57	2.11	2.76	
Margins									
Gross	97.5%	97.7%	97.3%	96.2%	96.6%	96.5%	97.2%	97.4%	
EBITDA	36.9%	36.4%	35.9%	35.7%	29.0%	36.7%	39.4%	42.5%	
Adj. EBITDA	36.9%	37.2%	35.9%	35.7%	66.5%	36.7%	39.4%	42.5%	
EBIT	31.1%	30.0%	26.7%	22.5%	-19.1%	20.9%	24.4%	28.5%	
Adj. EBIT	31.1%	30.8%	26.7%	22.5%	18.4%	20.9%	24.4%	28.5%	
FCF margin	25.0%	11.9%	5.4%	9.9%	16.1%	12.1%	15.5%	18.4%	
Rule of 40 (EBIT)	36.2%	42.5%	32.0%	14.2%	14.6%	31.3%	37.7%	39.8%	
ROCE	37.4%	28.1%	17.7%	12.4%	9.9%	12.4%	15.3%	18.0%	
Cash flow									
Cash flow from operating activities	123.9	92.6	105.7	118.4	131.6	121.3	149.4	174.8	
Capex	-19.0	-46.8	-83.6	-81.4	-74.1	-73.7	-79.9	-83.3	
Adj. FCF	104.9	45.8	22.1	37.0	57.5	47.6	69.4	91.5	17%
Cash conversion (FCF/EBIT)	98%	39%	20%	44%	88%	58%	63%	64%	
Balance sheet									
Cash	119.5	106.1	60.7	67.8	113.4	145.1	193.2	255.9	
Net cash (-) / net debt (+)	-117.0	-103.3	18.4	-1.5	-57.4	-105.1	-153.2	-215.9	
Net debt/EBITDA	-0.9x	-0.7x	0.1x	0.0x	-0.6x	-0.7x	-0.9x	-1.0x	

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

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Figure 15: Annual segment overview (SEKm, 2017–2024e)

(SEKm)	2017	2018	2019	2020	2021	2022e	2023e	2024e	21-24e CAGR
Net sales by segment									
Development tools	345.0	380.2	403.9	367.0	355.1	393.8	436.1	464.9	9%
Security solutions	0.0	5.0	1.7	5.0	0.7	1.4	11.5	33.5	263%
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Total	345.0	385.2	405.6	372.0	355.8	395.2	447.6	498.4	12%
Net sales growth by segment									
Development tools	5%	10%	6%	-9%	-3%	11%	11%	7%	
Security solutions			-66%	194%	-86%	98%	728%	192%	
Other									
Total	5%	10%	5%	-8%	-4%	11%	13%	11%	
Net sales by product									
License-based	217.3	242.9	236.3	212.4	196.1	222.3	265.1	305.1	16%
Support and softw are updates	108.6	119.4	146.3	145.2	141.6	154.9	163.7	173.7	7%
Other	19.1	22.9	23.0	14.4	18.1	18.0	18.8	19.6	3%
Total	345.0	385.2	405.6	372.0	355.8	395.2	447.6	498.4	12%
Net sales growth by product									
License-based		12%	-3%	-10%	-8%	13%	19%	15%	
Support and softw are updates		10%	23%	-1%	-2%	9%	6%	6%	
Other		20%	0%	-37%	26%	-1%	4%	4%	
Total	5%	10%	5%	-8%	-4%	11%	13%	11%	

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

Figure 16: Quarterly segment overview (SEKm, 2020-2022e)

(SEKm)	Q3'20	Q4'20	Q1'21	Q2'21	Q3'21	Q4'21	Q1'22e	Q2'22e	Q3'22e	Q4'22e
Net sales by segment										
Development tools	88.5	89.5	88.6	87.2	87.8	91.5	95.5	97.6	97.7	103.1
Security solutions	0.4	1.2	0.3	0.2	0.1	0.1	0.2	0.3	0.4	0.5
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	88.9	90.7	88.9	87.4	90.0	91.6	95.7	97.9	98.1	103.6
Net sales growth by segment										
Development tools	-11%	-16%	-3%	-11%	-1%	2%	8%	12%	11%	13%
Security solutions	33%	300%	-67%	-92%	-75%	-92%	-27%	31%	304%	404%
Other										
Total	-11%	-15%	-4%	-13%	-1%	1%	8%	12%	11%	13%
Net sales by product										
License-based	50.8	52.0	50.1	50.4	46.2	49.4	53.1	55.9	54.1	59.2
Support and softw are updates	35.5	35.3	34.7	33.9	36.9	36.1	38.1	37.4	39.5	39.9
Other	2.6	3.4	4.1	3.1	4.8	6.1	4.5	4.5	4.5	4.5
Total	88.9	90.7	88.9	87.4	90.0	91.6	95.7	97.9	98.1	103.6
Net sales growth by product										
License-based	-13%	-12%	-1%	-15%	-9%	-5%	6%	11%	17%	20%
Support and softw are updates	-2%	-14%	-7%	-8%	4%	2%	10%	10%	7%	11%
Other	-52%	-45%	-5%	-24%	85%	79%	10%	45%	-6%	-26%
Total	-11%	-15%	-4%	-13%	-1%	1%	8%	12%	11%	13%

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

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Figure 17: Quarterly income statement and key items (SEKm, 2020–2022e)

(SEKm)	Q3'20	Q4'20	Q1'21	Q2'21	Q3'21	Q4'21	Q1'22e	Q2'22e	Q3'22e	Q4'22e
Net sales	88.9	90.7	88.9	87.4	90.0	91.6	95.7	97.9	98.1	103.6
Grow th YOY, of w hich	-11%	-15%	-4%	-13%	-1%	1%	8%	12%	11%	13%
Organic	-6%	-11%	6%	-2%	-1%	2%	2%	6%	7%	9%
Structural	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
FX	-6%	-4%	-10%	-10%	0%	-1%	6%	6%	4%	4%
COGS	-2.7	-4.0	-3.4	-2.7	-2.8	-3.0	-3.4	-3.4	-3.4	-3.5
Gross profit	86.2	86.7	85.5	84.7	87.2	88.6	92.3	94.5	94.7	100.1
Other external expenses	-8.5	-7.2	-7.4	-10.4	-8.5	-12.0	-10.0	-10.7	-10.5	-10.5
Personnel costs	-40.9	-47.0	-48.3	-48.3	-43.9	-63.4	-48.0	-48.0	-48.6	-50.0
EBITDA	36.8	32.5	29.8	26.0	34.8	13.2	34.3	35.8	35.6	39.6
IAC	0.0	0.0	0.0	-2.0	2.1	-134.2	0.0	0.0	0.0	0.0
Adj. EBITDA	36.8	32.5	29.8	28.0	32.7	147.4	34.3	35.8	35.6	39.6
Depreciation and amortisation	-11.4	-13.5	-12.8	-13.3	-14.1	-132.2	-15.1	-15.3	-15.8	-16.4
EBIT	25.4	19.0	17.0	12.7	20.7	-119.0	19.1	20.5	19.8	23.1
Adj. EBIT	25.4	19.0	17.0	14.7	18.6	15.2	19.1	20.5	19.8	23.1
Financial items	-0.5	-4.5	-0.6	-1.2	-0.3	1.8	-0.9	-0.9	-0.9	-0.9
Profit before tax	24.9	14.5	16.4	11.5	20.4	-117.2	18.2	19.6	18.9	22.2
Taxes paid	-6.2	-2.5	-3.6	-2.2	-4.7	11.8	-4.0	-4.1	-4.8	-4.9
Adj. Net profit	18.7	12.0	12.8	11.3	13.6	28.8	14.2	15.4	14.1	17.4
EPS	1.37	0.88	0.94	0.68	1.17	-7.72	1.04	1.13	1.03	1.27
Adj. EPS (diluted)	1.37	0.88	0.94	0.83	1.00	2.11	1.04	1.13	1.03	1.27
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Margins										
Gross	97.0%	95.6%	96.2%	96.9%	96.9%	96.7%	96.4%	96.5%	96.5%	96.6%
EBITDA	41.4%	35.8%	33.5%	29.7%	38.7%	14.4%	35.8%	36.6%	36.3%	38.2%
Adj. EBITDA	41.4%	35.8%	33.5%	32.0%	36.3%	160.9%	35.8%	36.6%	36.3%	38.2%
EBIT	28.6%	20.9%	19.1%	14.5%	23.0%	-129.9%	20.0%	20.9%	20.1%	22.3%
Adj. EBIT	28.6%	20.9%	19.1%	16.8%	20.7%	16.6%	20.0%	20.9%	20.1%	22.3%
FCF margin	16.6%	10.6%	1.6%	12.6%	24.1%	25.5%	12.5%	13.5%	9.3%	12.9%
Rule of 40 (EBIT)	17.5%	5.9%	15.4%	4.1%	21.9%	17.6%	27.6%	32.9%	29.1%	35.4%
ROCE	13.5%	12.3%	12.5%	10.8%	9.7%	9.3%	9.8%	10.9%	11.3%	12.3%
Cash flow										
Cash flow from operating activities	32.7	27.8	22.0	27.7	41.4	40.5	29.2	31.7	27.5	32.9
Capex	-17.9	-18.2	-20.6	-16.7	-19.7	-17.1	-17.3	-18.4	-18.4	-19.6
Adj. FCF	14.8	9.6	1.4	11.0	21.7	23.4	11.9	13.2	9.1	13.4
Cash conversion (FCF/EBIT)	58%	51%	8%	75%	117%	154%	62%	65%	46%	58%
Balance sheet										
Cash	65.7	67.8	66.8	72.2	91.3	113.4	121.4	130.7	135.8	145.1
Net cash (-) / net debt (+)	0.4	-1.5	-3.0	-13.8	-36.4	-57.4	-69.4	-82.7	-91.8	-105.1
Net debt/EBITDA	0.0x	0.0x	0.0x	-0.1x	-0.3x	-0.6x	-0.6x	-0.7x	-0.8x	-0.7x

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

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Valuation

Figure 18: Valuation approaches (SEKm, %)

	Peers regression	DCF	Historical Average
Net sales (2022e)			395
Adj. EBIT (2022e)			82
Adj. EPS (2022e)			4.48
Sales CAGR (2021–2023e)	14.0		11.8
Adj. EBIT margin (2022e)	25.3		20.9
RO40 (22e)	44.8		32.7
Target multiple	RO40, P/B, EV/S	10% WACC	20x EV/EBIT
Enterprise value	2,901	2,781	1,649
Net debt (+) / cash (-)	-105	-105	-105
Equity value	3,006	2,886	1,755
NOSH	13.7	13.7	13.7
Implied price/share	220	211	128
Implied potential	57%	51%	-8%
2024e valuation multiples			
Implied EV/sales	5.8	5.6	3.3
Implied EV/EBIT	20.4	19.6	11.6
Implied P/E	27.9	26.8	16.3

Source: DNB Markets

Figure 19: Implied valuation multiples based on current share price

(SEKm)	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
Net sales	328	345	385	406	372	356	395	448	498
Growth YOY	5.4%	5.1%	10.2%	5.2%	-8.3%	-4.4%	11.1%	13.3%	11.3%
Gross profit	316	337	376	395	358	346	381	435	485
Gross margin	96.3%	97.5%	97.7%	97.3%	96.2%	96.6%	96.5%	97.2%	97.4%
Adj. EBITDA	117	127	140	146	133	104	145	176	212
EBITDA margin	36.9%	36.9%	37.2%	35.9%	35.7%	66.5%	36.7%	39.4%	42.5%
Adj. EBIT	101	107	119	108	84	66	82	109	142
EBIT margin	30.6%	31.1%	30.8%	26.7%	22.5%	18.4%	20.9%	24.4%	28.5%
Adj. Net profit	82	80	94	81	59	67	61	82	108
Adj. FCF	95	105	46	22	37	58	48	69	92
FCF margin	29.0%	30.4%	11.9%	5.4%	9.9%	16.2%	12.1%	15.5%	18.4%
Cash conversion	95%	98%	39%	20%	44%	88%	58%	63%	64%
Rule of 40 (EBIT)	36.0%	36.2%	41.0%	31.9%	14.2%	14.0%	31.9%	37.7%	39.8%
ROCE	35.0%	37.4%	28.1%	17.7%	12.4%	9.9%	12.4%	15.3%	18.0%
ROIC	27.4%	28.5%	21.9%	13.8%	10.1%	10.4%	10.0%	12.2%	14.4%
Market cap	2,602	2,387	3,310	2,535	1,905	1,606	1,914	1,914	1,914
Net debt	-97	-117	-103	18	-1	-57	-105	-153	-216
Enterprise value	2,505	2,270	3,206	2,554	1,904	1,548	1,809	1,761	1,698
EV/Sales	7.6x	6.6x	8.3x	6.3x	5.1x	4.4x	4.6x	3.9x	3.4x
EV/EBIT	24.9x	21.1x	27.0x	23.6x	22.7x	23.6x	21.9x	16.1x	12.0x
P/E	31.7x	29.8x	35.2x	31.2x	32.1x	24.0x	31.3x	23.2x	17.8x
FCF yield	3.7%	4.4%	1.4%	0.9%	1.9%	3.6%	2.5%	3.6%	4.8%

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

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Figure 20: EV/sales 12-month forward IAR Systems (2018–2022)



Source: Bloomberg

Figure 21: EV/EBITDA 12-month forward IAR Systems (2018–2022)



Source: Bloomberg

Figure 22: EV/EBIT 12-month forward IAR Systems (2018–2022)



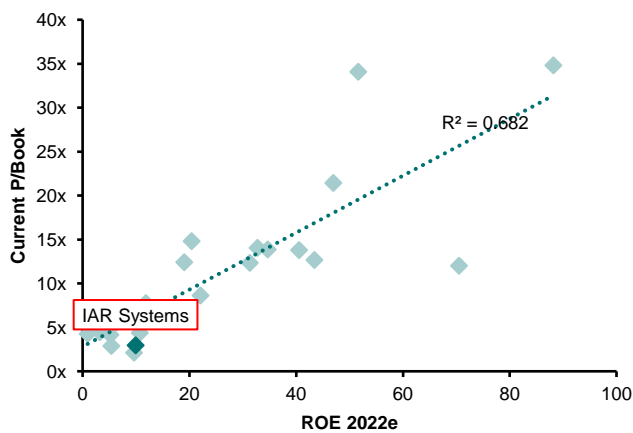
Source: Bloomberg

Figure 23: P/E 12-month forward IAR Systems (2018–2022)



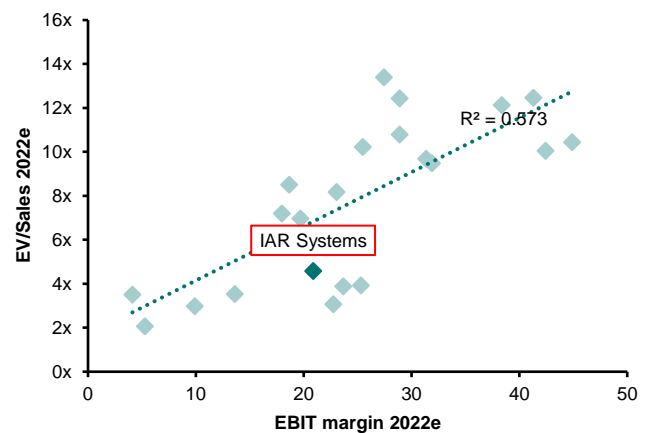
Source: Bloomberg

Figure 24: Current P/book versus ROE 2022e



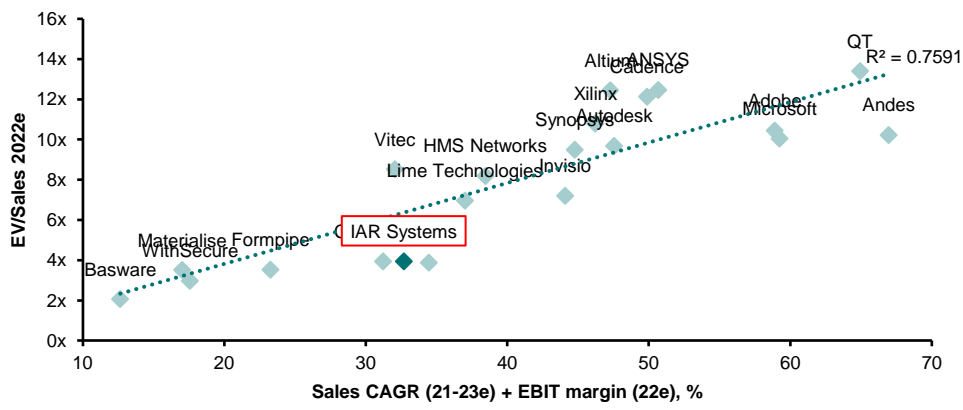
Source: Bloomberg (underlying data), DNB Markets (further calculations)

Figure 25: EV/sales versus EBIT margin (2022e)



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

Figure 26: EV/sales 2022e 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)			2022 yield (%)		ROE (%)		EBIT margin		CAGR 2021-2023e (%)		
	(SEKbn)	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e	DPS	FCF	2022e	2023e	2022e	2023e	Sales	EBIT	EPS	
IAR Systems (DNBe)	1.9	31	23	18	22	16	12	12	10	8	5	4	3	1.1	2.5	10	12	20.9	24.4	12	29	11	
Premium/discount		-50%	-39%	-40%	-47%	-46%	-50%	-57%	-56%	-57%	-50%	-50%	-50%										
IAR Systems (Cons.)	1.9	28	22	17							5	4	4	1.2	2.5	11	13	22.6	25.9	14	35	37	
Premium/discount		-55%	-43%	-44%	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	-50%	-49%	-47%										
Nordic software																							
Basware	3.2	323	54	25	42	24	14	15	12	9	2	2	2		3.9	1	9	5.3	8.3	7	46		
Enea	4.2	17	15	13	17	14	12	11	9	8	4	4	4	1.2	5.3	10	11	23.7	26.4	11	17	9	
Formpipe	2.0	38	29	24	29	22	18	16	14	12	4	4	3	2.1	0.5	11	14	13.6	15.9	10	19	39	
HMS Networks	20.7	49	45	41	38	34	31	32	29	27	9	8	8	0.8	2.0	33	28	23.0	23.4	15	16	15	
Invisio	7.1	72	44	33	47	33	24	40	27	20	8	7	6	0.7	1.2	20	28	18.0	21.3	26	117	123	
Karnov	6.5	19	17	14	18	15	23	15	12	12	4	3	3	2.3		5	7	22.8	22.2	61	44	20	
Lime Technologies	3.7	41	33	29	41	32	26	25	21	18	8	7	6	0.9	2.1	47	47	19.7	21.4	17	21	21	
QT	31.4	82	55	38	65	42	28	59	40	27	18	13	10	0.1	1.4	52	48	27.4	30.6	37	55	55	
Vitec	16.6	49	42	36	51	42	35	26	22	19	9	9	8	0.5	0.9	12	13	18.6	20.1	13	17	13	
WithSecure	8.7	34	28	23	32	23	18	21	16	13	3	3	3	1.0	3.6	18	21	9.9	12.1	8	22	23	
Engineering software																							
Adobe	1,988.8	33	28	24		23	19		21	17	12	10	9	0.0	3.5	41	41	44.9	45.2	14	13	14	
Altium	30.8	69	56	44	50	40	31	42	35	28	14	12	10	1.5	1.3	19	22	28.9	30.7	18	18	17	
Andes	6.6	81	42		55	28		38	22		14	10		1.0	1.3	5	10	25.5	35.8	41	81	60	
ANSYS	262.7	41	37	34	33	30	30	31	28	27	14	12	12	0.0	2.0	14	14	41.3	42.4	9	11	10	
Autodesk	445.1	44	33	27	35	25	21	34	24	20	11	10	8	0.0	3.0	88	128	31.4	36.6	16	32	31	
Cadence	422.4	43	38	34	34	29	25	31	27	23	13	12	11	1.2	2.4	35	32	38.3	39.7	12	15	14	
CDK Global	52.8	16	15	13							4	4	4	1.2		71	64	25.3	27.6	6		13	
Materialise	10.3	147	85	47	96	56	32	30	23	18	4	4	3	0.0	0.7	3	5	4.1	6.2	13	34	11	
Microsoft	21,598.8	33	29	25	27	23	19	23	20	16	11	10	9	0.8	2.8	43	39	42.4	42.7	17	19	17	
Synopsys	478.4	43	37	32	32	27	23	30	26	21	11	9	9		2.7	22	22	31.9	33.4	13	18	16	
Xilinx	450.0	44	40	37							12	11	10	0.2	2.6	31	28	28.9	31.2	17	31	26	
Average	1,231.0	63	38	30	41	30	24	29	23	19	9	8	7	0.8	2.3	28	30	25.0	27.3	18	32	27	
Median	20.7	43	37	31	37	28	24	30	22	19	9	9	8	0.8	2.1	20	22	25.3	27.6	14	20	17	

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

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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 embedded systems (computer hardware and software designed for a specific function) that enable the development and ensures the code quality in 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, we note that it has said it captures ~40% market share for commercial tools, and we note ample prospects for the market to show a mid-to-high single-digit CAGR over the medium term owing to: 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 the demand for more powerful software development tools.

Market dynamics benefiting the market leader

IAR Systems' key competitive advantages in our view stem from: 1) its complete toolchain for product developers across 8-, 16-, 32-, and 64-bit processors; 2) as it is independent, it can 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 shortages); and 3) superior industrial-quality, as its commercial customers cannot compromise tools' code performance, reliability, user-friendliness, or time-to-market by using inferior technologies, such as open-source alternatives. IAR Systems' solutions create code 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 such as an acceleration of its most promising new product launches: 1) digging where they stand with its existing 32-bit customers (~80% of 2021 sales) and migrating them into 64-bit; 2) broader RISC-V adoption; and 3) IoT security taking off. With ~95% customer retention, we believe it could scale with its existing customer base, which, in combination with 96%+ gross margins, provides a highly scalable cost structure over the coming years that could lend a tailwind to significant margin expansion at a high cash conversion.

Early leader in two of the embedded industry's hottest 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 large market potential to emerge as an early leader into 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 forced a SEK116m write-down of intangible assets in 2021). We expect a broader adoption over the coming years from securing IP being seen as a business imperative; increasingly stringent security legislation and 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 62bn units in 2025e and a ~USD70m–80m RISC-V tools market for a 40%+ CAGR to 2025e, where IAR should gain a sizeable share.

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Summary of negatives

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 licenses or be stuck in a single technology from one vendor.

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. That said, C++ is a language relatively hard to master and as developers often understand all the bits and bytes, 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 prove too costly and do not materialise as 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. That said, as organic growth abated IAR Systems underwent the most comprehensive investment phase in its nearly 40 year-long history, investing SEK500m+ over the past five years in its security offering, 64-bit support, and RISC-V tools. We believe these investment levels 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 that IAR Systems stands to reap the fruit of these investments. Instead, IAR Systems' 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 against its most important currencies (USD, EUR, JPY) as well as the GBP and KRW by ~10%, 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 versus traditional on-premises perpetual licence delivery models, since the SaaS model 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 several tens of thousands in SEK for its high-end license products. That said, such a transition would probably be 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, given it has the broadest support in the market for different processor vendors and design architectures.

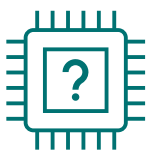
Business overview

IAR Systems was founded in 1983 by engineer Anders Rundgren and provides world-leading software for programming processors in embedded systems (computer system that is designed to perform a dedicated function in 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, you interact 30+ times a day with a product that is programmed by one IAR Systems' 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, Miele, etc.

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



Before a processor can be used in a product, it needs to be programmed with the correct instructions.



Product developers use IAR Embedded Workbench to program the processor and give it the correct instructions to control the finished product.



Once the processor has been programmed, it is ready for the finished product.

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

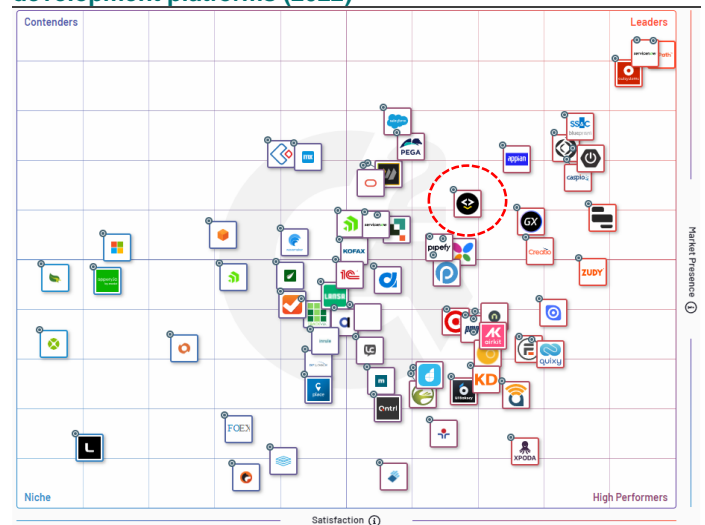
Headquartered in Uppsala, Sweden IAR Systems has 200+ employees in 15 offices at three continents with technical support teams in its customers' local time zones in 10+ languages. Its independent software supports more than 14,000 different processors from more than 70 different processor vendors, which 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, which 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

Long-standing embedded industry partnerships

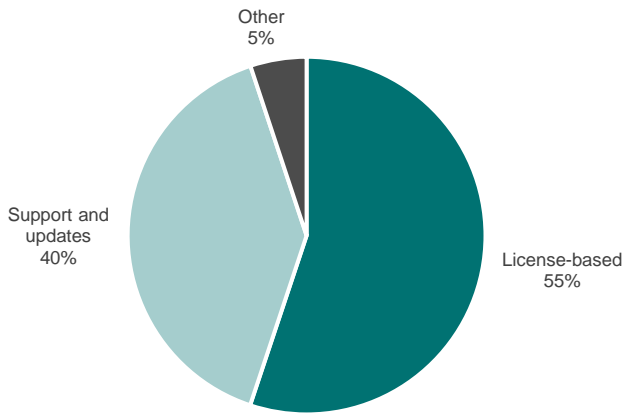
Security Foundation etc.); 3) services vendors (Cloud services vendors, programming companies, etc.); and 4) suppliers of integrated programs (real-time operating systems, graphics development, etc.).

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 is dependent on selling new licenses to facilitate growing net sales, we believe.

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

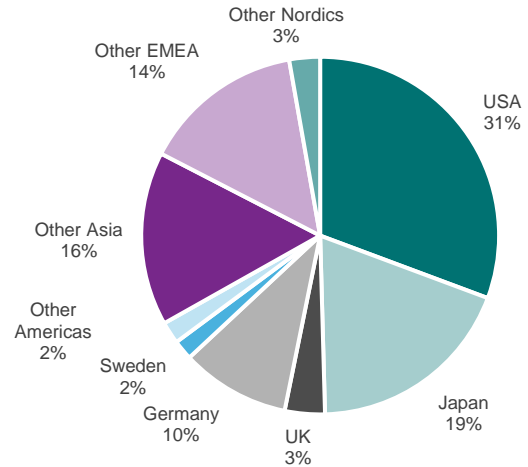
- **Development tools (~100% of net sales)** consists of IAR Embedded Workbench 8- to 64-bit) with world-leading code optimisation technology, compiler, debugger probes and analysis tools (ensuring code quality and coding standards), functional safety certifications (pre-certified build tools), RISV-V architecture, and Linux offering for continuous integration.
- **Security solutions (~0%)**, consists of: 1) Embedded Trust for the security specialist in an organisation sets security guidelines in accordance with company policy; 2) C-Trust makes it possible for developers to prepare encrypted code that automatically follows the prevailing security guidelines; and 3) Secure Desktop Provisioner helps its OEM customers to securely program 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 remains lucrative for IAR, especially in device production as opposed to product development (royalty-based instead of licences), but it will probably take time before security regulation and standards really affect the marketplace.

Figure 31: Net sales by revenue stream (2021)



Source: Company

Figure 32: Geographical net sales split (2021)



Source: Company

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Forecast changes – P&L

(SEKm)	New			Old			Change		
	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e
Revenues	395	448	498	406	460	514	-11	-13	-15
Cost of sales	-14	-13	-13	-12	-13	-13	-1	0	0
Gross profit	381	435	485	394	448	501	-13	-13	-15
Operating expenses	-236	-258	-273	-235	-261	-276	-2	2	3
EBITDA	145	176	212	160	187	225	-14	-10	-13
EBITDA adj	145	176	212	160	187	225	-14	-10	-13
EBITDA margin (%)	36.7	39.4	42.5	39.2	40.6	43.7	-2.5	-1.2	-1.2
Depreciation	-21	-23	-24	-5	-6	-7	-17	-17	-17
Amortisation	-42	-45	-46	-63	-62	-64	22	18	18
EBIT	82	109	142	92	119	153	-9	-9	-11
EBIT adj	82	109	142	92	119	153	-9	-9	-11
Net financial items	-4	-3	-3	-4	-5	-4	0	2	1
PBT	79	106	139	88	114	149	-9	-8	-11
Taxes	-18	-24	-31	-20	-26	-34	3	2	3
Minorities	0	0	0	0	0	0	0	0	0
Net profit	61	82	108	68	88	115	-7	-5	-7
Adjustments to net profit	0	0	0	0	0	0	0	0	0
Net profit adj	61	82	108	68	88	115	-7	-5	-7
<i>Per share data (SEK)</i>									
EPS	4.48	6.03	7.89	4.97	6.43	8.43	-0.50	-0.40	-0.54
EPS adj	4.48	6.03	7.89	4.97	6.43	8.43	-0.50	-0.40	-0.54
DPS ordinary	1.57	2.11	2.76	1.74	2.25	2.95	-0.17	-0.14	-0.19
DPS	1.57	2.11	2.76	1.74	2.25	2.95	-0.17	-0.14	-0.19
<i>Other key metrics (%)</i>									
Revenue growth	10.4	13.3	11.4	14.2	13.2	11.7	-3.8	0.0	-0.3
EBIT adj growth	25.5	32.7	29.7	39.7	29.6	29.0	-14.1	3.1	0.7
EPS adj growth	-8.6	34.7	30.8	1.5	29.3	31.1	-10.1	5.4	-0.3
Avg. number of shares (m)	14	14	14	14	14	14	0	0	0
Capex	-74	-80	-83	-72	-73	-75	-2	-7	-9
OpFCF	72	97	128	87	114	150	-16	-17	-21
Working capital	-27	-27	-25	101	160	241	-128	-187	-265
NIBD adj	-105	-153	-216	-133	-183	-256	28	30	40

Source: DNB Markets

Forecast changes – By segment and assumptions

(SEKm)	New			Old			Change		
	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e
Assumptions									
Revenue org. % YOY	6.12	13.36	11.35	8.44	12.78	11.66	-2.32	0.58	-0.31
Structure impact % YOY	0.00	0.00	0.00		0.00	0.00		0.00	0.00
Currency impact % YOY	4.96	-0.10	0.00	5.78	0.43	0.00	-0.82	-0.54	0.00

Source: DNB Markets

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Quarterly numbers

(SEKm)	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022e	Q2 2022e	Q3 2022e	Q4 2022e	Q1 2023e
Revenues	89	91	89	87	90	92	96	98	98	104	108
Cost of sales	-3	-4	-3	-3	-3	-3	-3	-3	-3	-4	-3
Gross profit	86	87	86	85	87	89	92	94	95	100	105
Operating expenses	-49	-54	-56	-59	-52	-75	-58	-59	-59	-61	-63
EBITDA	37	33	30	26	35	13	34	36	36	40	42
Depreciation	-5	-5	-5	-5	-5	-5	-5	-5	-5	-5	-5
Amortisation	-7	-8	-8	-8	-9	-127	-10	-10	-11	-11	-11
EBIT	25	19	17	13	21	-119	19	20	20	23	25
Net financial items	-1	-5	-1	-1	0	2	-1	-1	-1	-1	-1
PBT	25	15	16	12	20	-117	18	20	19	22	25
Taxes	-6	-3	-4	-2	-5	12	-4	-4	-5	-5	-6
Minorities	0	0	0	0	0	0	0	0	0	0	0
Net profit	19	12	13	9	16	-105	14	15	14	17	19
Adjustments to net profit	0	0	0	2	-2	134	0	0	0	0	0
Net profit adj	19	12	13	11	14	29	14	15	14	17	19
Dividend paid	0	0	0	0	0	0	0	0	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	1.37	0.88	0.94	0.68	1.17	-7.72	1.04	1.13	1.03	1.27	1.40
EPS adj	1.37	0.88	0.94	0.83	1.00	2.11	1.04	1.13	1.03	1.27	1.40
DPS ordinary	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
<i>Growth and margins (%)</i>											
Revenues, QOQ growth	-11.2	2.0	-2.0	-1.7	3.0	1.8	4.4	2.3	0.3	5.6	4.2
Revenues, YOY growth	-11.1	-15.1	-3.7	-12.7	1.2	1.0	7.6	12.0	9.0	13.1	12.8
EPS adj, YOY growth	-13.4	-40.0	15.4	-35.8	-27.3	140.0	11.2	36.5	3.8	-39.6	34.0
Gross margin	97.0	95.6	96.2	96.9	96.9	96.7	96.4	96.5	96.5	96.6	97.1
EBITDA adj margin	41.4	35.8	33.5	32.0	36.3	160.9	35.8	36.6	36.3	38.2	38.8
Depreciation/revenues	-5.4	-6.0	-5.5	-5.9	-5.7	-5.7	-5.4	-5.5	-5.4	-5.3	-5.0
EBIT adj margin	28.6	20.9	19.1	16.8	20.7	16.6	20.0	20.9	20.1	22.3	23.5
Net profit margin	21.0	13.2	14.4	10.6	17.4	nm	14.9	15.8	14.4	16.8	17.7

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

Adjustments to quarterly numbers

(SEKm)	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022e	Q2 2022e	Q3 2022e	Q4 2022e	Q1 2023e
EBITDA	37	33	30	26	35	13	34	36	36	40	42
EBITDA adj	37	33	30	28	33	147	34	36	36	40	42
EBIT	25	19	17	13	21	-119	19	20	20	23	25
Other EBIT adjustments	0	0	0	-2	2	-134	0	0	0	0	0
EBIT adj	25	19	17	15	19	15	19	20	20	23	25
Net profit	19	12	13	9	16	-105	14	15	14	17	19
Other EBIT adjustments	0	0	0	-2	2	-134	0	0	0	0	0
Net profit adj	19	12	13	11	14	29	14	15	14	17	19

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

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Quarterly numbers by segment and assumptions

(SEKm)	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022e	Q2 2022e	Q3 2022e	Q4 2022e	Q1 2023e
Assumptions											
Revenue org. % YOY	-5.60	-10.77	5.96	-2.40	-0.67	1.98	1.64	5.97	7.22	9.48	13.27
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	-5.50	-4.31	-9.64	-10.29	-0.45	-0.99	5.98	6.00	4.11	3.58	-0.43

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

Annual P&L

(SEKm)	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
Revenues	312	328	345	385	406	372	358	395	448	498
Cost of sales	-10	-12	-9	-9	-11	-14	-12	-14	-13	-13
Gross profit	301	316	337	376	395	358	346	381	435	485
Operating expenses	-203	-203	-209	-236	-249	-225	-242	-236	-258	-273
EBITDA	98	113	127	140	146	133	104	145	176	212
Depreciation	-3	-3	-2	-3	-13	-20	-20	-21	-23	-24
Amortisation	-12	-14	-17	-22	-25	-29	-152	-42	-45	-46
EBIT	83	97	107	116	108	84	-69	82	109	142
Net financial items	0	0	-2	-2	-1	-7	0	-4	-3	-3
PBT	83	100	106	117	107	77	-69	79	106	139
Taxes	-20	-22	-26	-26	-26	-17	1	-18	-24	-31
Effective tax rate (%)	24	22	24	22	24	23	2	23	23	23
Minorities	0	0	0	0	0	0	0	0	0	0
Net profit	63	78	80	91	81	59	-67	61	82	108
Adjustments to net profit	0	4	0	3	0	0	134	0	0	0
Net profit adj	63	82	80	94	81	59	67	61	82	108
Dividend paid	-63	-88	-63	-68	-68	0	0	0	-21	-29
Avg. number of shares	13	13	13	14	14	14	14	14	14	14
<i>Per share data (SEK)</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.48	6.03	7.89
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.48	6.03	7.89
DPS ordinary	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.57	2.11	2.76
DPS	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.57	2.11	2.76
<i>Growth and margins (%)</i>										
Revenue growth	21.9	5.4	5.1	11.7	5.3	-8.3	-3.8	10.4	13.3	11.4
EPS adj growth	50.2	23.0	2.6	5.3	-10.6	-26.8	12.5	-8.6	34.7	30.8
Gross margin	96.7	96.3	97.5	97.7	97.3	96.2	96.6	96.5	97.2	97.4
EBITDA margin	31.5	34.5	36.9	36.4	35.9	35.7	29.0	36.7	39.4	42.5
EBITDA adj margin	31.5	35.7	36.9	37.2	35.9	35.7	66.5	36.7	39.4	42.5
Depreciation/revenues	-0.8	-0.8	-0.7	-0.7	-3.2	-5.5	-5.7	-5.4	-5.0	-4.8
EBIT margin	26.8	29.4	31.1	30.0	26.7	22.5	nm	20.9	24.4	28.5
EBIT adj margin	26.8	30.6	31.1	30.8	26.7	22.5	18.4	20.9	24.4	28.5
PBT margin	26.7	30.5	30.6	30.4	26.4	20.6	nm	20.0	23.7	27.9
Net profit margin	20.3	23.8	23.2	23.6	20.0	16.0	nm	15.5	18.4	21.6

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

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Adjustments to annual P&L

(SEKm)	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
EBITDA	98	113	127	140	146	133	104	145	176	212
EBITDA adj	98	117	127	143	146	133	238	145	176	212
EBIT	83	97	107	116	108	84	-69	82	109	142
Other EBIT adjustments	0	-4	0	-3	0	0	-134	0	0	0
EBIT adj	83	101	107	119	108	84	66	82	109	142
Net profit	63	78	80	91	81	59	-67	61	82	108
Other EBIT adjustments	0	-4	0	-3	0	0	-134	0	0	0
Net profit adj	63	82	80	94	81	59	67	61	82	108
<i>Per share data (SEK)</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.48	6.03	7.89
Recommended adjustment	0.00	0.00	0.00	0.00	0.00	0.00	9.85	0.00	0.00	0.00
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.48	6.03	7.89

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

Cash flow

(SEKm)	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
Net profit	63	78	80	91	81	59	-67	61	82	108
Depreciation and amortisation	15	17	20	25	37	49	172	63	67	70
Cash flow from operations (CFO)	99	114	124	93	106	118	132	121	149	175
Capital expenditure	-19	-19	-19	-47	-84	-81	-74	-74	-80	-83
Acquisitions/Investments	0	0	0	-171	-19	0	0	0	0	0
Divestments	1	0	0	0	0	0	0	0	0	0
Cash flow from investing (CFI)	-18	-19	-38	-218	-102	-81	-74	-74	-80	-83
Free cash flow (FCF)	80	95	86	-125	4	37	58	48	69	92
Net change in debt	0	0	0	0	30	6	1	0	0	0
Dividends paid	-63	-88	-63	-68	-68	0	0	0	-21	-29
Share issue (repurchase)	0	0	0	172	0	0	0	0	0	0
Other	0	0	0	4	-14	-30	-16	-16	0	0
Cash flow from financing (CFF)	-64	-88	-63	108	-52	-25	-15	-16	-21	-29
Total cash flow (CFO+CFI+CFF)	17	7	23	-17	-49	12	42	32	48	63
<i>FCFF calculation</i>										
Free cash flow	80	95	86	-125	4	37	58	48	69	92
Less: tax shields/other	0	0	0	0	0	0	0	0	0	0
Less: acquisitions	0	0	0	171	19	0	0	0	0	0
Less: divestments	-1	0	0	0	0	0	0	0	0	0
Growth (%)										
CFO	40.4	15.7	8.5	-25.3	14.1	12.0	11.1	-7.8	23.1	17.0
CFI	42.3	-3.3	-98.9	-478.5	53.0	20.4	9.0	0.6	-8.5	-4.2
FCF	108.3	18.5	-9.4	-244.7	102.8	957.1	55.4	-17.2	45.8	31.8
CFF	-19.5	-39.0	28.5	270.4	-148.3	52.7	38.6	-6.0	-33.7	-34.7
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)	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
Assets	399	396	410	722	825	834	813	869	939	1,017
Inventories	5	6	5	7	7	6	10	10	10	11
Trade receivables	44	48	51	63	67	59	59	62	70	74
Other receivables	20	19	12	38	52	64	44	54	55	53
Current financial assets	0	0	0	0	0	0	0	0	0	0
Cash and cash equivalents	89	99	120	106	61	68	113	145	193	256
Current assets	158	172	187	214	186	196	226	271	328	393
Property, plant and equipment	7	6	6	9	7	8	15	16	16	17
Other intangible assets	192	197	194	484	624	624	567	577	589	602
Deferred tax assets	37	16	3	13	5	4	3	3	3	3
Non-current financial assets	5	5	20	2	2	3	3	3	3	3
Non-current assets	241	224	223	508	639	638	587	598	611	624
Total assets	399	396	410	722	825	834	813	869	939	1,017
Equity and liabilities	399	396	410	722	825	834	813	869	939	1,017
Total equity	291	280	290	550	592	613	585	646	707	786
Trade payables	5	5	6	7	9	5	9	11	10	11
Other payables and accruals	83	92	86	131	117	111	133	142	152	151
Short-term debt	1	1	1	0	25	18	18	18	18	18
Total current liabilities	90	99	102	140	164	150	179	189	199	198
Long-term debt	1	2	2	1	41	32	20	4	4	4
Deferred tax liabilities	17	15	14	30	27	37	28	28	28	28
Other non-current liabilities	1	1	2	2	1	1	1	1	1	1
Total non-current liabilities	18	18	17	32	69	70	49	33	33	33
Total liabilities	108	116	120	172	233	220	228	222	232	231
Total equity and liabilities	399	396	410	722	825	834	813	869	939	1,017
<i>Key metrics</i>										
Net interest bearing debt	-88	-97	-117	-103	18	-2	-57	-105	-153	-216

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

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Valuation ratios

(SEKm)	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
<i>Enterprise value</i>										
Share price (SEK)	150.00	206.00	189.00	243.00	186.00	139.80	117.80	141.20	141.20	141.20
Number of shares (m)	12.63	12.63	12.63	13.62	13.63	13.63	13.63	13.65	13.65	13.65
Market capitalisation	1,895	2,602	2,387	3,310	2,535	1,905	1,606	1,927	1,927	1,927
Net interest bearing debt	-88	-97	-117	-103	18	-2	-57	-105	-153	-216
Adjustments to NIBD	0	0	0	0	0	0	0	0	0	0
Net interest bearing debt adj	-88	-97	-117	-103	18	-2	-57	-105	-153	-216
EV	1,807	2,505	2,270	3,206	2,554	1,904	1,548	1,822	1,774	1,711
EV adj	1,807	2,505	2,270	3,206	2,554	1,904	1,548	1,822	1,774	1,711
<i>Valuation</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.48	6.03	7.89
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.48	6.03	7.89
DPS ordinary	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.57	2.11	2.76
DPS	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.57	2.11	2.76
P/E	29.9	33.4	29.8	36.4	31.2	32.1	-23.8	31.5	23.4	17.9
P/E adj	29.9	33.4	29.8	36.4	31.2	32.1	24.0	31.5	23.4	17.9
P/B	6.51	9.31	8.22	6.02	4.28	3.11	2.74	2.98	2.72	2.45
Average ROE	21.9%	27.3%	28.1%	21.6%	14.2%	9.9%	-11.2%	9.9%	12.2%	14.4%
Earnings yield adj	3.3%	3.0%	3.4%	2.7%	3.2%	3.1%	4.2%	3.2%	4.3%	5.6%
Dividend yield	3.3%	3.4%	2.6%	2.1%	1.6%	0.0%	0.0%	1.1%	1.5%	2.0%
Free cash flow yield	4.2%	3.7%	3.6%	-3.8%	0.1%	1.9%	3.6%	2.5%	3.6%	4.7%
EV/SALES	5.80	7.63	6.58	8.32	6.30	5.12	4.32	4.61	3.96	3.43
EV/SALES adj	5.80	7.63	6.58	8.32	6.30	5.12	4.32	4.61	3.96	3.43
EV/EBITDA	18.4	22.1	17.8	22.9	17.5	14.3	14.9	12.5	10.1	8.1
EV/EBITDA adj	18.4	21.4	17.8	22.4	17.5	14.3	6.5	12.5	10.1	8.1
EV/EBIT	21.7	26.0	21.1	27.7	23.6	22.7	-22.6	22.1	16.2	12.1
EV/EBIT adj	21.7	24.9	21.1	27.0	23.6	22.7	23.6	22.1	16.2	12.1
EV/capital employed	6.2	8.9	7.8	5.8	3.8	2.8	2.4	2.7	2.4	2.1
EV/NOPLAT	27.8	33.3	27.1	35.6	30.2	29.1	-29.0	28.3	20.8	15.5
EV/OpFCF (taxed)	29.8	32.8	26.8	45.6	66.6	57.9	10.4	34.1	24.5	17.6

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

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Key accounting ratios

	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
<i>Profitability (%)</i>										
ROA	16.4	19.6	19.9	16.0	10.5	7.2	-8.2	7.3	9.1	11.0
ROCE	28.6	35.0	37.4	28.1	17.7	12.4	9.9	12.4	15.3	18.0
ROCE after tax	22.3	27.3	29.1	21.9	13.8	9.7	7.8	9.7	11.9	14.1
<i>Return on invested capital (%)</i>										
Net PPE/revenues	2.1	1.9	1.8	2.3	1.8	2.0	4.1	4.0	3.7	3.4
Working capital/revenues	-6.1	-7.5	-6.9	-7.8	-0.2	3.4	-8.3	-6.9	-6.1	-4.9
<i>Cash flow ratios (%)</i>										
FCF/revenues	25.8	29.0	25.0	-32.4	0.9	9.9	16.1	12.1	15.5	18.4
FCF yield (%)	4.2	3.7	3.6	1.4	0.9	1.9	3.6	2.5	3.6	4.7
CFO/revenues	31.7	34.8	35.9	24.0	26.1	31.8	36.8	30.7	33.4	35.1
CFO/market capitalisation	5.2	4.4	5.2	2.8	4.2	6.2	8.2	6.3	7.7	9.1
CFO/capex	508.8	614.0	652.1	197.9	126.4	145.5	177.6	164.6	186.9	209.9
CFO/current liabilities	110.2	115.8	121.1	66.2	64.4	78.9	73.7	64.1	75.2	88.2
Cash conversion ratio	126.8	122.2	107.9	-137.6	4.3	62.3	-85.3	77.9	84.3	85.0
Capex/revenues	6.2	5.7	5.5	12.1	20.6	21.9	20.7	18.6	17.9	16.7
Capex/depreciation	776.0	744.0	791.7	1800.0	648.1	401.0	363.2	346.7	355.2	349.4
OpFCF margin	25.3	30.0	31.4	25.1	15.3	13.8	45.8	18.1	21.6	25.8
Total payout ratio	99.6	113.3	78.9	75.0	50.4	0.0	0.0	35.0	35.0	35.0
<i>Leverage and solvency (x)</i>										
Net debt/EBITDA	-0.89	-0.85	-0.92	-0.74	0.13	-0.01	-0.55	-0.72	-0.87	-1.02
Total debt/total capital (BV)	0.00	0.01	0.01	0.00	0.08	0.06	0.05	0.02	0.02	0.02
LTD / (LTD + equity (MV))	0.00	0.00	0.00	0.00	0.02	0.02	0.01	0.00	0.00	0.00
<i>Cash conversion cycle</i>										
Inventory turnover days	180.7	167.5	223.3	267.7	223.1	147.6	289.0	257.5	292.3	292.4
Receivables turnover days	74.5	74.7	66.2	96.1	106.8	120.2	104.7	107.1	101.7	92.7
Credit period	170.1	158.6	244.8	296.1	310.9	129.4	279.8	280.9	292.3	292.4
Cash conversion cycle	85.1	83.7	44.8	67.7	18.9	138.3	113.8	83.7	101.7	92.7

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

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Important Information

Company: IAR Systems
 Coverage by Analyst: Joachim Gunell
 Date: 29/03/2022

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