

IAR SYSTEMS

Soft start to 2023

IAR Systems' Q1 results were soft and missed our adj. EBIT forecast by 38% as it ramped up its sales organisation. We reiterate our SEK140–250 fair value as we appreciate the combination of being net cash positive, defensive elements from ~40% recurring revenues, and optionality from its embedded security offering. We note that insiders have accumulated shares at the current share-price levels in 2022–2023.

Weak Q1. IAR reported Q1 organic sales growth of 5% YOY (from 7% YOY in Q4 and 11% in Q3), which led to net sales 4% below our forecast in light of longer sales cycles. The positive surprise was 33% organic growth YOY in license-based sales and deferred income up 29% YOY. Adj. EBIT was 38% below our forecast (12.2% margin, down 4.6%-points YOY), suggesting a 20% decline YOY due to SEK4.2m less capitalised development costs, while hiring ~10 additional sales representatives QOQ to accelerate growth in the coming quarters. Cash flow from operations declined 9% YOY to set up an LTM cash conversion of 91% and net cash of SEK93m at end-Q1.

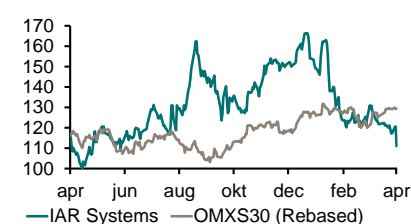
2023–2024e net sales and adj. EBITDA lowered by 3% and 14–7%, respectively, of which ~50% stems from negative FX (IAR has a high sensitivity to SEK movement, given its 97%+ gross margin and fixed cost base) and the rest reflecting lower organic growth assumptions and new sales hires. IAR's cost review should yield ~SEK25m in net annual savings in 2023 YOY, but we expect opex to increase by SEK22m YOY in 2023, baking in conservatism, and now forecast 7% YOY organic sales growth for 2023 (while it will implement ~5% price hikes in H2, we believe).

Fair value of SEK140–250 reiterated, corresponding to a 2023e EV/EBIT of 15–28x. IAR Systems is trading at a 15x 2023e EV/EBIT (or 13x EV/EBIT and 8.0% FCF yield, excluding Secure Thingz). We believe management's ambitious ramp-up of security sales for 2023e could be 2–3x higher than our forecasts, but should it not materialise, we believe IAR could make a strategic review to lessen the ~SEK60m/year drag on cash flows, with either outcome potentially acting as a catalyst for the business.

Year-end Dec	2019	2020	2021	2022	2023e	2024e	2025e
Revenue (SEKm)	406	372	358	423	462	511	556
EBITDA adj (SEKm)	146	133	238	133	155	199	230
EBIT adj (SEKm)	108	84	66	79	90	127	152
PTP (SEKm)	107	77	-69	74	79	115	140
EPS rep (SEK)	5.96	4.36	-4.94	4.23	4.19	6.39	7.85
EPS adj (SEK)	5.96	4.36	4.90	4.50	4.68	6.89	8.34
DPS (SEK)	3.00	0.00	0.00	1.50	1.64	2.41	2.92
Revenue growth (%)	5.3	-8.3	-3.8	18.1	9.3	10.6	8.8
EBITDA growth adj (%)	1.7	-9.0	79.4	-44.3	16.7	28.5	15.7
EPS growth adj (%)	-10.6	-26.8	12.5	-8.2	4.2	47.0	21.2
EBITDA margin adj (%)	35.9	35.7	66.5	31.4	33.5	38.9	41.4
EV/Sales adj (x)	6.30	5.12	4.32	4.67	3.00	2.59	2.27
EV/EBITDA adj (x)	17.5	14.3	6.5	14.9	9.0	6.7	5.5
EV/EBIT adj (x)	23.6	22.7	23.6	24.9	15.5	10.4	8.3
P/E adj (x)	31.2	32.1	24.0	33.4	23.7	16.1	13.3
P/Book (x)	4.28	3.11	2.74	3.08	2.14	1.96	1.79
ROE (%)	14.2	9.9	nm	9.2	8.3	11.8	13.2
ROCE (%)	17.7	12.4	9.9	11.5	11.9	15.9	17.8
Dividend yield (%)	1.6	0.0	0.0	1.0	1.5	2.2	2.6
FCF yield (%)	0.9	1.9	3.6	3.3	4.7	5.6	6.3

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

IARB versus OMXS30 (12m)



Source: Factset

SUMMARY

Share price (SEK)	111
Tickers	IARB SS

CAPITAL STRUCTURE

No. of shares (m)	13.7
No. of shares fully dil. (m)	13.8
Market cap. (SEKm)	1,516
NIBD adj end-2023e (SEKm)	-128
Enterprise value adj (SEKm)	1,388
Net debt/EBITDA adj (x)	-0.83
Free float (%)	100

Source: Company, DNB Markets (estimates)

NEXT EVENT

Q2 2023	17/08/2023
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ESTIMATE CHANGES (SEK)

Year-end Dec	2023e	2024e	2025e
Sales (old)	476.1	527.0	571.9
Sales (new)	462.0	510.9	555.8
Change (%)	-2.9	-3.1	-2.8
EPS adj (old)	6.22	7.99	9.64
EPS adj (new)	4.68	6.89	8.34
Change (%)	-24.7	-13.8	-13.4

Source: DNB Markets,

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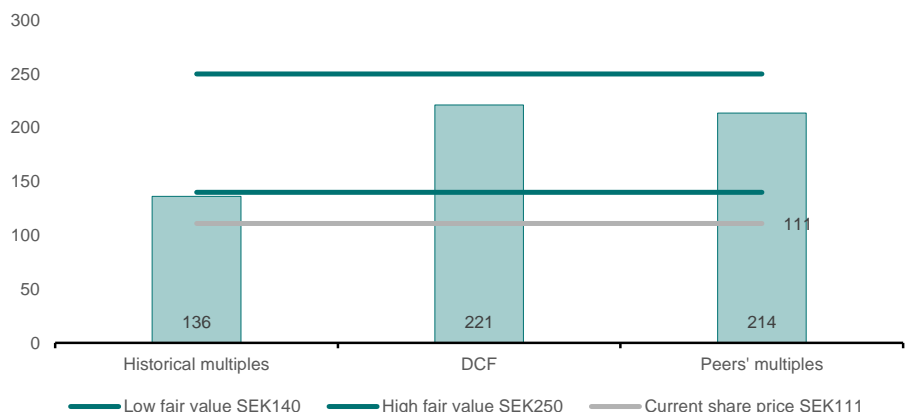
ANALYSTS

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 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

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 16x, EV/EBIT of 10x, and EV/sales of 3x.

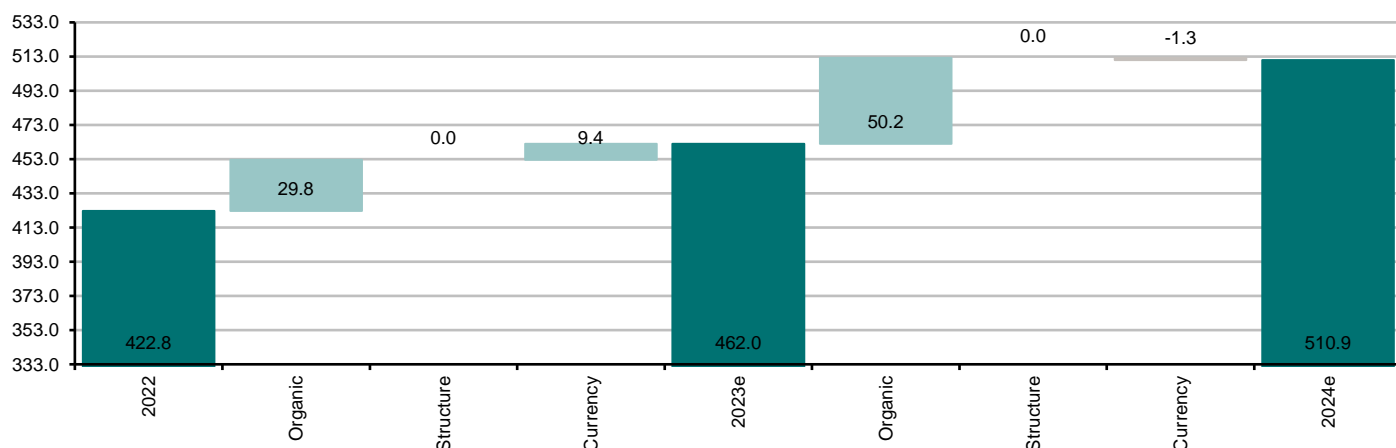
Source: DNB Markets

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.

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Q1 results

Figure 1: Q1 results versus expectations

Key highlights (SEKm, except per share data)	Q1 2023		Deviation	Deviation	Q1 2022	DNBe
	Actual	DNB	(%)	Absolute	Actual	2023e
Net sales	107.7	111.9	-4%	-4	97.4	461.1
Gross profit	104.5	108.5	-4%	-4	95.5	448.0
Gross margin	97.0%	97.0%	0.1pp		98.0%	97.2%
One-offs	-1.7	0		-2	1	-7
EBITDA adj.	27.0	37.1	-27%	-10	30.2	147.9
EBITDA adj. margin	25.1%	33.1%	-8.1pp		31.0%	32.1%
EBIT	11.4	21.0	-46%	-10	16.3	89.8
EBIT margin	10.6%	18.7%	-8.2pp		16.7%	19.5%
EBIT adj.	13.1	21.0	-38%	-8	16.3	89.8
EBIT adj. margin	12.2%	18.7%	-6.6pp		16.7%	19.5%
EPS adj.	0.47	1.11	-57%	-0.64	0.81	4.68
Adj. FCF (CFO - capex)	16.0	19.0	-16%	-3	15.4	71.7
Cash conversion	122%	91%	31.6pp		94%	80%
Rule of 40 (EBIT)	22.7%	32.6%	-9.8pp		27.2%	28.7%
Revenue growth YOY	10.6%	14.7%	-4.2pp		9.6%	10.0%
Organic	4.5%	8.3%	-3.8pp		3.0%	7.1%
Structural	0.0%	0.0%	0pp		0.0%	0.0%
FX	6.1%	6.4%	-0.3pp		6.5%	3.0%
Segment	Q1 2023		Deviation	Deviation	Q1 2022	DNBe
(SEKm)	Actual	DNB	(%)	Absolute	Actual	2023e
Net sales						
Development tools	107.3	111.3	-4%	-4	97.0	450.6
Security solutions	0.4	0.6	-36%	0	0.4	10.5
Other	0.0	0.0	n.a.	0	0.0	0.0
Total	107.7	111.9	-4%	-4	97.4	461.1
Net sales growth						
Development tools	10.6%	14.7%	-4.1pp		9.5%	7.7%
Security solutions	0.0%	56.5%	-56.5pp		33.3%	601.8%
Other						
Total	10.6%	14.7%	-4.2pp		9.6%	10.0%
Net sales						
License-based	72.4	63.4	14%	9	52.0	271.5
Support and softw are updates	33.3	43.9	-24%	-11	41.2	172.3
Other	2.0	4.7	-57%	-3	4.2	17.3
Total	107.7	111.9	-4%	-4	97.4	461.1

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

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Estimate revisions

Figure 2: Estimate changes

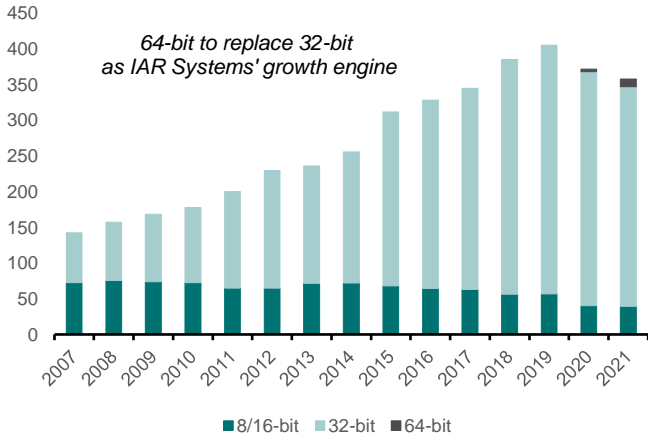
(SEKm, except per share data)	Old			New			Change		
	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
Net sales	476	527	572	462	511	556	-3%	-3%	-3%
Growth YOY, of which	12.6%	10.7%	8.5%	10.0%	10.6%	8.8%	-259bp	-12bp	27bp
Organic	7.9%	10.4%	8.5%	7.1%	10.9%	8.8%	-82bp	43bp	27bp
Structural	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0bp	0bp	0bp
FX	4.7%	0.3%	0.0%	3.0%	-0.3%	0.0%	-177bp	-55bp	0bp
Gross profit	462	513	558	448	496	541	-3%	-3%	-3%
Gross margin	97.0%	97.3%	97.5%	97.0%	97.1%	97.4%	-5bp	-16bp	-14bp
EBITDA	180	213	246	148	192	223	-18%	-10%	-9%
IAC	0	0	0	-7	-7	-7			
Adj. EBITDA	180	213	246	155	199	230	-14%	-7%	-7%
Depreciation and amortisation	-65	-67	-72	-60	-65	-71	-8%	-3%	-2%
EBIT	116	146	174	83	120	145	-28%	-18%	-16%
Adj. EBIT	116	146	174	90	127	152	-22%	-13%	-13%
Adj. EBIT margin	24.3%	27.6%	30.4%	18.0%	23.5%	26.2%	-630bp	-412bp	-427bp
Capitalised development costs (CDC)	56	56	59	53	54	56	-6%	-3%	-6%
EBIT excl. CDC	12.5%	17.1%	20.1%	8.0%	14.3%	17.4%	-450bp	-275bp	-273bp
Adj. Net profit	85	109	132	64	94	114	-25%	-14%	-13%
Adj. EPS (diluted)	6.22	7.99	9.64	4.68	6.89	8.34	-25%	-14%	-13%
DPS	2.18	2.80	3.37	1.64	2.41	2.92	-25%	-14%	-13%
Net sales by segment									
Development tools	461	492	517	451	480	504	-2%	-3%	-2%
Security solutions	15	35	55	11	31	52	-29%	-11%	-7%
Other	0	0	0	0	0	0			
Total	476	527	572	462	511	556	-3%	-3%	-3%
Net sales by product type									
License-based	275	321	357	271	308	344	-1%	-4%	-4%
Support and software updates	181	185	193	172	183	191	-5%	-1%	-1%
Other	20	21	22	17	20	21	-13%	-2%	-2%
Total	476	527	572	462	511	556	-3%	-3%	-3%
Balance sheet and cash flow									
Adj. FCF	85	112	109	72	85	95	-15%	-24%	-13%
Cash	204	279	342	188	242	297	-8%	-13%	-13%
Net cash (-) / net debt (+)	-143	-225	-297	-128	-191	-253	-10%	-15%	-15%

Source: DNB Markets

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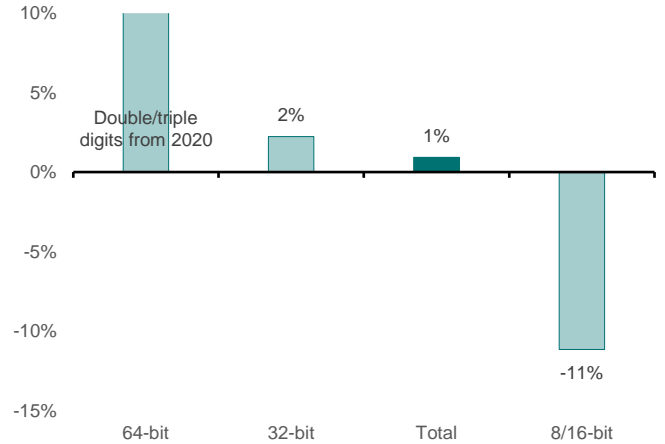
Key charts

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



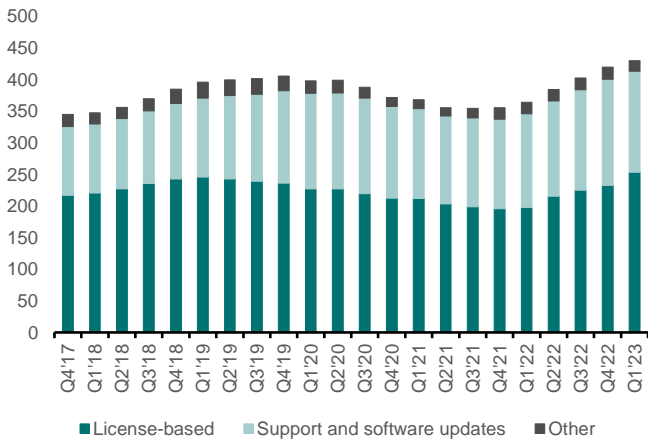
Source: Company (historical data), DNB Markets (further calculations)

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



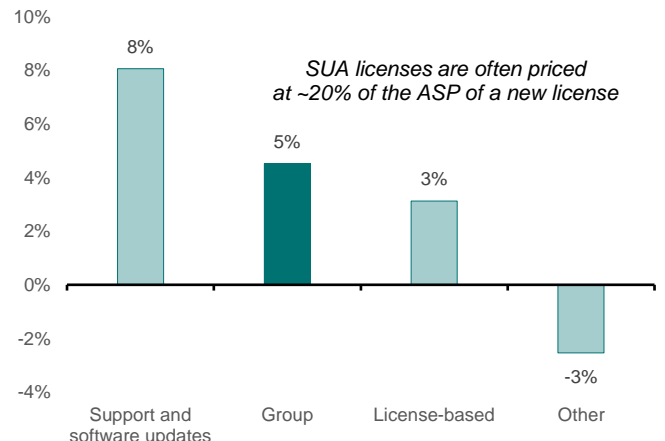
Source: Company (historical data), DNB Markets (further calculations)

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



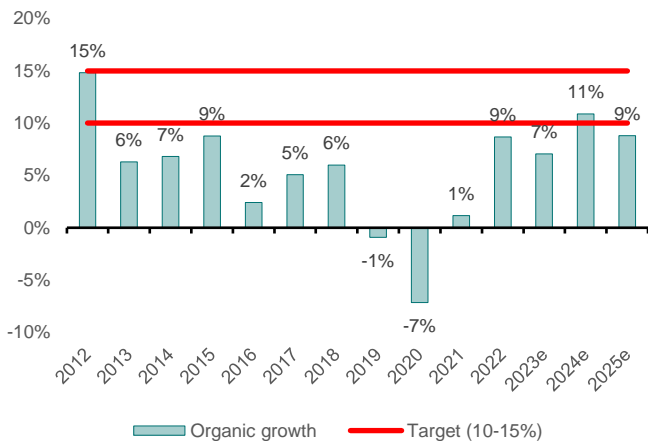
Source: Company (historical data), DNB Markets (further calculations)

Figure 6: Net sales CAGR by processor type (2017–2023)



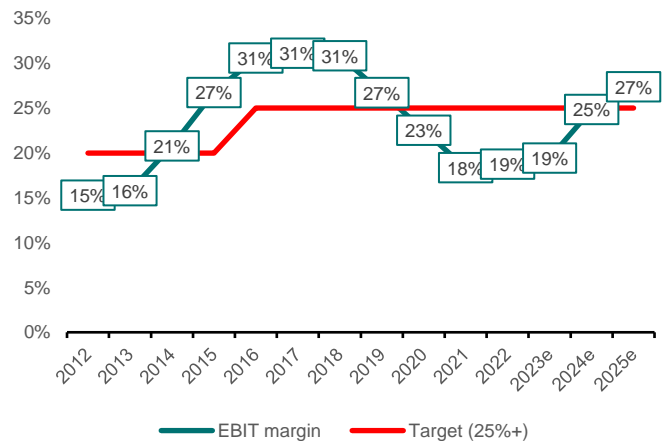
Source: Company (historical data), DNB Markets (further calculations)

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



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

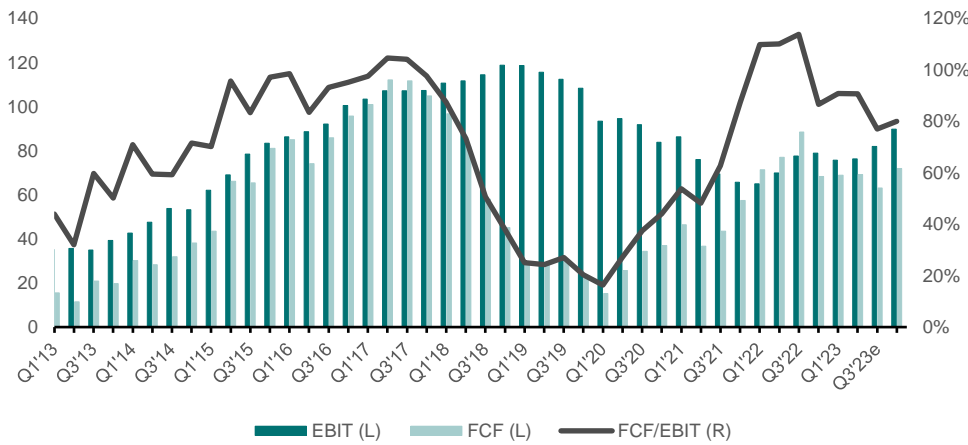
Figure 8: Financial goal 2 – EBIT margin >25%



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

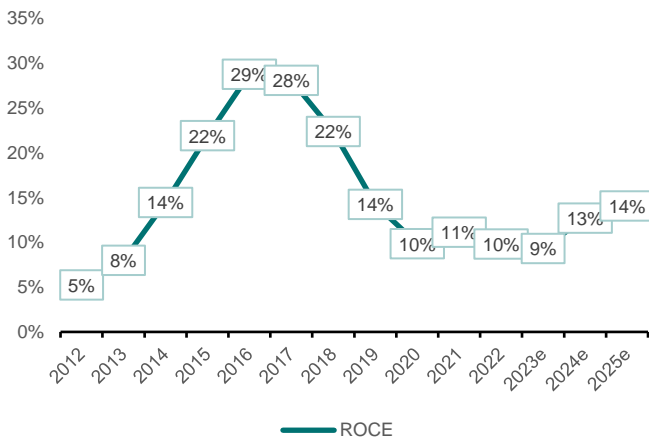
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Figure 9: LTM FCF versus LTM EBIT (2012–2023e) – coming out of an intense investment period to accelerate organic growth since 2018



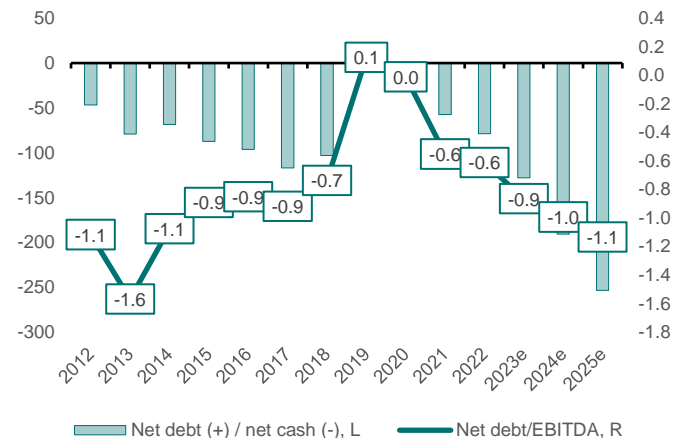
Source: DNB Markets (forecasts), company (historical data)

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



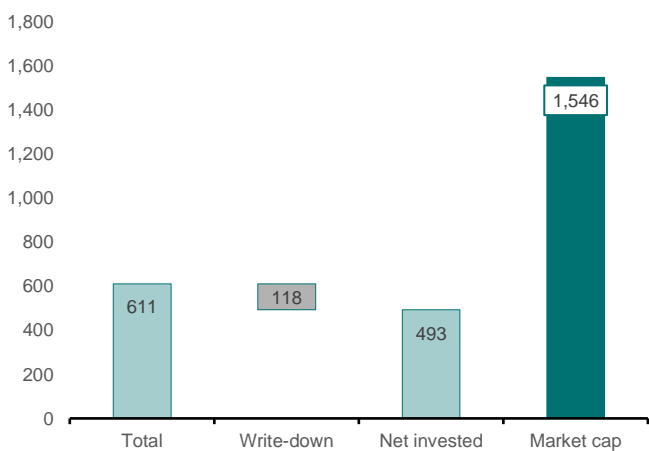
Source: DNB Markets (forecasts), company (historical data)

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



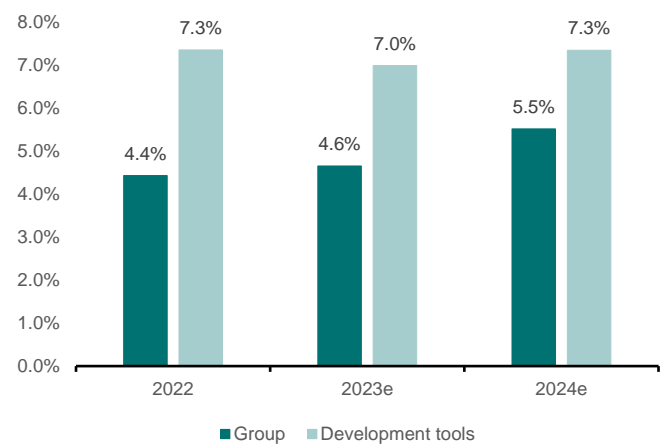
Source: DNB Markets (forecasts), company (historical data)

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)

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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	461.1	510.9	555.8	10%
Growth YOY, of which	10%	5%	-8%	-4%	18%	10%	11%	9%	
Organic	6%	-1%	-7%	1%	9%	7%	11%	9%	
Structural	0%	0%	0%	0%	0%	0%	0%	0%	
FX	4%	6%	-1%	-6%	9%	3%	0%	0%	
COGS	-9.0	-10.8	-14.1	-12.0	-12.8	-14.0	-14.6	-14.6	
Gross profit	376.2	394.8	357.9	346.0	410.0	448.0	496.3	541.2	
Capitalised work	0.0	0.0	0.0	64.4	50.2	52.9	53.7	55.8	
Other external expenses	-68.2	-63.7	-37.7	-48.3	-58.2	-60.2	-67.7	-72.2	
Personnel costs	-167.9	-185.3	-187.5	-258.2	-273.0	-292.8	-290.3	-301.6	
EBITDA	140.1	145.8	132.7	103.9	129.0	147.9	192.1	223.3	
IAC	-3.2	0.0	0.0	-134.2	-3.6	-6.8	-6.8	-6.8	
Adj. EBITDA	143.3	145.8	132.7	238.1	132.6	154.7	198.9	230.1	
Depreciation and amortisation	-24.5	-37.4	-48.9	-172.4	-53.3	-59.8	-65.1	-71.0	
EBIT	115.6	108.4	83.8	-68.5	75.7	83.0	120.2	145.5	
Adj. EBIT	118.8	108.4	83.8	65.7	79.3	89.8	127.0	152.3	24%
Financial items	-1.8	-1.4	-7.0	-0.1	-2.2	-4.2	-5.6	-5.2	
Profit before tax	117.0	107.0	76.8	-68.6	73.5	78.8	114.6	140.3	
Taxes paid	-26.2	-25.8	-17.4	1.2	-15.7	-21.5	-27.3	-33.1	
Adj. Net profit	94.0	81.2	59.4	66.8	61.4	64.1	94.1	114.0	23%
EPS	6.67	5.96	4.36	-4.94	4.23	4.19	6.39	7.85	
Adj. EPS (diluted)	6.67	5.96	4.36	4.90	4.50	4.68	6.89	8.34	
DPS	5.00	3.00	0.00	0.00	1.50	1.64	2.41	2.92	
Margins									
Gross	97.7%	97.3%	96.2%	96.6%	97.0%	97.0%	97.1%	97.4%	
EBITDA	36.4%	35.9%	35.7%	29.0%	30.5%	32.0%	37.6%	40.2%	
Adj. EBITDA	37.2%	35.9%	35.7%	66.5%	31.4%	33.5%	38.9%	41.4%	
EBIT	30.0%	26.7%	22.5%	-19.1%	17.9%	18.0%	23.5%	26.2%	
Adj. EBIT	30.8%	26.7%	22.5%	18.4%	18.8%	19.4%	24.9%	27.4%	
FCF margin	11.9%	5.4%	9.9%	16.1%	16.2%	15.6%	16.7%	17.2%	
Rule of 40 (EBIT)	42.5%	32.0%	14.2%	14.6%	36.9%	28.7%	35.4%	36.2%	
ROCE	28.1%	17.7%	12.4%	9.9%	11.5%	11.9%	15.9%	17.8%	
Cash flow									
Cash flow from operating activities	92.6	105.7	118.4	131.6	128.0	131.2	157.5	174.3	
Capex	-46.8	-83.6	-81.4	-74.1	-59.6	-59.5	-72.3	-78.9	
Adj. FCF	45.8	22.1	37.0	57.5	68.4	71.7	85.2	95.4	12%
Cash conversion (FCF/EBIT)	39%	20%	44%	88%	86%	80%	67%	63%	
Balance sheet									
Cash	106.1	60.7	67.8	113.4	148.2	187.6	242.4	296.9	
Net cash (-) / net debt (+)	-103.3	18.4	-1.5	-57.4	-78.9	-128.1	-190.9	-253.4	
Net debt/EBITDA	-0.7x	0.1x	0.0x	-0.6x	-0.6x	-0.9x	-1.0x	-1.1x	

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

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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	450.6	479.9	504.3	6%
Security solutions	5.0	1.7	5.0	0.7	1.5	10.5	31.0	51.5	225%
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	419.9	462.0	510.9	555.8	10%
Net sales growth by segment									
Development tools	10%	6%	-9%	-3%	18%	8%	7%	5%	
Security solutions		-66%	194%	-86%	114%	602%	195%	66%	
Other									
Total	10%	5%	-8%	-4%	18%	10%	11%	9%	
Net sales by product									
License-based	242.9	236.3	212.4	196.1	233.0	271.5	307.6	343.6	14%
Support and softw are updates	119.4	146.3	145.2	141.6	167.9	172.3	182.9	190.9	4%
Other	22.9	23.0	14.4	18.1	19.0	17.3	20.4	21.3	4%
Total	385.2	405.6	372.0	355.8	419.9	462.0	510.9	555.8	10%
Net sales growth by product									
License-based	12%	-3%	-10%	-8%	19%	17%	13%	12%	
Support and softw are updates	10%	23%	-1%	-2%	19%	3%	6%	4%	
Other	20%	0%	-37%	26%	5%	-9%	18%	4%	
Total	10%	5%	-8%	-4%	18%	10%	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	Q1'23	Q2'23e	Q3'23e	Q4'23e
Net sales by segment										
Development tools	87.8	91.5	97.0	107.2	105.6	108.6	107.3	114.3	114.8	114.2
Security solutions	0.1	0.1	0.4	0.4	0.5	0.2	0.4	1.4	3.5	5.2
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	108.6	115.7	118.3	119.4
Net sales growth by segment										
Development tools	-1%	2%	9%	23%	20%	19%	11%	7%	9%	5%
Security solutions	-75%	-92%	33%	100%	400%	100%	0%	255%	601%	2500%
Other										
Total	-1%	1%	10%	23%	20%	19%	10%	8%	12%	10%
Net sales by product										
License-based	46.2	49.4	52.0	67.8	56.2	57.0	72.4	69.4	64.9	64.8
Support and softw are updates	36.9	36.1	41.2	36.9	44.4	45.4	33.3	41.8	48.9	48.3
Other	4.8	6.1	4.2	2.9	5.5	6.4	2.0	4.5	4.5	6.3
Total	90.0	91.6	98.3	107.6	106.1	110.7	108.6	115.7	118.3	119.4
Net sales growth by product										
License-based	-9%	-5%	4%	35%	22%	15%	39%	2%	15%	14%
Support and softw are updates	4%	2%	19%	9%	20%	26%	-19%	13%	10%	6%
Other	85%	79%	2%	-6%	15%	5%	-52%	55%	-18%	-2%
Total	-1%	1%	10%	23%	20%	19%	10%	8%	12%	10%

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	Q1'23	Q2'23e	Q3'23e	Q4'23e
Net sales	90.0	91.6	98.3	107.6	106.1	110.7	108.6	115.7	118.3	119.4
Grow th YOY , of w hich	-1%	1%	10%	23%	20%	19%	10%	8%	12%	10%
Organic	-1%	2%	3%	14%	11%	7%	5%	2%	10%	10%
Structural	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
FX	0%	-1%	7%	9%	9%	12%	6%	5%	1%	0%
COGS	-2.8	-3.0	-2.8	-3.1	-3.1	-3.8	-3.2	-3.5	-3.5	-3.8
Gross profit	87.2	88.6	95.5	104.5	103.0	106.9	105.4	112.2	114.8	115.6
Capitalised w ork	13.7	14.1	12.2	10.5	11.3	16.2	9.4	14.0	14.5	15.0
Other external expenses	-10.3	-14.1	-11.5	-11.9	-18.8	-16.1	-12.7	-13.5	-18.0	-16.0
Personnel costs	-55.6	-75.4	-66.0	-71.2	-61.3	-74.6	-76.8	-77.0	-64.0	-75.0
EBITDA	35.0	13.2	30.2	31.9	34.2	32.4	25.3	35.7	47.3	39.6
IAC	2.1	-134.2	0.9	0.0	-4.5	0.0	-1.7	-1.7	-1.7	-1.7
Adj. EBITDA	32.9	147.4	29.3	31.9	38.7	32.4	27.0	37.4	49.0	41.3
Depreciation and amortisation	-14.1	-132.2	-13.0	-12.3	-12.1	-15.9	-13.9	-15.5	-15.1	-15.3
EBIT	20.9	-119.0	17.2	19.6	22.1	16.5	11.4	18.5	30.5	22.6
Adj. EBIT	18.8	15.2	16.3	19.6	26.6	16.5	13.1	20.2	32.2	24.3
Financial items	-0.3	1.8	-0.9	-0.5	1.1	-1.9	0.3	-1.5	-1.5	-1.5
Profit before tax	20.6	-117.2	16.3	19.1	23.2	14.6	11.7	17.0	29.0	21.1
Taxes paid	-4.7	11.8	-4.4	-4.8	-6.4	0.0	-5.3	-4.2	-6.9	-5.1
Adj. Net profit	13.8	28.8	11.0	14.3	21.3	14.6	8.1	14.5	23.8	17.7
EPS	1.17	-7.72	0.88	1.05	1.04	1.07	0.47	0.94	1.62	1.17
Adj. EPS (diluted)	1.01	2.11	0.81	1.05	1.56	1.07	0.59	1.06	1.74	1.29
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00
Margins										
Gross	96.9%	96.7%	97.2%	97.1%	97.1%	96.6%	97.1%	97.0%	97.0%	96.8%
EBITDA	38.9%	14.4%	30.7%	29.6%	32.2%	29.3%	23.3%	30.8%	40.0%	33.2%
Adj. EBITDA	36.6%	160.9%	29.8%	29.6%	36.5%	29.3%	24.9%	32.3%	41.4%	34.6%
EBIT	23.2%	-129.9%	17.5%	18.2%	20.8%	14.9%	10.5%	16.0%	25.8%	18.9%
Adj. EBIT	20.9%	16.6%	16.6%	18.2%	25.1%	14.9%	12.1%	17.4%	27.2%	20.4%
FCF margin	24.1%	25.5%	15.7%	15.3%	31.3%	3.0%	14.6%	14.6%	22.9%	10.1%
Rule of 40 (EBIT)	22.1%	17.6%	27.2%	41.3%	43.0%	35.8%	22.5%	25.0%	38.7%	28.2%
ROCE	9.7%	9.3%	9.5%	10.4%	11.8%	11.6%	10.8%	10.6%	11.1%	12.0%
Cash flow										
Cash flow from operating activities	41.4	40.5	28.8	26.0	47.4	25.8	26.1	33.0	43.3	28.8
Capex	-19.7	-17.1	-13.4	-9.5	-14.2	-22.5	-10.4	-16.2	-16.2	-16.8
Adj. FCF	21.7	23.4	15.4	16.5	33.2	3.3	15.7	16.9	27.1	12.0
Cash conversion (FCF/EBIT)	115%	154%	94%	84%	125%	20%	120%	84%	84%	49%
Balance sheet										
Cash	91.3	113.4	125.0	117.9	158.8	148.2	158.1	152.5	177.6	187.6
Net cash (-) / net debt (+)	-36.4	-57.4	-72.0	-85.9	-131.1	-78.9	-92.6	-89.0	-116.1	-128.1
Net debt/EBITDA	-0.3x	-0.6x	-0.7x	-0.8x	-1.2x	-0.6x	-0.7x	-0.7x	-0.8x	-0.9x

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

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Valuation

Figure 18: Valuation approaches (SEKm, %)

	Peers regression	DCF	Historical average
Net sales (2023e)			461
Adj. EBIT (2023e)			90
Adj. EPS (2023e)			4.68
Sales CAGR (2022–2024e)	12.6		9.9
Adj. EBIT margin (2023e)	21.7		19.4
RO40 (2023e)	47.1		29.4
Target multiple	RO40, P/B, EV/S	10% WACC	20x EV/EBIT
Enterprise value	2,862	2,965	1,796
Net debt (+)/cash (-)	-79	-79	-79
Equity value	2,940	3,044	1,875
Shares outstanding	13.8	13.8	13.8
Implied price/share	214	221	136
Implied potential	93%	99%	23%

2024e valuation multiples

Implied EV/sales	5.6	5.8	3.5
Implied EV/EBIT	22.5	23.3	14.1
Implied P/E	31.3	32.4	19.9

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	461	511	556
Growth YOY	5.4%	5.1%	10.2%	5.2%	-8.3%	-4.4%	18.1%	10.0%	10.6%	8.8%
Gross profit	316	337	376	395	358	346	410	448	496	541
Gross margin	96.3%	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	97.0%	97.1%	97.4%
Adj. EBITDA	117	127	140	146	133	104	129	148	192	223
EBITDA margin	36.9%	36.9%	37.2%	35.9%	35.7%	66.5%	31.4%	33.5%	38.9%	41.4%
Adj. EBIT	101	107	119	108	84	66	79	90	127	152
EBIT margin	30.6%	31.1%	30.8%	26.7%	22.5%	18.4%	18.8%	19.4%	24.9%	27.4%
Adj. Net profit	82	80	94	81	59	67	61	64	94	114
Adj. FCF	95	105	46	22	37	58	68	72	85	95
FCF margin	29.0%	30.4%	11.9%	5.4%	9.9%	16.2%	16.3%	15.5%	16.7%	17.2%
Cash conversion	95%	98%	39%	20%	44%	88%	86%	80%	67%	63%
Rule of 40 (EBIT)	36.0%	36.2%	41.0%	31.9%	14.2%	14.0%	36.8%	29.5%	35.4%	36.2%
ROCE	35.0%	37.4%	28.1%	17.7%	12.4%	9.9%	11.5%	11.9%	15.9%	17.8%
ROIC	27.4%	28.5%	21.9%	13.8%	10.1%	10.4%	9.4%	9.1%	12.5%	13.9%
Market cap	2,602	2,387	3,310	2,535	1,905	1,606	1,515	1,516	1,516	1,516
Net debt	-97	-117	-103	18	-1	-57	-79	-128	-191	-253
Enterprise value	2,505	2,270	3,206	2,554	1,904	1,548	1,436	1,388	1,325	1,263
EV/Sales	7.6x	6.6x	8.3x	6.3x	5.1x	4.4x	3.4x	3.0x	2.6x	2.3x
EV/EBIT	24.9x	21.1x	27.0x	23.6x	22.7x	23.6x	18.1x	15.5x	10.4x	8.3x
P/E	31.7x	29.8x	35.2x	31.2x	32.1x	24.0x	24.7x	23.7x	16.1x	13.3x
FCF yield	3.7%	4.4%	1.4%	0.9%	1.9%	3.6%	4.5%	4.7%	5.6%	6.3%

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

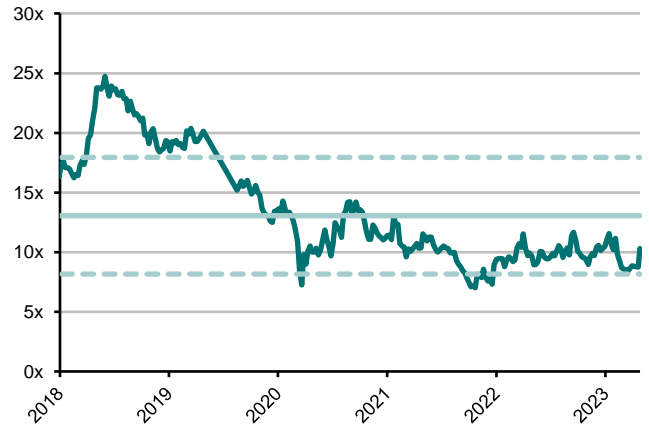
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Figure 20: EV/sales 12-month forward IAR Systems (2018–2023)



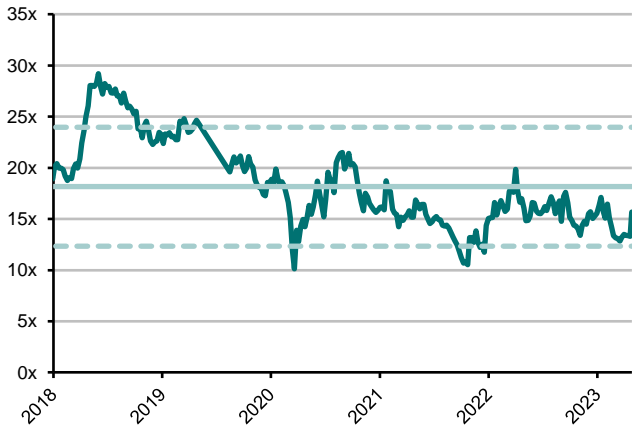
Source: Bloomberg

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



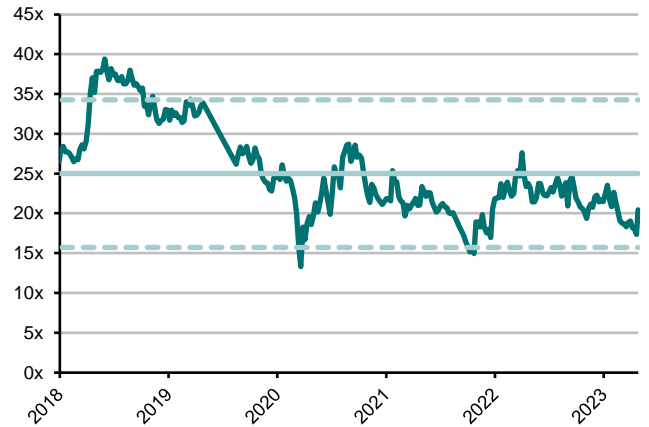
Source: Bloomberg

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



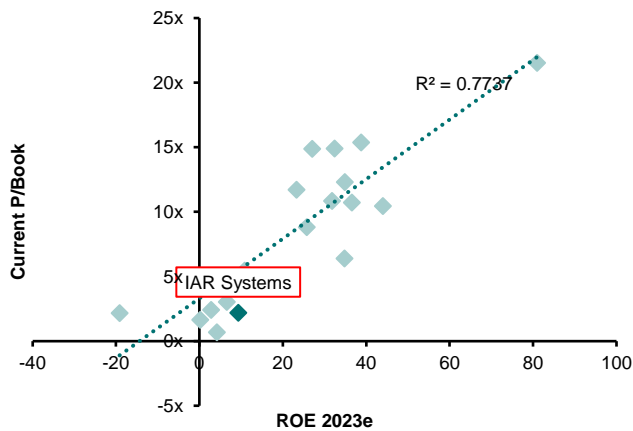
Source: Bloomberg

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



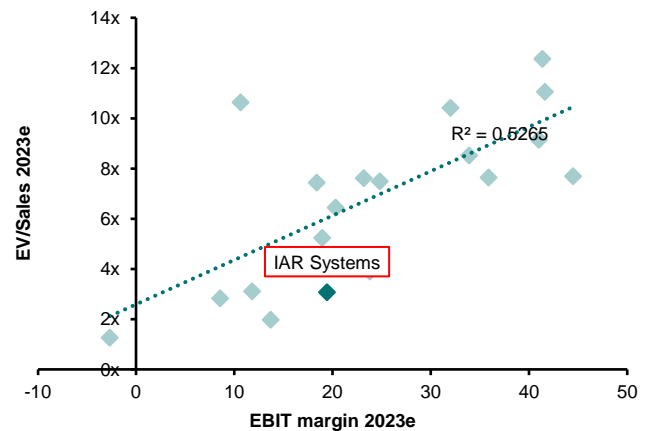
Source: Bloomberg

Figure 24: Current P/book versus ROE 2023e



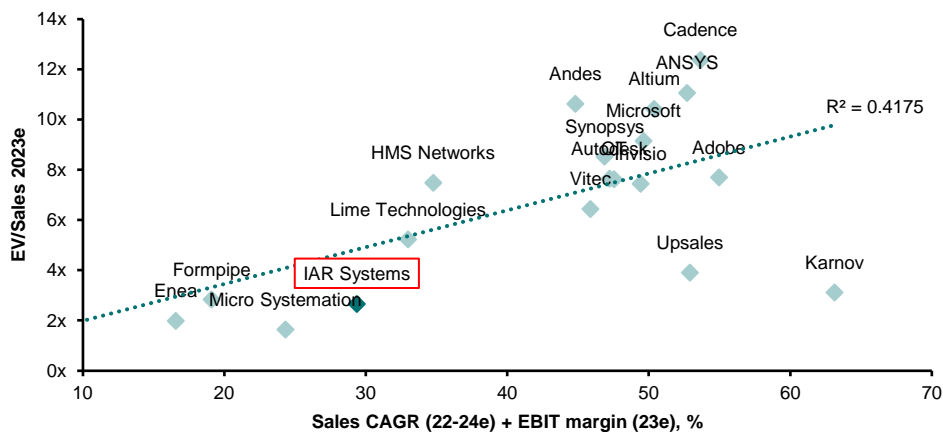
Source: Bloomberg (underlying data), DNB Markets (further calculations)

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



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

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)	1.5	26	17	14	15	10	8	9	7	6	3	3	2	1.5	4.7	9	13	19.4	24.9	10	27	23	
Premium/discount		-34%	-47%	-45%	-56%	-57%	-58%	-61%	-64%	-63%	-59%	-60%	-60%										
IAR Systems (Cons.)	1.5	18	14	12	12	9	7	8	6	5	3	3	3	2.0	5.6	12	14	24.4	27.7	12	29	32	
Premium/discount		-56%	-57%	-55%	-66%	-64%	-65%	-68%	-69%	-68%	-59%	-58%	-56%										
Nordic software																							
Enea	1.7	14	14	11	14	12	9	6	5	4	2	2	2		13.7	4	4	13.7	13.8	3	16	-3	
Formpipe	1.4	43	27	19	32	20	15	14	11	9	3	3	3	1.2	1.1	7	10	8.6	12.3	11	128	124	
HMS Networks	21.6	38	39	37	30	31	28	26	26	24	8	8	7	1.0	2.7	32	26	24.8	24.1	10	8	10	
Invisio	9.5	63	45	35	48	33	25	38	28	22	9	7	6	0.6	1.8	27	31	18.4	21.9	31	146	169	
Karnov	5.7	16	14	12	26	20	16	12	11	9	3	3	3	1.0	6.0	3	5	11.8	14.1	51	31	36	
Lime Technologies	3.3	42	33	29	32	27	22	20	18	15	6	6	5	1.1	3.6	35	33	18.9	19.3	14	16	11	
Micro Systemation	0.8	19	15	13	14	10	9	11	9	7	2	2	1	4.6	5.8	35	40	13.2	15.3	11	21	17	
QT	21.1	53	34	26	42	26	19	33	23	17	10	8	6	0.0	2.1	32	35	23.2	28.3	24	39	26	
Upsales	0.9	28	22	18	21	16	13	17	13	11	5	4	3		2.5	81	80	23.8	24.2	29	39	41	
Vitec	18.8	46	38	33	38	32	29	21	18	15	8	6	6	0.7		11	12	20.3	20.6	26	34	35	
WithSecure	3.0			38			30		33	11	1	1	1	0.0		-19	-4	-16.8	-2.8	13	-65	-76	
Engineering software																							
Adobe	1,731.0	24	21	18	19	17	14	18	16	13	9	8	7	0.0	4.6	44	42	44.5	44.5	10	10	14	
Altium	34.6	51	41	33	38	30	25	34	28	23	12	10	9	1.8	1.0	23	28	32.0	34.2	18	28	29	
Andes	7.5	116	47	26	136	42	21	66	29	17	15	11	8	0.7	1.3	4	9	10.6	24.8	34	221	-12	
ANSYS	282.8	36	33	29	29	26	22	26	24	21	12	11	10	0.0	2.5	13	13	41.6	41.9	11	12	12	
Autodesk	423.9	29	26	23	23	21	19	21	20	18	8	8	7	0.0	4.7	161	93	35.9	35.6	11	19	20	
Cadence	581.0	41	37	32	33	29	25	30	27	23	14	13	11	0.0	2.2	39	35	41.4	42.3	12	15	16	
Materialise	4.8		74	30			16	13	9	6	1	1	1	0.0		0	3	-2.7	-1.0	11	31	78	
Microsoft	22,721.1	31	27	23	25	22	19	21	19	16	10	9	8	0.9	2.8	37	34	41.1	42.0	9	8	7	
Synopsys	580.2	35	31	27	28	24	22	26	23	23	10	9	8		2.6	26	25	33.9	34.5	13	15	17	
Average	1,322.7	40	32	26	35	24	20	24	19	15	7	6	6	0.8	3.6	30	28	21.9	24.5	18	39	29	
Median	14.1	37	33	27	29	25	20	21	20	16	8	7	6	0.7	2.6	26	27	21.7	24.1	13	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 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.

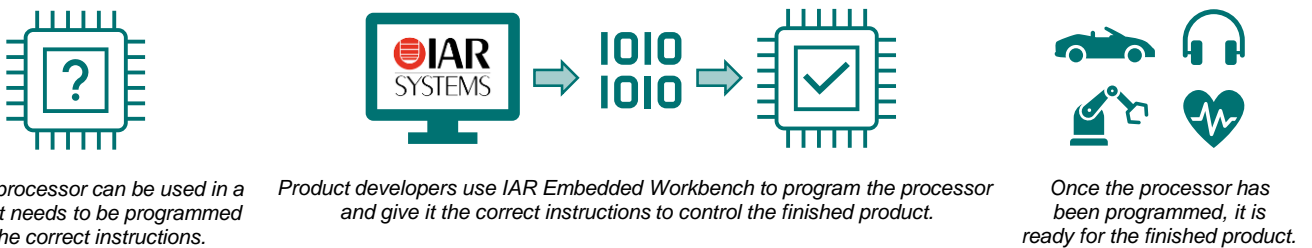
Business overview

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)

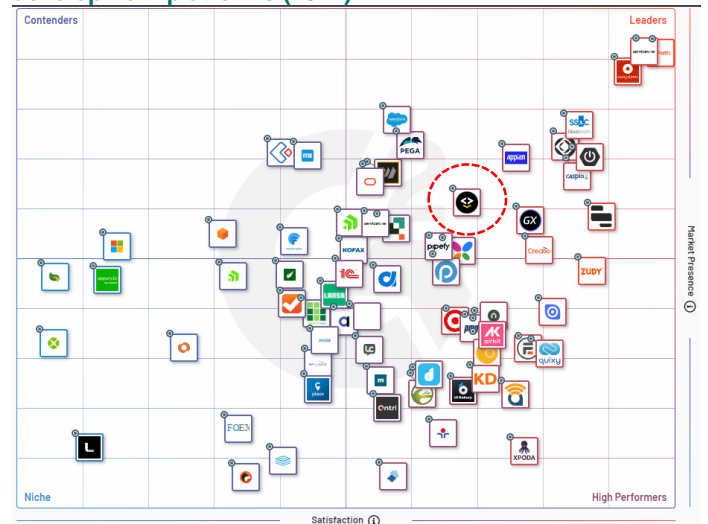
Headquartered in Uppsala, Sweden, IAR Systems has 200+ employees in 15 offices on three continents with technical support teams in its customers’ local time zones in 10+ languages. Its independent software supports more than 14,000 different processors from more than 70 processor vendors, which is more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

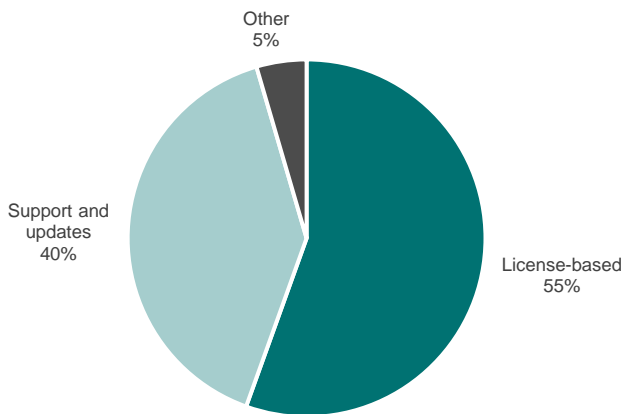
companies, etc.); and 4) suppliers of integrated programmes (real-time operating systems, graphics development, etc.).

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

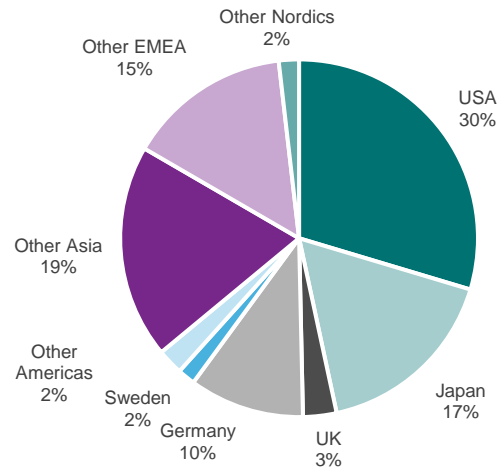
- **Development tools (~99% of net sales)** consist of IAR Embedded Workbench (8- to 64-bit) with world-leading code-optimisation technology, compiler, debugger probes and analysis tools (ensuring code quality and coding standards), functional safety certifications (pre-certified build tools), RISV-V 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 (2022)



Source: Company

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Forecast changes – P&L

(SEKm)	New			Old			Change		
	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
Revenues	462	511	556	476	527	572	-14	-16	-16
Cost of sales	-14	-15	-15	-14	-14	-14	0	0	0
Gross profit	448	496	541	462	513	558	-14	-16	-16
Operating expenses	-353	-358	-374	-338	-355	-371	-15	-3	-3
EBITDA	148	192	223	180	213	246	-32	-21	-23
EBITDA adj	155	199	230	180	213	246	-26	-14	-16
EBITDA margin (%)	32.0	37.6	40.2	37.9	40.4	43.1	-5.8	-2.8	-2.9
Depreciation	-30	-33	-35	-35	-35	-36	5	2	1
Amortisation	-30	-32	-36	-30	-32	-36	0	0	0
EBIT	83	120	145	116	146	174	-33	-25	-29
EBIT adj	90	127	152	116	146	174	-26	-19	-22
Net financial items	-4	-6	-5	-6	-5	-4	2	-1	-1
PBT	79	115	140	110	141	170	-31	-26	-29
Taxes	-22	-27	-33	-25	-32	-38	3	4	5
Minorities	0	0	0	0	0	0	0	0	0
Net profit	57	87	107	85	109	132	-28	-22	-24
Adjustments to net profit	7	7	7	0	0	0	7	7	7
Net profit adj	64	94	114	85	109	132	-21	-15	-18
<i>Per share data (SEK)</i>									
EPS	4.19	6.39	7.85	6.22	7.99	9.64	-2.03	-1.60	-1.79
EPS adj	4.68	6.89	8.34	6.22	7.99	9.64	-1.54	-1.10	-1.29
DPS ordinary	1.64	2.41	2.92	2.18	2.80	3.37	-0.54	-0.39	-0.45
DPS	1.64	2.41	2.92	2.18	2.80	3.37	-0.54	-0.39	-0.45
<i>Other key metrics (%)</i>									
Revenue growth	9.3	10.6	8.8	12.6	10.7	8.5	-3.3	-0.1	0.3
EBIT adj growth	13.2	41.4	19.9	46.2	26.1	19.5	-33.0	15.3	0.4
EPS adj growth	4.2	47.0	21.2	38.9	28.3	20.7	-34.7	18.7	0.5
Avg. number of shares (m)	14	14	14	14	14	14	0	0	0
Capex	-60	-72	-79	-73	-78	-83	14	5	4
OpFCF	95	127	151	107	135	163	-12	-9	-12
Working capital	-45	-50	-46	-51	-64	-54	6	14	7
NIBD adj	-128	-191	-253	-143	-225	-297	15	34	43

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	7.05	10.87	8.79	7.87	10.44	8.52	-0.82	0.43	0.27
Structure impact % YOY	0.00	0.00	0.00		0.00	0.00		0.00	0.00
Currency impact % YOY	2.98	-0.28	0.00	4.75	0.27	0.00	-1.77	-0.55	0.00

Source: DNB Markets

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Quarterly numbers

(SEKm)	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023e	Q3 2023e	Q4 2023e	Q1 2024e	Q2 2024e
Revenues	92	98	108	106	111	109	116	118	119	122	124
Cost of sales	-3	-3	-3	-3	-4	-3	-4	-4	-4	-4	-4
Gross profit	89	96	105	103	107	105	112	115	116	119	121
Operating expenses	-90	-78	-83	-80	-91	-90	-91	-82	-91	-92	-89
EBITDA	13	30	32	34	32	25	36	47	40	42	45
Depreciation	-5	-6	-6	-5	-9	-7	-8	-8	-8	-8	-9
Amortisation	-127	-7	-7	-7	-7	-7	-7	-7	-8	-8	-8
EBIT	-119	17	20	22	17	11	18	31	23	24	27
Net financial items	2	-1	-1	1	-2	0	-2	-2	-2	-1	-1
PBT	-117	16	19	23	15	12	17	29	21	22	25
Taxes	12	-4	-5	-6	0	-5	-4	-7	-5	-5	-6
Minorities	0	0	0	0	0	0	0	0	0	0	0
Net profit	-105	12	14	17	15	6	13	22	16	17	19
Adjustments to net profit	134	-1	0	5	0	2	2	2	2	2	2
Net profit adj	29	11	14	21	15	8	14	24	18	19	21
Dividend paid	0	0	0	0	0	0	-20	0	0	0	-22
Avg. number of shares (m)	14	14	14	14	14	14	14	14	14	14	14
<i>Per share data (SEK)</i>											
EPS	-7.72	0.88	1.05	1.04	1.07	0.47	0.94	1.62	1.17	1.24	1.40
EPS adj	2.11	0.81	1.05	1.56	1.07	0.59	1.06	1.74	1.29	1.37	1.53
DPS ordinary	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00	0.00	1.64
DPS	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00	0.00	1.64
<i>Growth and margins (%)</i>											
Revenues, QOQ growth	1.8	7.3	9.5	-1.4	4.3	-1.9	6.5	2.3	0.9	2.5	1.5
Revenues, YOY growth	1.0	10.6	23.1	17.9	20.9	10.5	7.5	11.5	7.9	12.8	7.5
EPS adj, YOY growth	140.0	-14.1	26.6	54.3	-49.3	-26.9	1.1	11.7	21.0	132.1	44.1
Gross margin	96.7	97.2	97.1	97.1	96.6	97.1	97.0	97.0	96.8	96.9	97.2
EBITDA adj margin	160.9	29.8	29.6	36.5	29.3	24.9	32.3	41.4	34.6	35.3	37.5
Depreciation/revenues	-5.7	-5.8	-5.3	-5.1	-7.9	-6.1	-7.0	-6.5	-6.5	-6.6	-6.9
EBIT adj margin	16.6	16.6	18.2	25.1	14.9	12.1	17.4	27.2	20.4	20.8	22.8
Net profit margin	nm	12.1	13.3	15.8	13.2	5.9	11.0	18.7	13.4	13.8	15.4

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

Adjustments to quarterly numbers

(SEKm)	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023e	Q3 2023e	Q4 2023e	Q1 2024e	Q2 2024e
EBITDA	13	30	32	34	32	25	36	47	40	42	45
EBITDA adj	147	29	32	39	32	27	37	49	41	43	47
EBIT	-119	17	20	22	17	11	18	31	23	24	27
Other EBIT adjustments	-134	1	0	-5	0	-2	-2	-2	-2	-2	-2
EBIT adj	15	16	20	27	17	13	20	32	24	25	28
Net profit	-105	12	14	17	15	6	13	22	16	17	19
Other EBIT adjustments	-134	1	0	-5	0	-2	-2	-2	-2	-2	-2
Net profit adj	29	11	14	21	15	8	14	24	18	19	21

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

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Quarterly numbers by segment and assumptions

(SEKm)	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023e	Q3 2023e	Q4 2023e	Q1 2024e	Q2 2024e
Assumptions											
Revenue org. % YOY	1.98	3.04	13.84	10.89	6.88	4.53	2.28	10.30	9.86	14.29	7.95
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	-0.99	6.52	9.27	9.33	11.90	5.95	5.24	1.21	-0.26	-0.70	-0.47

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	462	511	556	
Cost of sales	-12	-9	-9	-11	-14	-12	-13	-14	-15	-15	
Gross profit	316	337	376	395	358	346	410	448	496	541	
Operating expenses	-203	-209	-236	-249	-225	-307	-331	-353	-358	-374	
EBITDA	113	127	140	146	133	104	129	148	192	223	
Depreciation	-3	-2	-3	-13	-20	-20	-26	-30	-33	-35	
Amortisation	-14	-17	-22	-25	-29	-152	-28	-30	-32	-36	
EBIT	97	107	116	108	84	-69	76	83	120	145	
Net financial items	0	-2	-2	-1	-7	0	-2	-4	-6	-5	
PBT	100	106	117	107	77	-69	74	79	115	140	
Taxes	-22	-26	-26	-26	-17	1	-16	-22	-27	-33	
Effective tax rate (%)	22	24	22	24	23	2	21	27	24	24	
Minorities	0	0	0	0	0	0	0	0	0	0	
Net profit	78	80	91	81	59	-67	58	57	87	107	
Adjustments to net profit	4	0	3	0	0	134	4	7	7	7	
Net profit adj	82	80	94	81	59	67	61	64	94	114	
Dividend paid	-88	-63	-68	-68	0	0	0	-20	-22	-33	
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	4.23	4.19	6.39	7.85	
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.50	4.68	6.89	8.34	
DPS ordinary	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.64	2.41	2.92	
DPS	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.64	2.41	2.92	
<i>Growth and margins (%)</i>											
Revenue growth	5.4	5.1	11.7	5.3	-8.3	-3.8	18.1	9.3	10.6	8.8	
EPS adj growth	23.0	2.6	5.3	-10.6	-26.8	12.5	-8.2	4.2	47.0	21.2	
Gross margin	96.3	97.5	97.7	97.3	96.2	96.6	97.0	97.0	97.1	97.4	
EBITDA margin	34.5	36.9	36.4	35.9	35.7	29.0	30.5	32.0	37.6	40.2	
EBITDA adj margin	35.7	36.9	37.2	35.9	35.7	66.5	31.4	33.5	38.9	41.4	
Depreciation/revenues	-0.8	-0.7	-0.7	-3.2	-5.5	-5.7	-6.0	-6.5	-6.5	-6.3	
EBIT margin	29.4	31.1	30.0	26.7	22.5	nm	17.9	18.0	23.5	26.2	
EBIT adj margin	30.6	31.1	30.8	26.7	22.5	18.4	18.8	19.4	24.9	27.4	
PBT margin	30.5	30.6	30.4	26.4	20.6	nm	17.4	17.1	22.4	25.2	
Net profit margin	23.8	23.2	23.6	20.0	16.0	nm	13.7	12.4	17.1	19.3	

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	148	192	223
EBITDA adj	117	127	143	146	133	238	133	155	199	230
EBIT	97	107	116	108	84	-69	76	83	120	145
Other EBIT adjustments	-4	0	-3	0	0	-134	-4	-7	-7	-7
EBIT adj	101	107	119	108	84	66	79	90	127	152
Net profit	78	80	91	81	59	-67	58	57	87	107
Other EBIT adjustments	-4	0	-3	0	0	-134	-4	-7	-7	-7
Net profit adj	82	80	94	81	59	67	61	64	94	114
<i>Per share data (SEK)</i>										
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.23	4.19	6.39	7.85
Recommended adjustment	0.00	0.00	0.00	0.00	0.00	9.85	0.26	0.49	0.50	0.50
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.50	4.68	6.89	8.34

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	57	87	107
Depreciation and amortisation	17	20	25	37	49	172	53	60	65	71
Cash flow from operations (CFO)	114	124	93	106	118	132	128	131	157	174
Capital expenditure	-19	-19	-47	-84	-81	-74	-60	-60	-72	-79
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	-59	-72	-79
Free cash flow (FCF)	95	86	-125	4	37	58	68	72	85	95
Net change in debt	0	0	0	30	6	1	1	0	0	0
Dividends paid	-88	-63	-68	-68	0	0	0	-20	-22	-33
Share issue (repurchase)	0	0	172	0	0	0	0	0	0	0
Other	0	0	4	-14	-30	-16	-40	-11	-8	-8
Cash flow from financing (CFF)	-88	-63	108	-52	-25	-15	-40	-32	-30	-41
Total cash flow (CFO+CFI+CFF)	7	23	-17	-49	12	42	29	40	55	55
<i>FCFF calculation</i>										
Free cash flow	95	86	-125	4	37	58	68	72	85	95
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	2.5	20.0	10.7
CFI	-3.3	-98.9	-478.5	53.0	20.4	9.0	19.6	0.4	-21.8	-9.2
FCF	18.5	-9.4	-244.7	102.8	957.1	55.4	19.0	5.1	18.5	12.0
CFF	-39.0	28.5	270.4	-148.3	52.7	38.6	-162.3	19.5	4.7	-34.6
FCFF	nm	nm	nm	nm	nm	nm	nm	nm	nm	nm

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

27 April 2023

Balance sheet

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
Assets	396	410	722	825	834	813	922	969	1,024	1,078
Inventories	6	5	7	7	6	10	11	10	10	9
Trade receivables	48	51	63	67	59	59	67	67	63	58
Other receivables	19	12	38	52	64	44	34	34	31	28
Current financial assets	0	0	0	0	0	0	0	0	0	0
Cash and cash equivalents	99	120	106	61	68	113	148	188	242	297
Current assets	172	187	214	186	196	226	260	299	347	393
Property, plant and equipment	6	6	9	7	8	15	17	17	19	20
Other intangible assets	197	194	484	624	624	567	639	644	650	656
Deferred tax assets	16	3	13	5	4	3	3	5	5	5
Non-current financial assets	5	20	2	2	3	3	4	3	3	3
Non-current assets	224	223	508	639	638	587	663	670	677	685
Total assets	396	410	722	825	834	813	922	969	1,024	1,078
Equity and liabilities	396	410	722	825	834	813	922	969	1,024	1,078
Total equity	280	290	550	592	613	585	667	708	773	847
Trade payables	5	6	7	9	5	9	8	8	7	6
Other payables and accruals	92	86	131	117	111	133	146	149	148	136
Short-term debt	1	1	0	25	18	18	0	0	0	0
Total current liabilities	99	102	140	164	150	179	173	176	174	162
Long-term debt	2	2	1	41	32	20	50	40	32	24
Deferred tax liabilities	15	14	30	27	37	28	30	43	43	43
Other non-current liabilities	1	2	2	1	1	1	2	1	1	1
Total non-current liabilities	18	17	32	69	70	49	82	85	77	69
Total liabilities	116	120	172	233	220	228	255	260	250	230
Total equity and liabilities	396	410	722	825	834	813	922	969	1,024	1,078
<i>Key metrics</i>										
Net interest bearing debt	-97	-117	-103	18	-2	-57	-79	-128	-191	-253

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

27 April 2023

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	111.00	111.00	111.00
Number of shares (m)	12.63	12.63	13.62	13.63	13.63	13.63	13.65	13.66	13.66	13.66
Market capitalisation	2,602	2,387	3,310	2,535	1,905	1,606	2,053	1,516	1,516	1,516
Net interest bearing debt	-97	-117	-103	18	-2	-57	-79	-128	-191	-253
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	-128	-191	-253
EV	2,505	2,270	3,206	2,554	1,904	1,548	1,974	1,388	1,325	1,263
EV adj	2,505	2,270	3,206	2,554	1,904	1,548	1,974	1,388	1,325	1,263
<i>Valuation</i>										
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.23	4.19	6.39	7.85
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.50	4.68	6.89	8.34
DPS ordinary	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.64	2.41	2.92
DPS	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.64	2.41	2.92
P/E	33.4	29.8	36.4	31.2	32.1	-23.8	35.5	26.5	17.4	14.1
P/E adj	33.4	29.8	36.4	31.2	32.1	24.0	33.4	23.7	16.1	13.3
P/B	9.31	8.22	6.02	4.28	3.11	2.74	3.08	2.14	1.96	1.79
Average ROE	27.3%	28.1%	21.6%	14.2%	9.9%	-11.2%	9.2%	8.3%	11.8%	13.2%
Earnings yield adj	3.0%	3.4%	2.7%	3.2%	3.1%	4.2%	3.0%	4.2%	6.2%	7.5%
Dividend yield	3.4%	2.6%	2.1%	1.6%	0.0%	0.0%	1.0%	1.5%	2.2%	2.6%
Free cash flow yield	3.7%	3.6%	-3.8%	0.1%	1.9%	3.6%	3.3%	4.7%	5.6%	6.3%
EV/SALES	7.63	6.58	8.32	6.30	5.12	4.32	4.67	3.00	2.59	2.27
EV/SALES adj	7.63	6.58	8.32	6.30	5.12	4.32	4.67	3.00	2.59	2.27
EV/EBITDA	22.1	17.8	22.9	17.5	14.3	14.9	15.3	9.4	6.9	5.7
EV/EBITDA adj	21.4	17.8	22.4	17.5	14.3	6.5	14.9	9.0	6.7	5.5
EV/EBIT	26.0	21.1	27.7	23.6	22.7	-22.6	26.1	16.7	11.0	8.7
EV/EBIT adj	24.9	21.1	27.0	23.6	22.7	23.6	24.9	15.5	10.4	8.3
EV/capital employed	8.9	7.8	5.8	3.8	2.8	2.4	2.7	1.8	1.6	1.4
EV/NOPLAT	33.3	27.1	35.6	30.2	29.1	-29.0	33.4	21.4	14.1	11.1
EV/OpFCF (taxed)	32.8	26.8	45.6	66.6	57.9	10.4	35.5	18.4	13.4	10.7

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

27 April 2023

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	6.7	6.1	8.8	10.2
ROCE	35.0	37.4	28.1	17.7	12.4	9.9	11.5	11.9	15.9	17.8
ROCE after tax	27.3	29.1	21.9	13.8	9.7	7.8	9.0	9.3	12.4	13.8
<i>Return on invested capital (%)</i>										
Net PPE/revenues	1.9	1.8	2.3	1.8	2.0	4.1	3.9	3.8	3.7	3.7
Working capital/revenues	-7.5	-6.9	-7.8	-0.2	3.4	-8.3	-10.1	-9.7	-9.8	-8.3
<i>Cash flow ratios (%)</i>										
FCF/revenues	29.0	25.0	-32.4	0.9	9.9	16.1	16.2	15.6	16.7	17.2
FCF yield (%)	3.7	3.6	1.4	0.9	1.9	3.6	3.3	4.7	5.6	6.3
CFO/revenues	34.8	35.9	24.0	26.1	31.8	36.8	30.3	28.4	30.8	31.4
CFO/market capitalisation	4.4	5.2	2.8	4.2	6.2	8.2	6.2	8.7	10.4	11.5
CFO/capex	614.0	652.1	197.9	126.4	145.5	177.6	214.8	220.4	217.9	221.0
CFO/current liabilities	115.8	121.1	66.2	64.4	78.9	73.7	73.9	74.8	90.7	107.8
Cash conversion ratio	122.2	107.9	-137.6	4.3	62.3	-85.3	118.3	125.6	97.6	89.0
Capex/revenues	5.7	5.5	12.1	20.6	21.9	20.7	14.1	12.9	14.1	14.2
Capex/depreciation	744.0	791.7	1800.0	648.1	401.0	363.2	233.7	197.0	218.4	225.2
OpFCF margin	30.0	31.4	25.1	15.3	13.8	45.8	17.3	20.6	24.8	27.2
Total payout ratio	113.3	78.9	75.0	50.4	0.0	0.0	35.4	39.1	37.7	37.2
<i>Leverage and solvency (x)</i>										
Net debt/EBITDA	-0.85	-0.92	-0.74	0.13	-0.01	-0.55	-0.61	-0.87	-0.99	-1.13
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	0.03	0.02	0.02
<i>Cash conversion cycle</i>										
Inventory turnover days	167.5	223.3	267.7	223.1	147.6	289.0	322.2	258.2	257.3	237.3
Receivables turnover days	74.7	66.2	96.1	106.8	120.2	104.7	86.5	80.1	67.1	56.9
Credit period	158.6	244.8	296.1	310.9	129.4	279.8	239.5	198.7	171.5	158.2
Cash conversion cycle	83.7	44.8	67.7	18.9	138.3	113.8	169.2	139.7	152.9	136.0

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

27 April 2023

Important Information

Company: IAR Systems
 Coverage by Analyst: Joachim Gunell
 Date: 26/04/2023

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