

IAR SYSTEMS

Trending in the right direction

A quality Q2 beat reinforces our view that IAR Systems is gradually coming back to an accelerated profitable growth trajectory after a long negative EPS revisions trend. We do not believe IAR Systems is immune to weakening IT spending but highlight that its 2023 earnings should grow from base that is already ~30% below 2018 levels with positive commercial momentum from its new products exposed to high-growth megatrends, such as IoT, RISC-V and cybersecurity. We have raised our 2022–2023e EPS by 13% and our fair value to SEK140–250 (130–220).

Strong Q2 report any way we look at it. Organic sales growth accelerated to 14% (our estimate: 11%) driven mainly by an organic uptick in new license sales, which rose 25% YOY, and trends in Europe and Asia (up 19% YOY organic, respectively). With a 97.1% gross margin, tight opex control and less boost from capitalised development costs, this set up an EBIT margin of 18.2% (up 3.8%-points YOY, 2% above our estimate). We are encouraged that IAR's 'rule of 40' was finally back above 40%, after 12 quarters in the 0–30% range, while FCF rose 50%+ YOY. We are cautiously optimistic to its repackaged security offering, which appears to be gaining commercial momentum, where it has signed several deals in Q2 (including a US Federal department). Moreover, IAR's recently launched extension to Microsoft's VS Code (has 14m+ active users) should broaden user adoption considerably, we believe.

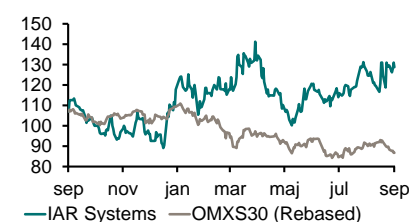
2022–2023e EPS raised by 13%, 3%-points of which we attribute to its strong Q2 performance (indicating accelerating operating momentum) and 10%-points to FX tailwinds. We now forecast 10% organic sales growth YOY for 2022e, considering IAR's 5% price increases (the first in six years) and a 20.9% adj. EBIT margin, which corresponds to 50%+ adj. EBIT growth in H2e.

Fair value raised to SEK140–250, based on a peers' multiples regression, IAR's historical valuation, and a DCF, corresponding to a 2023e EV/EBIT of 13–26x.

Year-end Dec	2018	2019	2020	2021	2022e	2023e	2024e
Revenue (SEKm)	385	406	372	358	421	482	525
EBITDA adj (SEKm)	143	146	133	238	140	188	222
EBIT adj (SEKm)	119	108	84	66	87	126	155
PTP (SEKm)	117	107	77	-69	85	123	152
EPS rep (SEK)	6.67	5.96	4.36	-4.94	4.69	7.00	8.65
EPS adj (SEK)	6.67	5.96	4.36	4.90	4.61	7.00	8.65
DPS (SEK)	5.00	3.00	0.00	0.00	1.61	2.45	3.03
Revenue growth (%)	11.7	5.3	-8.3	-3.8	17.5	14.7	8.9
EBITDA growth adj (%)	12.7	1.7	-9.0	79.4	-41.0	34.1	18.0
EPS growth adj (%)	5.3	-10.6	-26.8	12.5	-5.9	51.8	23.7
EBITDA margin adj (%)	37.2	35.9	35.7	66.5	33.4	39.0	42.3
EV/Sales adj (x)	8.32	6.30	5.12	4.32	3.89	3.27	2.85
EV/EBITDA adj (x)	22.4	17.5	14.3	6.5	11.7	8.4	6.7
EV/EBIT adj (x)	27.0	23.6	22.7	23.6	18.8	12.5	9.6
P/E adj (x)	36.4	31.2	32.1	24.0	27.9	18.4	14.9
P/Book (x)	6.02	4.28	3.11	2.74	2.64	2.38	2.13
ROE (%)	21.6	14.2	9.9	nm	10.2	13.6	15.1
ROCE (%)	28.1	17.7	12.4	9.9	13.1	17.4	19.3
Dividend yield (%)	2.1	1.6	0.0	0.0	1.3	1.9	2.4
FCF yield (%)	1.4	0.9	1.9	3.6	3.8	4.7	6.4

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

IARB versus OMXS30 (12m)



Source: Factset

SUMMARY

Share price (SEK)	129
Tickers	IARB SS

CAPITAL STRUCTURE

No. of shares (m)	13.7
No. of shares fully dil. (m)	13.7
Market cap. (SEKm)	1,758
NIBD adj end-2022e (SEKm)	-121
Enterprise value adj (SEKm)	1,638
Net debt/EBITDA adj (x)	-0.86
Free float (%)	100

Source: Company, DNB Markets (estimates)

NEXT EVENT

Q3 2022	27/10/2022
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ESTIMATE CHANGES (SEK)

Year-end Dec	2022e	2023e	2024e
Sales (old)	406.8	456.9	507.7
Sales (new)	420.6	482.4	525.2
Change (%)	3.4	5.6	3.5
EPS adj (old)	4.08	6.16	7.95
EPS adj (new)	4.61	7.00	8.65
Change (%)	13.0	13.5	8.9

Source: DNB Markets,

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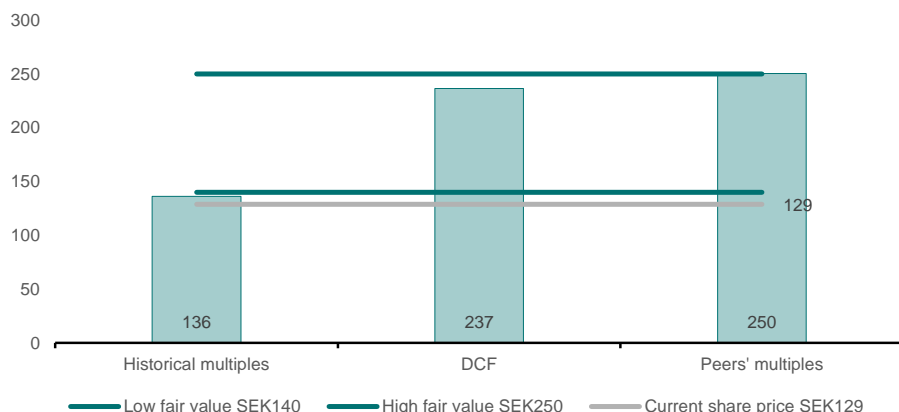
ANALYSTS

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 SEK140–250 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 15x, EV/EBIT of 10x, and EV/sales of 3x.

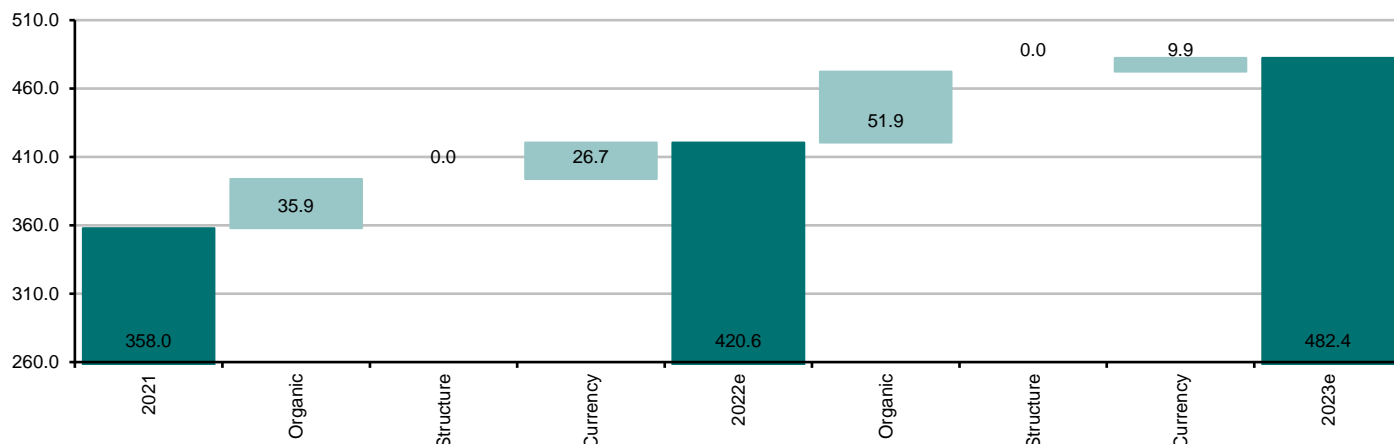
Source: DNB Markets

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 into microcontrollers.
- SaaS transition would support the revenue mix, lessen the cyclical, 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; 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.

Q2 results

Figure 1: Q2 results versus expectations

Key highlights (SEKm, except per share data)	Q2 2022		Deviation	Deviation	Q2 2021	DNBe
	Actual	DNB	(%)	Absolute	Actual	2022e
Net sales	107.6	101.2	6%	6	87.4	419.7
Gross profit	104.5	97.8	7%	7	84.7	407.8
Gross margin	97.1%	96.6%	0.5pp		96.9%	97.2%
One-offs	0.0	0		0	-2	1
EBITDA adj.	31.9	33.6	-5%	-2	26.0	141.4
EBITDA adj. margin	29.6%	33.2%	-3.5pp		29.7%	33.7%
EBIT	19.6	19.3	2%	0	14.7	87.0
EBIT margin	18.2%	19.1%	-0.8pp		16.8%	20.7%
EBIT adj.	19.6	19.3	2%	0	14.7	87.0
EBIT adj. margin	18.2%	19.1%	-0.8pp		16.8%	20.7%
EPS adj.	1.05	1.06	-1%	-0.01	0.83	4.61
Adj. FCF (CFO - capex)	16.5	8.3	99%	8	10.9	66.8
Cash conversion	84%	43%	41.2pp		74%	77%
Rule of 40 (EBIT)	41.3%	34.8%	6.5pp		4.1%	38.2%
Revenue growth YOY	23.1%	15.7%	7.4pp		-12.7%	18.2%
Organic	13.8%	10.6%	3.3pp		-2.4%	10.0%
Structural	0.0%	0.0%	0pp		0.0%	0.0%
FX	9.3%	5.2%	4.1pp		-10.3%	8.2%
Segment	Q2 2022		Deviation	Deviation	Q2 2021	DNBe
(SEKm)	Actual	DNB	(%)	Absolute	Actual	2022e
Net sales						
Development tools	107.2	100.9	6%	6	87.2	417.7
Security solutions	0.4	0.3	54%	0	0.2	2.0
Other	0.0	0.0	n.a.	0	0.0	0.0
Total	107.6	101.2	6%	6	87.4	419.7
Net sales growth						
Development tools	22.9%	15.7%	7.2pp			379.0%
Security solutions	100.0%	30.2%	69.8pp			908.4%
Other						
Total	23.1%	15.7%	7.4pp			380.2%
Net sales						
License-based	67.8	56.0	21%	12	50.4	242.4
Support and software updates	36.9	40.7	-9%	-4	33.9	161.2
Other	2.9	4.5	-36%	-2	3.1	16.1
Total	107.6	101.2	6%	6	87.4	419.7

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

2 September 2022

Estimate revisions

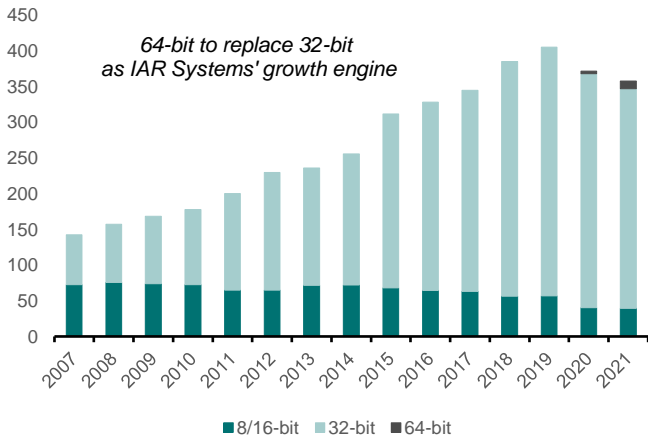
Figure 2: Estimate changes

(SEKm, except per share data)	Old			New			Change		
	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e
Net sales	407	457	508	421	482	525	3%	6%	3%
Growth YOY, of which	14.3%	12.3%	11.1%	18.2%	14.7%	8.9%	388bp	238bp	-225bp
Organic	9.2%	12.0%	11.1%	10.0%	12.3%	8.9%	80bp	31bp	-225bp
Structural	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0bp	0bp	0bp
FX	5.1%	0.3%	0.0%	8.2%	2.4%	0.0%	308bp	207bp	0bp
Gross profit	394	445	495	408	470	513	4%	6%	4%
Gross margin	96.8%	97.4%	97.5%	97.0%	97.4%	97.6%	18bp	7bp	12bp
EBITDA	135	177	212	141	188	222	5%	6%	5%
IAC	1	0	0	1	0	0	0%		
Adj. EBITDA	134	177	212	140	188	222	5%	6%	5%
Depreciation and amortisation	-57	-66	-69	-53	-62	-67	-7%	-6%	-3%
EBIT	78	112	143	88	126	155	13%	13%	9%
Adj. EBIT	77	112	143	87	126	155	13%	13%	9%
Adj. EBIT margin	19.1%	24.5%	28.2%	20.9%	26.2%	29.6%	179bp	175bp	144bp
Capitalised development costs (CDC)	55	63	66	52	57	62	-5%	-9%	-6%
EBIT excl. CDC	5.4%	10.7%	15.2%	8.4%	14.4%	17.8%	295bp	367bp	265bp
Adj. Net profit	56	84	108	63	96	118	13%	14%	9%
Adj. EPS (diluted)	4.08	6.16	7.95	4.61	7.00	8.65	13%	14%	9%
DPS	1.43	2.16	2.78	1.61	2.45	3.03	13%	14%	9%
Net sales by segment									
Development tools	404	445	474	418	469	489	3%	5%	3%
Security solutions	2	12	34	2	14	36	29%	19%	6%
Other	0	0	0	0	0	0			
Total	407	457	508	421	482	525	3%	6%	3%
Net sales by product type									
License-based	224	266	306	242	292	324	8%	10%	6%
Support and software updates	164	172	182	161	172	182	-2%	0%	0%
Other	18	19	19	16	18	19	-9%	-2%	-2%
Total	407	457	508	421	482	525	3%	6%	3%
Balance sheet and cash flow									
Adj. FCF	49	75	96	67	83	113	35%	12%	18%
Cash	147	202	268	145	206	285	-1%	2%	6%
Net cash (-) / net debt (+)	-106	-161	-227	-121	-182	-261	14%	13%	15%

Source: DNB Markets

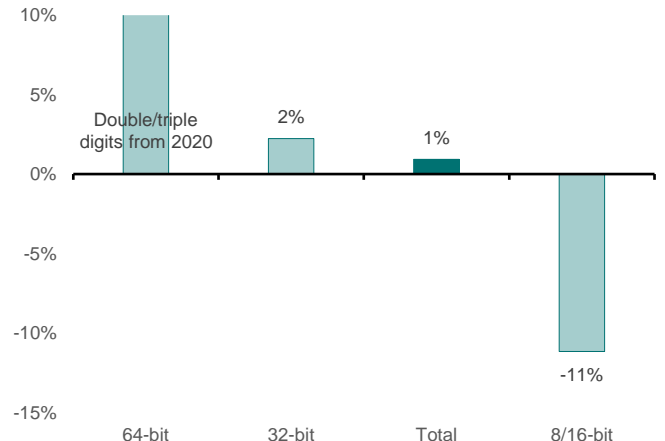
Key charts

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



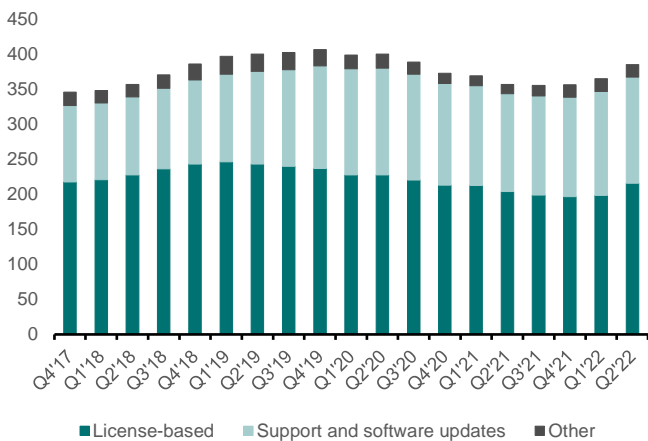
Source: Company (historical data), DNB Markets (further calculations)

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



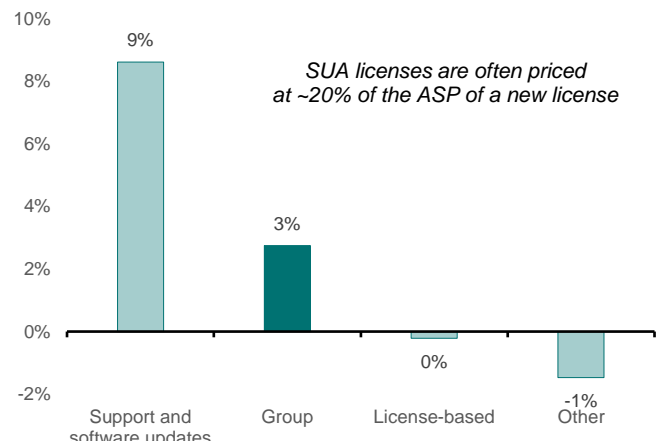
Source: Company (historical data), DNB Markets (further calculations)

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



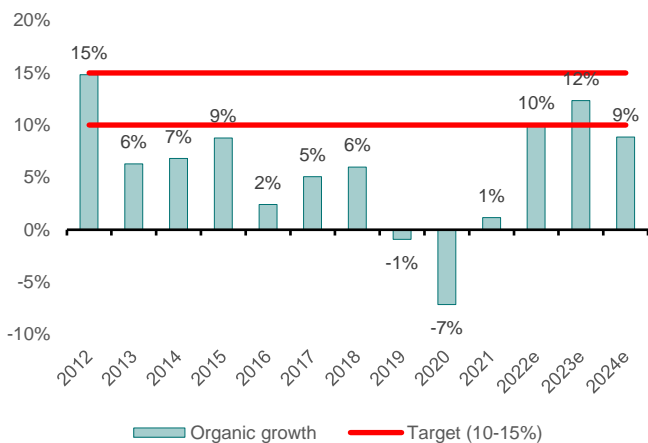
Source: Company (historical data), DNB Markets (further calculations)

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



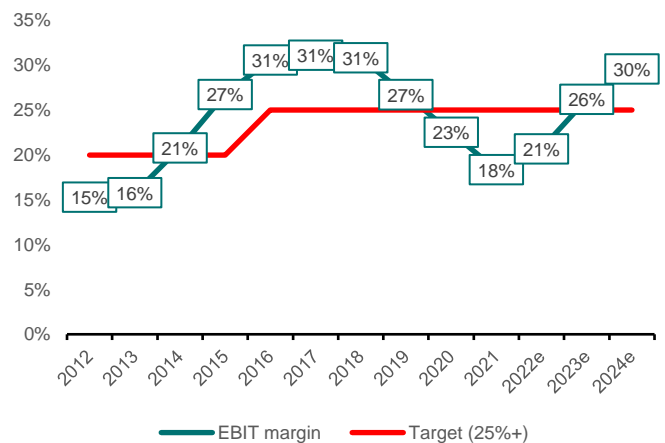
Source: Company (historical data), DNB Markets (further calculations)

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



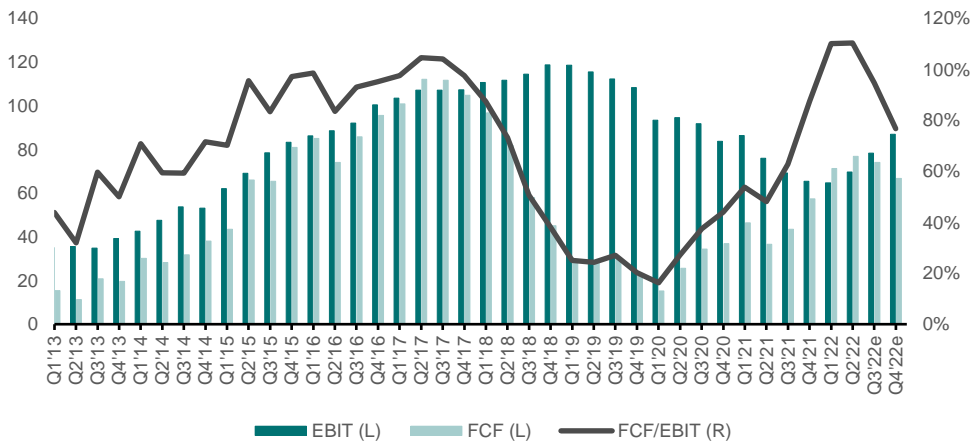
Source: DNB Markets (forecasts), company (historical data)

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



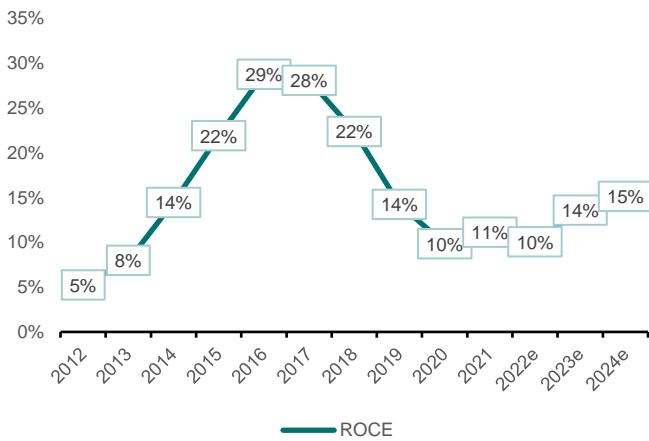
Source: DNB Markets (forecasts), company (historical data)

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



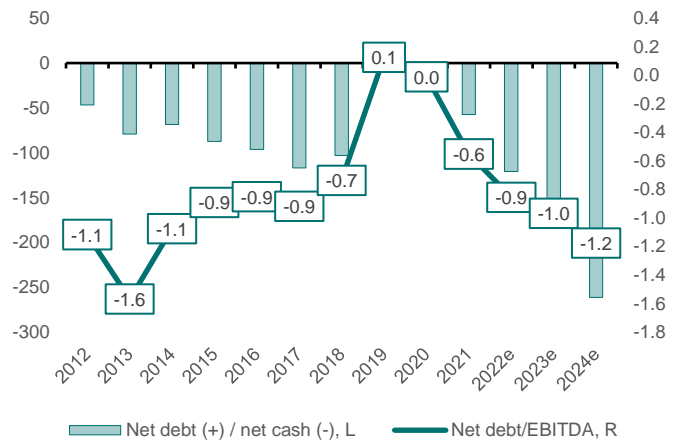
Source: DNB Markets (forecasts), company (historical data)

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



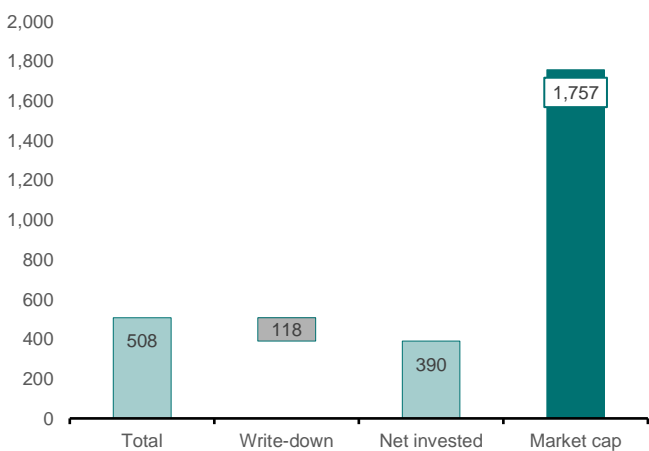
Source: DNB Markets (forecasts), company (historical data)

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



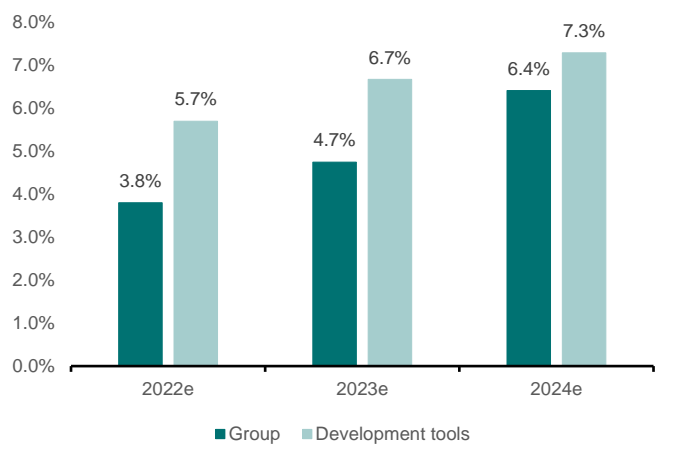
Source: DNB Markets (forecasts), company (historical data)

Figure 12: Investments (SEKm, 2016–2021)



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

Figure 13: FCF yield (2022–2024e)



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

Forecasts

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

(SEKm)	2017	2018	2019	2020	2021	2022e	2023e	2024e	21-24e CAGR
Net sales	345.0	385.2	405.6	372.0	355.8	419.7	482.4	525.2	14%
Growth YOY, of which	5%	10%	5%	-8%	-4%	18%	15%	9%	
Organic	5%	6%	-1%	-7%	1%	10%	12%	9%	
Structural	0%	0%	0%	0%	0%	0%	0%	0%	
FX	0%	4%	6%	-1%	-6%	8%	2%	0%	
COGS	-8.5	-9.0	-10.8	-14.1	-12.0	-12.8	-12.4	-12.4	
Gross profit	336.5	376.2	394.8	357.9	346.0	407.8	470.0	512.8	
Capitalised work	0.0	0.0	0.0	0.0	0.0	51.7	57.1	61.7	
Other external expenses	-49.2	-68.2	-63.7	-37.7	-38.3	-45.9	-50.9	-54.1	
Personnel costs	-160.1	-167.9	-185.3	-187.5	-203.8	-272.2	-287.9	-298.2	
EBITDA	127.2	140.1	145.8	132.7	103.9	141.4	188.3	222.2	
IAC	0.0	-3.2	0.0	0.0	-134.2	0.9	0.0	0.0	
Adj. EBITDA	127.2	143.3	145.8	132.7	238.1	140.5	188.3	222.2	
Depreciation and amortisation	-19.8	-24.5	-37.4	-48.9	-172.4	-53.5	-61.9	-66.8	
EBIT	107.4	115.6	108.4	83.8	-68.5	87.9	126.5	155.5	
Adj. EBIT	107.4	118.8	108.4	83.8	65.7	87.0	126.5	155.5	33%
Financial items	-1.7	-1.8	-1.4	-7.0	-0.1	-3.2	-3.2	-3.0	
Profit before tax	105.7	117.0	107.0	76.8	-68.6	84.7	123.3	152.5	
Taxes paid	-25.7	-26.2	-25.8	-17.4	1.2	-20.9	-27.7	-34.3	
Adj. Net profit	80.0	94.0	81.2	59.4	66.8	63.0	95.5	118.2	
EPS	6.33	6.67	5.96	4.36	-4.94	4.69	7.00	8.65	
Adj. EPS (diluted)	6.33	6.67	5.96	4.36	4.90	4.61	7.00	8.65	21%
DPS	5.00	5.00	3.00	0.00	0.00	1.61	2.45	3.03	
Margins									
Gross	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	97.4%	97.6%	
EBITDA	36.9%	36.4%	35.9%	35.7%	29.0%	33.6%	39.0%	42.3%	
Adj. EBITDA	36.9%	37.2%	35.9%	35.7%	66.5%	33.4%	39.0%	42.3%	
EBIT	31.1%	30.0%	26.7%	22.5%	-19.1%	20.9%	26.2%	29.6%	
Adj. EBIT	31.1%	30.8%	26.7%	22.5%	18.4%	20.7%	26.2%	29.6%	
FCF margin	25.0%	11.9%	5.4%	9.9%	16.1%	15.9%	17.3%	21.4%	
Rule of 40 (EBIT)	36.2%	42.5%	32.0%	14.2%	14.6%	38.2%	40.9%	38.5%	
ROCE	37.4%	28.1%	17.7%	12.4%	9.9%	13.1%	17.4%	19.3%	
Cash flow									
Cash flow from operating activities	123.9	92.6	105.7	118.4	131.6	122.7	154.1	189.1	
Capex	-19.0	-46.8	-83.6	-81.4	-74.1	-55.9	-70.8	-76.4	
Adj. FCF	104.9	45.8	22.1	37.0	57.5	66.8	83.3	112.7	25%
Cash conversion (FCF/EBIT)	98%	39%	20%	44%	88%	77%	66%	72%	
Balance sheet									
Cash	119.5	106.1	60.7	67.8	113.4	144.9	206.2	285.4	
Net cash (-) / net debt (+)	-117.0	-103.3	18.4	-1.5	-57.4	-120.9	-182.2	-261.4	
Net debt/EBITDA	-0.9x	-0.7x	0.1x	0.0x	-0.6x	-0.9x	-1.0x	-1.2x	

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

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	417.7	468.5	489.3	11%
Security solutions	0.0	5.0	1.7	5.0	0.7	2.0	13.9	35.9	271%
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	420.6	482.4	525.2	14%
Net sales growth by segment									
Development tools	5%	10%	6%	-9%	-3%	18%	12%	4%	
Security solutions			-66%	194%	-86%	188%	587%	159%	
Other									
Total	5%	10%	5%	-8%	-4%	18%	15%	9%	
Net sales by product									
License-based	217.3	242.9	236.3	212.4	196.1	242.4	292.1	324.1	18%
Support and softw are updates	108.6	119.4	146.3	145.2	141.6	161.2	172.0	182.0	9%
Other	19.1	22.9	23.0	14.4	18.1	16.1	18.3	19.1	2%
Total	345.0	385.2	405.6	372.0	355.8	420.6	482.4	525.2	14%
Net sales growth by product									
License-based		12%	-3%	-10%	-8%	24%	21%	11%	
Support and softw are updates		10%	23%	-1%	-2%	14%	7%	6%	
Other		20%	0%	-37%	26%	-11%	13%	4%	
Total	5%	10%	5%	-8%	-4%	18%	15%	9%	

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	Q1'22	Q2'22	Q3'22e	Q4'22e
Net sales by segment										
Development tools	88.5	89.5	88.6	87.2	87.8	91.5	97.0	107.2	105.7	107.8
Security solutions	0.4	1.2	0.3	0.2	0.1	0.1	0.4	0.4	0.5	0.7
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	98.3	107.6	106.2	108.5
Net sales growth by segment										
Development tools	-11%	-16%	-3%	-11%	-1%	2%	9%	23%	20%	18%
Security solutions	33%	300%	-67%	-92%	-75%	-92%	33%	100%	408%	609%
Other										
Total	-11%	-15%	-4%	-13%	-1%	1%	10%	23%	20%	18%
Net sales by product										
License-based	50.8	52.0	50.1	50.4	46.2	49.4	52.0	67.8	59.9	62.7
Support and softw are updates	35.5	35.3	34.7	33.9	36.9	36.1	41.2	36.9	41.8	41.3
Other	2.6	3.4	4.1	3.1	4.8	6.1	4.2	2.9	4.5	4.5
Total	88.9	90.7	88.9	87.4	90.0	91.6	98.3	107.6	106.2	108.5
Net sales growth by product										
License-based	-13%	-12%	-1%	-15%	-9%	-5%	4%	35%	30%	27%
Support and softw are updates	-2%	-14%	-7%	-8%	4%	2%	19%	9%	13%	14%
Other	-52%	-45%	-5%	-24%	85%	79%	2%	-6%	-6%	-26%
Total	-11%	-15%	-4%	-13%	-1%	1%	10%	23%	20%	18%

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	Q1'22	Q2'22	Q3'22e	Q4'22e
Net sales	88.9	90.7	88.9	87.4	90.0	91.6	98.3	107.6	106.2	108.5
Grow th YOY, of w hich	-11%	-15%	-4%	-13%	-1%	1%	10%	23%	20%	18%
Organic	-6%	-11%	6%	-2%	-1%	2%	3%	14%	13%	10%
Structural	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
FX	-6%	-4%	-10%	-10%	0%	-1%	7%	9%	8%	9%
COGS	-2.7	-4.0	-3.4	-2.7	-2.8	-3.0	-2.8	-3.1	-3.4	-3.5
Gross profit	86.2	86.7	85.5	84.7	87.2	88.6	95.5	104.5	102.8	105.0
Capitalised work	0.0	0.0	20.3	16.4	0.0	0.0	12.2	10.5	14.0	15.0
Other external expenses	-8.5	-7.2	-10.9	-12.9	-8.5	-12.0	-11.5	-11.9	-11.0	-11.5
Personnel costs	-40.9	-47.0	-65.1	-62.2	-43.9	-63.4	-66.0	-71.2	-65.0	-70.0
EBITDA	36.8	32.5	29.8	26.0	34.8	13.2	30.2	31.9	40.8	38.5
IAC	0.0	0.0	0.0	-2.0	2.1	-134.2	0.9	0.0	0.0	0.0
Adj. EBITDA	36.8	32.5	29.8	28.0	32.7	147.4	29.3	31.9	40.8	38.5
Depreciation and amortisation	-11.4	-13.5	-12.8	-13.3	-14.1	-132.2	-13.0	-12.3	-13.5	-14.6
EBIT	25.4	19.0	17.0	12.7	20.7	-119.0	17.2	19.6	27.3	23.9
Adj. EBIT	25.4	19.0	17.0	14.7	18.6	15.2	16.3	19.6	27.3	23.9
Financial items	-0.5	-4.5	-0.6	-1.2	-0.3	1.8	-0.9	-0.5	-0.9	-0.9
Profit before tax	24.9	14.5	16.4	11.5	20.4	-117.2	16.3	19.1	26.4	23.0
Taxes paid	-6.2	-2.5	-3.6	-2.2	-4.7	11.8	-4.4	-4.8	-6.6	-5.0
Adj. Net profit	18.7	12.0	12.8	11.3	13.6	28.8	11.0	14.3	19.7	17.9
EPS	1.37	0.88	0.94	0.68	1.17	-7.72	0.88	1.05	1.44	1.31
Adj. EPS (diluted)	1.37	0.88	0.94	0.83	1.00	2.11	0.81	1.05	1.44	1.31
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%	97.2%	97.1%	96.8%	96.8%
EBITDA	41.4%	35.8%	33.5%	29.7%	38.7%	14.4%	30.7%	29.6%	38.4%	35.5%
Adj. EBITDA	41.4%	35.8%	33.5%	32.0%	36.3%	160.9%	29.8%	29.6%	38.4%	35.5%
EBIT	28.6%	20.9%	19.1%	14.5%	23.0%	-129.9%	17.5%	18.2%	25.7%	22.0%
Adj. EBIT	28.6%	20.9%	19.1%	16.8%	20.7%	16.6%	16.6%	18.2%	25.7%	22.0%
FCF margin	16.6%	10.6%	1.6%	12.5%	24.1%	25.5%	15.7%	15.3%	17.8%	14.8%
Rule of 40 (EBIT)	17.5%	5.9%	15.4%	4.1%	21.9%	17.6%	27.2%	41.3%	43.7%	40.4%
ROCE	13.5%	12.3%	12.5%	10.8%	9.7%	9.3%	9.4%	10.4%	11.9%	13.0%
Cash flow										
Cash flow from operating activities	32.7	27.8	22.0	27.6	41.4	40.5	28.8	26.0	34.8	33.1
Capex	-17.9	-18.2	-20.6	-16.7	-19.7	-17.1	-13.4	-9.5	-16.0	-17.1
Adj. FCF	14.8	9.6	1.4	10.9	21.7	23.4	15.4	16.5	18.9	16.0
Cash conversion (FCF/EBIT)	58%	51%	8%	74%	117%	154%	94%	84%	69%	67%
Balance sheet										
Cash	65.7	67.8	66.8	72.2	91.3	113.4	125.0	117.9	132.9	144.9
Net cash (-) / net debt (+)	0.4	-1.5	-3.0	-13.8	-36.4	-57.4	-72.0	-85.9	-104.9	-120.9
Net debt/EBITDA	0.0x	0.0x	0.0x	-0.1x	-0.3x	-0.6x	-0.7x	-0.8x	-0.9x	-0.9x

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

Valuation

Figure 18: Valuation approaches (SEKm, %)

	Peers regression	DCF	Historical Average
Net sales (2022e)			420
Adj. EBIT (2022e)			87
Adj. EPS (2022e)			4.61
Sales CAGR (2021–2023e)	15.5		16.1
Adj. EBIT margin (2022e)	21.6		20.7
RO40 (2022e)	45.7		36.8
Target multiple	RO40, P/B, EV/S	10% WACC	20x EV/EBIT
Enterprise value	3,299	3,110	1,740
Net debt (+)/cash (-)	-121	-121	-121
Equity value	3,419	3,230	1,861
NOSH	13.7	13.7	13.7
Implied price/share	250	237	136
Implied potential	94%	84%	6%
2024e valuation multiples			
Implied EV/sales	6.3	5.9	3.3
Implied EV/EBIT	21.2	20.0	11.2
Implied P/E	28.9	27.3	15.8

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	420	482	525
Growth YOY	5.4%	5.1%	10.2%	5.2%	-8.3%	-4.4%	18.2%	14.7%	8.9%
Gross profit	316	337	376	395	358	346	408	470	513
Gross margin	96.3%	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	97.4%	97.6%
Adj. EBITDA	117	127	140	146	133	104	141	188	222
EBITDA margin	36.9%	36.9%	37.2%	35.9%	35.7%	66.5%	33.4%	39.0%	42.3%
Adj. EBIT	101	107	119	108	84	66	87	126	155
EBIT margin	30.6%	31.1%	30.8%	26.7%	22.5%	18.4%	20.7%	26.2%	29.6%
Adj. Net profit	82	80	94	81	59	67	63	96	118
Adj. FCF	95	105	46	22	37	58	67	83	113
FCF margin	29.0%	30.4%	11.9%	5.4%	9.9%	16.2%	15.9%	17.3%	21.4%
Cash conversion	95%	98%	39%	20%	44%	88%	77%	66%	72%
Rule of 40 (EBIT)	36.0%	36.2%	41.0%	31.9%	14.2%	14.0%	38.9%	40.9%	38.5%
ROCE	35.0%	37.4%	28.1%	17.7%	12.4%	9.9%	13.1%	17.4%	19.3%
ROIC	27.4%	28.5%	21.9%	13.8%	10.1%	10.4%	10.1%	13.6%	15.0%
Market cap	2,602	2,387	3,310	2,535	1,905	1,606	1,758	1,758	1,758
Net debt	-97	-117	-103	18	-1	-57	-121	-182	-261
Enterprise value	2,505	2,270	3,206	2,554	1,904	1,548	1,638	1,576	1,497
EV/Sales	7.6x	6.6x	8.3x	6.3x	5.1x	4.4x	3.9x	3.3x	2.9x
EV/EBIT	24.9x	21.1x	27.0x	23.6x	22.7x	23.6x	18.8x	12.5x	9.6x
P/E	31.7x	29.8x	35.2x	31.2x	32.1x	24.0x	27.9x	18.4x	14.9x
FCF yield	3.7%	4.4%	1.4%	0.9%	1.9%	3.6%	3.8%	4.7%	6.4%

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

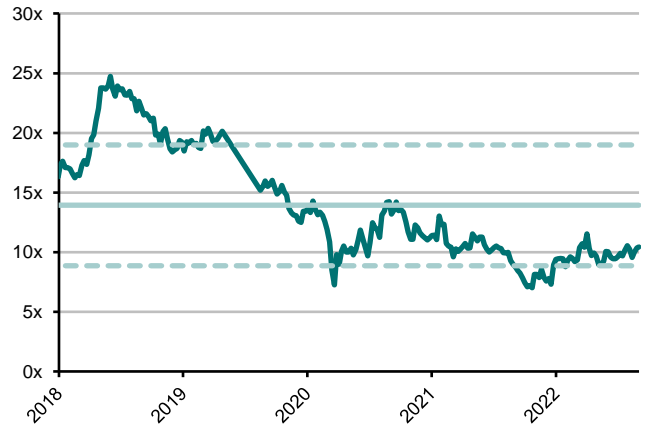
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Figure 20: EV/sales 12-month forward IAR Systems (2018–2022)



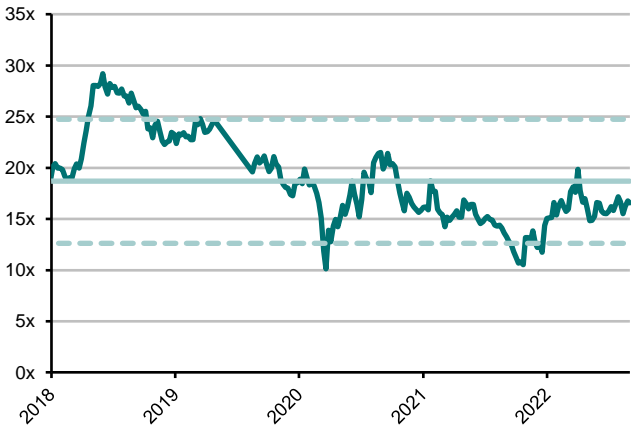
Source: Bloomberg

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



Source: Bloomberg

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



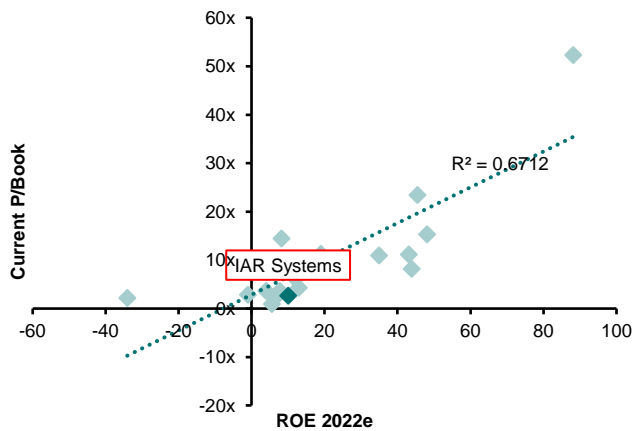
Source: Bloomberg

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



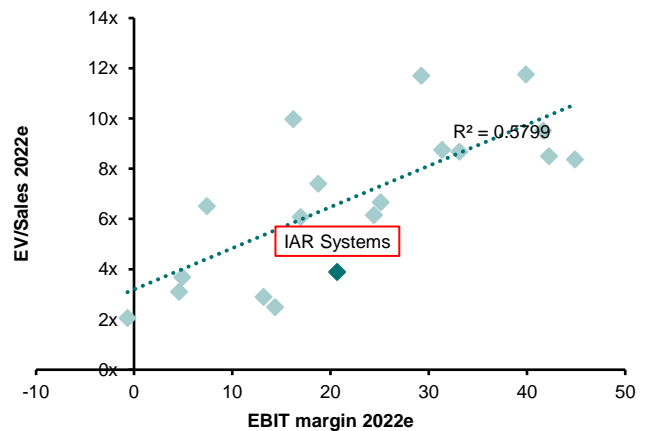
Source: Bloomberg

Figure 24: Current P/book versus ROE 2022e



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

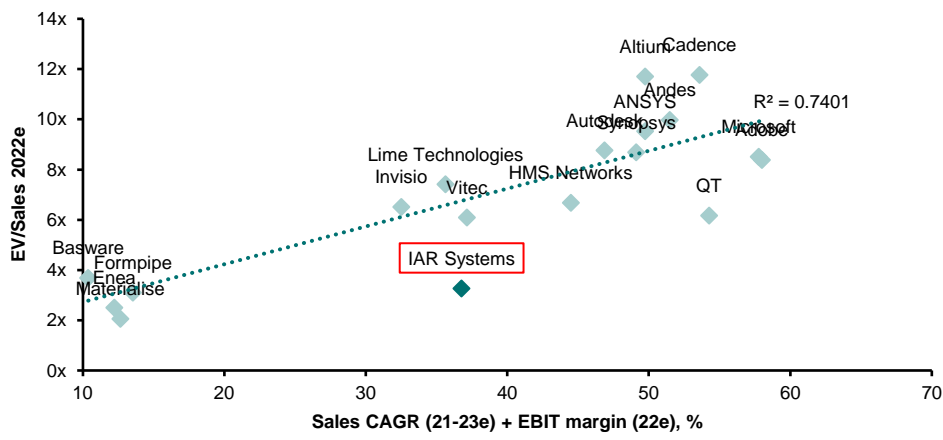
Figure 25: EV/sales versus EBIT margin (2022e)



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

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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)	1.8	28	18	15	19	12	10	12	8	7	4	3	3	1.3	3.8	10	14	20.7	26.2	16	39	20	
Premium/discount		-64%	-51%	-45%	-59%	-59%	-55%	-61%	-59%	-67%	-50%	-51%	-51%										
IAR Systems (Cons.)	1.8	32	21	16	21	14	11	12	9	7	4	4	3	1.1	3.8	9	13	19.2	24.5	13	31	34	
Premium/discount		-58%	-44%	-41%	-54%	-53%	-49%	-59%	-56%	-65%	-48%	-45%	-43%										
Nordic software																							
Basware	6.1	233	94	57	81	52		53	22		4	4	3				9	4.9	7.1	5	33		
Enea	2.0	14	11	10	16	12	10	8	6	5	3	2	2	0.0	15.9	6	5	14.3	17.5	-2	-16	-14	
Formpipe	1.5	99	32	21	70	26	17	20	13	10	3	3	3	2.8		4	11	4.6	10.9	9	-2	16	
HMS Networks	17.7	38	34	31	29	26	23	25	22	21	7	7	6	1.0	1.4	35	30	25.1	25.0	19	24	24	
Invisio	6.3	155	46	31	119	35	23	63	28	20	9	7	5	0.4	0.6	8	23	7.4	18.3	25	99	105	
Karnov	6.1	20	14	12	48	28	20	19	12	10	5	3	3	2.4		7	11	13.2	12.3	60	7	26	
Lime Technologies	4.0	48	37	35	46	35	32	27	23	22	9	7	7	0.9	2.0	46	45	18.8	20.8	17	19	20	
QT	13.4	37	29	20	31	22	15	28	20	14	8	6	5	0.0	2.4	48	41	24.4	26.3	30	36	36	
Vitec	13.3	36	30	27	44	34	29	22	18	16	7	6	6	0.6		12	16	17.0	18.7	20	19	21	
WithSecure	3.0									81	1	1	1	0.0		-34	-15	-29.7	-13.9	-19			
Engineering software																							
Adobe	1,834.5	27	23	20	21	18	15	19	17	14	10	8	7	0.0	4.3	43	38	44.9	45.1	13	12	13	
Altium	35.0	66	48	39	48	36	29	41	32	26	14	12	10	1.7	1.2	19	23	29.2	32.0	21	22	25	
Andes	6.7	49	43	24	87	30		58	26		14	10	7	1.1	1.1	8	9	16.2	32.9	35	66	52	
ANSYS	225.9	31	28	25	25	22	20	23	21	20	10	10	9	0.0	2.7	13	14	41.6	42.0	8	9	8	
Autodesk	459.1	39	30	25	31	23	20	30	22	19	10	9	8	0.0	3.4	88	132	31.4	36.0	16	30	30	
Cadence	495.8	41	36	32	32	28	25	30	26	19	13	12	11	0.0	2.4	40	36	39.9	40.3	14	18	19	
CDK Global																		24.9	30.1	6		12	
Materialise	6.5	363	80	32		69	24	23	16	11	2	2	2	0.0	0.3	-1	2	-0.7	2.9	13	-9	-11	
Microsoft	20,666.2	27	25	21	22	20	17	19	17	15	9	8	7	0.9	3.5	44	37	42.3	42.2	16	17	14	
Synopsys	539.9	37	32	29	29	24	21	27	24	27	10	9	8		3.0	25	25	33.1	34.1	16	23	22	
Average	1,281.2	75	37	27	46	30	21	30	20	21	8	7	6	0.7	3.2	23	26	20.1	24.0	16	23	23	
Median	13.3	39	32	26	32	27	21	26	22	19	9	7	6	0.4	2.4	16	23	21.6	25.6	16	19	20	

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

Summary of positives

Attractive position in a structural growth niche

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

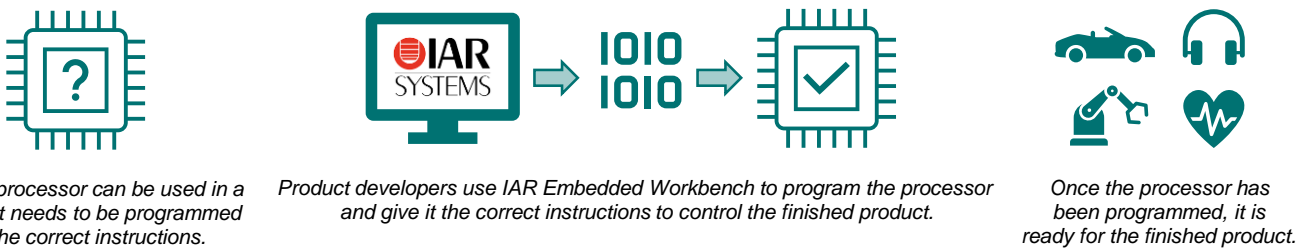
Business overview

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)

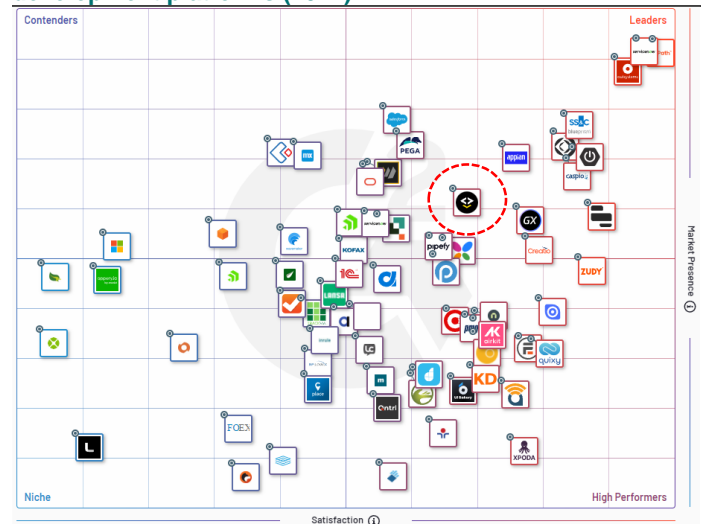
Headquartered in Uppsala, Sweden, IAR Systems has 200+ employees in 15 offices on three continents with technical support teams in its customers’ local time zones in 10+ languages. Its independent software supports more than 14,000 different processors from more than 70 processor vendors, which is more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

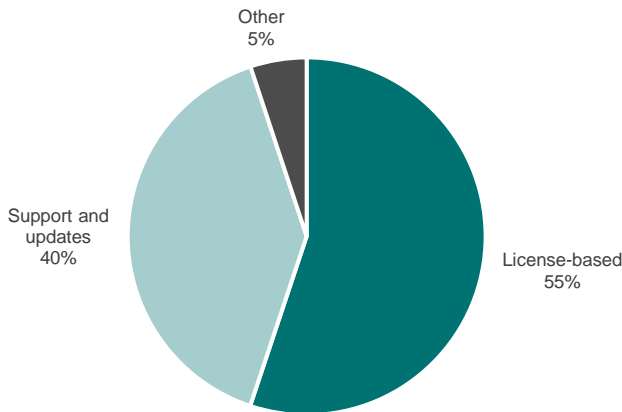
companies, etc.); and 4) suppliers of integrated programmes (real-time operating systems, graphics development, etc.).

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

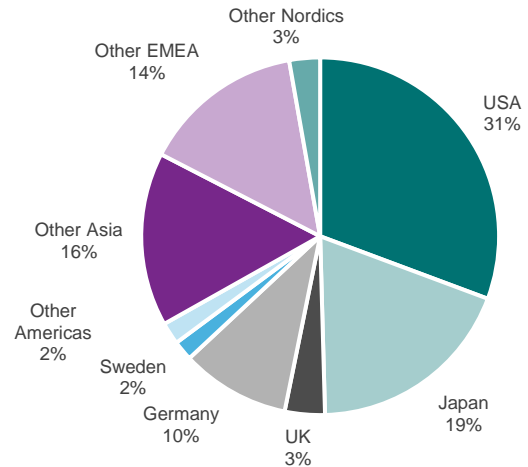
- **Development tools (~100% of net sales)** consist of IAR Embedded Workbench (8- to 64-bit) with world-leading code-optimisation technology, compiler, debugger probes and analysis tools (ensuring code quality and coding standards), functional safety certifications (pre-certified build tools), RISV-V architecture, and a Linux offering for continuous integration.
- **Security solutions (~0%)** 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 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 (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	421	482	525	407	457	508	14	26	18
Cost of sales	-13	-12	-12	-13	-12	-13	0	0	0
Gross profit	408	470	513	394	445	495	14	25	18
Operating expenses	-318	-339	-352	-313	-330	-349	-5	-9	-3
EBITDA	141	188	222	135	177	212	6	11	10
EBITDA adj	140	188	222	134	177	212	6	11	10
EBITDA margin (%)	33.6	39.0	42.3	33.2	38.8	41.7	0.4	0.2	0.6
Depreciation	-23	-23	-23	-22	-22	-23	-1	-1	0
Amortisation	-31	-39	-44	-36	-44	-46	5	5	3
EBIT	88	126	155	78	112	143	10	15	13
EBIT adj	87	126	155	77	112	143	10	15	13
Net financial items	-3	-3	-3	-4	-3	-3	0	0	0
PBT	85	123	152	74	109	140	11	15	13
Taxes	-21	-28	-34	-18	-24	-31	-3	-3	-3
Minorities	0	0	0			0			0
Net profit	64	96	118	57	84	108	7	11	10
Adjustments to net profit	-1	0	0	-1	0	0	0	0	0
Net profit adj	63	96	118	56	84	108	7	11	10
<i>Per share data (SEK)</i>									
EPS	4.69	7.00	8.65	4.16	6.16	7.95	0.53	0.83	0.71
EPS adj	4.61	7.00	8.65	4.08	6.16	7.95	0.53	0.83	0.71
DPS ordinary	1.61	2.45	3.03	1.43	2.16	2.78	0.19	0.29	0.25
DPS	1.61	2.45	3.03	1.43	2.16	2.78	0.19	0.29	0.25
<i>Other key metrics (%)</i>									
Revenue growth	17.5	14.7	8.9	13.6	12.3	11.1	3.9	2.4	-2.2
EBIT adj growth	32.4	45.4	22.9	17.0	45.4	27.9	15.4	-0.1	-5.0
EPS adj growth	-5.9	51.8	23.7	-16.7	51.0	28.9	10.8	0.7	-5.2
Avg. number of shares (m)	14	14	14	14	14	14	0	0	0
Capex	-56	-71	-76	-60	-75	-79	4	5	3
OpFCF	85	118	146	74	102	133	11	15	13
Working capital	-37	-34	-38	-27	-27	-24	-10	-7	-13
NIBD adj	-121	-182	-261	-106	-161	-227	-15	-21	-34

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	10.04	12.33	8.87	9.24	12.02	11.12	0.80	0.31	-2.25
Structure impact % YOY	0.00	0.00	0.00			0.00			0.00
Currency impact % YOY	8.17	2.36	0.00	5.09	0.29	0.00	3.08	2.07	0.00

Source: DNB Markets

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Quarterly numbers

(SEKm)	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022e	Q4 2022e	Q1 2023e	Q2 2023e	Q3 2023e
Revenues	89	87	90	92	98	108	106	108	114	126	121
Cost of sales	-3	-3	-3	-3	-3	-3	-3	-4	-3	-3	-3
Gross profit	86	85	87	89	96	105	103	105	111	123	118
Operating expenses	-76	-75	-52	-75	-78	-83	-76	-82	-84	-86	-84
EBITDA	30	26	35	13	30	32	41	38	40	51	49
Depreciation	-5	-5	-5	-5	-6	-6	-6	-6	-5	-6	-6
Amortisation	-8	-8	-9	-127	-7	-7	-8	-9	-10	-10	-10
EBIT	17	13	21	-119	17	20	27	24	25	35	33
Net financial items	-1	-1	0	2	-1	-1	-1	-1	-1	-1	-1
PBT	16	12	20	-117	16	19	26	23	25	35	32
Taxes	-4	-2	-5	12	-4	-5	-7	-5	-6	-8	-7
Minorities	0	0	0	0	0	0	0	0	0	0	0
Net profit	13	9	16	-105	12	14	20	18	19	27	25
Adjustments to net profit	0	2	-2	134	-1	0	0	0	0	0	0
Net profit adj	13	11	14	29	11	14	20	18	19	27	25
Dividend paid	0	0	0	0	0	0	0	0	0	-22	0
Avg. number of shares (m)	14	14	14	14	14	14	14	14	14	14	14
<i>Per share data (SEK)</i>											
EPS	0.94	0.68	1.17	-7.72	0.88	1.05	1.44	1.31	1.40	1.97	1.82
EPS adj	0.94	0.83	1.00	2.11	0.81	1.05	1.44	1.31	1.40	1.97	1.82
DPS ordinary	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.61	0.00
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.61	0.00
<i>Growth and margins (%)</i>											
Revenues, QOQ growth	-2.0	-1.7	3.0	1.8	7.3	9.5	-1.3	2.2	5.1	10.3	-3.9
Revenues, YOY growth	-3.7	-12.7	1.2	1.0	10.6	23.1	18.0	18.4	16.0	16.9	13.8
EPS adj, YOY growth	15.4	-35.8	-27.3	140.0	-14.1	26.6	45.1	-37.7	73.4	87.7	26.0
Gross margin	96.2	96.9	96.9	96.7	97.2	97.1	96.8	96.8	97.1	97.5	97.6
EBITDA adj margin	33.5	32.0	36.3	160.9	29.8	29.6	38.4	35.5	35.4	40.4	40.2
Depreciation/revenues	-5.5	-5.9	-5.7	-5.7	-5.8	-5.3	-5.2	-5.2	-4.8	-4.6	-4.7
EBIT adj margin	19.1	16.8	20.7	16.6	16.6	18.2	25.7	22.0	22.3	28.2	27.2
Net profit margin	14.4	10.6	17.4	nm	12.1	13.3	18.6	16.5	16.7	21.3	20.6

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

Adjustments to quarterly numbers

(SEKm)	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022e	Q4 2022e	Q1 2023e	Q2 2023e	Q3 2023e
EBITDA	30	26	35	13	30	32	41	38	40	51	49
EBITDA adj	30	28	33	147	29	32	41	38	40	51	49
EBIT	17	13	21	-119	17	20	27	24	25	35	33
Other EBIT adjustments	0	-2	2	-134	1	0	0	0	0	0	0
EBIT adj	17	15	19	15	16	20	27	24	25	35	33
Net profit	13	9	16	-105	12	14	20	18	19	27	25
Other EBIT adjustments	0	-2	2	-134	1	0	0	0	0	0	0
Net profit adj	13	11	14	29	11	14	20	18	19	27	25

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

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Quarterly numbers by segment and assumptions

(SEKm)	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022e	Q4 2022e	Q1 2023e	Q2 2023e	Q3 2023e
Assumptions											
Revenue org. % YOY	5.96	-2.40	-0.67	1.98	3.04	13.84	12.58	9.68	12.41	13.20	12.43
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	-9.64	-10.29	-0.45	-0.99	6.52	9.27	7.76	8.76	4.53	3.71	1.37

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	421	482	525
Cost of sales	-10	-12	-9	-9	-11	-14	-12	-13	-12	-12
Gross profit	301	316	337	376	395	358	346	408	470	513
Operating expenses	-203	-203	-209	-236	-249	-225	-242	-318	-339	-352
EBITDA	98	113	127	140	146	133	104	141	188	222
Depreciation	-3	-3	-2	-3	-13	-20	-20	-23	-23	-23
Amortisation	-12	-14	-17	-22	-25	-29	-152	-31	-39	-44
EBIT	83	97	107	116	108	84	-69	88	126	155
Net financial items	0	0	-2	-2	-1	-7	0	-3	-3	-3
PBT	83	100	106	117	107	77	-69	85	123	152
Taxes	-20	-22	-26	-26	-26	-17	1	-21	-28	-34
Effective tax rate (%)	24	22	24	22	24	23	2	25	23	23
Minorities	0	0	0	0	0	0	0	0	0	0
Net profit	63	78	80	91	81	59	-67	64	96	118
Adjustments to net profit	0	4	0	3	0	0	134	-1	0	0
Net profit adj	63	82	80	94	81	59	67	63	96	118
Dividend paid	-63	-88	-63	-68	-68	0	0	0	-22	-33
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	4.69	7.00	8.65
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.61	7.00	8.65
DPS ordinary	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.61	2.45	3.03
DPS	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.61	2.45	3.03
<i>Growth and margins (%)</i>										
Revenue growth	21.9	5.4	5.1	11.7	5.3	-8.3	-3.8	17.5	14.7	8.9
EPS adj growth	50.2	23.0	2.6	5.3	-10.6	-26.8	12.5	-5.9	51.8	23.7
Gross margin	96.7	96.3	97.5	97.7	97.3	96.2	96.6	97.0	97.4	97.6
EBITDA margin	31.5	34.5	36.9	36.4	35.9	35.7	29.0	33.6	39.0	42.3
EBITDA adj margin	31.5	35.7	36.9	37.2	35.9	35.7	66.5	33.4	39.0	42.3
Depreciation/revenues	-0.8	-0.8	-0.7	-0.7	-3.2	-5.5	-5.7	-5.4	-4.7	-4.4
EBIT margin	26.8	29.4	31.1	30.0	26.7	22.5	nm	20.9	26.2	29.6
EBIT adj margin	26.8	30.6	31.1	30.8	26.7	22.5	18.4	20.7	26.2	29.6
PBT margin	26.7	30.5	30.6	30.4	26.4	20.6	nm	20.1	25.6	29.0
Net profit margin	20.3	23.8	23.2	23.6	20.0	16.0	nm	15.2	19.8	22.5

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	141	188	222
EBITDA adj	98	117	127	143	146	133	238	140	188	222
EBIT	83	97	107	116	108	84	-69	88	126	155
Other EBIT adjustments	0	-4	0	-3	0	0	-134	1	0	0
EBIT adj	83	101	107	119	108	84	66	87	126	155
Net profit	63	78	80	91	81	59	-67	64	96	118
Other EBIT adjustments	0	-4	0	-3	0	0	-134	1	0	0
Net profit adj	63	82	80	94	81	59	67	63	96	118
<i>Per share data (SEK)</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.69	7.00	8.65
Recommended adjustment	0.00	0.00	0.00	0.00	0.00	0.00	9.85	-0.08	0.00	0.00
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.61	7.00	8.65

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	64	96	118
Depreciation and amortisation	15	17	20	25	37	49	172	53	62	67
Cash flow from operations (CFO)	99	114	124	93	106	118	132	123	154	189
Capital expenditure	-19	-19	-19	-47	-84	-81	-74	-56	-71	-76
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	-56	-71	-76
Free cash flow (FCF)	80	95	86	-125	4	37	58	67	83	113
Net change in debt	0	0	0	0	30	6	1	0	0	0
Dividends paid	-63	-88	-63	-68	-68	0	0	0	-22	-33
Share issue (repurchase)	0	0	0	172	0	0	0	0	0	0
Other	0	0	0	4	-14	-30	-16	-35	0	0
Cash flow from financing (CFF)	-64	-88	-63	108	-52	-25	-15	-35	-22	-33
Total cash flow (CFO+CFI+CFF)	17	7	23	-17	-49	12	42	32	61	79
<i>FCFF calculation</i>										
Free cash flow	80	95	86	-125	4	37	58	67	83	113
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	-6.7	25.6	22.7
CFI	42.3	-3.3	-98.9	-478.5	53.0	20.4	9.0	24.5	-26.6	-7.9
FCF	108.3	18.5	-9.4	-244.7	102.8	957.1	55.4	16.2	24.7	35.2
CFF	-19.5	-39.0	28.5	270.4	-148.3	52.7	38.6	-129.1	36.3	-51.8
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	878	946	1,029
Inventories	5	6	5	7	7	6	10	9	10	10
Trade receivables	44	48	51	63	67	59	59	63	60	55
Other receivables	20	19	12	38	52	64	44	52	52	52
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	206	285
Current assets	158	172	187	214	186	196	226	269	328	402
Property, plant and equipment	7	6	6	9	7	8	15	15	16	16
Other intangible assets	192	197	194	484	624	624	567	586	594	603
Deferred tax assets	37	16	3	13	5	4	3	4	4	4
Non-current financial assets	5	5	20	2	2	3	3	3	3	3
Non-current assets	241	224	223	508	639	638	587	608	617	627
Total assets	399	396	410	722	825	834	813	878	946	1,029
Equity and liabilities	399	396	410	722	825	834	813	878	946	1,029
Total equity	291	280	290	550	592	613	585	666	739	824
Trade payables	5	5	6	7	9	5	9	10	10	10
Other payables and accruals	83	92	86	131	117	111	133	151	146	144
Short-term debt	1	1	1	0	25	18	18	0	0	0
Total current liabilities	90	99	102	140	164	150	179	177	171	171
Long-term debt	1	2	2	1	41	32	20	8	8	8
Deferred tax liabilities	17	15	14	30	27	37	28	26	26	26
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	35	35	35
Total liabilities	108	116	120	172	233	220	228	212	206	206
Total equity and liabilities	399	396	410	722	825	834	813	878	946	1,029
<i>Key metrics</i>										
Net interest bearing debt	-88	-97	-117	-103	18	-2	-57	-121	-182	-261

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	128.80	128.80	128.80
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	1,758	1,758	1,758
Net interest bearing debt	-88	-97	-117	-103	18	-2	-57	-121	-182	-261
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	-121	-182	-261
EV	1,807	2,505	2,270	3,206	2,554	1,904	1,548	1,638	1,576	1,497
EV adj	1,807	2,505	2,270	3,206	2,554	1,904	1,548	1,638	1,576	1,497
<i>Valuation</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.69	7.00	8.65
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.61	7.00	8.65
DPS ordinary	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.61	2.45	3.03
DPS	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.61	2.45	3.03
P/E	29.9	33.4	29.8	36.4	31.2	32.1	-23.8	27.5	18.4	14.9
P/E adj	29.9	33.4	29.8	36.4	31.2	32.1	24.0	27.9	18.4	14.9
P/B	6.51	9.31	8.22	6.02	4.28	3.11	2.74	2.64	2.38	2.13
Average ROE	21.9%	27.3%	28.1%	21.6%	14.2%	9.9%	-11.2%	10.2%	13.6%	15.1%
Earnings yield adj	3.3%	3.0%	3.4%	2.7%	3.2%	3.1%	4.2%	3.6%	5.4%	6.7%
Dividend yield	3.3%	3.4%	2.6%	2.1%	1.6%	0.0%	0.0%	1.3%	1.9%	2.4%
Free cash flow yield	4.2%	3.7%	3.6%	-3.8%	0.1%	1.9%	3.6%	3.8%	4.7%	6.4%
EV/SALES	5.80	7.63	6.58	8.32	6.30	5.12	4.32	3.89	3.27	2.85
EV/SALES adj	5.80	7.63	6.58	8.32	6.30	5.12	4.32	3.89	3.27	2.85
EV/EBITDA	18.4	22.1	17.8	22.9	17.5	14.3	14.9	11.6	8.4	6.7
EV/EBITDA adj	18.4	21.4	17.8	22.4	17.5	14.3	6.5	11.7	8.4	6.7
EV/EBIT	21.7	26.0	21.1	27.7	23.6	22.7	-22.6	18.6	12.5	9.6
EV/EBIT adj	21.7	24.9	21.1	27.0	23.6	22.7	23.6	18.8	12.5	9.6
EV/capital employed	6.2	8.9	7.8	5.8	3.8	2.8	2.4	2.4	2.1	1.8
EV/NOPLAT	27.8	33.3	27.1	35.6	30.2	29.1	-29.0	23.9	16.0	12.3
EV/OpFCF (taxed)	29.8	32.8	26.8	45.6	66.6	57.9	10.4	25.0	17.6	13.4

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

2 September 2022

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	7.6	10.5	12.0
ROCE	28.6	35.0	37.4	28.1	17.7	12.4	9.9	13.1	17.4	19.3
ROCE after tax	22.3	27.3	29.1	21.9	13.8	9.7	7.8	10.2	13.6	15.1
<i>Return on invested capital (%)</i>										
Net PPE/revenues	2.1	1.9	1.8	2.3	1.8	2.0	4.1	3.5	3.2	3.1
Working capital/revenues	-6.1	-7.5	-6.9	-7.8	-0.2	3.4	-8.3	-8.8	-7.0	-7.2
<i>Cash flow ratios (%)</i>										
FCF/revenues	25.8	29.0	25.0	-32.4	0.9	9.9	16.1	15.9	17.3	21.4
FCF yield (%)	4.2	3.7	3.6	1.4	0.9	1.9	3.6	3.8	4.7	6.4
CFO/revenues	31.7	34.8	35.9	24.0	26.1	31.8	36.8	29.2	32.0	36.0
CFO/market capitalisation	5.2	4.4	5.2	2.8	4.2	6.2	8.2	7.0	8.8	10.8
CFO/capex	508.8	614.0	652.1	197.9	126.4	145.5	177.6	219.5	217.7	247.4
CFO/current liabilities	110.2	115.8	121.1	66.2	64.4	78.9	73.7	69.4	89.9	110.9
Cash conversion ratio	126.8	122.2	107.9	-137.6	4.3	62.3	-85.3	104.6	87.2	95.3
Capex/revenues	6.2	5.7	5.5	12.1	20.6	21.9	20.7	13.3	14.7	14.6
Capex/depreciation	776.0	744.0	791.7	1800.0	648.1	401.0	363.2	247.7	309.7	328.6
OpFCF margin	25.3	30.0	31.4	25.1	15.3	13.8	45.8	20.1	24.4	27.8
Total payout ratio	99.6	113.3	78.9	75.0	50.4	0.0	0.0	34.4	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	-0.86	-0.97	-1.18
Total debt/total capital (BV)	0.00	0.01	0.01	0.00	0.08	0.06	0.05	0.01	0.01	0.01
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	263.1	285.3	302.6
Receivables turnover days	74.5	74.7	66.2	96.1	106.8	120.2	104.7	99.7	84.9	74.0
Credit period	170.1	158.6	244.8	296.1	310.9	129.4	279.8	287.0	285.3	302.6
Cash conversion cycle	85.1	83.7	44.8	67.7	18.9	138.3	113.8	75.8	84.9	74.0

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

2 September 2022

Important Information

Company: IAR Systems
 Coverage by Analyst: Joachim Gunell
 Date: 01-9-2022

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