

IAR SYSTEMS

Fair value cut to SEK120–200

Amid 1) a hiccup in its turnaround; 2) a shift in the investor base; and 3) low liquidity in the shares, IAR Systems' share price is back at 2015 levels. We have reduced our 2023–2024e EPS by 33–20% to factor in slower organic growth (with high drop-through). Although 2023 seems to be a difficult year, we appreciate the combination of profitable growth, being net cash positive, defensive elements from c40% recurring revenues, and optionality from its embedded security offering. We note insiders have accumulated shares above current share-price levels recently. We have lowered our fair value to SEK120–200 (140–250).

Q2 preview. We expect Q2 organic net sales growth of -8% YOY, hurt by a tough YOY comparable, with extended perpetual licence sales cycles amid customer capex scrutiny offset by resilience in support-and-update sales (deferred revenues have grown 25–30% YOY in recent quarters), leading to sales of SEK105m. We forecast a 7.4% adj. EBIT margin (down 10.8%-points YOY), corresponding to a 'rule of 40' of 5.1%. IAR Systems recently announced a cost-savings programme targeting SEK27m in annual savings (aiming for a full run-rate by end-Q3 by reducing the group headcount by c11% in relation to its embedded security offering). Combined with softer IT spending and its ambition to pilot a SaaS offering in North America, we now forecast -2% YOY organic revenue growth in 2023. The Q2 results are due on 16 August.

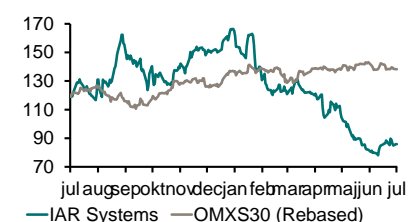
2023–2024e net sales reduced by 8–9% and EPS by 33–20%, to reflect a reset of embedded security forecasts, while we have lowered our organic growth assumptions for development tools given extended sales cycles for its licence-based revenues (~40% of group revenues). Given its 97% gross margin, such net sales changes have a high drop-through on EPS, offset by our lowered opex assumptions for 2024 (SEK19m versus its SEK27m targeted savings).

Fair value lowered to SEK120–200, corresponding to 2024e EV/EBIT of 15–26x.

Year-end Dec	2019	2020	2021	2022	2023e	2024e	2025e
Revenue (SEKm)	406	372	358	423	425	463	508
EBITDA adj (SEKm)	146	133	238	133	128	171	202
EBIT adj (SEKm)	108	84	66	79	60	99	124
PTP (SEKm)	107	77	-69	74	48	90	114
EPS rep (SEK)	5.96	4.36	-4.94	4.23	2.35	4.99	6.36
EPS adj (SEK)	5.96	4.36	4.90	4.50	3.14	5.49	6.86
DPS (SEK)	3.00	0.00	0.00	1.50	1.10	1.92	2.40
Revenue growth (%)	5.3	-8.3	-3.8	18.1	0.6	8.9	9.7
EBITDA growth adj (%)	1.7	-9.0	79.4	-44.3	-3.1	33.3	17.9
EPS growth adj (%)	-10.6	-26.8	12.5	-8.2	-30.2	74.9	25.0
EBITDA margin adj (%)	35.9	35.7	66.5	31.4	30.2	37.0	39.7
EV/Sales adj (x)	6.30	5.12	4.32	4.67	2.49	2.16	1.86
EV/EBITDA adj (x)	17.5	14.3	6.5	14.9	8.2	5.9	4.7
EV/EBIT adj (x)	23.6	22.7	23.6	24.9	17.8	10.1	7.6
P/E adj (x)	31.2	32.1	24.0	33.4	27.4	15.7	12.5
P/Book (x)	4.28	3.11	2.74	3.08	1.72	1.59	1.47
ROE (%)	14.2	9.9	nm	9.2	4.8	9.6	11.3
ROCE (%)	17.7	12.4	9.9	11.5	8.1	13.0	15.2
Dividend yield (%)	1.6	0.0	0.0	1.0	1.3	2.2	2.8
FCF yield (%)	0.9	1.9	3.6	3.3	5.0	6.1	6.9

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

IARB versus OMXS30 (12m)



Source: Factset

SUMMARY

Share price (SEK)	85.9
Tickers	IARB SS

CAPITAL STRUCTURE

No. of shares (m)	13.7
No. of shares fully dil. (m)	13.8
Market cap. (SEKm)	1,173
NIBD adj end-2023e (SEKm)	-115
Enterprise value adj (SEKm)	1,059
Net debt/EBITDA adj (x)	-0.89
Free float (%)	100

Source: Company, DNB Markets (estimates)

Note: Unless otherwise stated, the share prices in this note are the last closing price.

NEXT EVENT

Q2 2023	16/08/2023
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ESTIMATE CHANGES (SEK)

Year-end Dec	2023e	2024e	2025e
Sales (old)	462.0	510.9	555.8
Sales (new)	425.3	463.3	508.2
Change (%)	-8.0	-9.3	-8.6
EPS adj (old)	4.68	6.89	8.34
EPS adj (new)	3.14	5.49	6.86
Change (%)	-33.0	-20.3	-17.8

Source: DNB Markets.

This report has been commissioned and paid for by the company, and is deemed to constitute an acceptable minor non-monetary benefit as defined in MiFID II

ANALYSTS

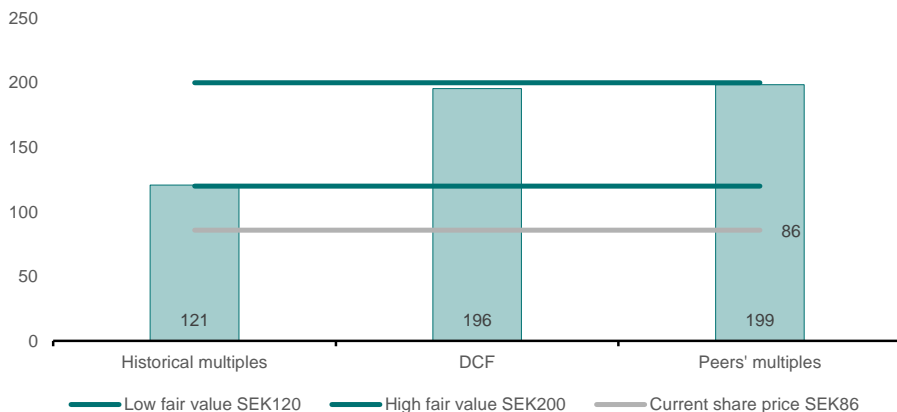
Joachim Gunell

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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 2x.

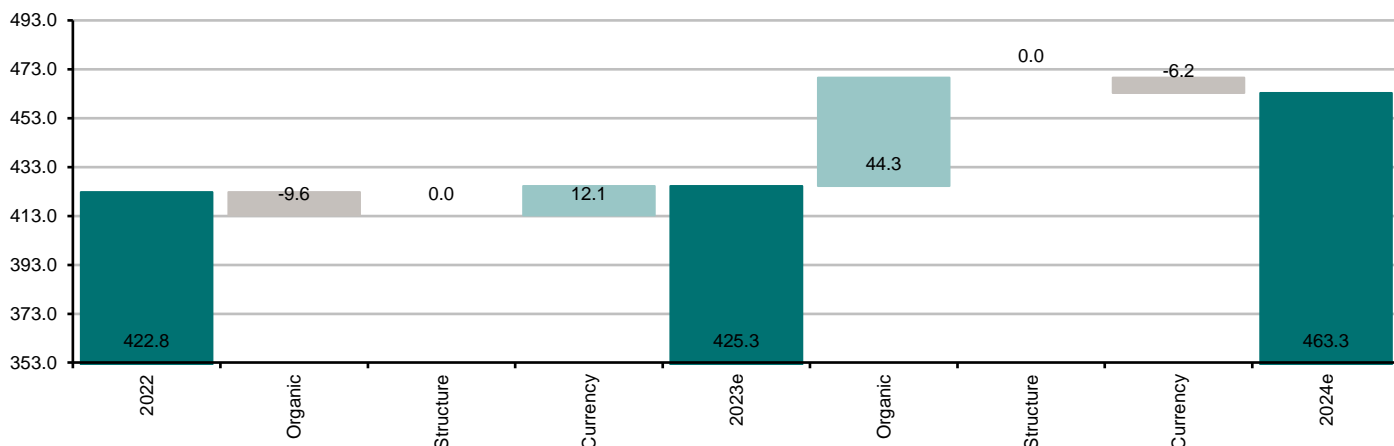
Source: DNB Markets

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 45,000+ OEM customers and 22,000+ active 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 large 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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Q2 preview

Figure 1: Q2 estimates

Key highlights (SEKm, except per share data)	Q2 2023e		Deviation	Deviation	Q2 2022	DNBe
	Actual	DNB	(%)	Absolute	Actual	2023e
Net sales		105.1			107.6	424.4
Gross profit		101.8			104.5	411.8
Gross margin		96.9%			97.1%	97.0%
One-offs		-2			0	-11
EBITDA adj.		23.3			31.9	117.7
EBITDA adj. margin		22.2%			29.6%	27.7%
EBIT		7.8			19.6	59.5
EBIT margin		7.4%			18.2%	14.0%
EBIT adj.		7.8			19.6	59.5
EBIT adj. margin		7.4%			18.2%	14.0%
EPS adj.		0.42			1.05	3.14
Adj. FCF (CFO - capex)		15.5			16.5	58.3
Cash conversion		198%			84%	98%
Rule of 40 (EBIT)		5.1%			41.3%	14.6%
Revenue growth YOY		-2.3%			23.1%	1.3%
Organic		-8.4%			13.8%	-2.3%
Structural		0.0%			0.0%	0.0%
FX		6.1%			9.3%	3.6%
Segment (SEKm)		Q2 2023e	Deviation	Deviation	Q2 2022	DNBe
		Actual	(%)	Absolute	Actual	2023e
Net sales						
Development tools		104.6			107.2	421.6
Security solutions		0.5			0.4	2.7
Other		0.0			0.0	0.0
Total		105.1			107.6	424.4
Net sales growth						
Development tools		-2.4%			22.9%	0.8%
Security solutions		31.1%			100.0%	82.6%
Other						
Total		-2.3%			23.1%	1.3%
Net sales						
License-based		57.0			67.8	215.8
Support and softw are updates		44.2			36.9	189.7
Other		4.0			2.9	18.9
Total		105.1			107.6	424.4

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

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Estimate revisions

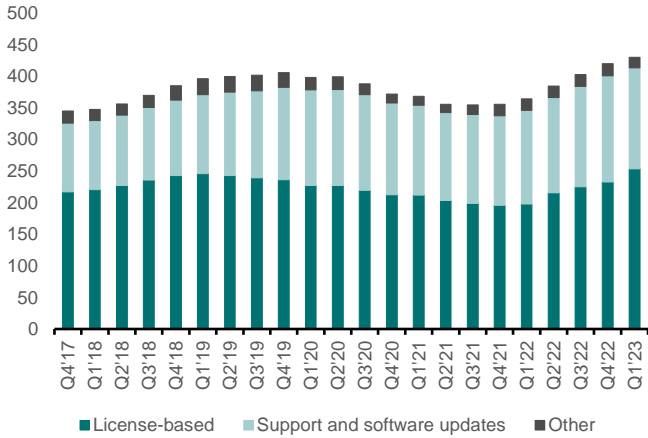
Figure 2: Estimate changes

(SEKm, except per share data)	Old			New			Change		
	2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
Net sales	462	511	556	425	463	508	-8%	-9%	-9%
Growth YOY, of which	10.0%	10.6%	8.8%	1.3%	8.9%	9.7%	-876bp	-164bp	90bp
Organic	7.1%	10.9%	8.8%	-2.3%	10.4%	9.7%	-933bp	-46bp	90bp
Structural	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0bp	0bp	0bp
FX	3.0%	-0.3%	0.0%	3.6%	-1.5%	0.0%	57bp	-118bp	0bp
Gross profit	448	496	541	412	449	494	-8%	-9%	-9%
Gross margin	97.0%	97.1%	97.4%	96.8%	97.0%	97.3%	-14bp	-14bp	-11bp
EBITDA	148	192	223	118	164	195	-20%	-14%	-13%
IAC	-7	-7	-7	-11	-7	-7	59%	0%	0%
Adj. EBITDA	155	199	230	128	171	202	-17%	-14%	-12%
Depreciation and amortisation	-60	-65	-71	-60	-65	-71	0%	0%	0%
EBIT	83	120	145	49	93	117	-41%	-23%	-19%
Adj. EBIT	90	127	152	60	99	124	-34%	-22%	-19%
Adj. EBIT margin	19.4%	24.9%	27.4%	14.0%	21.4%	24.4%	-544bp	-341bp	-298bp
Capitalised development costs (CDC)	53	54	56	49	55	63	-8%	3%	14%
EBIT excl. CDC	8.0%	14.3%	17.4%	2.5%	9.5%	11.9%	-549bp	-486bp	-542bp
Adj. Net profit	64	94	114	43	75	94	-33%	-20%	-18%
Adj. EPS (diluted)	4.68	6.89	8.34	3.14	5.49	6.86	-33%	-20%	-18%
DPS	1.64	2.41	2.92	1.10	1.92	2.40	-33%	-20%	-18%
Net sales by segment									
Development tools	451	480	504	422	448	477	-6%	-7%	-5%
Security solutions	11	31	52	3	15	31	-74%	-51%	-39%
Other	0	0	0	0	0	0			
Total	462	511	556	425	463	508	-8%	-9%	-9%
Net sales by product type									
License-based	271	308	344	216	246	278	-21%	-20%	-19%
Support and software updates	172	183	191	190	199	211	10%	9%	10%
Other	17	20	21	19	19	20	9%	-8%	-7%
Total	462	511	556	425	463	508	-8%	-9%	-9%
Balance sheet and cash flow									
Adj. FCF	72	85	95	59	72	81	-19%	-16%	-15%
Cash	188	242	297	174	223	270	-7%	-8%	-9%
Net cash (-) / net debt (+)	-128	-191	-253	-115	-171	-226	-10%	-10%	-11%

Source: DNB Markets

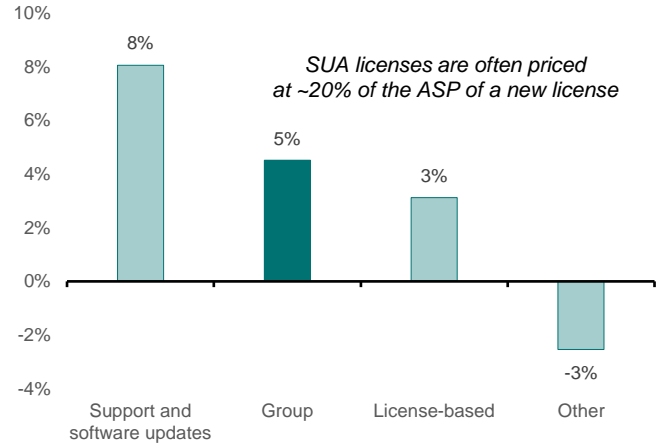
Key charts

Figure 3: Net sales mix by product type (LTM, 2017–2022)



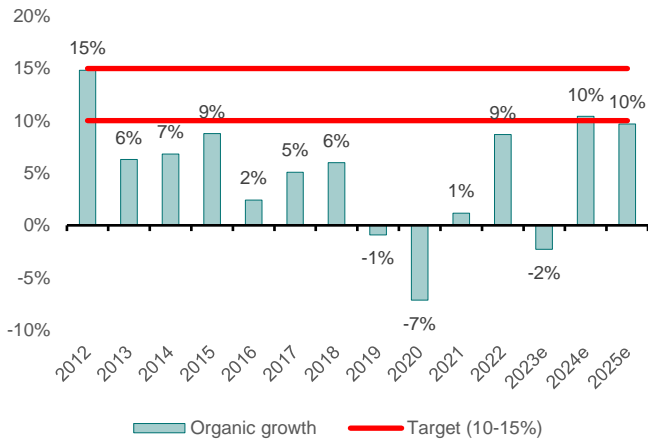
Source: Company (historical data), DNB Markets (further calculations)

Figure 4: Net sales CAGR by processor type (2017–2023)



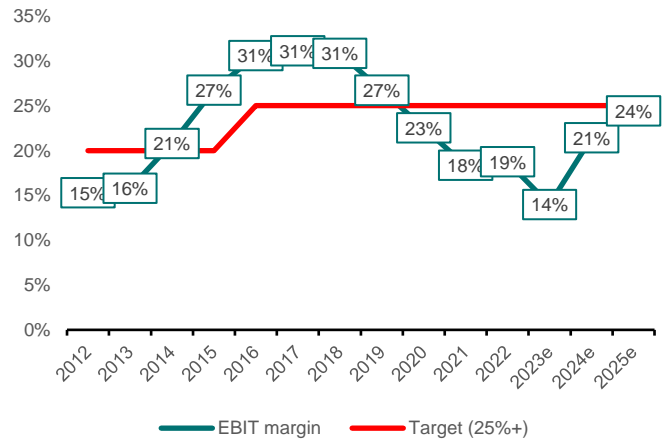
Source: Company (historical data), DNB Markets (further calculations)

Figure 5: Financial goal 1 – organic sales growth of 10–15%



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

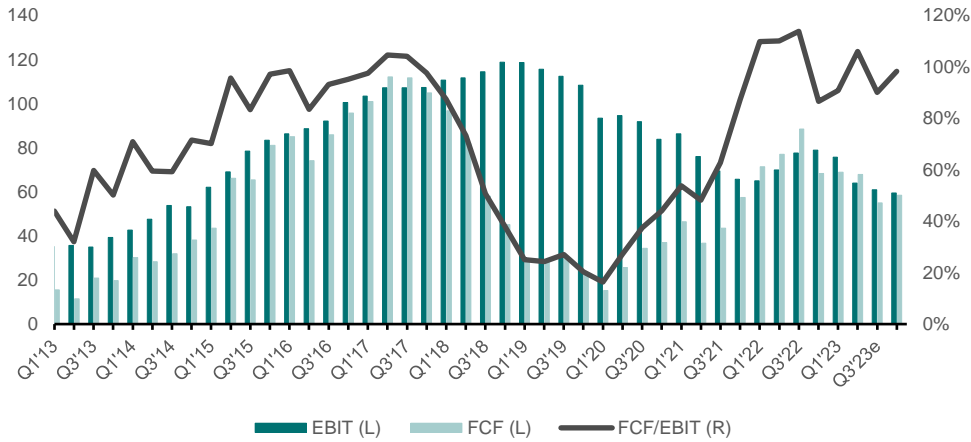
Figure 6: Financial goal 2 – EBIT margin >25%



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

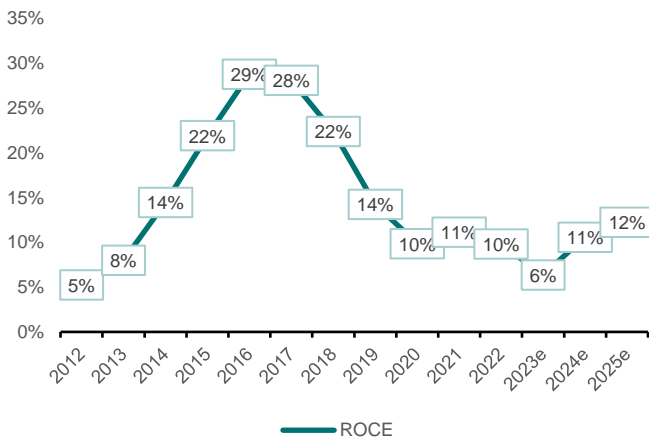
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Figure 7: LTM FCF versus LTM EBIT (2012–2023e) – coming out of an intense investment period to accelerate organic growth since 2018



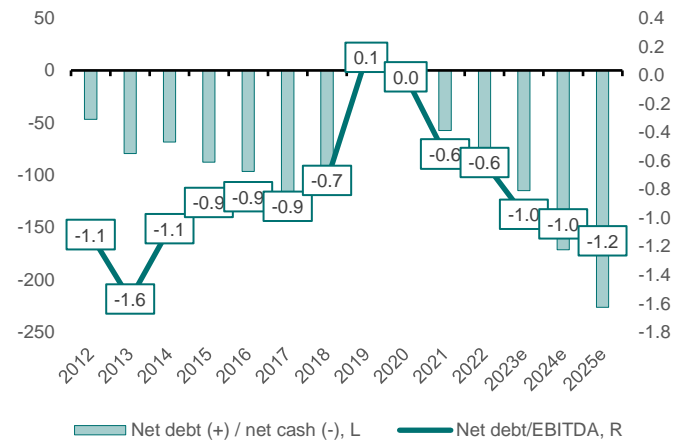
Source: DNB Markets (forecasts), company (historical data)

Figure 8: Return on capital employed (2012–2025e)



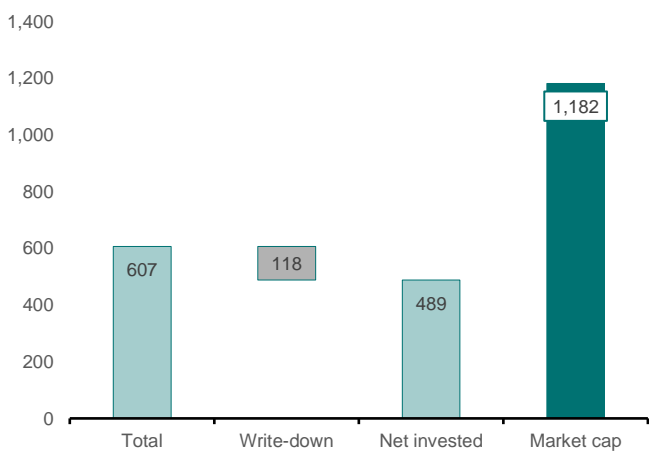
Source: DNB Markets (forecasts), company (historical data)

Figure 9: Net debt to EBITDA (x, SEKm)



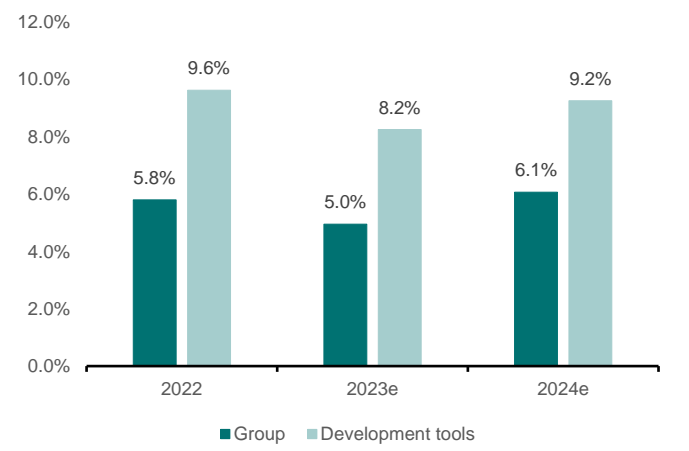
Source: DNB Markets (forecasts), company (historical data)

Figure 10: Investments (SEKm, 2016–2023e)



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

Figure 11: FCF yield (2022–2024e)



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

Forecasts

Figure 12: 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	424.4	463.3	508.2	7%
Growth YOY, of which	10%	5%	-8%	-4%	18%	1%	9%	10%	
Organic	6%	-1%	-7%	1%	9%	-2%	10%	10%	
Structural	0%	0%	0%	0%	0%	0%	0%	0%	
FX	4%	6%	-1%	-6%	9%	4%	-1%	0%	
COGS	-9.0	-10.8	-14.1	-12.0	-12.8	-13.5	-13.9	-13.9	
Gross profit	376.2	394.8	357.9	346.0	410.0	411.8	449.4	494.3	
Capitalised work	0.0	0.0	0.0	64.4	50.2	48.9	55.4	63.4	
Other external expenses	-68.2	-63.7	-37.7	-48.3	-58.2	-54.2	-60.1	-64.6	
Personnel costs	-167.9	-185.3	-187.5	-258.2	-273.0	-288.8	-280.2	-298.0	
EBITDA	140.1	145.8	132.7	103.9	129.0	117.7	164.4	195.1	
IAC	-3.2	0.0	0.0	-134.2	-3.6	-10.8	-6.8	-6.8	
Adj. EBITDA	143.3	145.8	132.7	238.1	132.6	128.5	171.2	201.9	
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	48.7	92.5	117.3	
Adj. EBIT	118.8	108.4	83.8	65.7	79.3	59.5	99.3	124.1	16%
Financial items	-1.8	-1.4	-7.0	-0.1	-2.2	-1.2	-2.6	-3.2	
Profit before tax	117.0	107.0	76.8	-68.6	73.5	47.5	89.9	114.1	
Taxes paid	-26.2	-25.8	-17.4	1.2	-15.7	-15.4	-21.8	-27.2	
Adj. Net profit	94.0	81.2	59.4	66.8	61.4	42.9	75.0	93.7	15%
EPS	6.67	5.96	4.36	-4.94	4.23	2.35	4.99	6.36	
Adj. EPS (diluted)	6.67	5.96	4.36	4.90	4.50	3.14	5.49	6.86	
DPS	5.00	3.00	0.00	0.00	1.50	1.10	1.92	2.40	
Margins									
Gross	97.7%	97.3%	96.2%	96.6%	97.0%	96.8%	97.0%	97.3%	
EBITDA	36.4%	35.9%	35.7%	29.0%	30.5%	27.7%	35.5%	38.4%	
Adj. EBITDA	37.2%	35.9%	35.7%	66.5%	31.4%	30.2%	37.0%	39.7%	
EBIT	30.0%	26.7%	22.5%	-19.1%	17.9%	11.5%	20.0%	23.1%	
Adj. EBIT	30.8%	26.7%	22.5%	18.4%	18.8%	14.0%	21.4%	24.4%	
FCF margin	11.9%	5.4%	9.9%	16.1%	16.2%	13.8%	15.5%	16.0%	
Rule of 40 (EBIT)	42.5%	32.0%	14.2%	14.6%	36.9%	14.6%	30.4%	34.1%	
ROCE	28.1%	17.7%	12.4%	9.9%	11.5%	8.1%	13.0%	15.2%	
Cash flow									
Cash flow from operating activities	92.6	105.7	118.4	131.6	128.0	112.9	137.5	153.1	
Capex	-46.8	-83.6	-81.4	-74.1	-59.6	-54.6	-65.8	-71.8	
Adj. FCF	45.8	22.1	37.0	57.5	68.4	58.3	71.7	81.3	6%
Cash conversion (FCF/EBIT)	39%	20%	44%	88%	86%	98%	72%	66%	
Balance sheet									
Cash	106.1	60.7	67.8	113.4	148.2	174.2	222.9	270.0	
Net cash (-) / net debt (+)	-103.3	18.4	-1.5	-57.4	-78.9	-114.7	-171.4	-226.5	
Net debt/EBITDA	-0.7x	0.1x	0.0x	-0.6x	-0.6x	-1.0x	-1.0x	-1.2x	

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

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Figure 13: 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	421.6	448.1	477.0	4%
Security solutions	5.0	1.7	5.0	0.7	1.5	2.7	15.2	31.2	175%
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	425.3	463.3	508.2	7%
Net sales growth by segment									
Development tools	10%	6%	-9%	-3%	18%	1%	6%	6%	
Security solutions		-66%	194%	-86%	114%	83%	455%	105%	
Other									
Total	10%	5%	-8%	-4%	18%	1%	9%	10%	
Net sales by product									
License-based	242.9	236.3	212.4	196.1	233.0	215.8	245.5	277.5	6%
Support and softw are updates	119.4	146.3	145.2	141.6	167.9	189.7	198.9	210.9	8%
Other	22.9	23.0	14.4	18.1	19.0	18.9	18.8	19.7	1%
Total	385.2	405.6	372.0	355.8	419.9	425.3	463.3	508.2	7%
Net sales growth by product									
License-based	12%	-3%	-10%	-8%	19%	-7%	14%	13%	
Support and softw are updates	10%	23%	-1%	-2%	19%	13%	5%	6%	
Other	20%	0%	-37%	26%	5%	-1%	0%	5%	
Total	10%	5%	-8%	-4%	18%	1%	9%	10%	

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

Figure 14: 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	104.6	105.4	104.3
Security solutions	0.1	0.1	0.4	0.4	0.5	0.2	0.4	0.5	0.6	1.2
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	105.1	106.1	105.5
Net sales growth by segment										
Development tools	-1%	2%	9%	23%	20%	19%	11%	-2%	0%	-4%
Security solutions	-75%	-92%	33%	100%	400%	100%	0%	31%	23%	499%
Other										
Total	-1%	1%	10%	23%	20%	19%	10%	-2%	0%	-3%
Net sales by product										
License-based	46.2	49.4	52.0	67.8	56.2	57.0	53.3	57.0	54.0	51.5
Support and softw are updates	36.9	36.1	41.2	36.9	44.4	45.4	49.7	44.2	47.8	48.0
Other	4.8	6.1	4.2	2.9	5.5	6.4	4.7	4.0	4.2	6.0
Total	90.0	91.6	98.3	107.6	106.1	110.7	108.6	105.1	106.1	105.5
Net sales growth by product										
License-based	-9%	-5%	4%	35%	22%	15%	2%	-16%	-4%	-10%
Support and softw are updates	4%	2%	19%	9%	20%	26%	21%	20%	8%	6%
Other	85%	79%	2%	-6%	15%	5%	12%	38%	-24%	-6%
Total	-1%	1%	10%	23%	20%	19%	10%	-2%	0%	-3%

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

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Figure 15: 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	105.1	106.1	105.5
Grow th YOY , of w hich	-1%	1%	10%	23%	20%	19%	10%	-2%	0%	-3%
Organic	-1%	2%	3%	14%	11%	7%	5%	-8%	-3%	-2%
Structural	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
FX	0%	-1%	7%	9%	9%	12%	6%	6%	3%	-1%
COGS	-2.8	-3.0	-2.8	-3.1	-3.1	-3.8	-3.2	-3.3	-3.4	-3.6
Gross profit	87.2	88.6	95.5	104.5	103.0	106.9	105.4	101.8	102.7	101.9
Capitalised w ork	13.7	14.1	12.2	10.5	11.3	16.2	9.4	12.0	13.0	14.5
Other external expenses	-10.3	-14.1	-11.5	-11.9	-18.8	-16.1	-12.7	-13.5	-14.0	-14.0
Personnel costs	-55.6	-75.4	-66.0	-71.2	-61.3	-74.6	-76.8	-77.0	-63.0	-72.0
EBITDA	35.0	13.2	30.2	31.9	34.2	32.4	25.3	23.3	38.7	30.4
IAC	2.1	-134.2	0.9	0.0	-4.5	0.0	-1.7	-1.7	-5.7	-1.7
Adj. EBITDA	32.9	147.4	29.3	31.9	38.7	32.4	27.0	25.0	44.4	32.1
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	6.1	17.8	13.4
Adj. EBIT	18.8	15.2	16.3	19.6	26.6	16.5	13.1	7.8	23.5	15.1
Financial items	-0.3	1.8	-0.9	-0.5	1.1	-1.9	0.3	-0.5	-0.5	-0.5
Profit before tax	20.6	-117.2	16.3	19.1	23.2	14.6	11.7	5.6	17.3	12.9
Taxes paid	-4.7	11.8	-4.4	-4.8	-6.4	0.0	-5.3	-1.6	-5.2	-3.3
Adj. Net profit	13.8	28.8	11.0	14.3	21.3	14.6	8.1	5.7	17.9	11.3
EPS	1.17	-7.72	0.88	1.05	1.04	1.07	0.47	0.29	0.89	0.70
Adj. EPS (diluted)	1.01	2.11	0.81	1.05	1.56	1.07	0.59	0.42	1.31	0.83
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%	96.9%	96.8%	96.6%
EBITDA	38.9%	14.4%	30.7%	29.6%	32.2%	29.3%	23.3%	22.2%	36.4%	28.8%
Adj. EBITDA	36.6%	160.9%	29.8%	29.6%	36.5%	29.3%	24.9%	23.8%	41.8%	30.4%
EBIT	23.2%	-129.9%	17.5%	18.2%	20.8%	14.9%	10.5%	5.8%	16.8%	12.7%
Adj. EBIT	20.9%	16.6%	16.6%	18.2%	25.1%	14.9%	12.1%	7.4%	22.2%	14.3%
FCF margin	24.1%	25.5%	15.7%	15.3%	31.3%	3.0%	14.6%	14.7%	19.1%	6.5%
Rule of 40 (EBIT)	22.1%	17.6%	27.2%	41.3%	43.0%	35.8%	22.5%	5.1%	22.2%	9.6%
ROCE	9.7%	9.3%	9.5%	10.4%	11.8%	11.6%	10.8%	8.9%	8.3%	8.1%
Cash flow										
Cash flow from operating activities	41.4	40.5	28.8	26.0	47.4	25.8	26.1	29.3	34.7	22.9
Capex	-19.7	-17.1	-13.4	-9.5	-14.2	-22.5	-10.4	-13.8	-14.4	-16.0
Adj. FCF	21.7	23.4	15.4	16.5	33.2	3.3	15.7	15.5	20.3	6.9
Cash conversion (FCF/EBIT)	115%	154%	94%	84%	125%	20%	120%	198%	86%	46%
Balance sheet										
Cash	91.3	113.4	125.0	117.9	158.8	148.2	158.1	151.1	169.3	174.2
Net cash (-) / net debt (+)	-36.4	-57.4	-72.0	-85.9	-131.1	-78.9	-92.6	-87.6	-107.8	-114.7
Net debt/EBITDA	-0.3x	-0.6x	-0.7x	-0.8x	-1.2x	-0.6x	-0.7x	-0.8x	-0.9x	-1.0x

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

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Valuation

Figure 16: Valuation approaches (SEKm, %)

	Peers regression	DCF	Historical average
Net sales (2023e)			463
Adj. EBIT (2023e)			99
Adj. EPS (2023e)			5.49
Sales CAGR (2022–2024e)	12.2		4.7
Adj. EBIT margin (2023e)	22.8		14.0
RO40 (2023e)	47.4		18.7
Target multiple	RO40, P/B, EV/S	10% WACC	15x EV/EBIT
Enterprise value	2,560	2,519	1,490
Net debt (+)/cash (-)	-171	-171	-171
Equity value	2,732	2,691	1,661
Shares outstanding	13.8	13.8	13.8
Implied price/share	199	196	121
Implied potential	131%	128%	41%

2024e valuation multiples

Implied EV/sales	5.5	5.4	3.2
Implied EV/EBIT	25.8	25.4	15.0
Implied P/E	36.4	35.9	22.2

Source: DNB Markets

Figure 17: 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	424	463	508
Growth YOY	5.4%	5.1%	10.2%	5.2%	-8.3%	-4.4%	18.1%	1.3%	8.9%	9.7%
Gross profit	316	337	376	395	358	346	410	412	449	494
Gross margin	96.3%	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	96.8%	97.0%	97.3%
Adj. EBITDA	117	127	140	146	133	104	129	118	164	195
EBITDA margin	36.9%	36.9%	37.2%	35.9%	35.7%	66.5%	31.4%	30.2%	37.0%	39.7%
Adj. EBIT	101	107	119	108	84	66	79	60	99	124
EBIT margin	30.6%	31.1%	30.8%	26.7%	22.5%	18.4%	18.8%	14.0%	21.4%	24.4%
Adj. Net profit	82	80	94	81	59	67	61	43	75	94
Adj. FCF	95	105	46	22	37	58	68	58	72	81
FCF margin	29.0%	30.4%	11.9%	5.4%	9.9%	16.2%	16.3%	13.7%	15.5%	16.0%
Cash conversion	95%	98%	39%	20%	44%	88%	86%	98%	72%	66%
Rule of 40 (EBIT)	36.0%	36.2%	41.0%	31.9%	14.2%	14.0%	36.8%	15.3%	30.4%	34.1%
ROCE	35.0%	37.4%	28.1%	17.7%	12.4%	9.9%	11.5%	8.1%	13.0%	15.2%
ROIC	27.4%	28.5%	21.9%	13.8%	10.1%	10.4%	9.4%	6.0%	10.1%	11.9%
Market cap	2,602	2,387	3,310	2,535	1,905	1,606	1,173	1,173	1,173	1,173
Net debt	-97	-117	-103	18	-1	-57	-79	-115	-171	-226
Enterprise value	2,505	2,270	3,206	2,554	1,904	1,548	1,094	1,059	1,002	947
EV/Sales	7.6x	6.6x	8.3x	6.3x	5.1x	4.4x	2.6x	2.5x	2.2x	1.9x
EV/EBIT	24.9x	21.1x	27.0x	23.6x	22.7x	23.6x	13.8x	17.8x	10.1x	7.6x
P/E	31.7x	29.8x	35.2x	31.2x	32.1x	24.0x	19.1x	27.3x	15.7x	12.5x
FCF yield	3.7%	4.4%	1.4%	0.9%	1.9%	3.6%	5.8%	5.0%	6.1%	6.9%

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

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Figure 18: EV/sales 12-month forward IAR Systems (2018–2023)



Source: Bloomberg

Figure 19: EV/EBITDA 12-month forward IAR Systems (2018–2023)



Source: Bloomberg

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



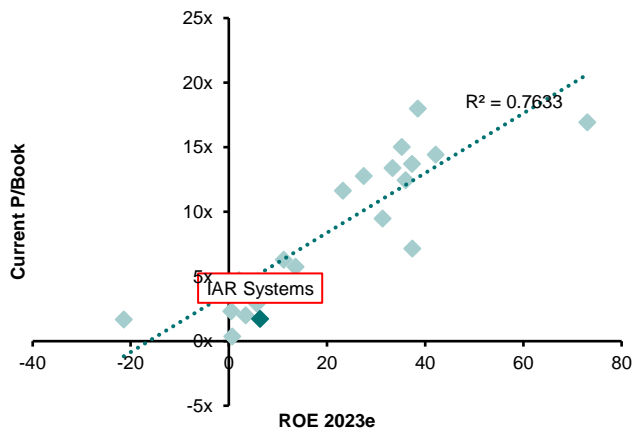
Source: Bloomberg

Figure 21: P/E 12-month forward IAR Systems (2018–2023)



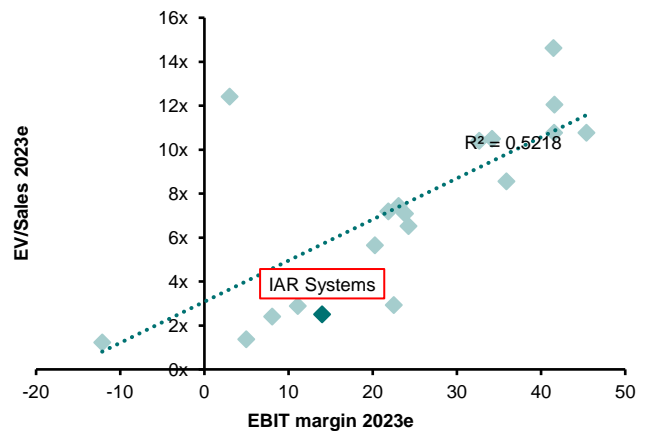
Source: Bloomberg

Figure 22: Current P/book versus ROE (2023e)



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

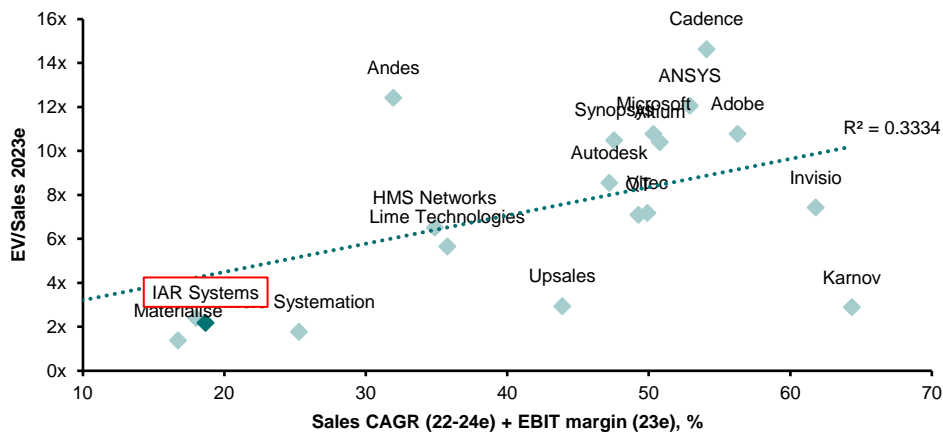
Figure 23: EV/sales versus EBIT margin (2023e)



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

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Figure 24: EV/sales 2023e versus sales CAGR + EBIT margin



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

Figure 25: 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)	1.2	37	17	14	18	10	8	9	6	5	2	2	2	1.3	5.0	6	11	14.0	21.4	5	12	9	
Premium/discount		-19%	-48%	-49%	-70%	-63%	-65%	-64%	-73%	-69%	-68%	-69%	-69%										
IAR Systems (Cons.)	1.2	18	12	10	12	8	6	7	5	4	2	2	2	1.9	6.1	8	12	18.7	24.2	10	19	22	
Premium/discount		-59%	-62%	-61%	-79%	-71%	-72%	-72%	-77%	-74%	-70%	-69%	-68%										
Nordic software																							
Enea	0.8	26	14	10			7	4		3	1	1	1		14.2	1	2	-12.1	9.3	-1	-8	-31	
Formpipe	1.4	43	25	18	33	20	14	13	10	8	3	2	2	1.2	1.6	6	9	8.1	12.1	10	125	132	
HMS Networks	18.6	33	34	32	26	27	24	23	23	21	6	6	6	1.1	3.1	31	25	24.2	23.4	11	7	10	
Invisio	10.6	50	40	34	37	30	24	31	26	21	9	7	6	0.7	1.7	35	33	23.1	24.4	39	175	199	
Karnov	5.4	16	14	12	26	20	17	12	11	9	3	3	3	1.0	4.5	1	3	11.1	13.3	53	29	32	
Lime Technologies	3.6	42	34	29	32	26	21	20	18	15	6	6	5	1.1	3.4	37	36	20.3	21.1	15	23	14	
Micro Systemation	0.9	20	16	14	15	11	9	13	9	8	2	2	2	4.1	5.3	37	42	13.6	15.8	12	23	19	
QT	20.0	47	31	23	37	24	17	30	21	16	9	7	6	0.0	2.5	33	35	23.9	28.0	25	39	30	
Upsales	0.6	23	17	15	17	13	10	13	10	8	4	3	2	3.2	3.3	73	80	22.5	23.7	21	29	31	
Vitec	21.5	49	38	34	39	34	31	23	20	17	8	7	6	0.6		11	13	21.9	21.5	28	40	44	
WithSecure	2.2			36			57		51	11	1	1	1	0.0		-21	-9	-21.6	-5.3	10	-53	-59	
Engineering software																							
Adobe	2,423.8	33	29	26	26	23	21	24	22	19	12	11	10	0.0	3.3	42	37	45.4	44.7	11	11	14	
Altium	34.2	51	41	33	37	30	24	33	27	22	12	10	9	1.8	1.1	23	28	32.7	34.8	18	29	29	
Andes	7.8	172	76	37	542	78	33	78	37	21	16	12	10	0.3	0.6	2	6	3.0	15.7	29	145	-29	
ANSYS	306.7	40	36	32	31	28	24	31	27	24	13	12	11	0.0	2.2	14	14	41.6	41.9	11	12	12	
Autodesk	471.3	33	30	26	26	24	20	24	23	20	9	9	8	0.0	4.2	161	90	35.9	35.6	11	19	21	
Cadence	677.3	48	42	38	39	34	29	35	31	26	16	15	13	0.0	1.9	39	34	41.5	42.6	13	16	16	
Materialise	5.5	56	40	27	31	22	12	12	10	7	2	1	1	0.0	0.9	3	5	5.0	6.0	12		160	
Microsoft	26,338.7	36	31	27	29	25	21	25	21	18	12	11	10	0.8	2.3	36	33	41.6	42.3	9	9	8	
Synopsys	713.6	42	37	32	34	29	24	31	27	23	12	11	9	0.3	2.2	28	26	34.2	35.4	13	17	18	
Average	1,553.2	45	33	27	59	28	22	25	22	16	8	7	6	0.9	3.2	30	27	20.8	24.3	18	36	33	
Median	14.6	42	34	28	32	25	21	24	22	18	8	7	6	0.6	2.4	29	27	22.8	23.6	12	23	19	

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 (22,000+ active technology users) at OEMs (45,000+) 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 2023 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 generate 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.

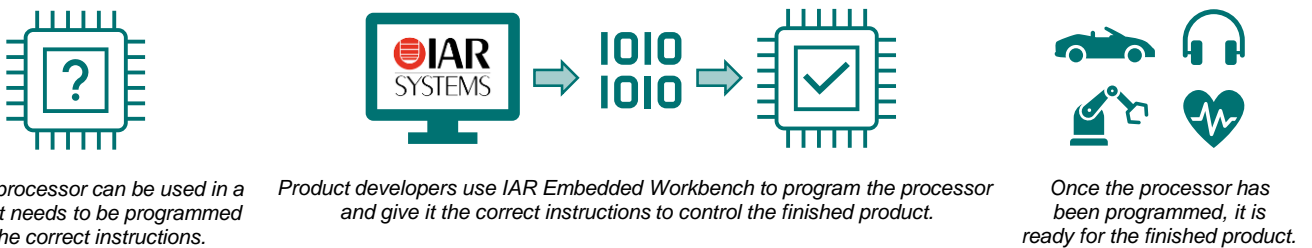
Business overview

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 26: IAR Embedded Workbench in the customer’s product development



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

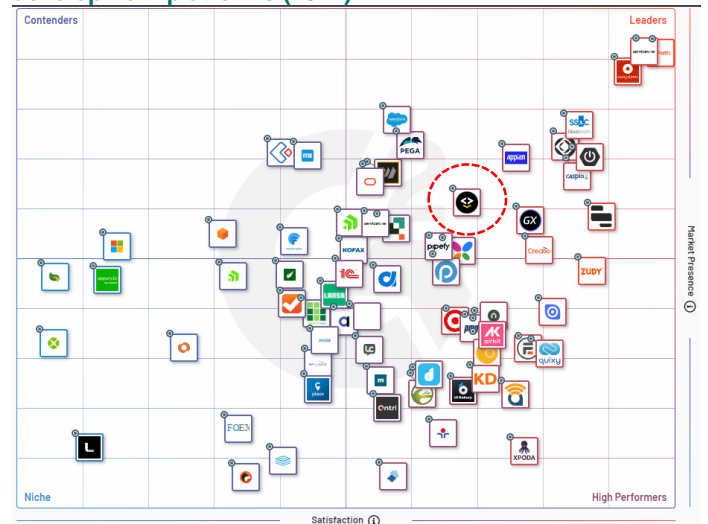
Headquartered in Uppsala, Sweden, IAR Systems has 200+ employees in 15 offices on three continents with technical support teams in its customers’ local time zones in 10+ languages. Its independent software supports more than 14,000 different processors from more than 70 processor vendors, which is more 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 27: Example of customers



Source: Company

Figure 28: 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

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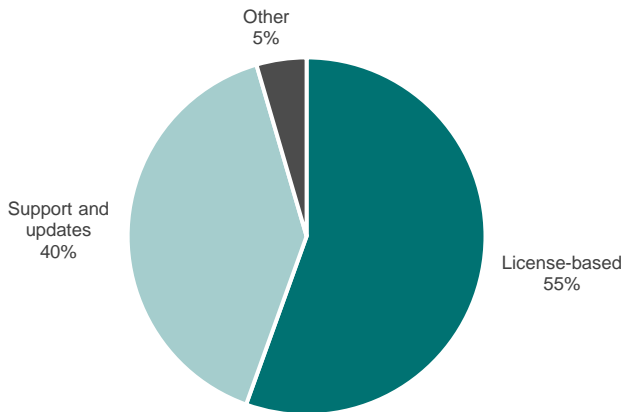
companies, etc.); and 4) suppliers of integrated programmes (real-time operating systems, graphics development, etc.).

IAR Systems' business model is primarily licence- and transaction-based, where customers (users, developers) pay upfront for 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

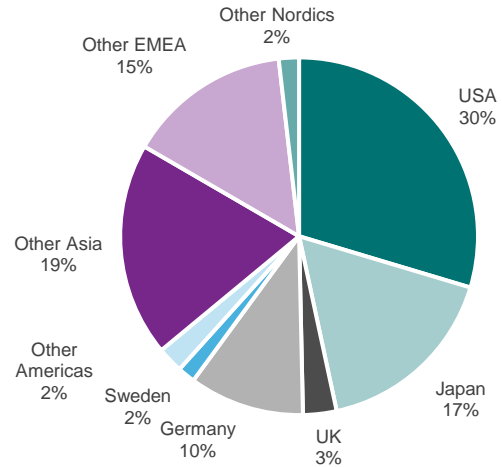
- **Development tools (~99% of net sales)** consist of IAR Embedded Workbench (8- to 64-bit) with world-leading code-optimisation technology, compiler, debugger probes and analysis tools (ensuring code quality and coding standards), functional safety certifications (pre-certified build tools), RISV-V 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 29: Net sales by revenue stream (2022)



Source: Company

Figure 30: 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	425	463	508	462	511	556	-37	-48	-48
Cost of sales	-14	-14	-14	-14	-15	-15	1	1	1
Gross profit	412	449	494	448	496	541	-36	-47	-47
Operating expenses	-343	-340	-363	-353	-358	-374	10	18	11
EBITDA	118	164	195	148	192	223	-30	-28	-28
EBITDA adj	128	171	202	155	199	230	-26	-28	-28
EBITDA margin (%)	27.7	35.5	38.4	32.0	37.6	40.2	-4.4	-2.1	-1.8
Depreciation	-30	-33	-35	-30	-33	-35	0	0	0
Amortisation	-30	-32	-36	-30	-32	-36	0	0	0
EBIT	49	93	117	83	120	145	-34	-28	-28
EBIT adj	60	99	124	90	127	152	-30	-28	-28
Net financial items	-1	-3	-3	-4	-6	-5	3	3	2
PBT	48	90	114	79	115	140	-31	-25	-26
Taxes	-15	-22	-27	-22	-27	-33	6	6	6
Minorities	0	0	0	0	0	0	0	0	0
Net profit	32	68	87	57	87	107	-25	-19	-20
Adjustments to net profit	11	7	7	7	7	7	4	0	0
Net profit adj	43	75	94	64	94	114	-21	-19	-20
<i>Per share data (SEK)</i>									
EPS	2.35	4.99	6.36	4.19	6.39	7.85	-1.84	-1.40	-1.49
EPS adj	3.14	5.49	6.86	4.68	6.89	8.34	-1.55	-1.40	-1.49
DPS ordinary	1.10	1.92	2.40	1.64	2.41	2.92	-0.54	-0.49	-0.52
DPS	1.10	1.92	2.40	1.64	2.41	2.92	-0.54	-0.49	-0.52
<i>Other key metrics (%)</i>									
Revenue growth	0.6	8.9	9.7	9.3	10.6	8.8	-8.7	-1.6	0.9
EBIT adj growth	-24.9	66.9	24.9	13.2	41.4	19.9	-38.2	25.4	5.0
EPS adj growth	-30.2	74.9	25.0	4.2	47.0	21.2	-34.4	27.9	3.8
Avg. number of shares (m)	14	14	14	14	14	14	0	0	0
Capex	-55	-66	-72	-60	-72	-79	5	7	7
OpFCF	74	105	130	95	127	151	-21	-21	-21
Working capital	-52	-56	-51	-45	-50	-46	-7	-6	-5
NIBD adj	-115	-171	-226	-128	-191	-253	13	20	27

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	-2.28	10.41	9.69	7.05	10.87	8.79	-9.33	-0.46	0.90
Structure impact % YOY	0.00	0.00	0.00		0.00	0.00		0.00	0.00
Currency impact % YOY	3.56	-1.47	0.00	2.98	-0.28	0.00	0.57	-1.18	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	105	106	105	116	114
Cost of sales	-3	-3	-3	-3	-4	-3	-3	-3	-4	-4	-3
Gross profit	89	96	105	103	107	105	102	103	102	112	111
Operating expenses	-90	-78	-83	-80	-91	-90	-91	-77	-86	-87	-85
EBITDA	13	30	32	34	32	25	23	39	30	40	40
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	6	18	13	22	22
Net financial items	2	-1	-1	1	-2	0	-1	-1	-1	-1	-1
PBT	-117	16	19	23	15	12	6	17	13	21	21
Taxes	12	-4	-5	-6	0	-5	-2	-5	-3	-5	-5
Minorities	0	0	0	0	0	0	0	0	0	0	0
Net profit	-105	12	14	17	15	6	4	12	10	16	16
Adjustments to net profit	134	-1	0	5	0	2	2	6	2	2	2
Net profit adj	29	11	14	21	15	8	6	18	11	18	18
Dividend paid	0	0	0	0	0	0	-20	0	0	0	-15
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	0.29	0.89	0.70	1.17	1.16
EPS adj	2.11	0.81	1.05	1.56	1.07	0.59	0.42	1.31	0.83	1.30	1.28
DPS ordinary	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00	0.00	1.10
DPS	0.00	0.00	0.00	0.00	0.00	0.00	1.50	0.00	0.00	0.00	1.10
<i>Growth and margins (%)</i>											
Revenues, QOQ growth	1.8	7.3	9.5	-1.4	4.3	-1.9	-3.2	0.9	-0.5	9.8	-1.3
Revenues, YOY growth	1.0	10.6	23.1	17.9	20.9	10.5	-2.3	0.0	-4.7	6.7	8.7
EPS adj, YOY growth	140.0	-14.1	26.6	54.3	-49.3	-26.9	-60.4	-16.1	-22.8	120.3	209.5
Gross margin	96.7	97.2	97.1	97.1	96.6	97.1	96.9	96.8	96.6	96.9	97.1
EBITDA adj margin	160.9	29.8	29.6	36.5	29.3	24.9	23.8	41.8	30.4	35.6	36.4
Depreciation/revenues	-5.7	-5.8	-5.3	-5.1	-7.9	-6.1	-7.7	-7.3	-7.4	-7.0	-7.5
EBIT adj margin	16.6	16.6	18.2	25.1	14.9	12.1	7.4	22.2	14.3	20.3	20.4
Net profit margin	nm	12.1	13.3	15.8	13.2	5.9	3.8	11.5	9.1	13.8	13.9

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	23	39	30	40	40
EBITDA adj	147	29	32	39	32	27	25	44	32	41	42
EBIT	-119	17	20	22	17	11	6	18	13	22	22
Other EBIT adjustments	-134	1	0	-5	0	-2	-2	-6	-2	-2	-2
EBIT adj	15	16	20	27	17	13	8	24	15	24	23
Net profit	-105	12	14	17	15	6	4	12	10	16	16
Other EBIT adjustments	-134	1	0	-5	0	-2	-2	-6	-2	-2	-2
Net profit adj	29	11	14	21	15	8	6	18	11	18	18

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	-8.44	-3.28	-2.12	8.81	10.65
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	6.14	3.24	-0.89	-1.32	-1.95

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	425	463	508	
Cost of sales	-12	-9	-9	-11	-14	-12	-13	-14	-14	-14	
Gross profit	316	337	376	395	358	346	410	412	449	494	
Operating expenses	-203	-209	-236	-249	-225	-307	-331	-343	-340	-363	
EBITDA	113	127	140	146	133	104	129	118	164	195	
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	49	93	117	
Net financial items	0	-2	-2	-1	-7	0	-2	-1	-3	-3	
PBT	100	106	117	107	77	-69	74	48	90	114	
Taxes	-22	-26	-26	-26	-17	1	-16	-15	-22	-27	
Effective tax rate (%)	22	24	22	24	23	2	21	32	24	24	
Minorities	0	0	0	0	0	0	0	0	0	0	
Net profit	78	80	91	81	59	-67	58	32	68	87	
Adjustments to net profit	4	0	3	0	0	134	4	11	7	7	
Net profit adj	82	80	94	81	59	67	61	43	75	94	
Dividend paid	-88	-63	-68	-68	0	0	0	-20	-15	-26	
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	2.35	4.99	6.36	
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.50	3.14	5.49	6.86	
DPS ordinary	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.10	1.92	2.40	
DPS	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.10	1.92	2.40	
<i>Growth and margins (%)</i>											
Revenue growth	5.4	5.1	11.7	5.3	-8.3	-3.8	18.1	0.6	8.9	9.7	
EPS adj growth	23.0	2.6	5.3	-10.6	-26.8	12.5	-8.2	-30.2	74.9	25.0	
Gross margin	96.3	97.5	97.7	97.3	96.2	96.6	97.0	96.8	97.0	97.3	
EBITDA margin	34.5	36.9	36.4	35.9	35.7	29.0	30.5	27.7	35.5	38.4	
EBITDA adj margin	35.7	36.9	37.2	35.9	35.7	66.5	31.4	30.2	37.0	39.7	
Depreciation/revenues	-0.8	-0.7	-0.7	-3.2	-5.5	-5.7	-6.0	-7.1	-7.1	-6.9	
EBIT margin	29.4	31.1	30.0	26.7	22.5	nm	17.9	11.5	20.0	23.1	
EBIT adj margin	30.6	31.1	30.8	26.7	22.5	18.4	18.8	14.0	21.4	24.4	
PBT margin	30.5	30.6	30.4	26.4	20.6	nm	17.4	11.2	19.4	22.4	
Net profit margin	23.8	23.2	23.6	20.0	16.0	nm	13.7	7.6	14.7	17.1	

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	118	164	195
EBITDA adj	117	127	143	146	133	238	133	128	171	202
EBIT	97	107	116	108	84	-69	76	49	93	117
Other EBIT adjustments	-4	0	-3	0	0	-134	-4	-11	-7	-7
EBIT adj	101	107	119	108	84	66	79	60	99	124
Net profit	78	80	91	81	59	-67	58	32	68	87
Other EBIT adjustments	-4	0	-3	0	0	-134	-4	-11	-7	-7
Net profit adj	82	80	94	81	59	67	61	43	75	94
<i>Per share data (SEK)</i>										
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.23	2.35	4.99	6.36
Recommended adjustment	0.00	0.00	0.00	0.00	0.00	9.85	0.26	0.78	0.50	0.50
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.50	3.14	5.49	6.86

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	32	68	87
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	113	137	153
Capital expenditure	-19	-19	-47	-84	-81	-74	-60	-55	-66	-72
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	-54	-66	-72
Free cash flow (FCF)	95	86	-125	4	37	58	68	59	72	81
Net change in debt	0	0	0	30	6	1	1	0	0	0
Dividends paid	-88	-63	-68	-68	0	0	0	-20	-15	-26
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	-23	-34
Total cash flow (CFO+CFI+CFF)	7	23	-17	-49	12	42	29	27	49	47
<i>FCFF calculation</i>										
Free cash flow	95	86	-125	4	37	58	68	59	72	81
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	-11.8	21.7	11.4
CFI	-3.3	-98.9	-478.5	53.0	20.4	9.0	19.6	8.7	-20.9	-9.2
FCF	18.5	-9.4	-244.7	102.8	957.1	55.4	19.0	-14.5	22.5	13.4
CFF	-39.0	28.5	270.4	-148.3	52.7	38.6	-162.3	19.5	27.9	-48.8
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)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
Assets	396	410	722	825	834	813	922	964	1,005	1,043
Inventories	6	5	7	7	6	10	11	10	12	11
Trade receivables	48	51	63	67	59	59	67	76	71	64
Other receivables	19	12	38	52	64	44	34	39	35	32
Current financial assets	0	0	0	0	0	0	0	0	0	0
Cash and cash equivalents	99	120	106	61	68	113	148	174	223	270
Current assets	172	187	214	186	196	226	260	299	339	376
Property, plant and equipment	6	6	9	7	8	15	17	17	17	18
Other intangible assets	197	194	484	624	624	567	639	640	640	640
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	665	665	666
Total assets	396	410	722	825	834	813	922	964	1,005	1,043
Equity and liabilities	396	410	722	825	834	813	922	964	1,005	1,043
Total equity	280	290	550	592	613	585	667	683	736	797
Trade payables	5	6	7	9	5	9	8	9	8	7
Other payables and accruals	92	86	131	117	111	133	146	168	165	151
Short-term debt	1	1	0	25	18	18	0	0	0	0
Total current liabilities	99	102	140	164	150	179	173	196	192	177
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	281	269	246
Total equity and liabilities	396	410	722	825	834	813	922	964	1,005	1,043
<i>Key metrics</i>										
Net interest bearing debt	-97	-117	-103	18	-2	-57	-79	-115	-171	-226

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

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Valuation ratios

(SEKm)	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
<i>Enterprise value</i>										
Share price (SEK)	206.00	189.00	243.00	186.00	139.80	117.80	150.40	85.90	85.90	85.90
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	1,173	1,173	1,173
Net interest bearing debt	-97	-117	-103	18	-2	-57	-79	-115	-171	-226
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	-115	-171	-226
EV	2,505	2,270	3,206	2,554	1,904	1,548	1,974	1,059	1,002	947
EV adj	2,505	2,270	3,206	2,554	1,904	1,548	1,974	1,059	1,002	947
<i>Valuation</i>										
EPS	6.18	6.33	6.67	5.96	4.36	-4.94	4.23	2.35	4.99	6.36
EPS adj	6.18	6.33	6.67	5.96	4.36	4.90	4.50	3.14	5.49	6.86
DPS ordinary	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.10	1.92	2.40
DPS	7.00	5.00	5.00	3.00	0.00	0.00	1.50	1.10	1.92	2.40
P/E	33.4	29.8	36.4	31.2	32.1	-23.8	35.5	36.5	17.2	13.5
P/E adj	33.4	29.8	36.4	31.2	32.1	24.0	33.4	27.4	15.7	12.5
P/B	9.31	8.22	6.02	4.28	3.11	2.74	3.08	1.72	1.59	1.47
Average ROE	27.3%	28.1%	21.6%	14.2%	9.9%	-11.2%	9.2%	4.8%	9.6%	11.3%
Earnings yield adj	3.0%	3.4%	2.7%	3.2%	3.1%	4.2%	3.0%	3.7%	6.4%	8.0%
Dividend yield	3.4%	2.6%	2.1%	1.6%	0.0%	0.0%	1.0%	1.3%	2.2%	2.8%
Free cash flow yield	3.7%	3.6%	-3.8%	0.1%	1.9%	3.6%	3.3%	5.0%	6.1%	6.9%
EV/SALES	7.63	6.58	8.32	6.30	5.12	4.32	4.67	2.49	2.16	1.86
EV/SALES adj	7.63	6.58	8.32	6.30	5.12	4.32	4.67	2.49	2.16	1.86
EV/EBITDA	22.1	17.8	22.9	17.5	14.3	14.9	15.3	9.0	6.1	4.9
EV/EBITDA adj	21.4	17.8	22.4	17.5	14.3	6.5	14.9	8.2	5.9	4.7
EV/EBIT	26.0	21.1	27.7	23.6	22.7	-22.6	26.1	21.7	10.8	8.1
EV/EBIT adj	24.9	21.1	27.0	23.6	22.7	23.6	24.9	17.8	10.1	7.6
EV/capital employed	8.9	7.8	5.8	3.8	2.8	2.4	2.7	1.4	1.3	1.1
EV/NOPLAT	33.3	27.1	35.6	30.2	29.1	-29.0	33.4	27.9	13.9	10.4
EV/OpFCF (taxed)	32.8	26.8	45.6	66.6	57.9	10.4	35.5	17.4	12.0	9.2

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

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Key accounting ratios

	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e
<i>Profitability (%)</i>										
ROA	19.6	19.9	16.0	10.5	7.2	-8.2	6.7	3.4	6.9	8.5
ROCE	35.0	37.4	28.1	17.7	12.4	9.9	11.5	8.1	13.0	15.2
ROCE after tax	27.3	29.1	21.9	13.8	9.7	7.8	9.0	6.3	10.1	11.9
<i>Return on invested capital (%)</i>										
Net PPE/revenues	1.9	1.8	2.3	1.8	2.0	4.1	3.9	3.9	3.7	3.5
Working capital/revenues	-7.5	-6.9	-7.8	-0.2	3.4	-8.3	-10.1	-12.2	-12.1	-10.1
<i>Cash flow ratios (%)</i>										
FCF/revenues	29.0	25.0	-32.4	0.9	9.9	16.1	16.2	13.8	15.5	16.0
FCF yield (%)	3.7	3.6	1.4	0.9	1.9	3.6	3.3	5.0	6.1	6.9
CFO/revenues	34.8	35.9	24.0	26.1	31.8	36.8	30.3	26.6	29.7	30.1
CFO/market capitalisation	4.4	5.2	2.8	4.2	6.2	8.2	6.2	9.6	11.7	13.0
CFO/capex	614.0	652.1	197.9	126.4	145.5	177.6	214.8	206.8	209.0	213.2
CFO/current liabilities	115.8	121.1	66.2	64.4	78.9	73.7	73.9	57.6	71.7	86.5
Cash conversion ratio	122.2	107.9	-137.6	4.3	62.3	-85.3	118.3	182.2	105.2	93.6
Capex/revenues	5.7	5.5	12.1	20.6	21.9	20.7	14.1	12.8	14.2	14.1
Capex/depreciation	744.0	791.7	1800.0	648.1	401.0	363.2	233.7	180.6	198.8	204.9
OpFCF margin	30.0	31.4	25.1	15.3	13.8	45.8	17.3	17.4	22.8	25.6
Total payout ratio	113.3	78.9	75.0	50.4	0.0	0.0	35.4	46.7	38.5	37.7
<i>Leverage and solvency (x)</i>										
Net debt/EBITDA	-0.85	-0.92	-0.74	0.13	-0.01	-0.55	-0.61	-0.98	-1.04	-1.16
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	0.03	0.02
<i>Cash conversion cycle</i>										
Inventory turnover days	167.5	223.3	267.7	223.1	147.6	289.0	322.2	279.9	302.0	276.0
Receivables turnover days	74.7	66.2	96.1	106.8	120.2	104.7	86.5	98.5	82.8	68.9
Credit period	158.6	244.8	296.1	310.9	129.4	279.8	239.5	233.3	201.4	184.0
Cash conversion cycle	83.7	44.8	67.7	18.9	138.3	113.8	169.2	145.1	183.4	160.9

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

Important Information

Company: IAR Systems
 Coverage by Analyst: Joachim Gunell
 Date: 18/07/2023

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18 July 2023

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