

IAR SYSTEMS

First glimpse of security traction

Delving into the Q3 results, we note adj. EBIT grew 41% YOY (in line with our forecast), lending credence to our case that IAR is three quarters into a profitable growth turnaround. Although perpetual licence sales are not immune to weakening IT spend, we are encouraged that its long-awaited security offering is starting to ramp up, suggesting leverage to 10–15% organic sales growth ambitions. We reiterate our fair value of SEK140–250 on broadly unchanged 2023–2024 forecasts, on which IAR is trading at an EV/EBIT of 13–10x.

A look beyond the headline results revealed: 1) organic sales growth of 11% (we forecast 13%), with security (3% of net sales) being a positive surprise (0% in recent quarters); 2) licence-based and SUA grew 12% and 11% organic, respectively; 3) adj. EBIT of SEK27m (broadly in line with our forecast) adjusted for one-offs related to moving its production to Sweden, while it is now capitalising SEK2m lower development costs YOY; 4) FCF grew 53% YOY, with 125% cash conversion; and 5) the company is well capitalised, with a SEK131m net cash position.

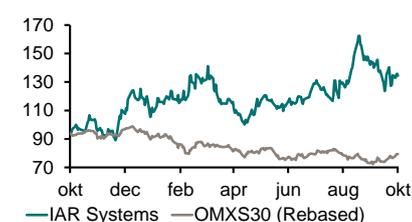
2023–2024e adj. EBIT relatively unchanged (-1%), reflecting: 1) slightly softer new licence sales offset by increased security assumptions; 2) positive FX (+4%), offset by 3) lower capitalised development costs and D&A. IAR Systems' perpetual licence sales (57% of group sales) are not immune should IT spend slow in 2023e, although ~40% of net sales are based on support and update licences, which have historically proven resilient given the durability of design activity through downturns for customers to remain competitive.

Fair value of SEK140–250 reiterated, corresponding to a 2023e EV/EBIT of 14–26x. Over the coming quarters, we will monitor how IAR's end-to-end security platform will benefit from growing demand from developers to secure valuable IP from regulatory tailwinds such as the EU Cyber Resilience Act proposal, DCMS, ETSI, NIST, etc.

Year-end Dec	2018	2019	2020	2021	2022e	2023e	2024e
Revenue (SEKm)	385	406	372	358	420	481	526
EBITDA adj (SEKm)	143	146	133	238	135	183	217
EBIT adj (SEKm)	119	108	84	66	85	125	154
PTP (SEKm)	117	107	77	-69	81	122	151
EPS rep (SEK)	6.67	5.96	4.36	-4.94	4.23	6.91	8.60
EPS adj (SEK)	6.67	5.96	4.36	4.90	4.68	6.91	8.60
DPS (SEK)	5.00	3.00	0.00	0.00	1.64	2.42	3.01
Revenue growth (%)	11.7	5.3	-8.3	-3.8	17.3	14.6	9.3
EBITDA growth adj (%)	12.7	1.7	-9.0	79.4	-43.3	35.4	18.8
EPS growth adj (%)	5.3	-10.6	-26.8	12.5	-4.6	47.7	24.5
EBITDA margin adj (%)	37.2	35.9	35.7	66.5	32.2	38.0	41.3
EV/Sales adj (x)	8.32	6.30	5.12	4.32	4.02	3.38	2.94
EV/EBITDA adj (x)	22.4	17.5	14.3	6.5	12.5	8.9	7.1
EV/EBIT adj (x)	27.0	23.6	22.7	23.6	19.8	13.0	10.0
P/E adj (x)	36.4	31.2	32.1	24.0	28.7	19.5	15.6
P/Book (x)	6.02	4.28	3.11	2.74	2.74	2.48	2.22
ROE (%)	21.6	14.2	9.9	nm	9.6	13.4	15.0
ROCE (%)	28.1	17.7	12.4	9.9	12.8	17.2	19.3
Dividend yield (%)	2.1	1.6	0.0	0.0	1.2	1.8	2.2
FCF yield (%)	1.4	0.9	1.9	3.6	4.3	4.7	6.2

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

IARB versus OMXS30 (12m)



Source: Factset

SUMMARY

Share price (SEK)	134
Tickers	IARB SS

CAPITAL STRUCTURE

No. of shares (m)	13.6
No. of shares fully dil. (m)	13.6
Market cap. (SEKm)	1,834
NIBD adj end-2022e (SEKm)	-145
Enterprise value adj (SEKm)	1,689
Net debt/EBITDA adj (x)	-1.08
Free float (%)	100

Source: Company, DNB Markets (estimates)

NEXT EVENT

Q4 2022	09/02/2023
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ESTIMATE CHANGES (SEK)

Year-end Dec	2022e	2023e	2024e
Sales (old)	420.6	482.4	525.2
Sales (new)	419.8	481.0	525.9
Change (%)	-0.2	-0.3	0.1
EPS adj (old)	4.61	7.00	8.65
EPS adj (new)	4.68	6.91	8.60
Change (%)	1.4	-1.3	-0.6

Source: DNB Markets,

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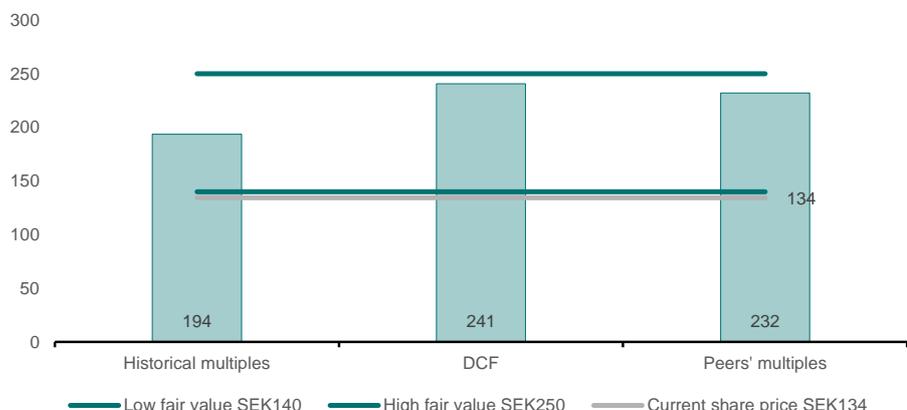
ANALYSTS

Joachim Gunell

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Overview

Valuation (SEK)



Source: DNB Markets

Valuation methodology

- We continue to base our fair value on a DCF, IAR Systems' historical valuation multiples, and a peers' multiple regression analysis (methodology unchanged).
- On our estimates, IAR Systems is trading at a 2024e P/E of 15x, EV/EBIT of 10x, and EV/sales of 3x.

Source: DNB Markets

Downside risks to our fair value

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

Source: DNB Markets

DNB Markets estimates

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

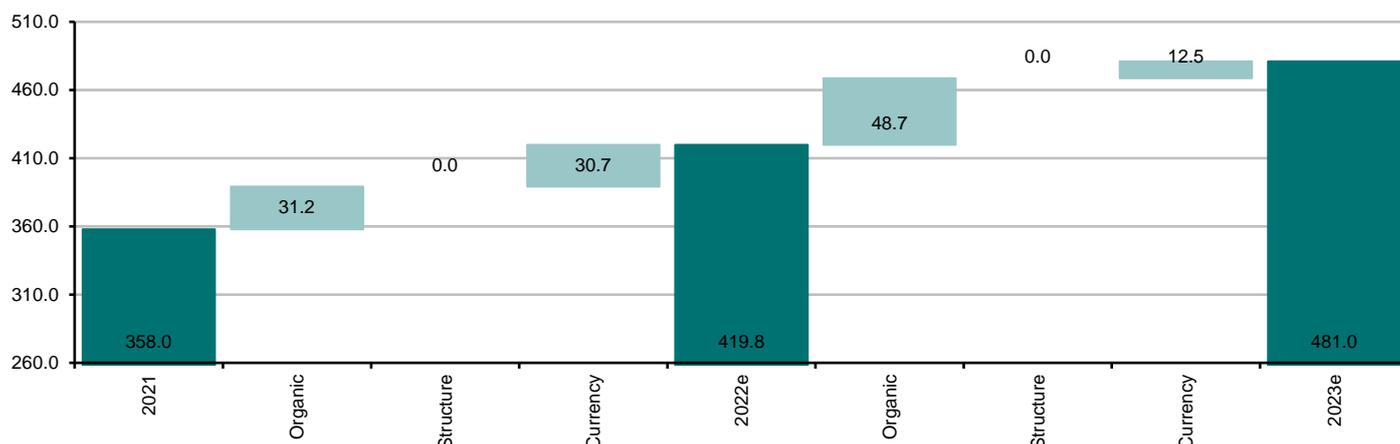
Source: DNB Markets

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.

Q3 results

Figure 1: Q3 results versus expectations

Key highlights (SEKm, except per share data)	Q3 2022		Deviation	Deviation	Q3 2021	DNBe
	Actual	DNB	(%)	Absolute	Actual	2022e
Net sales	106.1	106.2	0%	0	87.9	418.9
Gross profit	103.0	102.8	0%	0	87.2	407.3
Gross margin	97.1%	96.8%	0.3pp		99.2%	97.2%
One-offs	-4.5	0		-5	2	-4
EBITDA adj.	38.7	40.8	-5%	-2	35.0	131.4
EBITDA adj. margin	36.5%	38.4%	-1.9pp		39.8%	31.4%
EBIT	22.1	27.3	-19%	-5	18.8	85.5
EBIT margin	20.8%	25.7%	-4.8pp		21.4%	20.4%
EBIT adj.	26.6	27.3	-2%	-1	18.8	85.5
EBIT adj. margin	25.1%	25.7%	-0.6pp		21.4%	20.4%
EPS adj.	1.04	1.44	-28%	-0.40	1.01	4.68
Adj. FCF (CFO - capex)	33.2	18.9	76%	14	21.7	79.6
Cash conversion	125%	69%	55.5pp		115%	93%
Rule of 40 (EBIT)	45.8%	43.7%	2.1pp		22.1%	37.6%
Revenue growth YOY	20.7%	20.3%	0.4pp		-1.1%	18.0%
Organic	10.9%	12.6%	-1.7pp		-0.7%	8.7%
Structural	0.0%	0.0%	0pp		0.0%	0.0%
FX	9.8%	7.8%	2pp		-0.4%	9.3%
Segment	Q3 2022		Deviation	Deviation	Q3 2021	DNBe
(SEKm)	Actual	DNB	(%)	Absolute	Actual	2022e
Net sales						
Development tools	103.3	105.7	-2%	-2	87.8	413.2
Security solutions	2.8	0.5	451%	2	0.1	5.7
Other	0.0	0.0	n.a.	0	0.0	0.0
Total	106.1	106.2	0%	0	87.9	418.9
Net sales growth						
Development tools	17.7%	20.4%	-2.7pp			370.7%
Security solutions	2700.0%	407.9%	2292.1pp			5611.5%
Other						
Total	20.7%	18.0%	2.7pp			376.6%
Net sales						
License-based	56.2	59.9	-6%	-4	46.2	238.1
Support and softw are updates	44.4	41.8	6%	3	36.9	163.8
Other	5.5	4.5	22%	1	4.8	17.1
Total	106.1	106.2	0%	0	87.9	418.9

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

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Estimate revisions

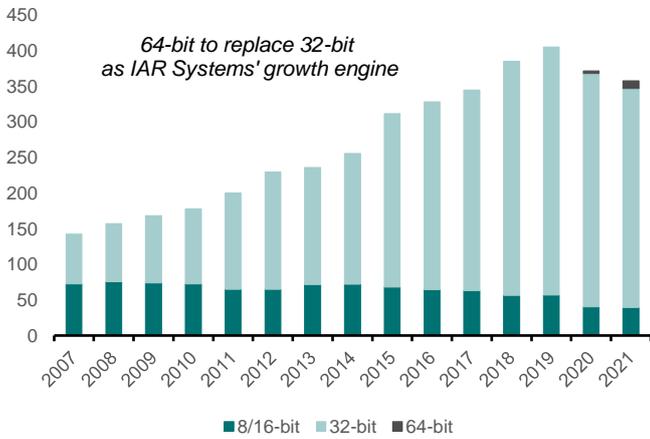
Figure 2: Estimate changes

(SEKm, except per share data)	Old			New			Change		
	2022e	2023e	2024e	2022e	2023e	2024e	2022e	2023e	2024e
Net sales	421	482	525	420	481	526	0%	0%	0%
Growth YOY, of which	18.2%	14.7%	8.9%	18.0%	14.6%	9.3%	-21bp	-13bp	46bp
Organic	10.0%	12.3%	8.9%	8.7%	11.6%	9.3%	-133bp	-73bp	46bp
Structural	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0bp	0bp	0bp
FX	8.2%	2.4%	0.0%	9.3%	3.0%	0.0%	112bp	60bp	0bp
Gross profit	408	470	513	407	469	514	0%	0%	0%
Gross margin	97.0%	97.4%	97.6%	97.0%	97.5%	97.7%	7bp	5bp	6bp
EBITDA	141	188	222	131	183	217	-7%	-3%	-2%
IAC	1	0	0	-4	0	0	-500%		
Adj. EBITDA	140	188	222	135	183	217	-4%	-3%	-2%
Depreciation and amortisation	-53	-62	-67	-50	-58	-63	-7%	-6%	-6%
EBIT	88	126	155	82	125	154	-7%	-1%	-1%
Adj. EBIT	87	126	155	85	125	154	-2%	-1%	-1%
Adj. EBIT margin	20.9%	26.2%	29.6%	19.5%	26.0%	29.4%	-140bp	-25bp	-23bp
Capitalised development costs (CDC)	52	57	62	47	51	55	-10%	-10%	-11%
EBIT excl. CDC	8.4%	14.4%	17.8%	9.2%	15.3%	18.9%	83bp	90bp	111bp
Adj. Net profit	63	96	118	64	94	117	1%	-1%	-1%
Adj. EPS (diluted)	4.61	7.00	8.65	4.68	6.91	8.60	1%	-1%	-1%
DPS	1.61	2.45	3.03	1.64	2.42	3.01	1%	-1%	-1%
Net sales by segment									
Development tools	418	469	489	413	462	486	-1%	-1%	-1%
Security solutions	2	14	36	6	19	40	183%	39%	11%
Other	0	0	0	0	0	0			
Total	421	482	525	420	481	526	0%	0%	0%
Net sales by product type									
License-based	242	292	324	238	286	322	-2%	-2%	-1%
Support and software updates	161	172	182	164	177	185	2%	3%	1%
Other	16	18	19	17	18	19	6%	0%	0%
Total	421	482	525	420	481	526	0%	0%	0%
Balance sheet and cash flow									
Adj. FCF	67	83	113	80	85	113	19%	2%	0%
Cash	145	206	285	171	228	308	18%	11%	8%
Net cash (-) / net debt (+)	-121	-182	-261	-145	-208	-289	20%	14%	10%

Source: DNB Markets

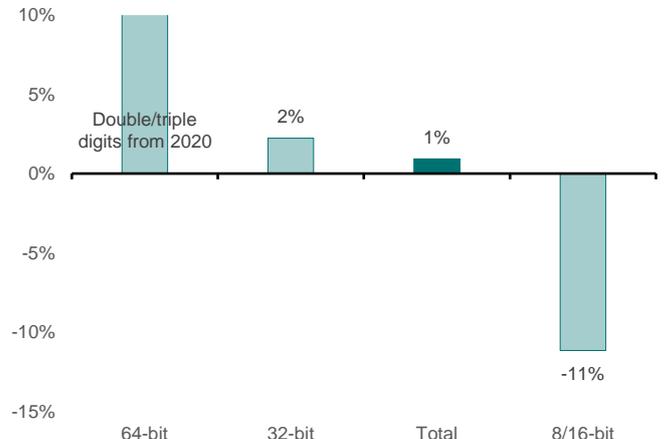
Key charts

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



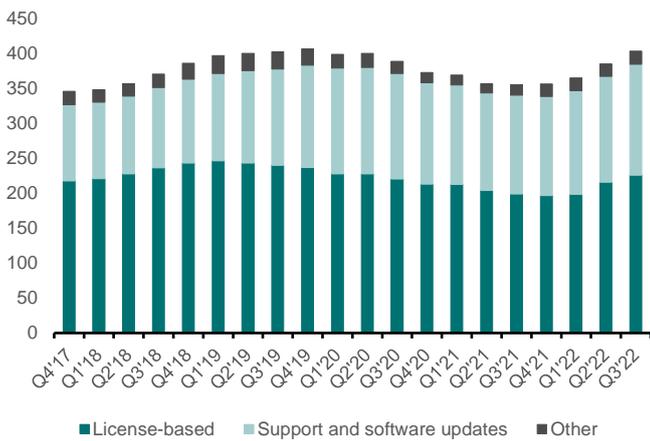
Source: Company (historical data), DNB Markets (further calculations)

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



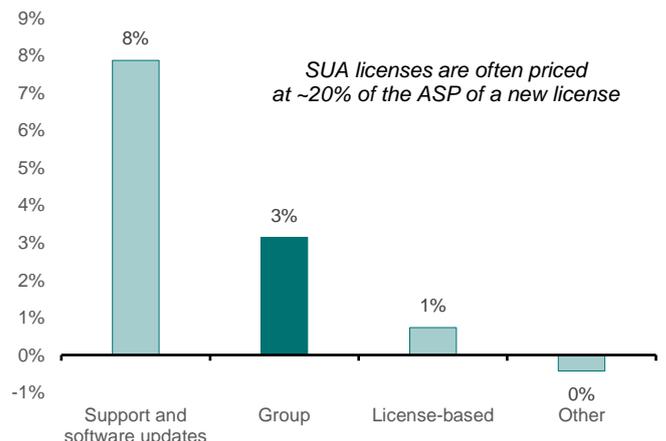
Source: Company (historical data), DNB Markets (further calculations)

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



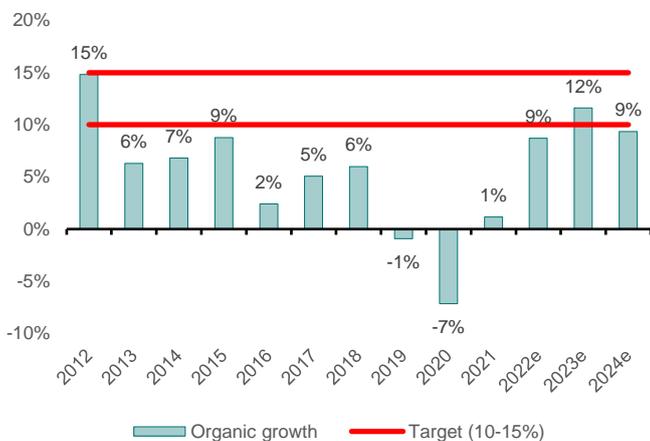
Source: Company (historical data), DNB Markets (further calculations)

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



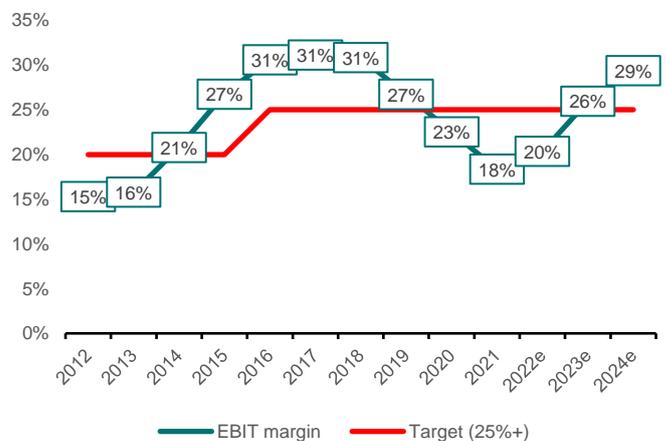
Source: Company (historical data), DNB Markets (further calculations)

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



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

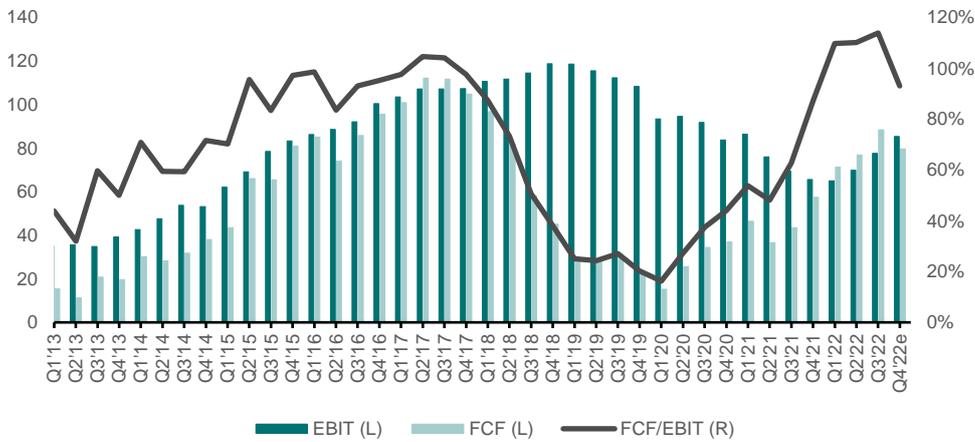
Figure 8: Financial goal 2 – EBIT margin >25%



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

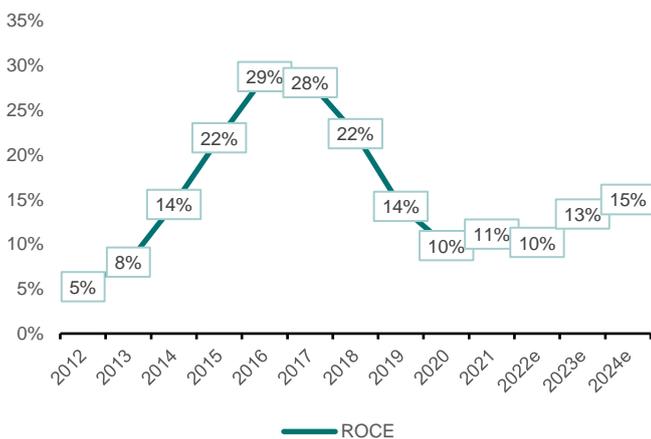
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Figure 9: LTM FCF versus LTM EBIT (2012–2022e) – coming out of an intense investment period to accelerate organic growth since 2018



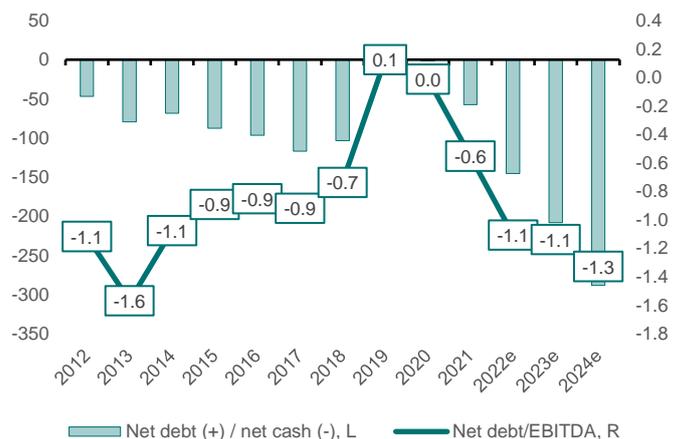
Source: DNB Markets (forecasts), company (historical data)

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



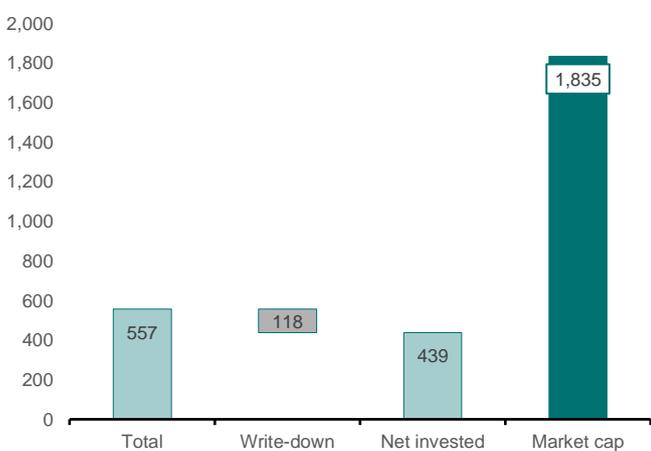
Source: DNB Markets (forecasts), company (historical data)

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



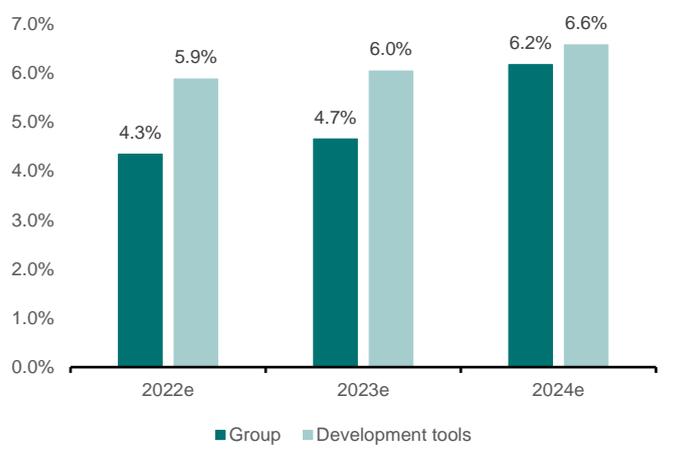
Source: DNB Markets (forecasts), company (historical data)

Figure 12: Investments (SEKm, 2016–2022)



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

Figure 13: FCF yield (2022–2024e)



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

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Forecasts

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

(SEKm)	2017	2018	2019	2020	2021	2022e	2023e	2024e	21-24e CAGR
Net sales	345.0	385.2	405.6	372.0	355.8	418.9	481.0	525.9	14%
Growth YOY, of which	5%	10%	5%	-8%	-4%	18%	15%	9%	
Organic	5%	6%	-1%	-7%	1%	9%	12%	9%	
Structural	0%	0%	0%	0%	0%	0%	0%	0%	
FX	0%	4%	6%	-1%	-6%	9%	3%	0%	
COGS	-8.5	-9.0	-10.8	-14.1	-12.0	-12.5	-12.1	-12.1	
Gross profit	336.5	376.2	394.8	357.9	346.0	407.3	468.9	513.8	
Capitalised work	0.0	0.0	0.0	0.0	0.0	46.8	51.4	54.8	
Other external expenses	-49.2	-68.2	-63.7	-37.7	-38.3	-54.2	-54.1	-57.9	
Personnel costs	-160.1	-167.9	-185.3	-187.5	-203.8	-268.5	-283.3	-293.4	
EBITDA	127.2	140.1	145.8	132.7	103.9	131.4	182.8	217.3	
IAC	0.0	-3.2	0.0	0.0	-134.2	-3.6	0.0	0.0	
Adj. EBITDA	127.2	143.3	145.8	132.7	238.1	135.0	182.8	217.3	
Depreciation and amortisation	-19.8	-24.5	-37.4	-48.9	-172.4	-49.5	-58.0	-62.9	
EBIT	107.4	115.6	108.4	83.8	-68.5	81.9	124.9	154.4	
Adj. EBIT	107.4	118.8	108.4	83.8	65.7	85.5	124.9	154.4	33%
Financial items	-1.7	-1.8	-1.4	-7.0	-0.1	-1.2	-3.2	-3.0	
Profit before tax	105.7	117.0	107.0	76.8	-68.6	80.7	121.7	151.4	
Taxes paid	-25.7	-26.2	-25.8	-17.4	1.2	-20.4	-27.4	-34.1	
Adj. Net profit	80.0	94.0	81.2	59.4	66.8	63.9	94.3	117.4	
EPS	6.33	6.67	5.96	4.36	-4.94	4.23	6.91	8.60	
Adj. EPS (diluted)	6.33	6.67	5.96	4.36	4.90	4.68	6.91	8.60	21%
DPS	5.00	5.00	3.00	0.00	0.00	1.64	2.42	3.01	
Margins									
Gross	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	97.5%	97.7%	
EBITDA	36.9%	36.4%	35.9%	35.7%	29.0%	31.3%	38.0%	41.3%	
Adj. EBITDA	36.9%	37.2%	35.9%	35.7%	66.5%	32.2%	38.0%	41.3%	
EBIT	31.1%	30.0%	26.7%	22.5%	-19.1%	19.5%	26.0%	29.4%	
Adj. EBIT	31.1%	30.8%	26.7%	22.5%	18.4%	20.4%	26.0%	29.4%	
FCF margin	25.0%	11.9%	5.4%	9.9%	16.1%	19.0%	17.7%	21.5%	
Rule of 40 (EBIT)	36.2%	42.5%	32.0%	14.2%	14.6%	37.6%	40.5%	38.7%	
ROCE	37.4%	28.1%	17.7%	12.4%	9.9%	12.8%	17.2%	19.3%	
Cash flow									
Cash flow from operating activities	123.9	92.6	105.7	118.4	131.6	133.8	152.8	185.1	
Capex	-19.0	-46.8	-83.6	-81.4	-74.1	-54.2	-67.5	-71.9	
Adj. FCF	104.9	45.8	22.1	37.0	57.5	79.6	85.3	113.2	25%
Cash conversion (FCF/EBIT)	98%	39%	20%	44%	88%	93%	68%	73%	
Balance sheet									
Cash	119.5	106.1	60.7	67.8	113.4	171.0	228.0	308.2	
Net cash (-) / net debt (+)	-117.0	-103.3	18.4	-1.5	-57.4	-145.3	-208.3	-288.5	
Net debt/EBITDA	-0.9x	-0.7x	0.1x	0.0x	-0.6x	-1.1x	-1.1x	-1.3x	

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

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

(SEKm)	2017	2018	2019	2020	2021	2022e	2023e	2024e	21-24e CAGR
Net sales by segment									
Development tools	345.0	380.2	403.9	367.0	355.1	413.2	461.7	486.1	11%
Security solutions	0.0	5.0	1.7	5.0	0.7	5.7	19.3	39.8	284%
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	419.8	481.0	525.9	14%
Net sales growth by segment									
Development tools	5%	10%	6%	-9%	-3%	16%	12%	5%	
Security solutions			-66%	194%	-86%	716%	238%	106%	
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	238.1	286.2	322.2	18%
Support and softw are updates	108.6	119.4	146.3	145.2	141.6	163.8	176.6	184.6	9%
Other	19.1	22.9	23.0	14.4	18.1	17.1	18.2	19.1	2%
Total	345.0	385.2	405.6	372.0	355.8	419.8	481.0	525.9	14%
Net sales growth by product									
License-based		12%	-3%	-10%	-8%	21%	20%	13%	
Support and softw are updates		10%	23%	-1%	-2%	16%	8%	5%	
Other		20%	0%	-37%	26%	-6%	7%	5%	
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)	Q3'21	Q4'21	Q1'22	Q2'22	Q3'22	Q4'22e	Q1'23e	Q2'23e	Q3'23e	Q4'23e
Net sales by segment										
Development tools	87.8	91.5	97.0	107.2	103.3	105.7	114.1	118.0	115.1	114.5
Security solutions	0.1	0.1	0.4	0.4	2.8	2.1	2.4	3.4	6.4	7.1
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	107.8	116.5	121.4	121.5	121.6
Net sales growth by segment										
Development tools	-1%	2%	9%	23%	18%	16%	18%	10%	11%	8%
Security solutions	-75%	-92%	33%	100%	2700%	2012%	506%	755%	127%	236%
Other										
Total	-1%	1%	10%	23%	20%	18%	19%	13%	14%	13%
Net sales by product										
License-based	46.2	49.4	52.0	67.8	56.2	62.1	66.2	76.3	69.7	74.0
Support and softw are updates	36.9	36.1	41.2	36.9	44.4	41.3	45.7	40.8	47.2	42.9
Other	4.8	6.1	4.2	2.9	5.5	4.5	4.7	4.3	4.5	4.8
Total	90.0	91.6	98.3	107.6	106.1	107.8	116.5	121.4	121.5	121.6
Net sales growth by product										
License-based	-9%	-5%	4%	35%	22%	26%	27%	13%	24%	19%
Support and softw are updates	4%	2%	19%	9%	20%	14%	11%	11%	6%	4%
Other	85%	79%	2%	-6%	15%	-26%	11%	48%	-18%	6%
Total	-1%	1%	10%	23%	20%	18%	19%	13%	14%	13%

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

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

(SEKm)	Q3'21	Q4'21	Q1'22	Q2'22	Q3'22	Q4'22e	Q1'23e	Q2'23e	Q3'23e	Q4'23e
Net sales	90.0	91.6	98.3	107.6	106.1	107.8	116.5	121.4	121.5	121.6
Grow th YOY , of w hich	-1%	1%	10%	23%	20%	18%	19%	13%	14%	13%
Organic	-1%	2%	3%	14%	11%	6%	13%	8%	13%	14%
Structural	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
FX	0%	-1%	7%	9%	9%	12%	6%	5%	2%	-1%
COGS	-2.8	-3.0	-2.8	-3.1	-3.1	-3.5	-3.3	-3.1	-2.6	-3.1
Gross profit	87.2	88.6	95.5	104.5	103.0	104.3	113.2	118.3	118.8	118.5
Capitalised w ork	13.7	0.0	12.2	10.5	11.3	12.8	12.7	12.7	13.2	12.7
Other external expenses	-10.3	-12.0	-11.5	-11.9	-18.8	-12.0	-12.9	-12.8	-15.4	-12.9
Personnel costs	-55.6	-63.4	-66.0	-71.2	-61.3	-70.0	-71.7	-72.6	-66.7	-72.2
EBITDA	35.0	13.2	30.2	31.9	34.2	35.1	41.3	45.6	49.9	46.1
IAC	2.1	-134.2	0.9	0.0	-4.5	0.0	0.0	0.0	0.0	0.0
Adj. EBITDA	32.9	147.4	29.3	31.9	38.7	35.1	41.3	45.6	49.9	46.1
Depreciation and amortisation	-14.1	-132.2	-13.0	-12.3	-12.1	-12.1	-13.9	-14.8	-14.4	-14.8
EBIT	20.9	-119.0	17.2	19.6	22.1	23.0	27.4	30.7	35.5	31.3
Adj. EBIT	18.8	15.2	16.3	19.6	26.6	23.0	27.4	30.7	35.5	31.3
Financial items	-0.3	1.8	-0.9	-0.5	1.1	-0.9	-0.8	-0.8	-0.8	-0.8
Profit before tax	20.6	-117.2	16.3	19.1	23.2	22.1	26.6	29.9	34.7	30.5
Taxes paid	-4.7	11.8	-4.4	-4.8	-6.4	-4.8	-6.0	-6.7	-7.8	-6.9
Adj. Net profit	13.8	28.8	11.0	14.3	21.3	17.3	20.6	23.2	26.9	23.6
EPS	1.17	-7.72	0.88	1.05	1.04	1.26	1.51	1.70	1.97	1.73
Adj. EPS (diluted)	1.01	2.11	0.81	1.05	1.56	1.26	1.51	1.70	1.97	1.73
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.64	0.00	0.00
Margins										
Gross	96.9%	96.7%	97.2%	97.1%	97.1%	96.8%	97.2%	97.4%	97.8%	97.5%
EBITDA	38.9%	14.4%	30.7%	29.6%	32.2%	32.5%	35.5%	37.5%	41.1%	37.9%
Adj. EBITDA	36.6%	160.9%	29.8%	29.6%	36.5%	32.5%	35.5%	37.5%	41.1%	37.9%
EBIT	23.2%	-129.9%	17.5%	18.2%	20.8%	21.3%	23.5%	25.3%	29.2%	25.7%
Adj. EBIT	20.9%	16.6%	16.6%	18.2%	25.1%	21.3%	23.5%	25.3%	29.2%	25.7%
FCF margin	24.1%	25.5%	15.7%	15.3%	31.3%	13.5%	14.8%	21.5%	18.6%	15.9%
Rule of 40 (EBIT)	22.1%	17.6%	27.2%	41.3%	43.0%	39.1%	42.1%	38.1%	43.7%	38.5%
ROCE	9.7%	9.3%	9.5%	10.4%	11.8%	12.7%	14.1%	15.4%	16.3%	17.1%
Cash flow										
Cash flow from operating activities	41.4	40.5	28.8	26.0	47.4	31.6	33.8	43.1	39.7	36.2
Capex	-19.7	-17.1	-13.4	-9.5	-15.6	-17.1	-16.5	-16.9	-17.1	-16.9
Adj. FCF	21.7	23.4	15.4	16.5	31.8	14.5	17.2	26.1	22.7	19.3
Cash conversion (FCF/EBIT)	115%	154%	94%	84%	120%	63%	63%	85%	64%	62%
Balance sheet										
Cash	91.3	113.4	125.0	117.9	158.8	171.0	186.3	188.1	208.7	228.0
Net cash (-) / net debt (+)	-36.4	-57.4	-72.0	-85.9	-131.1	-145.3	-162.6	-166.4	-189.0	-208.3
Net debt/EBITDA	-0.3x	-0.6x	-0.7x	-0.8x	-1.2x	-1.1x	-1.1x	-1.1x	-1.1x	-1.1x

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

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Valuation

Figure 18: Valuation approaches (SEKm, %)

	Peers regression	DCF	Historical average
Net sales (2022e)			481
Adj. EBIT (2022e)			125
Adj. EPS (2022e)			6.91
Sales CAGR (2021–2023e)	15.9		15.9
Adj. EBIT margin (2022e)	21.9		20.4
RO40 (2022e)	48.1		36.3
Target multiple	RO40, P/B, EV/S	10% WACC	20x EV/EBIT
Enterprise value	3,023	3,141	2,498
Net debt (+)/cash (-)	-145	-145	-145
Equity value	3,168	3,286	2,643
NOSH	13.6	13.6	13.6
Implied price/share	232	241	194
Implied potential	73%	79%	44%

2024e valuation multiples

Implied EV/sales	5.7	6.0	4.7
Implied EV/EBIT	19.6	20.3	16.2
Implied P/E	27.0	28.0	22.5

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	419	481	526
Grow th YOY	5.4%	5.1%	10.2%	5.2%	-8.3%	-4.4%	18.0%	14.6%	9.3%
Gross profit	316	337	376	395	358	346	407	469	514
Gross margin	96.3%	97.5%	97.7%	97.3%	96.2%	96.6%	97.0%	97.5%	97.7%
Adj. EBITDA	117	127	140	146	133	104	131	183	217
EBITDA margin	36.9%	36.9%	37.2%	35.9%	35.7%	66.5%	32.2%	38.0%	41.3%
Adj. EBIT	101	107	119	108	84	66	85	125	154
EBIT margin	30.6%	31.1%	30.8%	26.7%	22.5%	18.4%	20.4%	26.0%	29.4%
Adj. Net profit	82	80	94	81	59	67	64	94	117
Adj. FCF	95	105	46	22	37	58	80	85	113
FCF margin	29.0%	30.4%	11.9%	5.4%	9.9%	16.2%	19.0%	17.7%	21.5%
Cash conversion	95%	98%	39%	20%	44%	88%	93%	68%	73%
Rule of 40 (EBIT)	36.0%	36.2%	41.0%	31.9%	14.2%	14.0%	38.4%	40.5%	38.7%
ROCE	35.0%	37.4%	28.1%	17.7%	12.4%	9.9%	12.8%	17.2%	19.3%
ROIC	27.4%	28.5%	21.9%	13.8%	10.1%	10.4%	9.9%	13.4%	15.0%
Market cap	2,602	2,387	3,310	2,535	1,905	1,606	1,834	1,834	1,834
Net debt	-97	-117	-103	18	-1	-57	-145	-208	-289
Enterprise value	2,505	2,270	3,206	2,554	1,904	1,548	1,689	1,626	1,546
EV/Sales	7.6x	6.6x	8.3x	6.3x	5.1x	4.4x	4.0x	3.4x	2.9x
EV/EBIT	24.9x	21.1x	27.0x	23.6x	22.7x	23.6x	19.8x	13.0x	10.0x
P/E	31.7x	29.8x	35.2x	31.2x	32.1x	24.0x	28.7x	19.5x	15.6x
FCF yield	3.7%	4.4%	1.4%	0.9%	1.9%	3.6%	4.3%	4.7%	6.2%

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)



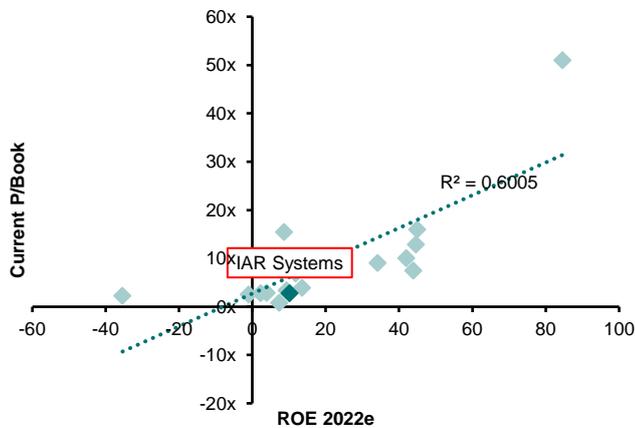
Source: Bloomberg

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



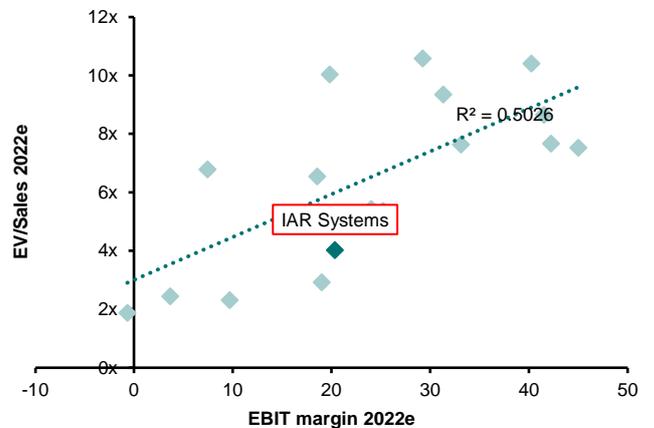
Source: Bloomberg

Figure 24: Current P/book versus ROE 2022e



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

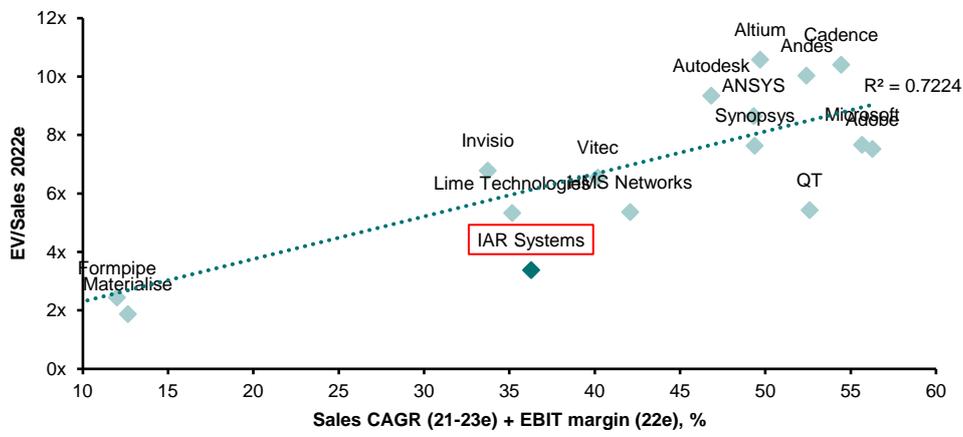
Figure 25: EV/sales versus EBIT margin (2022e)



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	30	19	16	20	13	10	13	9	7	4	3	3	1.2	4.3	10	13	20.4	26.0	16	38	19	
Premium/discount		-50%	-39%	-34%	-48%	-51%	-49%	-48%	-51%	-65%	-46%	-46%	-46%										
IAR Systems (Cons.)	1.8	29	19	16	19	13	10	12	9	7	4	4	3	1.2	4.3			20.9	26.3	16	40	43	
Premium/discount		-52%	-40%	-35%	-48%	-51%	-49%	-51%	-52%	-66%	-44%	-42%	-38%										
Nordic software																							
Enea	1.8	13	16	14	24	17	13	8	7	6	2	2	2	0.0	17.2	7	3	9.7	12.0	-3	-31	-33	
Formpipe	1.1	98	28	17	67	23	14	16	11	8	3	2	2	3.3		2	9	3.7	9.7	8	-8	9	
HMS Networks	13.6	30	28	27	22	22	20	19	19	18	6	5	5	1.2	1.3	34	27	25.2	24.1	17	19	19	
Invisio	6.7	151	48	33	124	37	25	72	30	21	9	7	6	0.4	0.5	9	27	7.4	18.1	26	100	107	
Karnov	6.2	22	15	13	34	22	21	19	12	11	5	3	3	2.4		4	8	19.0	15.6	61	21	22	
Lime Technologies	2.7	31	26	23	32	26	22	19	16	14	6	5	5	1.3	2.9	45	42	18.7	19.4	16	15	18	
QT	11.8	33	27	19	29	20	13	25	18	12	7	5	4	0.0	1.7	45	36	24.0	25.6	29	33	30	
Vitec	14.7	46	37	32	45	34	29	23	18	16	8	7	6	0.6		12	14	18.6	20.3	22	26	14	
WithSecure	3.1									105	2	1	1	0.0		-35	-16	-31.1	-15.0	-19			
Engineering software																							
Adobe	1,617.3	23	21	18	18	17	14	17	15	13	8	8	7	0.0	4.9	42	40	45.0	43.5	11	8	11	
Altium	32.2	60	45	36	44	33	26	37	29	24	13	11	9	1.9	1.3	19	23	29.2	32.1	20	22	23	
Andes	6.3	40	38	20							14	10	7	0.7		9	9	19.8	35.0	33	68	60	
ANSYS	206.2	28	26	23	22	20	18	21	19	17	9	9	8	0.0	3.0	14	14	41.5	41.9	8	9	8	
Autodesk	496.8	42	32	27	33	25	22	32	24	20	11	9	8	0.0	3.2	85	149	31.3	36.0	16	30	30	
Cadence	443.5	35	32	28	28	26	23	26	23	19	11	10	9	0.0	2.8	38	36	40.2	39.3	14	18	19	
Materialise	6.1	335	74	30		63	21	21	15	10	2	2	2	0.0	0.3	-1	2	-0.7	2.9	13	-9	-11	
Microsoft	18,465.5	24	23	20	19	18	15	16	15	13	8	8	7	1.1	3.9	44	37	42.3	41.6	13	13	12	
Synopsys	483.9	33	29	25	25	21	19	23	21	21	9	8	7		3.3	24	24	33.1	34.1	16	23	22	
Average	1,212.2	61	32	24	38	27	20	25	18	21	7	6	5	0.8	3.6	22	27	21.0	24.2	17	21	21	
Median	12.7	33	28	23	29	22	20	21	18	16	8	7	6	0.4	2.9	16	23	21.9	24.8	16	19	19	

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

Summary of positives

Attractive position in a structural growth niche

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

Market dynamics benefiting the market leader

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

96%+ gross margins ensure high level of scalability

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

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

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

Summary of negatives

Possible shift in the competitive landscape

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

Potential weakening of the Embedded Workbench community

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

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

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

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

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

SaaS transition still ahead for IAR Systems

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

Continued market consolidation among processor vendors

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

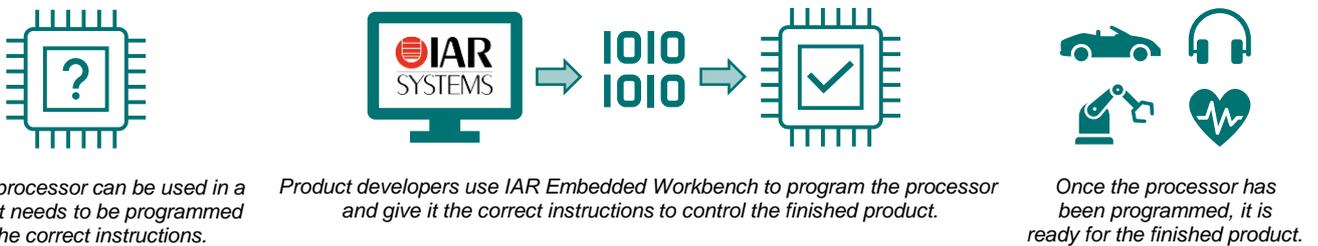
Business overview

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

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

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

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



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

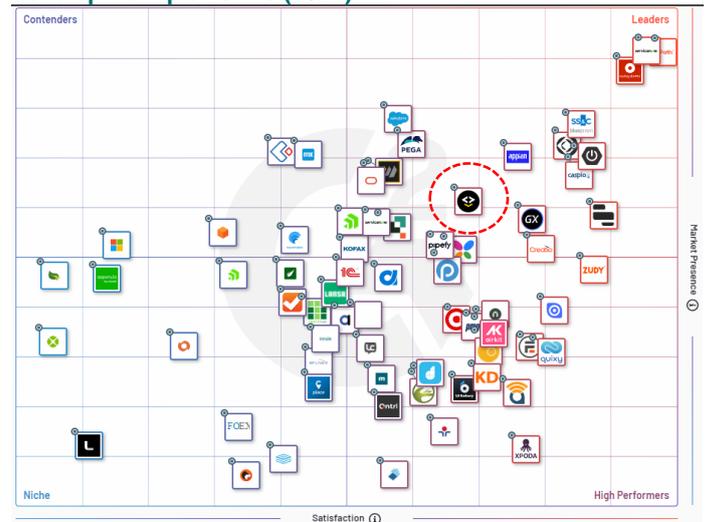
Headquartered in Uppsala, Sweden, IAR Systems has 200+ employees in 15 offices on three continents with technical support teams in its customers’ local time zones in 10+ languages. Its independent software supports more than 14,000 different processors from more than 70 processor vendors, which is more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

Figure 29: Example of customers



Source: Company

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



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

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

Long-standing embedded industry partnerships

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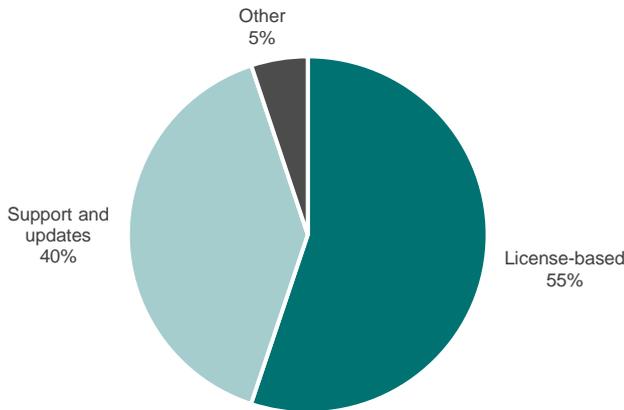
companies, etc.); and 4) suppliers of integrated programmes (real-time operating systems, graphics development, etc.).

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

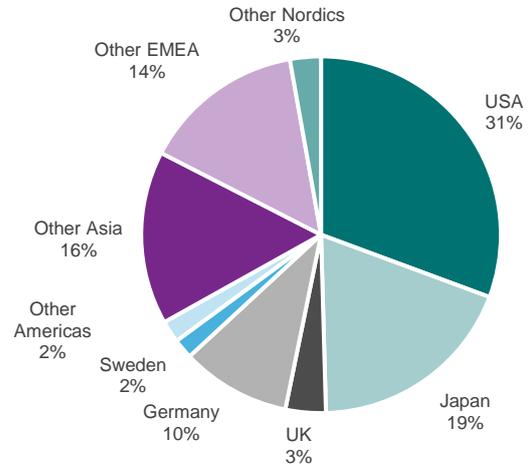
- **Development tools (~100% of net sales)** consist of IAR Embedded Workbench (8- to 64-bit) with world-leading code-optimisation technology, compiler, debugger probes and analysis tools (ensuring code quality and coding standards), functional safety certifications (pre-certified build tools), RISV-V 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 to securely programme products by giving each device a unique identity. The medium-term embedded security market opportunity with an 'out of the box' solution for mainstream MCUs appears likely to be beneficial for IAR, especially in device production as opposed to product development (royalty-based instead of licences). However, it will probably take time for security regulations and standards to significantly affect the marketplace.

Figure 31: Net sales by revenue stream (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	420	481	526	421	482	525	-1	-1	1
Cost of sales	-13	-12	-12	-13	-12	-12	0	0	0
Gross profit	407	469	514	408	470	513	0	-1	1
Operating expenses	-323	-337	-351	-318	-339	-352	-5	1	1
EBITDA	131	183	217	141	188	222	-10	-5	-5
EBITDA adj	135	183	217	140	188	222	-5	-5	-5
EBITDA margin (%)	31.3	38.0	41.3	33.6	39.0	42.3	-2.3	-1.0	-1.0
Depreciation	-22	-20	-21	-23	-23	-23	1	2	2
Amortisation	-28	-38	-42	-31	-39	-44	3	2	2
EBIT	82	125	154	88	126	155	-6	-2	-1
EBIT adj	85	125	154	87	126	155	-2	-2	-1
Net financial items	-1	-3	-3	-3	-3	-3	2	0	0
PBT	81	122	151	85	123	152	-4	-2	-1
Taxes	-20	-27	-34	-21	-28	-34	0	0	0
Minorities	0	0	0			0			0
Net profit	60	94	117	64	96	118	-4	-1	-1
Adjustments to net profit	4	0	0	-1	0	0	5	0	0
Net profit adj	64	94	117	63	96	118	1	-1	-1
<i>Per share data (SEK)</i>									
EPS	4.23	6.91	8.60	4.69	7.00	8.65	-0.45	-0.09	-0.06
EPS adj	4.68	6.91	8.60	4.61	7.00	8.65	0.07	-0.09	-0.06
DPS ordinary	1.64	2.42	3.01	1.61	2.45	3.03	0.02	-0.03	-0.02
DPS	1.64	2.42	3.01	1.61	2.45	3.03	0.02	-0.03	-0.02
<i>Other key metrics (%)</i>									
Revenue growth	17.3	14.6	9.3	17.5	14.7	8.9	-0.2	-0.1	0.5
EBIT adj growth	30.1	46.1	23.7	32.4	45.4	22.9	-2.3	0.7	0.7
EPS adj growth	-4.6	47.7	24.5	-5.9	51.8	23.7	1.3	-4.0	0.8
Avg. number of shares (m)	14	14	14	14	14	14	0	0	0
Capex	-54	-67	-72	-56	-71	-76	2	3	4
OpFCF	81	115	145	85	118	146	-4	-2	0
Working capital	-55	-55	-60	-37	-34	-38	-18	-22	-22
NIBD adj	-145	-208	-289	-121	-182	-261	-24	-26	-27

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	8.71	11.60	9.33	10.04	12.33	8.87	-1.33	-0.73	0.46
Structure impact % YOY	0.00	0.00	0.00			0.00			0.00
Currency impact % YOY	9.29	2.97	0.00	8.17	2.36	0.00	1.12	0.60	0.00

Source: DNB Markets

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Quarterly numbers

(SEKm)	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022e	Q1 2023e	Q2 2023e	Q3 2023e	Q4 2023e
Revenues	87	90	92	98	108	106	108	117	121	121	122
Cost of sales	-3	-3	-3	-3	-3	-3	-4	-3	-3	-3	-3
Gross profit	85	87	89	96	105	103	104	113	118	119	119
Operating expenses	-75	-66	-75	-78	-83	-80	-82	-85	-85	-82	-85
EBITDA	26	35	13	30	32	34	35	41	46	50	46
Depreciation	-5	-5	-5	-6	-6	-5	-5	-5	-5	-5	-5
Amortisation	-8	-9	-127	-7	-7	-7	-7	-9	-10	-10	-10
EBIT	13	21	-119	17	20	22	23	27	31	35	31
Net financial items	-1	0	2	-1	-1	1	-1	-1	-1	-1	-1
PBT	12	21	-117	16	19	23	22	27	30	35	30
Taxes	-2	-5	12	-4	-5	-6	-5	-6	-7	-8	-7
Minorities	0	0	0	0	0	0	0	0	0	0	0
Net profit	9	16	-105	12	14	17	17	21	23	27	24
Adjustments to net profit	2	-2	134	-1	0	5	0	0	0	0	0
Net profit adj	11	14	29	11	14	21	17	21	23	27	24
Dividend paid	0	0	0	0	0	0	0	0	-22	0	0
Avg. number of shares (m)	14	14	14	14	14	14	14	14	14	14	14
<i>Per share data (SEK)</i>											
EPS	0.68	1.17	-7.72	0.88	1.05	1.04	1.26	1.51	1.70	1.97	1.73
EPS adj	0.83	1.01	2.11	0.81	1.05	1.56	1.26	1.51	1.70	1.97	1.73
DPS ordinary	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.64	0.00	0.00
DPS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.64	0.00	0.00
<i>Growth and margins (%)</i>											
Revenues, QOQ growth	-1.7	3.0	1.8	7.3	9.5	-1.4	1.6	8.1	4.2	0.1	0.1
Revenues, YOY growth	-12.7	1.2	1.0	10.6	23.1	17.9	17.7	18.6	12.8	14.5	12.7
EPS adj, YOY growth	-35.8	-26.2	140.0	-14.1	26.6	54.3	-40.0	87.7	62.3	26.3	36.8
Gross margin	96.9	96.9	96.7	97.2	97.1	97.1	96.8	97.2	97.4	97.8	97.5
EBITDA adj margin	32.0	36.6	160.9	29.8	29.6	36.5	32.5	35.5	37.5	41.1	37.9
Depreciation/revenues	-5.9	-5.7	-5.7	-5.8	-5.3	-5.1	-4.7	-4.2	-4.4	-4.0	-4.4
EBIT adj margin	16.8	20.9	16.6	16.6	18.2	25.1	21.3	23.5	25.3	29.2	25.7
Net profit margin	10.6	17.7	nm	12.1	13.3	15.8	16.0	17.7	19.1	22.1	19.4

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

Adjustments to quarterly numbers

(SEKm)	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022e	Q1 2023e	Q2 2023e	Q3 2023e	Q4 2023e
EBITDA	26	35	13	30	32	34	35	41	46	50	46
EBITDA adj	28	33	147	29	32	39	35	41	46	50	46
EBIT	13	21	-119	17	20	22	23	27	31	35	31
Other EBIT adjustments	-2	2	-134	1	0	-5	0	0	0	0	0
EBIT adj	15	19	15	16	20	27	23	27	31	35	31
Net profit	9	16	-105	12	14	17	17	21	23	27	24
Other EBIT adjustments	-2	2	-134	1	0	-5	0	0	0	0	0
Net profit adj	11	14	29	11	14	21	17	21	23	27	24

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

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Quarterly numbers by segment and assumptions

(SEKm)	Q2 2021	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022e	Q1 2023e	Q2 2023e	Q3 2023e	Q4 2023e
Assumptions											
Revenue org. % YOY	-2.40	-0.67	1.98	3.04	13.84	10.89	6.22	13.43	7.67	12.63	13.72
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	-10.29	-0.45	-0.99	6.52	9.27	9.33	11.52	6.05	5.15	1.86	-0.98

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	420	481	526
Cost of sales	-10	-12	-9	-9	-11	-14	-12	-13	-12	-12
Gross profit	301	316	337	376	395	358	346	407	469	514
Operating expenses	-203	-203	-209	-236	-249	-225	-242	-323	-337	-351
EBITDA	98	113	127	140	146	133	104	131	183	217
Depreciation	-3	-3	-2	-3	-13	-20	-20	-22	-20	-21
Amortisation	-12	-14	-17	-22	-25	-29	-152	-28	-38	-42
EBIT	83	97	107	116	108	84	-69	82	125	154
Net financial items	0	0	-2	-2	-1	-7	0	-1	-3	-3
PBT	83	100	106	117	107	77	-69	81	122	151
Taxes	-20	-22	-26	-26	-26	-17	1	-20	-27	-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	60	94	117
Adjustments to net profit	0	4	0	3	0	0	134	4	0	0
Net profit adj	63	82	80	94	81	59	67	64	94	117
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	4.23	6.91	8.60
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.68	6.91	8.60
DPS ordinary	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.64	2.42	3.01
DPS	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.64	2.42	3.01
<i>Growth and margins (%)</i>										
Revenue growth	21.9	5.4	5.1	11.7	5.3	-8.3	-3.8	17.3	14.6	9.3
EPS adj growth	50.2	23.0	2.6	5.3	-10.6	-26.8	12.5	-4.6	47.7	24.5
Gross margin	96.7	96.3	97.5	97.7	97.3	96.2	96.6	97.0	97.5	97.7
EBITDA margin	31.5	34.5	36.9	36.4	35.9	35.7	29.0	31.3	38.0	41.3
EBITDA adj margin	31.5	35.7	36.9	37.2	35.9	35.7	66.5	32.2	38.0	41.3
Depreciation/revenues	-0.8	-0.8	-0.7	-0.7	-3.2	-5.5	-5.7	-5.2	-4.3	-4.0
EBIT margin	26.8	29.4	31.1	30.0	26.7	22.5	nm	19.5	26.0	29.4
EBIT adj margin	26.8	30.6	31.1	30.8	26.7	22.5	18.4	20.4	26.0	29.4
PBT margin	26.7	30.5	30.6	30.4	26.4	20.6	nm	19.2	25.3	28.8
Net profit margin	20.3	23.8	23.2	23.6	20.0	16.0	nm	14.4	19.6	22.3

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	131	183	217
EBITDA adj	98	117	127	143	146	133	238	135	183	217
EBIT	83	97	107	116	108	84	-69	82	125	154
Other EBIT adjustments	0	-4	0	-3	0	0	-134	-4	0	0
EBIT adj	83	101	107	119	108	84	66	85	125	154
Net profit	63	78	80	91	81	59	-67	60	94	117
Other EBIT adjustments	0	-4	0	-3	0	0	-134	-4	0	0
Net profit adj	63	82	80	94	81	59	67	64	94	117
<i>Per share data (SEK)</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.23	6.91	8.60
Recommended adjustment	0.00	0.00	0.00	0.00	0.00	0.00	9.85	0.44	0.00	0.00
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.68	6.91	8.60

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	60	94	117
Depreciation and amortisation	15	17	20	25	37	49	172	50	58	63
Cash flow from operations (CFO)	99	114	124	93	106	118	132	134	153	185
Capital expenditure	-19	-19	-19	-47	-84	-81	-74	-54	-67	-72
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	-54	-67	-72
Free cash flow (FCF)	80	95	86	-125	4	37	58	80	85	113
Net change in debt	0	0	0	0	30	6	1	1	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	-31	-6	0
Cash flow from financing (CFF)	-64	-88	-63	108	-52	-25	-15	-30	-28	-33
Total cash flow (CFO+CFI+CFF)	17	7	23	-17	-49	12	42	49	57	80
<i>FCFF calculation</i>										
Free cash flow	80	95	86	-125	4	37	58	80	85	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	1.7	14.2	21.2
CFI	42.3	-3.3	-98.9	-478.5	53.0	20.4	9.0	26.9	-24.5	-6.6
FCF	108.3	18.5	-9.4	-244.7	102.8	957.1	55.4	38.5	7.1	32.7
CFF	-19.5	-39.0	28.5	270.4	-148.3	52.7	38.6	-100.0	6.2	-16.5
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	892	962	1,046
Inventories	5	6	5	7	7	6	10	9	10	10
Trade receivables	44	48	51	63	67	59	59	63	66	63
Other receivables	20	19	12	38	52	64	44	34	34	31
Current financial assets	0	0	0	0	0	0	0	0	0	0
Cash and cash equivalents	89	99	120	106	61	68	113	171	228	308
Current assets	158	172	187	214	186	196	226	277	337	412
Property, plant and equipment	7	6	6	9	7	8	15	16	17	17
Other intangible assets	192	197	194	484	624	624	567	592	601	609
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	615	624	634
Total assets	399	396	410	722	825	834	813	892	962	1,046
Equity and liabilities	399	396	410	722	825	834	813	892	962	1,046
Total equity	291	280	290	550	592	613	585	668	740	825
Trade payables	5	5	6	7	9	5	9	7	7	7
Other payables and accruals	83	92	86	131	117	111	133	154	157	158
Short-term debt	1	1	1	0	25	18	18	0	0	0
Total current liabilities	90	99	102	140	164	150	179	175	178	178
Long-term debt	1	2	2	1	41	32	20	12	6	6
Deferred tax liabilities	17	15	14	30	27	37	28	36	36	36
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	49	43	43
Total liabilities	108	116	120	172	233	220	228	224	221	221
Total equity and liabilities	399	396	410	722	825	834	813	892	962	1,046
<i>Key metrics</i>										
Net interest bearing debt	-88	-97	-117	-103	18	-2	-57	-145	-208	-289

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	134.40	134.40	134.40
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	1,834	1,834	1,834
Net interest bearing debt	-88	-97	-117	-103	18	-2	-57	-145	-208	-289
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	-145	-208	-289
EV	1,807	2,505	2,270	3,206	2,554	1,904	1,548	1,689	1,626	1,546
EV adj	1,807	2,505	2,270	3,206	2,554	1,904	1,548	1,689	1,626	1,546
<i>Valuation</i>										
EPS	5.02	6.18	6.33	6.67	5.96	4.36	-4.94	4.23	6.91	8.60
EPS adj	5.02	6.18	6.33	6.67	5.96	4.36	4.90	4.68	6.91	8.60
DPS ordinary	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.64	2.42	3.01
DPS	5.00	7.00	5.00	5.00	3.00	0.00	0.00	1.64	2.42	3.01
P/E	29.9	33.4	29.8	36.4	31.2	32.1	-23.8	31.7	19.5	15.6
P/E adj	29.9	33.4	29.8	36.4	31.2	32.1	24.0	28.7	19.5	15.6
P/B	6.51	9.31	8.22	6.02	4.28	3.11	2.74	2.74	2.48	2.22
Average ROE	21.9%	27.3%	28.1%	21.6%	14.2%	9.9%	-11.2%	9.6%	13.4%	15.0%
Earnings yield adj	3.3%	3.0%	3.4%	2.7%	3.2%	3.1%	4.2%	3.5%	5.1%	6.4%
Dividend yield	3.3%	3.4%	2.6%	2.1%	1.6%	0.0%	0.0%	1.2%	1.8%	2.2%
Free cash flow yield	4.2%	3.7%	3.6%	-3.8%	0.1%	1.9%	3.6%	4.3%	4.7%	6.2%
EV/SALES	5.80	7.63	6.58	8.32	6.30	5.12	4.32	4.02	3.38	2.94
EV/SALES adj	5.80	7.63	6.58	8.32	6.30	5.12	4.32	4.02	3.38	2.94
EV/EBITDA	18.4	22.1	17.8	22.9	17.5	14.3	14.9	12.9	8.9	7.1
EV/EBITDA adj	18.4	21.4	17.8	22.4	17.5	14.3	6.5	12.5	8.9	7.1
EV/EBIT	21.7	26.0	21.1	27.7	23.6	22.7	-22.6	20.6	13.0	10.0
EV/EBIT adj	21.7	24.9	21.1	27.0	23.6	22.7	23.6	19.8	13.0	10.0
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	26.4	16.7	12.8
EV/OpFCF (taxed)	29.8	32.8	26.8	45.6	66.6	57.9	10.4	27.2	18.5	13.9

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

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Key accounting ratios

	2015	2016	2017	2018	2019	2020	2021	2022e	2023e	2024e
<i>Profitability (%)</i>										
ROA	16.4	19.6	19.9	16.0	10.5	7.2	-8.2	7.1	10.2	11.7
ROCE	28.6	35.0	37.4	28.1	17.7	12.4	9.9	12.8	17.2	19.3
ROCE after tax	22.3	27.3	29.1	21.9	13.8	9.7	7.8	10.0	13.4	15.0
<i>Return on invested capital (%)</i>										
Net PPE/revenues	2.1	1.9	1.8	2.3	1.8	2.0	4.1	3.8	3.5	3.3
Working capital/revenues	-6.1	-7.5	-6.9	-7.8	-0.2	3.4	-8.3	-13.1	-11.5	-11.5
<i>Cash flow ratios (%)</i>										
FCF/revenues	25.8	29.0	25.0	-32.4	0.9	9.9	16.1	19.0	17.7	21.5
FCF yield (%)	4.2	3.7	3.6	1.4	0.9	1.9	3.6	4.3	4.7	6.2
CFO/revenues	31.7	34.8	35.9	24.0	26.1	31.8	36.8	31.9	31.8	35.2
CFO/market capitalisation	5.2	4.4	5.2	2.8	4.2	6.2	8.2	7.3	8.3	10.1
CFO/capex	508.8	614.0	652.1	197.9	126.4	145.5	177.6	247.0	226.5	257.4
CFO/current liabilities	110.2	115.8	121.1	66.2	64.4	78.9	73.7	76.6	85.7	104.0
Cash conversion ratio	126.8	122.2	107.9	-137.6	4.3	62.3	-85.3	132.2	90.5	96.5
Capex/revenues	6.2	5.7	5.5	12.1	20.6	21.9	20.7	12.9	14.0	13.7
Capex/depreciation	776.0	744.0	791.7	1800.0	648.1	401.0	363.2	247.2	329.9	345.0
OpFCF margin	25.3	30.0	31.4	25.1	15.3	13.8	45.8	19.2	24.0	27.6
Total payout ratio	99.6	113.3	78.9	75.0	50.4	0.0	0.0	38.7	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	-1.11	-1.14	-1.33
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	0.01	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	271.0	292.4	309.0
Receivables turnover days	74.5	74.7	66.2	96.1	106.8	120.2	104.7	84.4	75.5	65.2
Credit period	170.1	158.6	244.8	296.1	310.9	129.4	279.8	197.1	224.9	206.0
Cash conversion cycle	85.1	83.7	44.8	67.7	18.9	138.3	113.8	158.3	143.0	168.1

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

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Important Information

Company: IAR Systems
 Coverage by Analyst: Joachim Gunell
 Date: 27/10/2022

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