

Ependion

Sector: Technology

Creating growth through focus

Redeye updates its estimates of Ependion and discusses both the most recent report and Beijer Electronics' strategic review in depth. Q1 2024 was almost perfectly in line with our estimates and showed a good sequential uptick. However, the near-term appears to be quite uncertain and Westermo's ongoing cost reduction to adjust for volumes carries a signal value. On the other hand, the structural growth stays intact and Ependion is well-positioned in the medium-to long-term. Beijer Electronics's strategic review was such a confirmation.

Up sequentially, but uncertainty looms large in the near-term

Ependion's Q1 2024 was in line with our estimates. Sales and EBIT amounted to SEK598.5m and SEK74.5m, translating into a negative growth rate of 4% y/y and a margin of 12.4%. Redeye's estimates were SEK596m and SEK72m (12.1% margin), and thus the sales barely differed, and the EBIT was 3% stronger (i.e., negligible). Sales and margins did strengthen sequentially, up from SEK589.7m and SEK61.5m, which was positive. However, there is some near-term uncertainty, based on the macroeconomic environment. This has led to a cost-savings program at Beijer Electronics and an ongoing reduction in costs adjusted for volumes on the Westermo side as well.

Solid new strategy from Beijer Electronics

Beijer Electronics showed its new strategy which can be boiled down to creating profitable growth through focus. Beijer Electronics has tried to be "a little bit to everyone" and will henceforth instead focus on three main segments (similar to Westermo's WeGrow), which are: 1) marine, 2) manufacturing, and 3) rugged environment, where it adds the most value. It is also exiting low-margin areas like Display Solutions. We argue that the strategy appears to be sound, and in this update, we go through all the main takeaways, which we thought were really interesting, as they are based on market research, in-depth interviews with more than 30 customers and internal employees with good business knowledge.

Small changes to our estimates

Prior to the Capital Markets Day, we had already incorporated improvements in our Beijer Electronics estimates, and thus, the actual presentation was more of a confirmation. Our long-term view of Ependion (and both business entities) is positive. With that being said, we are a bit unsure about the near-term, and the uncertainty is high. In order to be slightly more conservative, not least in the next couple of quarters, we lower our estimates one notch for the bear and base cases, while keeping the bull case intact. Our new fair value range is SEK63-190 (previously SEK65-180), with the new base case being SEK125 (SEK130). We hope to be able to readjust upward going forward once some near-term clouds disappear.

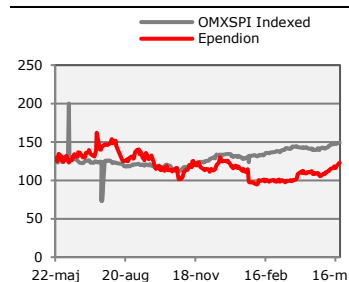
Ependion - near-term forecasts											Share price: 135		
(SEKm)	2020	2021	2022	2023	Q1'24a	Q2'24e	Q3'24e	Q4'24e	2024e	2025e	2026e		
Net sales	1438	1619	2128	2471	599	549	586	610	2343	2593	2868		
Growth (%)	-7,8%	13%	31%	16,1%	-3,9%	-14,1%	-5,4%	3,4%	-5,2%	10,7%	10,6%		
EBITDA	164	218	355	474	117	104	115	120	455	540	611		
EBITDA margin (%)	11%	13%	17%	19,2%	19,6%	18,9%	19,6%	19,6%	19,4%	20,8%	21,3%		
EBIT	16	68	201	322	75	65	73	76	289	363	416		
EBIT margin (%)	1,1%	4,2%	9,4%	13,0%	12,5%	11,8%	12,5%	12,5%	12,3%	14,0%	14,5%		
EV/Sales				1,9					1,9	1,7	1,4		
EV/EBITDA				9,8					10,0	8,0	6,6		
EV/EBIT				14,5					15,7	11,9	9,8		

Source: Ependion, Redeye Research

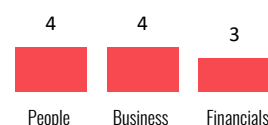
FAIR VALUE RANGE

BEAR	BASE	BULL
63	125	190

VERSUS OMXS30



REDEYE RATING



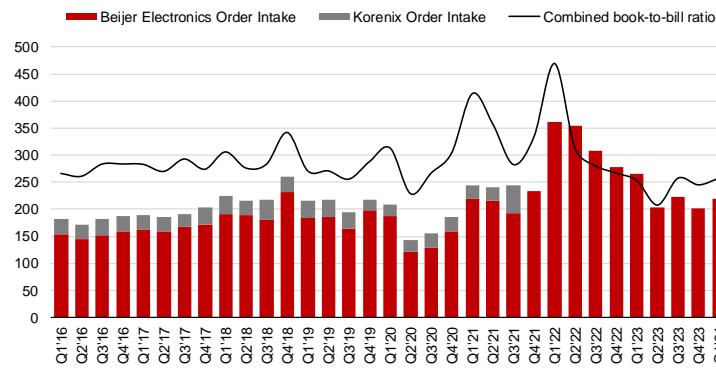
KEY STATS

Ticker	EPEN
Market	Mid Cap
Share Price (SEK)	135
Market Cap (SEKm)	3950
Net Debt (SEKm)	732
Free Float	54%
Avg. daily volume ('000)	16

ANALYSTS

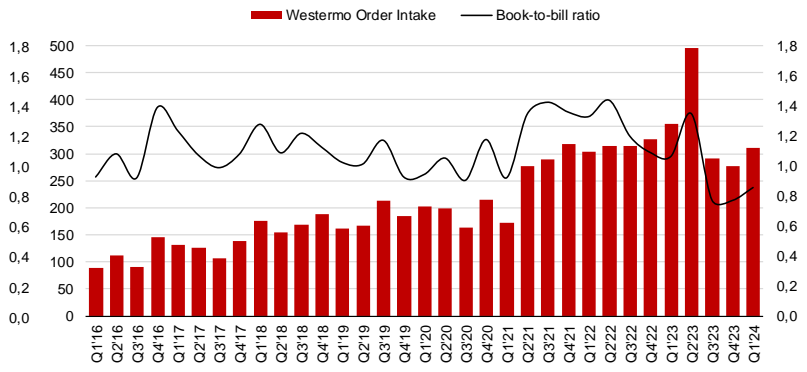
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New operating segment - Beijer Electronics and Korenix, quarterly development since 2016 (SEKm)



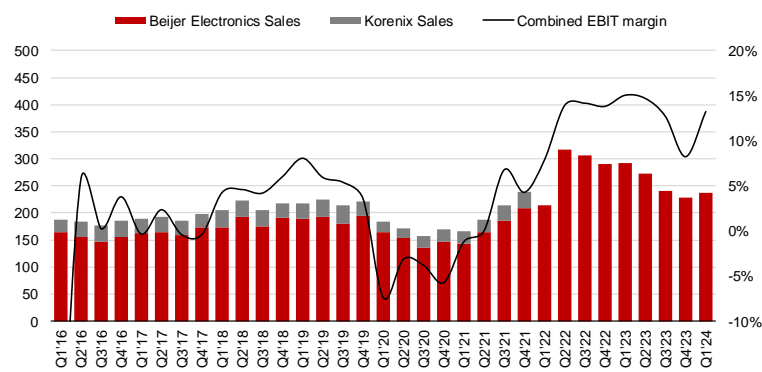
Source: Ependion, Redeye Research

Westermo's order intake (SEKm) and book-to-bill ratio, quarterly development since 2016



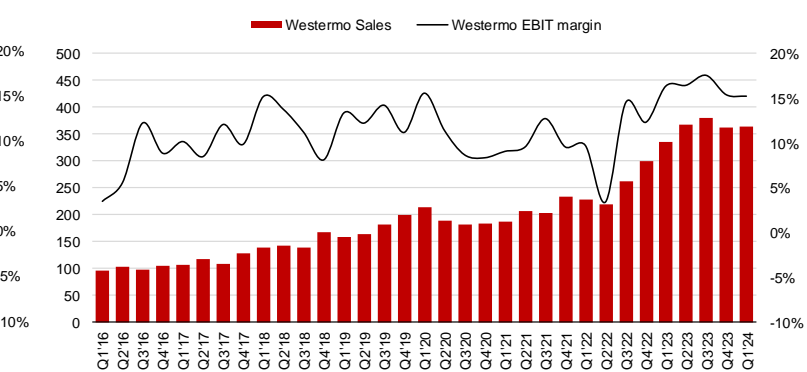
Source: Ependion, Redeye Research

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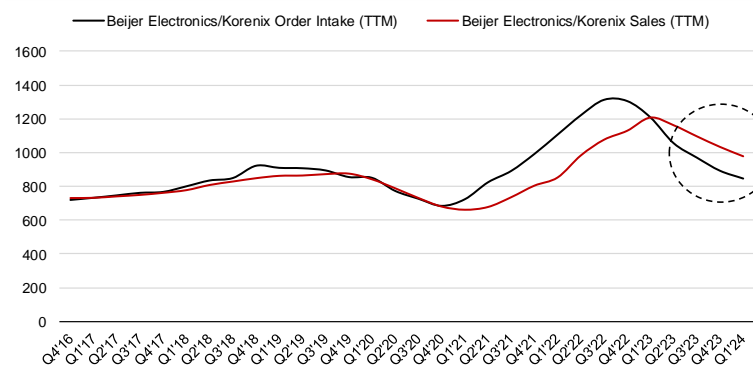
Source: Ependion, Redeye Research

Westermo's sales (SEKm) and EBIT margin (%), quarterly development since 2016



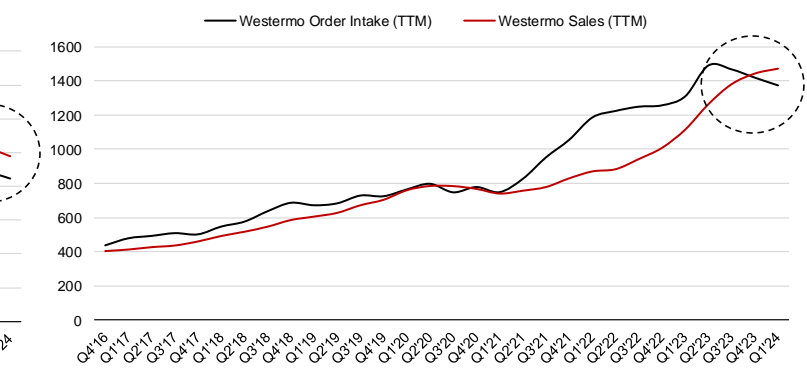
Source: Ependion, Redeye Research

Order intake and sales rolling-twelve (SEKm)



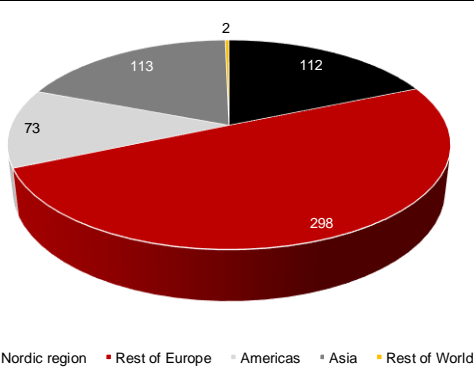
Source: Ependion, Redeye Research

Order intake and sales rolling-twelve (SEKm)



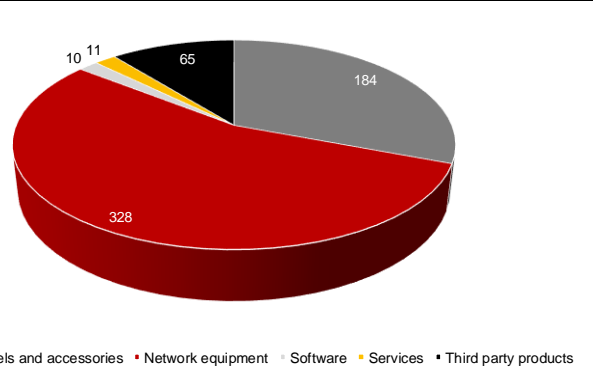
Source: Ependion, Redeye Research

Ependion's geographical sales distribution in Q1 2024



Source: Ependion, Redeye Research

Ependion's category sales distribution in Q1 2024



Source: Ependion, Redeye Research

Q1 2024 Recap

SEKm	Westermo			Beijer Electronics			Ependion		
	Q1'24	Q1'23	change	Q1'24	Q1'23	change	Q1'24	Q1'23	change
Order intal	310	356	-13%	219	265	-17%	528	617	-15%
Sales	364	335	9%	236	291	-19%	599	623	-4%
EBIT	55	55	1%	31	44	-29%	75	85	-13%
EBIT-març	15,2%	16,4%		13,3%	15,1%		12,4%	13,7%	

Sources: Ependion

SEKm	Q1e 2024	Q1a 2024	diff
Net sales	596	599	0%
Growth (%)	-4,4%	-4,0%	
EBIT	72	75	3%
Margin (%)	12,1%	12,4%	

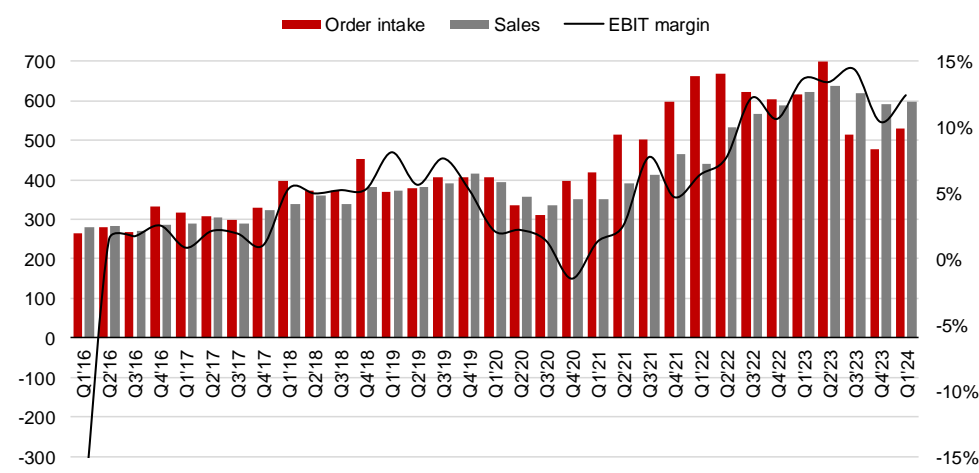
Sources: Redeye Research, Ependion

Order intake, sales and margins on a group level

Ependion's Q1 2024 was in line with our estimates. Sales and EBIT amounted to SEK598.5m and SEK74.5m, translating into a negative growth rate of 4% y/y and a margin of 12.4%. Redeye's estimates were SEK596m and SEK72m (12.1% margin), and thus the sales barely differed, and the EBIT was 3% stronger (i.e., negligible). Sales and margins did strengthen sequentially, up from SEK589.7m and SEK61.5m, which was positive.

Rest of Europe was the only region growing y/y, with 18%. This is, on the other hand, by far the largest region in term of sales, representing about 50% of the group's total. The Nordics, Americas, Asia, and Rest of World declined by 12%, 18%, 25% and 26%, respectively.

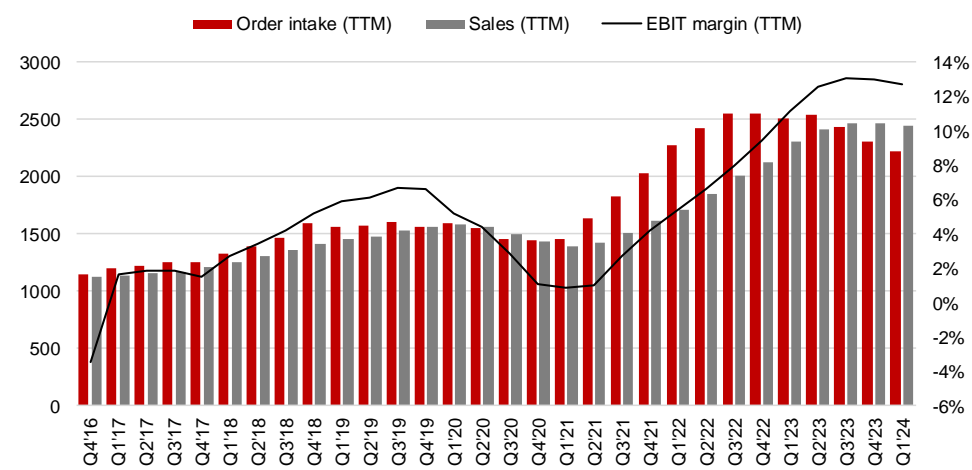
Ependion's order intake (SEKm), sales (SEKm) and EBIT margin (%)



Source: Ependion, Redeye Research



Ependion's trailing twelve-month order intake (SEKm), sales (SEKm) and EBIT margin (%)



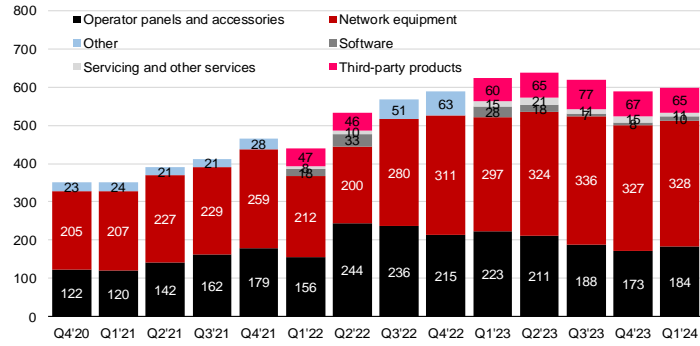
Source: Ependion, Redeye Research

The order intake amounted to SEK528m, down by 15% y/y, but up by approximately 10% q/q, where it was SEK478m. After two quarters with lower order intakes, it was good to see a slight trend shift/stabilisation. One should, however, keep in mind that H1 2023 was boosted by a Westermo customer extending its order horizon. CEO Sjö Dahl wrote about that in the report: "the record-breaking first half of 2023 is disturbing the comparison because Westermo's, and also the Group's, largest customer then extended their order horizon, which led to a very high order booking that did not reflect the underlying demand." Mrs Sjö Dahl also said on the conf call that: "the general market situation is still uncertain. It is hard for us to predict what is going to happen in the second half of the year. So, we actually refraining from doing that. But we keep close attention on the development and are, of course, prepared to act further if need to be."

Q3 2023 broke 11 quarters in a row-trend with a book-to-bill ratio at or above 1x. While Q3 and Q4 2023 saw book-to-bill ratios of 0.81-0.83x, Q1 2024 had a somewhat higher ratio of 0.88x, but still below 1x. Although we want to see this level go up again and exceed 1x (implying growth), it is also important that the sales conversion has improved in the last couple of quarters and that especially Westermo now is able to ship to its customers, as the component situation has eased. During the component crisis, the book-to-bill ratio was too high, and some orders took a long time to ship. Now both business entities have had a few quarters where they have been able to trim and ship their big order backlogs (not least Westermo).

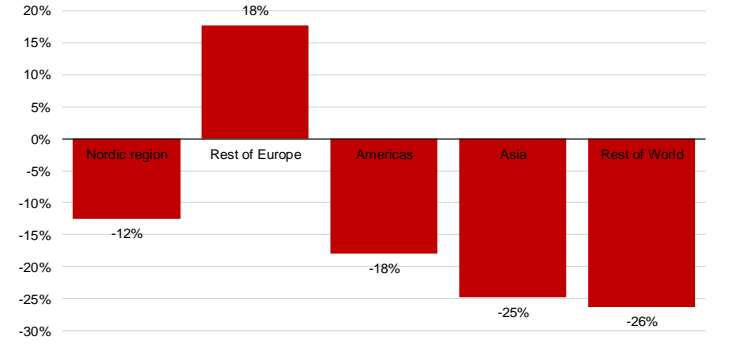
With a book-to-bill ratio of less than 1 and management's somewhat cautious near-term outlook, we believe there could be one or a few so-so quarters ahead. The uncertainty remains high due to the macroeconomic environment. This impacts the confidence we have in our near-term estimates.

Product and service category sales



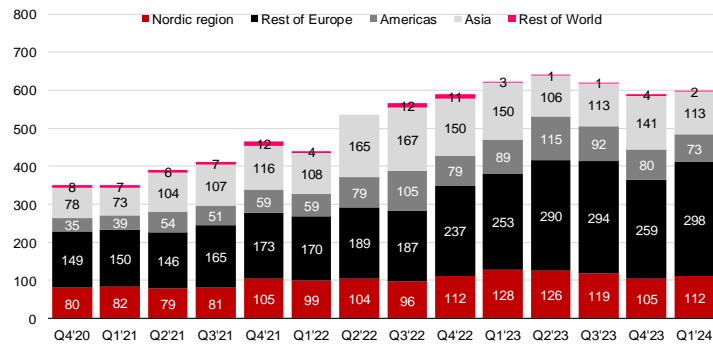
Source: Ependion, Redeye Research

Geographical growth rates in Q1 2024



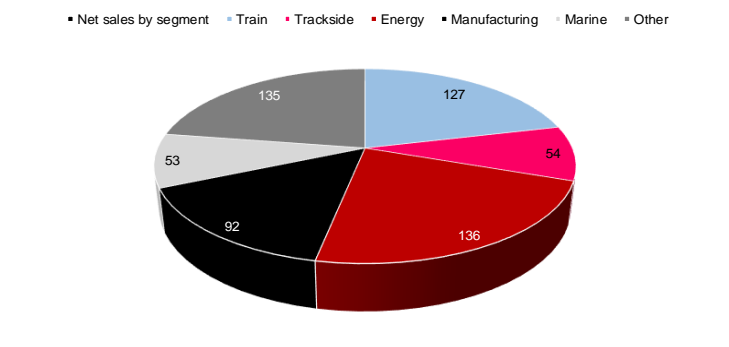
Source: Ependion, Redeye Research

Geographical sales distribution



Source: Ependion, Redeye Research

Net sales by segment

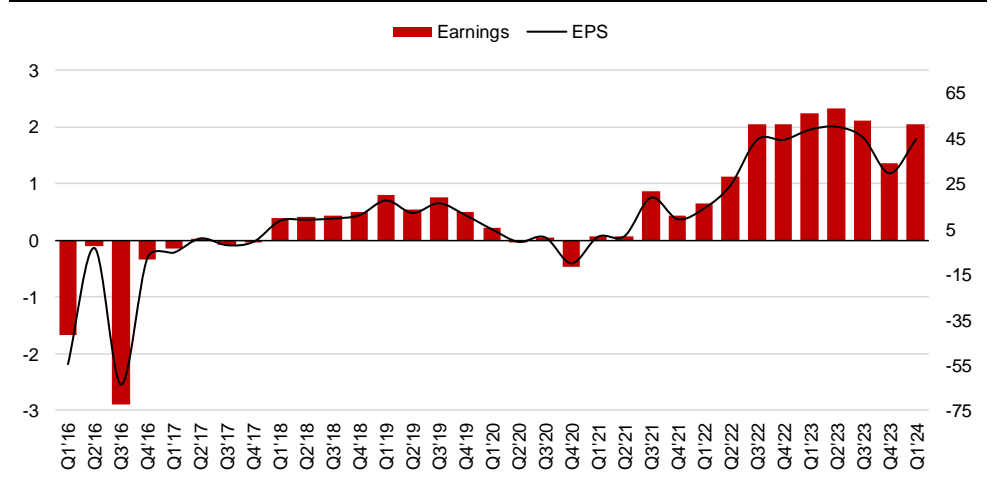


Source: Ependion, Redeye Research

Ependion's EBIT amounted to SEK74.5m (12.4% margin), down compared to Q1 2023 (SEK85.2m or 13.7% margin), but up from SEK61.5m in Q4 2023 (10.4% margin). The margin was impacted by a "temporarily poorer product mix in deliveries" but gained from good cost control, not least on Beijer Electronics' side. Mrs Sjö Dahl writes: "The cost reduction program that was initiated in the third quarter of 2023 with the main focus on Asia has now given the desired effect, which contributes to strengthened margins compared to the previous quarter."

Ependion continues to invest in R&D and product development, and the post was 12.6% of sales in the period. We like that fact that Ependion has a long-term view and does not "put lipstick on a pig" and tries to optimise short-term results at the expense of its long-term competitiveness. The improved operating result q/q led the EPS to strengthen sequentially as well, to SEK1.78 per share. A year ago, however, it was SEK1.95 per share.

Ependion's earnings (SEKm) and Earnings per share (SEK)



Source: Ependion, Redeye Research



Westermo

If one takes a more granular look at the two business segments, starting with the biggest, Westermo, one can see that there is somewhat of a mixed picture. The order intake was SEK310.3m, a decrease of 13% y/y (down from SEK355.7m in Q1 2023), but stronger compared to Q4 2023, where it was SEK277.4m. The extended order horizon from Westermo’s largest customer in H1 2023 which boosted the numbers, will impact the comparison numbers for H1 2024 negatively. However, management pointed out that “the train network segment, adjusted for these effects, shows stable underlying demand.” Nonetheless, there seems to be a more cautious market overall, despite a rather high customer activity and good pipeline of business opportunities (not least in the medium to long-term). Mrs Sjö Dahl said on the conf call that: “we also do see a little bit of a softer market situation right now.”

Sales increased by 9% y/y and amounted to SEK363.8m. This was also better than Q4 2023, where it was SEK361.9m, i.e., a good quarter. The strong order backlog supported the growth in Q1 2024, but an unfavourable product mix led to somewhat lower profitability. EBIT came in at SEK55.4m (15.2% margin), compared to SEK54.8m in Q1 2023 (16.4% margin) and SEK55.7m (15.4% margin) in Q4 2023.

In the report, Ependion states that: “to offset the temporarily weaker demand, the business entity is working to reduce ongoing costs and adjust them to volumes, a process that was initiated during the period and continues in the second quarter.” On the conf call, Mrs Sjö Dahl also said that: “due to the somewhat lower order intake pace in Westermo in the last 3 quarters, we do see a weaker backlog now for the second quarter of this year. And of course, we are doing everything to fill up that backlog.” These statements and actions are not exuding confidence in the near-term. During Q1, Westermo continued to ship parts of the delayed order book, stemming from the component crisis, which now is basically over. The order backlog was SEK906.4m at the end of Q1 2024, down from SEK935.8m in Q4 2023 (-3% q/q). Thus, it has some backlog left to ship (most is earmarked for 2024) but the order intake must pick up soon, otherwise we might see a dip in sales for a few quarters. Nonetheless, in the medium to long-term, we argue that Westermo is well-positioned to grow strongly as its target markets grow by 5-10% a year. Today, it is a market leader in the train segment with a 20% market share, a successful player in the trackside with c5% market share, and a challenger in the energy segment <5% market share (but steadily gaining).

	Verticals			Technology	
	Train Market leader	Trackside	Energy	Ethernet	Wireless 3 acquisitions made to fill gaps
Share of sales 2023	35%	13%	15%	60%	25%
Market size and CAGR	~250 MUSD CAGR 5-10%	~350 MUSD CAGR ~10%	~900 MUSD CAGR ~10%	~2,500 MUSD CAGR 10%	~1,500 MUSD CAGR 14%
Westermo market share	20%	~5%	<5%	5%	<5%
Market drivers	Urbanization Passenger experience Climate challenge Cyber security	Cyber security Ageing Infrastructure Safety Digitalization	Decarbonization Digitalization Electrification Cyber security	Digitalization Technology transition legacy to ethernet Cyber security	Digitalization Electrification Deployment cost Cyber security
Customer structure	Limited number of large rolling stock manufacturers (OEM's)	Large number of customers: national & local transport authorities, OEM's, System Integrators	Large number of customers: National, regional or local grid owners/operators, System Integrators		



In the Q4 2023 report, Ependion mentioned that Westermo is strategically expanding its global presence by establishing a legal entity in Bangalore/Bengaluru, India, focusing on sales and production. This move aligns with India's significant plans for major investments in railway infrastructure over the next decade. Today, it already boasts the 4th largest railway system in the world. The decision to have a local presence is driven by the need to actively participate in the anticipated growth, particularly as a partner to leading train builders. There are also great business opportunities in the growing energy market in India. Worth pointing out is that India *prefers/demands* locally manufactured products.

We do not think it is a coincidence that Alstom, one of Westermo's largest and most long-standing customers/partners highlighted on its investor deck on January 24 the Indian ramp-up. Moreover, when we checked Alstom India's website, we saw that the country headquarter is situated in Bangalore/Bengaluru, as well. Alstom has 9,000 employees and 6 manufacturing sites spread across the country according to its website. Furthermore, it seems like Alstom is also partly exporting, to Australia, for example, from its Indian operations. However, when we asked management about India being a hub for Asia-Pacific as a whole, the response was rather that this investment would serve the Indian market. The establishment in Bangalore requires an initial investment of around SEK10m and involves the recruitment of approximately 10 employees for sales, support, and local assembly of products related to trains and railways. We believe this is just the first stepping-stone, and that India will likely become a significant market for Westermo (and Beijer Electronics) over the next decade. As a reference, China, a market with a similar population size, accounted for 11% of Ependion's sales in 2022 (a strong year).



Additionally, Westermo has also decided to open a unit in Denmark to tap into the growing energy segment. Given the fact that Denmark has a lot of renewable energy in its energy mix, being a pioneer in wind farms, it seems like a good idea having resources locally and available for the grid upgrade. It also shows that there are small growth pockets close to the home markets, too.

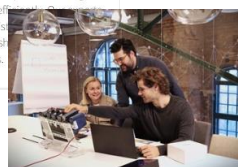
In Q1 2024, Westermo continued to strengthen its product portfolio with new or updated products. In the wireless network segment, products targeting train customers, the Ibox and CyBox families, were upgraded to support the new WiFi6 standard, providing faster and more secure connectivity. In the Viper product family (ethernet onboard trains), a new powerline bridge was launched, which enables fast and secure network connections between train set.

We also note that Westermo has launched a range of pre-packaged service agreements in early 2024 that "will help manufacturers, utilities, transportation and other industries to maintain, secure and improve data communications networks over their lifecycle." Westermo states that: "The service agreements, which can cover a specific installation, facility or geographic region, include comprehensive technical support, with prioritised fast response units available to diagnose issues and help minimise network downtime. To combat cyber threats, Westermo will identify network vulnerabilities and provide correctional actions. Continuous cybersecurity advisories are provided and a security incident response team is available to give immediate support, if required. Online and in-person certified training courses are designed to increase the efficiency of commissioning, maintenance and troubleshooting, and ultimately to enhance network performance and reliability." We will monitor whether these pre-packaged service agreements will gain traction over time and support both stronger growth, but not least improved margins over time. It is an exciting step in a direction that management has talked about previously, an increased focus on service and software revenues. In Q1 2024, services and software only accounted for SEK11.2m (1.9% of total sales) and SEK10.1m (1.7% of total sales), respectively. Thus, there is a big untapped potential here if the customers are willing to pay.



Technical support offerings

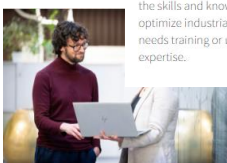
Maximizing uptime requires resolving issues quickly and efficiently. Our technical support offerings are available to assist you with your hardware problems.



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Beijer Electronics

Beijer Electronics' order intake decreased to SEK218.9m, down from SEK264.8m a year ago. However, and in line with much else in this report, it was importantly up q/q. And for Beijer Electronics, especially, this was a relief sign. Now, the business entity has 4 quarters in a row where it has been flattish, after a very strong period in 2022/2021, boosted in part by demand in China. Beijer Electronics has also had a couple of quarters where customers' order horizon patterns have normalised. During 2021-2022, when there were general component shortages in the industry, many customers opted for an order horizon of up to 12 months, which has now returned the more normal 2-3 months, thereby negatively affecting the order intake for a couple of quarters. This should now more or less be over, and the comps are starting to get easier to match. On the other hand, there are some signs of a deteriorating general industrial economy which will impact depending how deep it becomes. Thus, given the flattish order intake in the past 12 months, we do not see any severe stress symptoms as of now. One should also be mindful that there has been a price component in the latest order intake, which means that product volumes are likely slightly weaker.

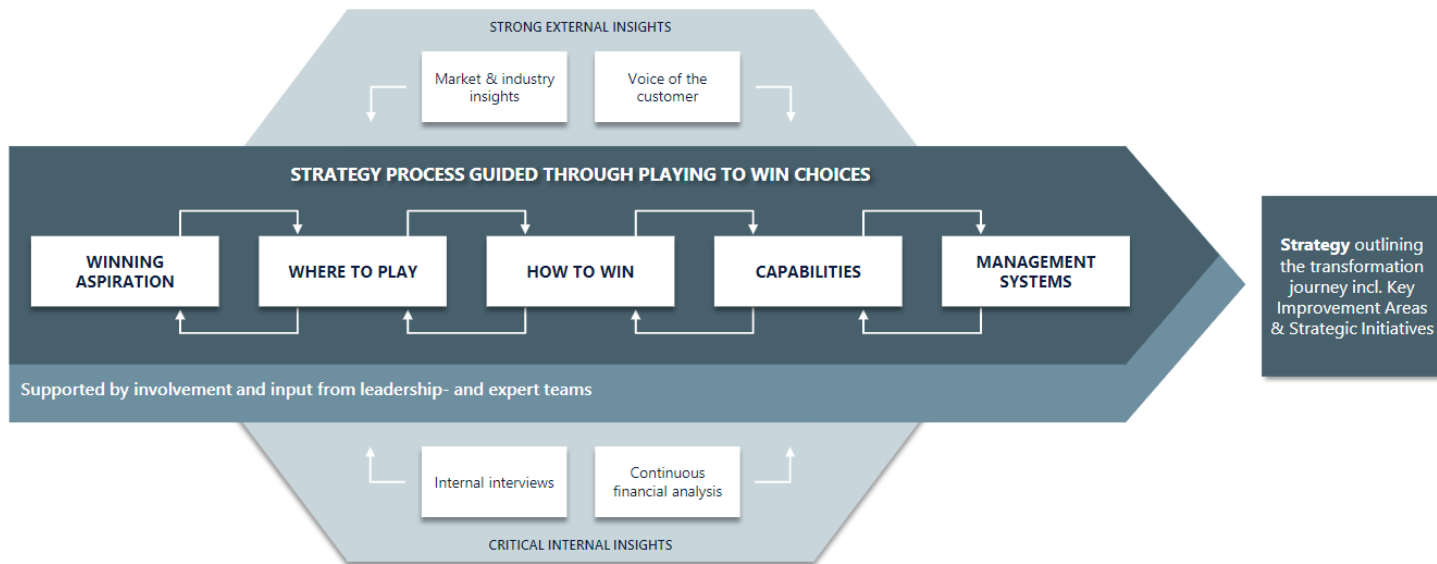
As in previous quarters, the demand was weak in Asia, while Europe was a bit stronger (showing growth) and North America remained stable. On the Q4 2023 conf call, we asked about the geographical split for Beijer Electronics and about the health of the different markets. Mrs Sjö Dahl said that: "The customer structure is a little bit different. In Europe, we have a very broad customer base. Lots of customers, some are up, and some are down, and that kind of helps with the stability, whereas in the U.S., we are more dependent on a few customers. And there, we also see a little bit of seasonality in the demand when it comes to North America." CFO Joakim Laurén added: "It is relatively stable in the U.S. also. We don't expect it to go more down. That is not what we want to convey. So, it is both on the EMEA and the U.S. side, it's quite stable. And Asia, it's still on a low we'll see when we see things picking up in Asia. That's very hard to say when."

Beijer Electronics order backlog stood at SEK302m, down from SEK311.5m (-3% q/q). In the strategic review, presented on March 5, Beijer Electronics also announced that it will discontinue the low-margin business Display Solutions. In the report, Ependion states: "The decision affected the order intake from the fourth quarter of 2023 onwards." In 2023, the segment accounted for SEK50m in sales (i.e., about 5%) and in 2024, there is expected to be orders filled of about SEK30m. Thus, the segment is minor and even smaller on the EBIT side, given the low-margin nature. Most of the Display Solutions sales were in Asia.

Sales amounted to SEK236.4m, down by 19% y/y, from SEK291.4m in Q1 2023, but up compared to Q4 2023, where it was SEK228.3m. Beijer Electronics' EBIT was SEK31.4m (13.3% margin), which was considerably stronger than Q4 2023's margin of 8.3% (or SEK18.9m). In Q3 2023, Beijer Electronics initiated a cost reduction package focusing mainly on Asia, which has led to a cost reduction of SEK20m on an annual level, with full effect from 2024.

Sharpened strategy for Beijer Electronics to achieve stable profitable growth

In Q3 2023, Beijer Electronics' new CEO, Kristine Lindberg, and her team, began a task to review, clarify, and sharpen the business entity's long-term growth strategy. The review and key takeaways were presented in March 2024.



Source: Ependion

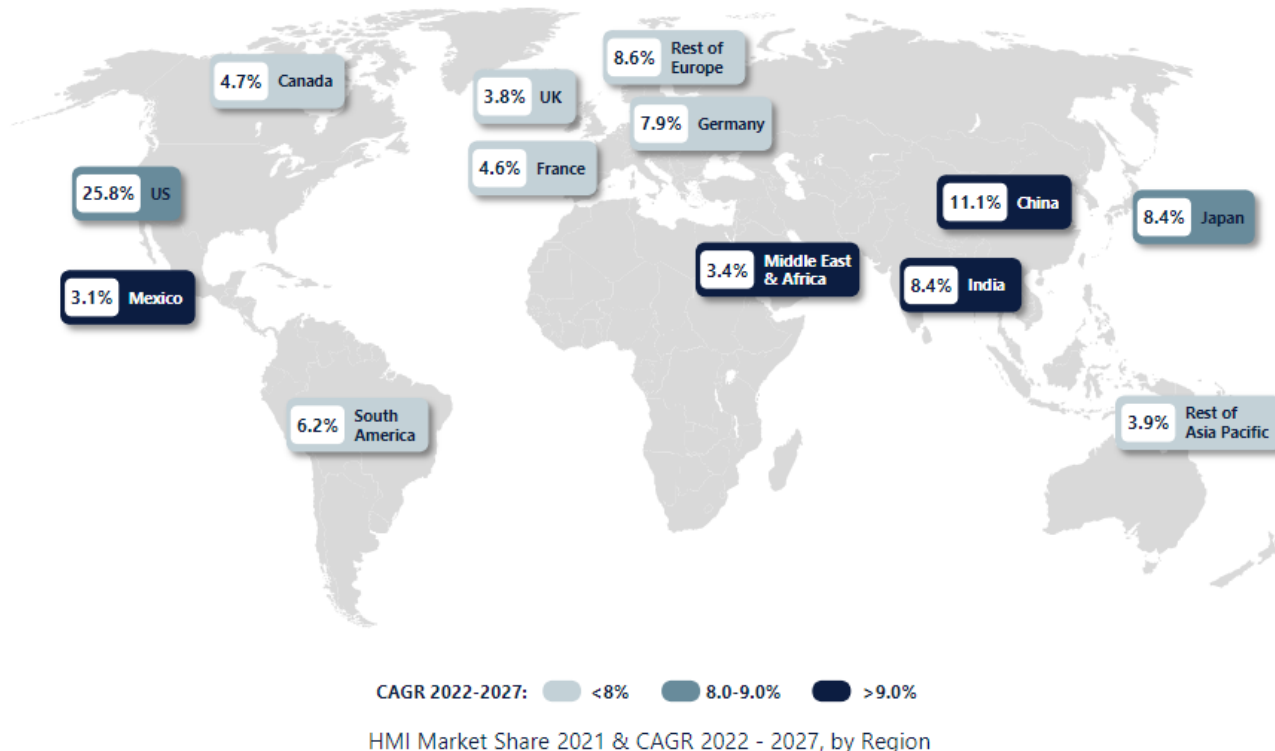
Trends and markets

Beijer Electronics' new strategy has been thoroughly conducted with the aim to find where the business entity ought to focus its resources, based on extensive analysis of the markets, global trends, and interviews with customers. Beijer Electronics has conducted in-depth interviews with more than 30 customers around three areas: 1) its own strengths and weaknesses, 2) what the customers require from Beijer Electronics in the future and what they expect in terms of adaption, and 3) the customers were presented with 15 buying criteria and were asked to rank them in importance (and rank Beijer Electronics' achievement on each one). The outside-in perspective was also complemented by involving 50 internal employees in the review, giving the process a sound internal anchor and know-how, too.



Source: Ependion

There are two primary trends that are shaping the markets Beijer Electronics operates in. First, there is a big digitalisation trend. Although Industry 4.0 has been around for quite some time already, there has been an additional push towards mobility. Previously, much focus has been on the HMI at the machine (panel focus), while now the focus is more on the availability of data wherever it is needed, meaning that it is becoming more people centric. Moreover, it is not the sheer mass of data that is the most critical aspect, but the right data, easily visualised, to support decisions. The second major trend is sustainability, and customers ask Beijer Electronics how they can become more effective with their solutions. This overlaps with questions regarding durability, lifetime costs, waste reduction, and so on.



Source: Ependion, Industry Journals, Interviews with Experts, Company Websites, White Papers, and MarketsandMarkets Analysis

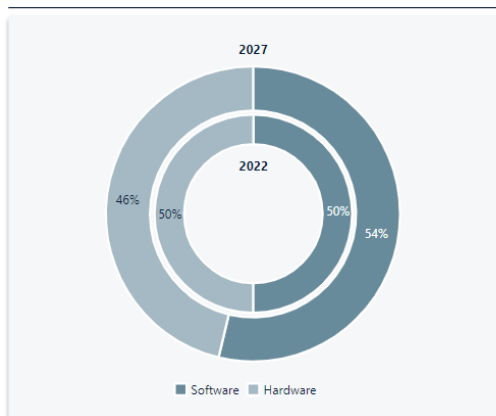
On the CMD, Beijer Electronics showed market data which was very interesting. In 2022, the global HMI market was estimated to be valued at USD5bn and had an expected CAGR of 7.9% between 2022-2027 (i.e., the next five years). The presented chart also shows that China, India, Middle East, and Mexico are the fastest growing markets, while the US is the largest with close to 26% of the world’s HMIs. However, Europe also boasts a sizeable market, although the growth rate is a bit lower compared to certain other markets, not least China and India’s. Beijer Electronics is already well-positioned geographically.

Another interesting data point was that software was growing considerably faster than hardware, 9.6% compared to 6.4%. Thus, software is expected to outgrow hardware at accelerated speed and to reach a market size of about USD4bn by 2027 (up by 60% compared to the 2022 level). Moreover, although hardware is still growing, it is increasingly becoming a commodity. Instead, software will serve as the key point of differentiation and drive sales, according to Beijer Electronics. This notion is reflected in Beijer Electronics’ R&D strategy, where the majority of its budget is allocated to software-related development. However, an interesting aspect, which came through via the customer interviews, was that

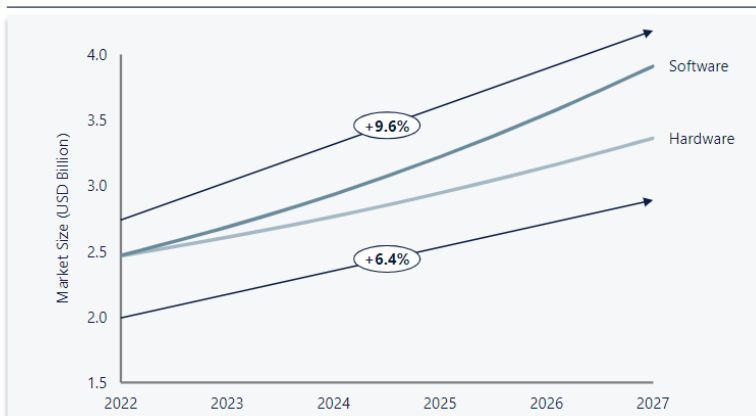
customers still want to by the combined solution (i.e., hardware and software) from the same vendor, as it is safer and usually adds value to have it seamlessly combined.

In addition, cloud-based HMIs are set to grow faster (13%) than on-premise HMIs (8%), and overtake on-prem in 2025. The cloud-transition is tied to the mobility notion, that data needs to be available close to the decision-making (or maker), rather than tied to a specific machine. Beijer Electronics' acquisition of WebIQ is in line with the cloud-trend and it has opened up new business opportunities according to management.

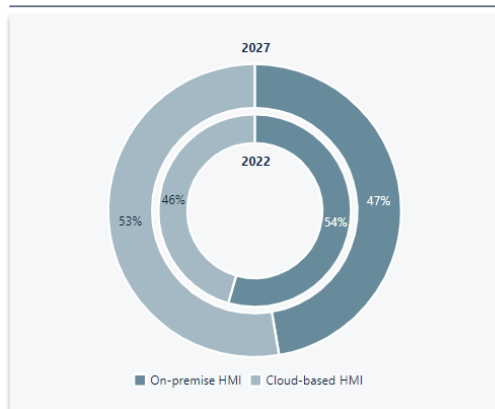
HMI Market 2022 vs. 2027, by Product¹



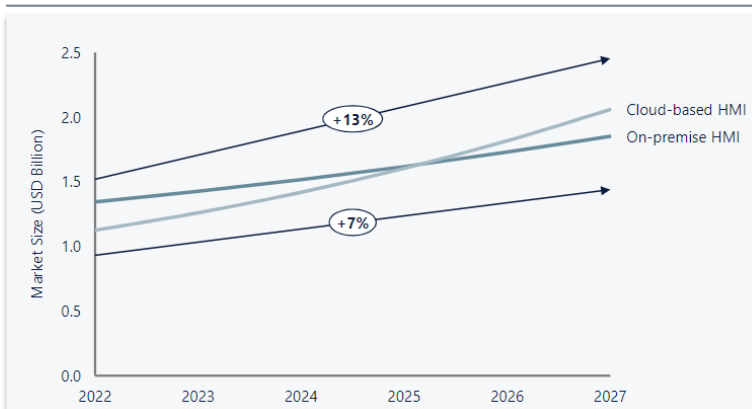
HMI Market 2022 – 2027, by Product²



HMI Software Market 2022 vs 2027, by Software



HMI Market 2022 – 2027, by Software



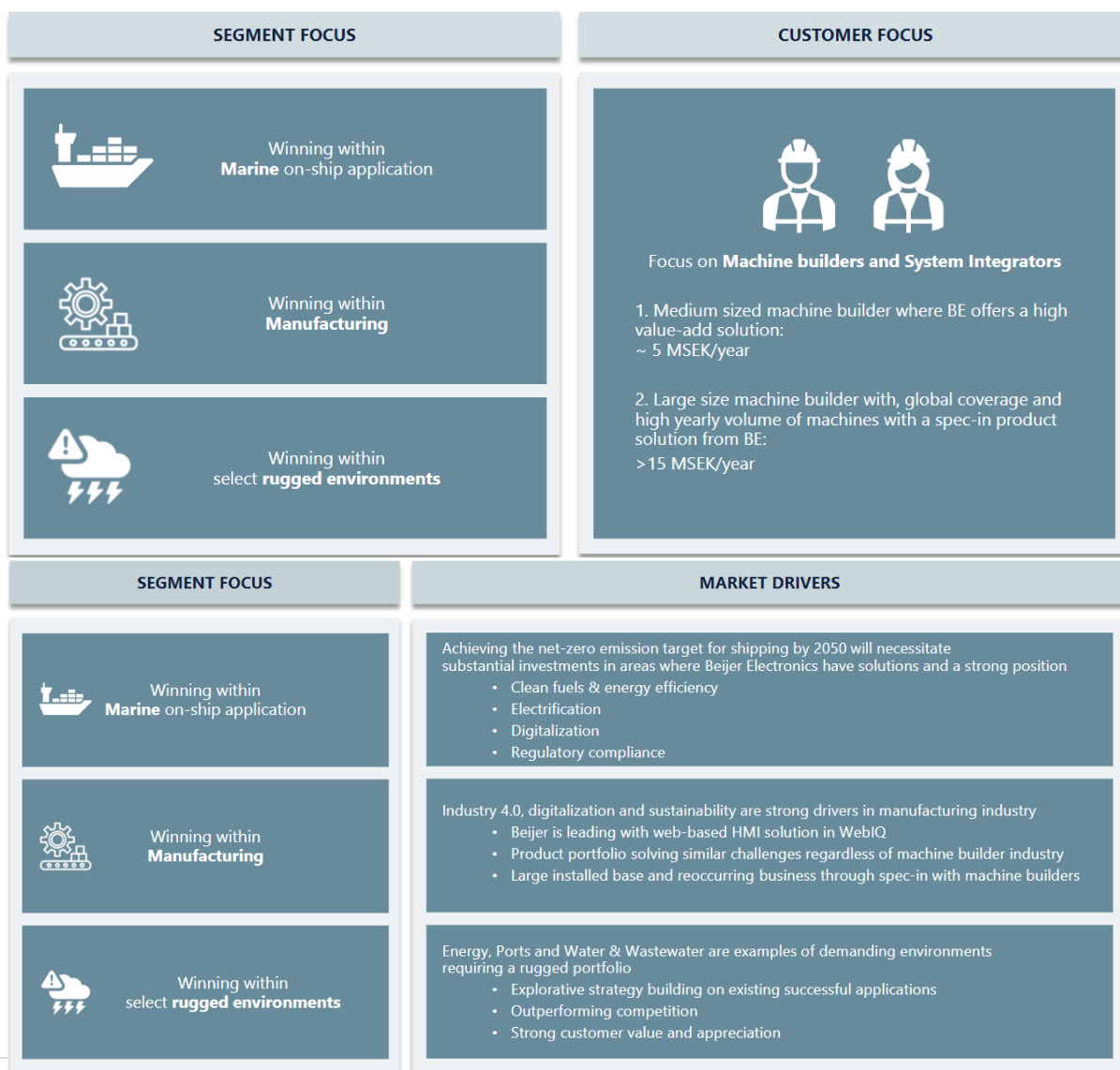
Source: Ependion, Press Releases, Expert Interviews, MarketsandMarkets Analysis, Automation World, Control Design, and Control Engineering

Customer feedback and focus segments

Beijer Electronics conducted more than 30 in-depth interviews with customers in conjunction with the strategic review, and these interviews painted a picture of what Beijer Electronics is doing well, and where it can improve. There are three differentiators that give Beijer Electronics an edge over competitors: 1) customer relationships and technical support, 2) product offering, and 3) specifications and certifications. The first one is about the relationship part, where Beijer Electronics seems to have very competent employees that support customers well in both pre-sales (finding the right solution) and post-sales along the lifetime of the product. The second reason has to do with Beijer Electronics' open and flexible portfolio, stemming from the company's place as a small player in the market. The third reason is tied to Beijer Electronics' various certifications and specifications, not least on the marine side and all-things rugged (outdoors). The products withstand harsh environments that are exposed to weather, different temperatures, vibrations, dust, etc. Beijer Electronics also noted that where customers appreciated it the most, was in areas where it can bring the most value, and thus earn better margins.

From the interviews, customers also stated requirements going forward, with the three top ones being: 1) cyber-security and certification, 2) software functionality and innovation, and 3) brand awareness. Cyber-security has become a hygiene factor, and all the right certifications are imperative to win deals in the industry. Software is becoming ever more important, and customers are requiring Beijer Electronics to be able to develop and deliver functionality over time, i.e., continuous improvements, as the customers' requirements change over time. The new X3 series, which will be launched by the end of 2024, is built in a containerised manner, meaning that Beijer Electronics can build and unlock new functionality over time, thus matching the customer requests well. This is also important from the cyber-security standpoint. The last requirement is tied to brand awareness. Beijer Electronics primarily sells to machine builders. When these builders sell solutions to end-customers, they often need to explain Beijer Electronics and how its solutions work, which is not necessary if they use Siemens, for example. Therefore, Beijer Electronics will focus on increasing its recognition among end-users in the target segments, helping its machine-building customers smoothen their sales processes.

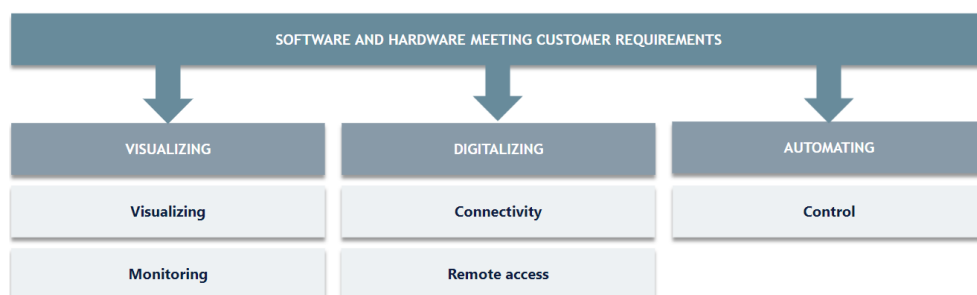
The key takeaways here are that Beijer Electronics has tried to be a little bit to everyone, and that it now has chosen a path of increased focus on target segments: 1) marine, 2) manufacturing, and 3) rugged environment, where it adds the most value. This also means that Beijer Electronics is set to exit areas where it struggles or are in tough price fights with no-to-little value-add. Thus, Beijer Electronics follows a similar path as Westermo's WeGrow.



In the marine segment, Beijer Electronics is well-known and has a strong brand. Machine builders here are either smaller niche companies focusing only on marine, or larger corporations, such as Alfa Laval, with a marine division. The second group is manufacturing, the area where Beijer Electronics has its larger installed base today. Although manufacturing is a wide area, Beijer Electronics sees a good opportunity not least among mid-sized machine builders that build complex machines (i.e., usually not in large quantities). Here it can add a substantial amount of value. It will also target system integrators, who often come into play with smaller customers, who do not have their own automation departments. Thus, Beijer Electronics partners up or sells through system integrators to gain a broader reach. The last target group is rugged environment, or outdoor applications, and span areas such as energy, ports, mining, waste-water treatment where installations are outdoors. Beijer Electronics' products are well-known and appreciated by customers in this area due to its durability.

All three target segments have different growth drives, but common themes include the green transition and increased digitalisation. For example, there are a lot of investments in the marine area to reach a net-zero emission target by 2025 (counter-acting the cyclicality), requiring solutions that Beijer Electronics supplies, tied to alternative fuels or propulsion (i.e., better efficiency/sustainability).

Geographically, Beijer Electronics is already well-positioned, and it can grow considerably more in already established markets, such as the US, which is the largest one for HMIs. Thus, Beijer Electronics is set to work through its current geographical presence, i.e., through its own offices and value-added distributions.



Source: Ependion

On the portfolio-side, we know that HMIs stand for roughly 65% of Beijer Electronics' invoiced sales and thus the visualising leg is the core part of the business (it also includes monitoring). The second leg, digitalising, is an area Beijer Electronics believes will grow quite a bit going forward, as connectivity (data communication) and remote access are being increasingly sought-after from customers. Remote access translates into both being able to view data, but also take action on the data, from a distance and is well-aligned with the increased mobility part of what customers were discussing. The last part, automation, is tied to PLC, i.e., control.

Innovative solutions positioning Beijer Electronics for profitable growth

Before we dive into WebIQ and X3, two key product families that will pave the way for profitable growth, we want to quickly reiterate where Beijer Electronics does not want to be. In conjunction with the CMD, Beijer Electronics announced that it is discontinuing its Display solutions segment, which are small display screens with low software functionality, and which are very price pressured, due to a large number of other players competing in the area. Beijer Electronics has tried to sell these and realised that it takes a lot of time and effort, to a low margin, and thus it will exit the field. In 2023, Display Solution accounted for about SEK50m in sales (c5% of the total), mainly in Asia, and in 2024, there is an expectation of

SEK30m in sales, although Beijer Electronics is not accepting new orders any longer. The impact is smaller on EBIT, due to the low-margin nature.



Source: Beijer Electronics

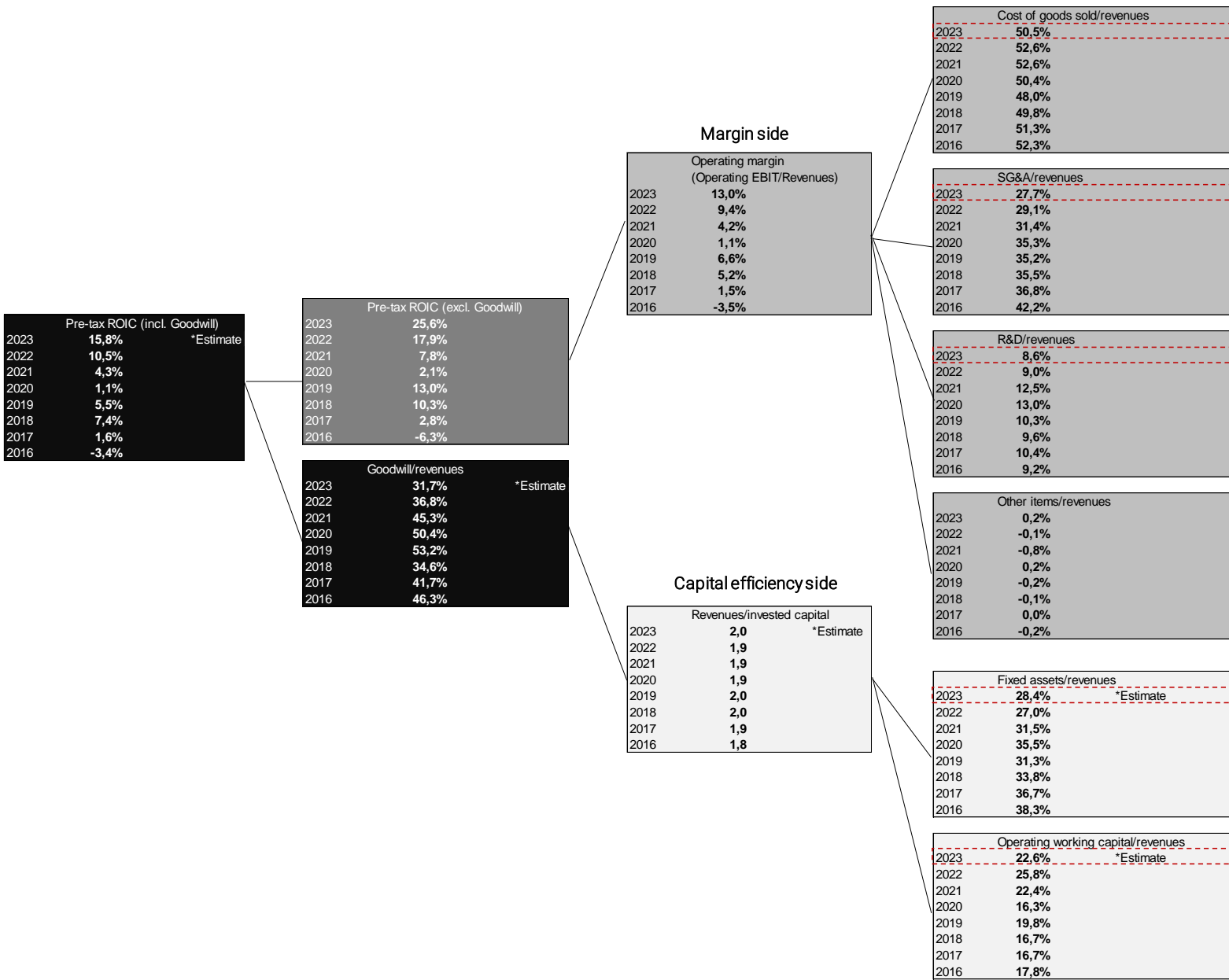
Instead, emphasis will be on WebIQ and X3, two products that are well-aligned with the abovementioned trends and customer requirements. WebIQ, which was acquired in April 2023, is described as a “web-based HMI solution, platform independent and fully responsive.” Thus, it works on any device (on a phone, an iPad), requires no programming skills, only configuration (thereby reducing a lot of time for the customers), and it is built as a drag-and-drop, with widgets, thus making it easy to design. It has several applications that can run simultaneously, targeting different roles and thus the right data and insights can be available for a plant manager and an operator at the same time. A customer might have a 40-year-old factory with 25 machines and needs to connect the OT to the IT to integrate data into an ERP system, enabling further analysis, documentation, control, and optimisation. The flexible WebIQ enables that.



Source: Ependion

Then we have X3, the successor to the successful X2 series, and which will be launched at the end of 2024. It is a new, improved, and open HMI platform with a cyber-security focus. It has been developed to allow for regular releases and updates, such as those needed for cyber-security reasons. X3 has also been developed with an easy transition in mind for customers already using X2. The range is slightly narrower compared to X2, in line with the focused markets Beijer Electronics is seeking to win.

Ependion's pre-tax ROIC tree 2016-2023 (Redeye's estimates - be mindful that we assume some numbers, as the reporting does not include them)



Source: Ependion, Redeye Research



Estimates

We have repeatedly emphasised in the latest updates that the near-term uncertainty is quite high, and as a result, our forecasts in the short term are uncertain as well. We have revised our estimates downward a bit recently, in part because of the macroeconomic environment, but also due to a more cautious management. The order intake has to pick up pace soon for the near-term sales not to dip considerably. But, with that being said, we are fully confident in Ependion's long-term competitiveness and market position, and we believe that the company is set to grow well over time, not least thanks to the sharpened growth strategies both business entities are pursuing. But industrials' sales are rarely entirely smooth, and there will be some softer quarters sprinkled out, too.

Although the pick-up q/q was a relief sign, we feel that Q2 and possibly Q3 might be somewhat softer. Not only are the comps hard, but we felt that management was signalling that temporarily weaker demand, not least on the Westermo-side, might impact the next quarter(s). Ependion states: "To offset the temporarily weaker demand, the business entity is working to reduce ongoing costs and adjust them to volumes, a process that was initiated during the period and continues in the second quarter." Thus, we believe this to be more than a timing effect of a few orders, and that uncertainty is high, even for management. Although this is not a cost reduction program like Beijer Electronics' in Asia, to our understanding, it still signals that Westermo is not likely to fire on all cylinders in the next 6 months or so, otherwise there would not be a reduction in ongoing costs.

Thus, we lower our near-term sales a bit once again, and this time mainly at Westermo. Thus, we continue to see a negative growth in Q2 as well, in part because of the slower order intake, but also due to hard comps. This also impacts the profitability for 2024. On the other hand, we still see Ependion grow considerably (and closely in line with its financial target of 10%) in the medium to long-term, as we believe its sharpened growth strategy will bear fruit over time. We keep the margins somewhat stable in the near-term, even though we lower the sales, in part because of Ependion leaving lower-margin areas, and due to its seeking new revenue streams from increased service and software-related business.

We have not changed our view on the medium- to long-term prospects and see Ependion as a very well-managed and well-positioned company in interesting niches and growing markets. We believe it will reach its financial targets over time, both in terms of growth and margins.

Ependion: Estimate changes, '24e-'26e

(SEKm)	Old			New			Changes		
	2024e	2025e	2026e	2024e	2025e	2026e	2024e	2025e	2026e
Sales	2471	2688	2932	2343	2593	2868	-5%	-4%	-2%
EBIT	322	374	425	289	363	416	-10%	-3%	-2%

Source: Redeye Research

Ependion: Actuals & Estimates, '21-'26e

(SEKm)	2021	2022	2023	Q1'24a	Q2'24e	Q3'24e	Q4'24e	2024e	2025e	2026e
Sales (group adjusted)	1 619	2 128	2 471	599	549	586	610	2 343	2 593	2 868
<i>growth y/y</i>	3,9%	31%	16%	-3,9%	-14,1%	-5,4%	3,4%	-5,2%	10,7%	10,6%
Beijer Electronics	806	1128	1033	236	237	234	237	944	1039	1143
Westermo	831	1010	1444	364	312	353	373	1402	1557	1728
Total costs (excl. D&A)	1 401	1 774	1 774	524	484	513	533	2 149	2 030	2 219
EBITDA	218	355	474	117	104	115	120	455	540	611
(%)	13,5%	16,7%	19,2%	19,6%	18,9%	19,6%	19,6%	19,4%	20,8%	21,3%
D&A	150	154	154	38	37	39	38	157	188	196
EBIT	68	201	322	75	65	73	76	289	363	416
(%)	4,2%	9,4%	13,0%	12,5%	11,8%	12,5%	12,5%	12,3%	14,0%	14,5%

Source: Ependion, Redeye Research

Valuation

SaaS Company	EV/SALES			EV/EBIT			Sales growth			EBIT margin		
	24E	25E	26E	24E	25E	26E	24E	25E	26E	24E	25E	26E
CTT	9,5	7,0	5,8	28	21	18	34%	36%	20%	34%	33%	33%
Hexagon	5,5	5,0	4,6	19	17	15	8%	7%	7%	29%	29%	30%
Tomra	3,1	2,8	2,4	25	20	16	3%	11%	13%	12%	14%	15%
Troax	3,8	3,5	3,1	21	18	16	14%	9%	9%	18%	19%	20%
HMS	6,7	5,5	4,9	35	25	22	7%	21%	10%	19%	22%	22%
Belden	1,7	1,5	1,4	12	10	8	-8%	11%	5%	14%	16%	17%
Advantech	4,3	3,8	3,4	23	19	17	7%	11%	9%	19%	20%	20%
Spectris	2,2	2,0	1,9	12	11	9	-5%	5%	4%	18%	19%	20%
Siemens	2,2	2,0	1,9	16	14	12	3%	6%	6%	14%	15%	16%
Rockwell	3,7	3,5	3,3	20	17	16	0%	5%	5%	19%	20%	20%
Cisco	3,5	3,4	3,2	10	10	9	-7%	3%	3%	34%	34%	34%
Average	4,2	3,6	3,3	20	17	14	5%	11%	8%	21%	22%	22%
Median	3,7	3,5	3,2	20	17	16	3%	9%	7%	19%	20%	20%
Ependion	1,9	1,7	1,4	16	12	10	-5%	11%	11%	12%	14%	15%

Source: Redeye, Company reports, FactSet

Ependion is priced well below many of its peers, which many times are substantially larger in size. We also believe, although to a lesser extent than before, that Ependion has had a "historical discount" because of its turnaround years. The product portfolio's market reception in recent years, together with added volumes and improved margins, paint a more optimistic picture. We believe that Ependion, over time and with increased size, will move closer to its peers, not least if it can bring up its margins and keep them stable. We lower our bear and base cases one notch on the back of the uncertainties we see on the macroeconomic front in the near-term. Meanwhile, we keep the bull case intact.

Bear Case SEK63 (65)

- 6% sales CAGR 2024-2028
- 6% sales CAGR 2029-2037
- 10% EBIT margin on average 2024-2028
- 9% EBIT margin on average 2029-2037
- Terminal growth rate of 2%
- Terminal EBIT margin of ~8%

In our bear case, we assume slower overall growth and a lower profit profile, where competition takes a larger bite of the market cake. Ependion continues to have below average margins and profitability on invested capital (ROIC). It is still profitable. The WACC is about 9% throughout the full DCF, in part due to debt financing.

Base Case SEK125 (130)

- c8% sales CAGR 2024-2028
- 9% sales CAGR 2029-2037
- 14% EBIT margin on average 2024-2028
- 12.5% EBIT margin on average 2029-2037
- Terminal growth rate of 2%
- Terminal EBIT margin of ~10%

Ependion grows slightly less than the financial target. Meanwhile, it strengthens its margins and has an average of about 14%, which is also slightly more conservative compared to the >15% margin target. The EBIT margin peaks at around 15% and then goes down as competition increases in its segment (although slower than previously estimated). Ependion has, nonetheless, substantially higher 'lower levels' in this scenario compared to its history. The WACC is about 9% throughout the full DCF, in part due to debt financing.

Bull Case SEK190 (190)

- 10% sales CAGR 2024-2028 (impacted slightly by near-term growth)
- 6% sales CAGR 2029-2037
- 15% EBIT margin on average 2024-2028
- 15% EBIT margin on average 2029-2037
- Terminal growth rate of 2%
- Terminal EBIT margin of ~13%

Ependion reaches the growth target of a 10% annual growth and EBIT margins of around 15% in our bull case. Westermo's WeGrow strategy is successful, and it creates market-leading roles in trackside and power distribution. Beijer Electronics also improves its profitability with fewer product platform families and more cooperation. Ependion's profitability is in line with other well-managed industrial companies. The WACC is about 9% throughout the full DCF, in part due to debt financing.

	2021	2022	2023	2024E
INCOME STATEMENT				
Net sales	1619	2128	2471	2343
Cost of Revenues	795	1052	1248	1145
Gross Profit	823	1076	1223	1198
Operating Expenses	605	722	749	742
EBITDA	218	355	474	455
Depreciation & Amortization	150	154	152	167
EBIT	68	201	322	289
Net Financial Items	-19	-15	-46	-40
EBT	50	186	275	249
Income Tax Expenses	14	40	75	52
Non-Controlling Interest	4	5	5	4
Net Income	36	146	200	197
BALANCE SHEET				
Assets				
Current assets				
Cash & Equivalents	147	160	142	269
Inventories	257	437	487	454
Accounts Receivable	363	396	407	435
Other Current Assets	67	83	52	53
Total Current Assets	834	1076	1089	1211
Non-current assets				
Property, Plant & Equipment, Net	85	80	86	93
Goodwill	785	785	783	783
Intangible Assets	274	347	474	566
Right-of-Use Assets	96	82	99	68
Shares in Associates	0	0	0	0
Other Long-Term Assets	65	62	42	46
Total Non-Current Assets	1305	1357	1484	1556
Total Assets	2139	2433	2572	2767
Liabilities				
Current liabilities				
Short-Term Debt	247	310	168	180
Short-Term Lease Liabilities	48	38	39	41
Accounts Payable	166	166	195	169
Other Current Liabilities	247	221	228	225
Total Current Liabilities	708	734	630	615
Non-current liabilities				
Long-Term Debt	355	388	463	461
Long-Term Lease Liabilities	59	60	60	61
Other Long-Term Liabilities	282	257	256	255
Total Non-current Liabilities	697	704	779	777
Non-Controlling Interest	4	5	5	4
Shareholder's Equity	729	989	1159	1370
Total Liabilities & Equity	2139	2433	2572	2767
CASH FLOW				
NOPAT	49	158	234	228
Change in Working Capital	-226	-266	8	-23
Operating Cash Flow	85	201	212	338
Capital Expenditures				
Investment in Intangible Assets	-42	-109	-152	-162
Investing Cash Flow	-174	-125	-232	-185
Financing Cash Flow				
Free Cash Flow	114	-38	-111	-29
	22	76	38	153

Summary Redeye Rating

The rating consists of three valuation keys, each constituting an overall assessment of several factors that are rated on a scale of 0 to 1 point. The maximum score for a valuation key is 5 points.

Rating changes in the report

Rating changes in the report

People: 4

The People rating is based on quantitative scores in seven sub-categories: Passion, Execution, Capital Allocation, Communication, Compensation, Ownership, and Board. In our rating assessment, Ependion gains the highest points from its open communication, qualified and experienced board, and compensation. Relevant industry experience characterizes Ependion's management and board of directors. Management shows a good understanding for the targeted markets and has a clear long-term focus. Ependion has shown solid progress with current management, which we judge to have completed the company's turnaround.

Business: 4

The Business rating is based on quantitative scores in five sub-categories: Business Scalability, Market Structure, Value Proposition, Economic Moat, and Operational Risks. Ependion receives the highest scores in Value Proposition and Operational Risk. The company operates in large, fragmented growth markets, primarily related to the digitalization trend. Long customer relationships characterize its business, where products are designed into customers' systems -laying the ground for potentially durable competitive advantages (switching costs).

Financials: 3

The Financials rating is based on quantitative scores in five sub-categories: Earnings Power, Profit Margin, Growth Rate, Financial Health, and Earnings Quality. Although currently showing solid progress, Ependion's financial rating is burdened by a couple of years of negative results and free cash flow. As additional profitability improvements are expected, we see room for an increased rating going forward. The company has a solid capital structure, the business is diversified, and we see no risk of needing to raise external capital going forward. On the negative side, the business is cyclical, implying that there is a risk of negative growth in a period of economic downturn.

Redeye Rating and Background Definitions

Company Quality

Company Quality is based on a set of quality checks across three categories; PEOPLE, BUSINESS, FINANCE. These are the building blocks that enable a company to deliver sustained operational outperformance and attractive long-term earnings growth.

Each category is grouped into multiple sub-categories assessed by five checks. These are based on widely accepted and tested investment criteria and used by demonstrably successful investors and investment firms. Each sub-category may also include a complementary check that provides additional information to assist with investment decision-making.

If a check is successful, it is assigned a score of one point; the total successful checks are added to give a score for each sub-category. The overall score for a category is the average of all sub-category scores, based on a scale that ranges from 0 to 5 rounded up to the nearest whole number. The overall score for each category is then used to generate the size of the bar in the Company Quality graphic.

People

At the end of the day, people drive profits. Not numbers. Understanding the motivations of people behind a business is a significant part of understanding the long-term drive of the company. It all comes down to doing business with people you trust, or at least avoiding dealing with people of questionable character.

The People rating is based on quantitative scores in seven categories:

- Passion, Execution, Capital Allocation, Communication, Compensation, Ownership, and Board.

Business

If you don't understand the competitive environment and don't have a clear sense of how the business will engage customers, create value and consistently deliver that value at a profit, you won't succeed as an investor. Knowing the business model inside out will provide you some level of certainty and reduce the risk when you buy a stock.

The Business rating is based on quantitative scores grouped into five sub-categories:

- Business Scalability, Market Structure, Value Proposition, Economic Moat, and Operational Risks.

Financials

Investing is part art, part science. Financial ratios make up most of the science. Ratios are used to evaluate the financial soundness of a business. Also, these ratios are key factors that will impact a company's financial performance and valuation. However, you only need a few to determine whether a company is financially strong or weak.

The Financial rating is based on quantitative scores that are grouped into five separate categories:

- Earnings Power, Profit Margin, Growth Rate, Financial Health, and Earnings Quality.

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Disclaimer

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Redeye Rating (2024-05-29)

Rating	People	Business	Financials
5	32	15	4
3-4	149	133	44
0-2	5	38	138
total	186	186	186

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CONFLICT OF INTERESTS

Mark Siöstedt owns shares in the company: No

Redeye performs/have performed services for the Company and receives/have received compensation from the Company in connection with this.