

Hanza: Positive Outlook

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Redeye takes a positive stance towards Hanza following a solid Q2 report, with the strong margin in Main Markets being the highlight. The order intake remains strong in basically all markets, both industry- and geography-wise. We increase our Base Case and forecasts.



Fredrik Nilsson



Fredrik Reuterhäll

Excellent Margins in Main Markets

Sales grew by 13% y/y and matched our forecast. Main Markets had slightly higher sales than expected, while Other Markets had lower sales, partly due to component shortages. EBITA beat our forecast by 16%, following an exceptional margin of 11.1% in Main Markets. While we knew that the Swedish cluster can perform in line with this level, this strong segment-level figure implies a significant improvement in the German cluster. The order intake remains strong in basically all markets, and Hanza cites strong demand from customers within defence, mining, energy, and agriculture in particular.

Major Full-Service Deal

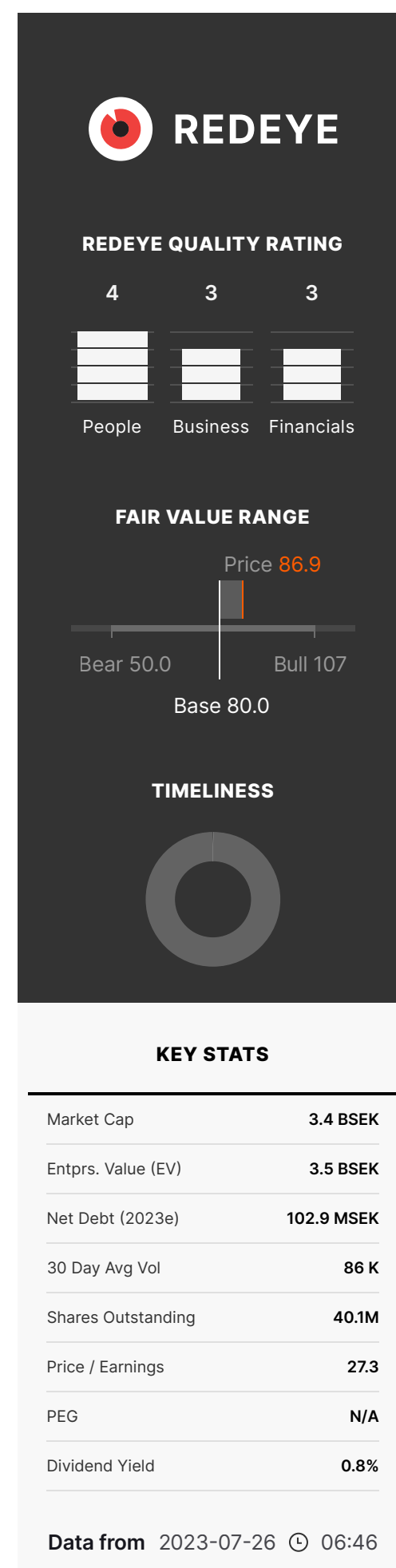
After the end of Q2, Hanza announced that Mitsubishi Logisnext Europe (MLE) would increase its volumes by above SEK100m annually. While being a large order, it is just as important that MLE will become a full-service customer, utilizing the full potential of Hanza's cluster offering. We are encouraged to see Hanza gaining a large full-service deal, especially as it highlights product companies' interest in the cluster offering but also as it adds sales – likely with above-average margins.

New Base Case SEK92 (80)

We raise our Base Case to SEK92 (80). While we do not fully extrapolate the excellent 11.1% EBITA margin in Main Markets seen in this quarter, the number suggests management has done a solid job in the German cluster, and we raise our margin assumptions somewhat. Although soft macroeconomics is a risk going forward, Hanza has exposure to many structurally growing markets and tailwinds thanks to back shoring.

Key financials

SEKm	2022	2023E	2024E	2025E	2026E
Revenues	3,549	4,268	4,628	4,999	5,299
Revenue Growth	41.1%	20.3%	8.4%	8.0%	6.0%
EBITDA	316	472	522	565	612
EBIT	193	339	382	420	455
EBIT Margin	5.4%	7.9%	8.2%	8.4%	8.6%
Net Income	121	237	274	306	336
EV/Revenue	0.6	0.8	0.8	0.7	0.6
EV/EBIT	11.0	10.5	9.1	8.1	7.3



IMPORTANT INFORMATION

All information regarding limitation of liability and potential conflicts of interest can be found at the end of the report.

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Table of contents

Impressive Margin in Main Markets	3
Financial Forecasts	5
Valuation	6
Investment thesis	7
Quality Rating	7
Financials	9
Rating definitions	11
The team	12

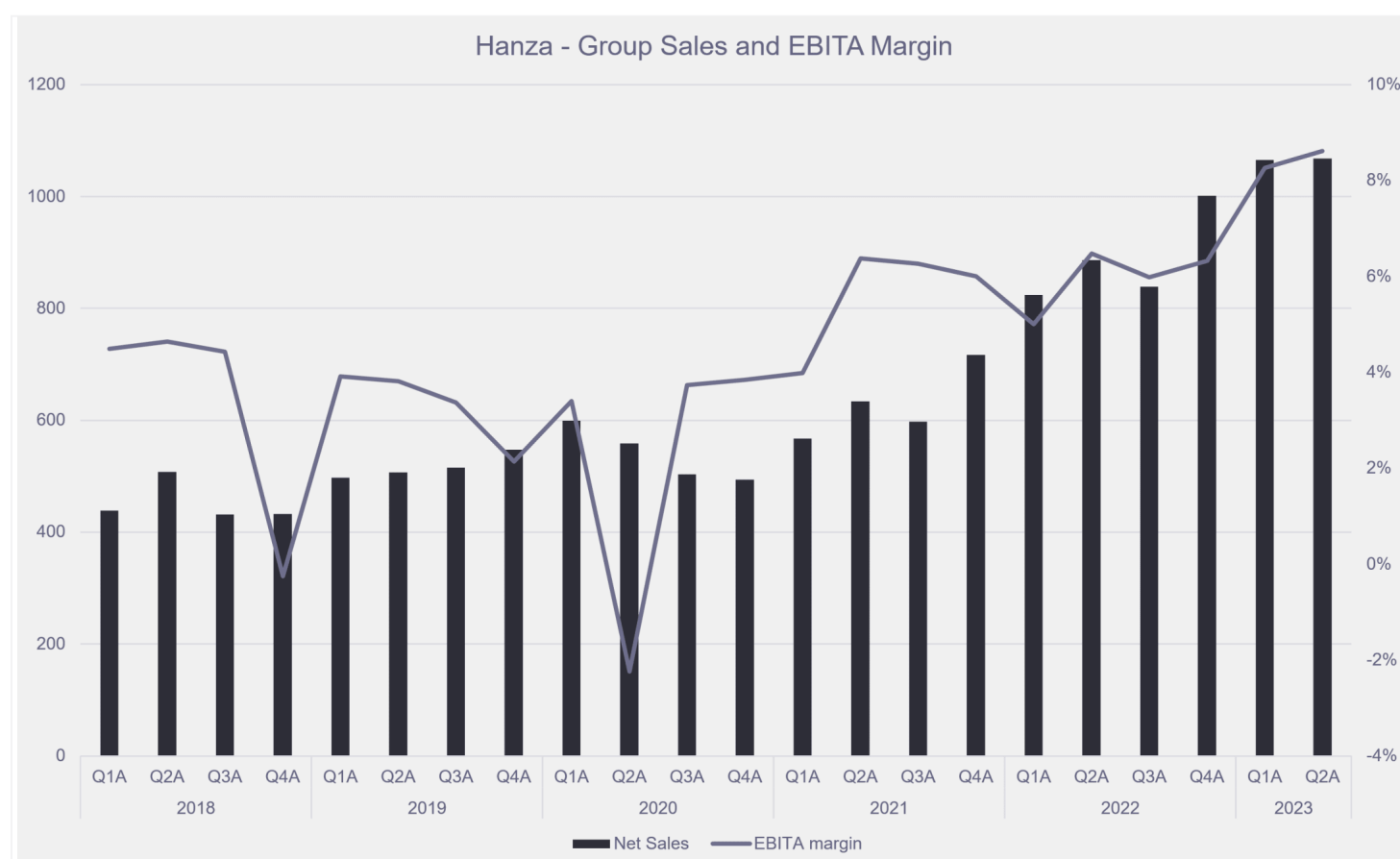
Impressive Margin in Main Markets

	Q2E 2023	Q2A 2023	Diff	Q2A 2022	Q1A 2023
Net sales	1 061.3	1 068.0	0.6%	886.0	1 065.0
Y/Y Growth (%)	19.8%	20.5%		39.8%	29.3%
Main Markets	571.7	605.0	5.8%	484.5	594.0
Y/Y Growth (%)	18.0%	24.9%		43.0%	23.3%
EBITA (MM)	48.6	67.0	37.9%	36.7	58.0
EBITA margin	8.5%	11.1%		7.6%	9.8%
Other Markets	489.6	458.0	(6.5%)	401.3	468.0
Y/Y Growth (%)	22.0%	14.1%		36.1%	36.8%
EBITA (OM)	32.3	28.0	(13.3%)	22.6	30.0
EBITA margin	6.6%	6.1%		5.6%	6.4%
EBITA	79.4	92.0	15.9%	57.4	88.0
EBITA Margin (%)	7.5%	8.6%		6.5%	8.3%

Source: Hanza & Redeye Research

Sales grew by 13% organically y/y and matched our forecast. Main Markets beat our forecast by 6% and grew organically by 19% y/y. Other Markets came in somewhat short relative to our expectations, with organic growth of 5% y/y. While the organic growth of 13% was lower than the 23% seen in the last quarter, we still believe it is a solid level. Also, in Other Markets, sales was dampened by component shortages related to a specific customer. The order intake remains strong in basically all markets, both industry- and geography-wise. Hanza cites strong demand from customers within defence, mining, energy, and agriculture in particular – mentioning one defence customer increasing its order backlog at Hanza to SEK150m from SEK65m.

EBITA beat our forecast by 16%, following an exceptional margin in Main Markets. EBITA in Main Markets beat our forecast by 36%, while Other Markets came in short by 13%. On the group level, we note that Hanza beat its >8% EBITA margin target for the second consecutive quarter.



After the end of Q2, Hanza announced that Mitsubishi Logisnext Europe (MLE) would increase its volumes by above SEK100m annually. While being a large order, it is just as important that MLE will become a full-service customer. Starting out with Hanza's consulting service MIG (Manufacturing Solutions for Increased Growth & Earnings), MLE will gather production, final assembly, testing, logistics and more in Hanza's Estonian cluster. We are encouraged to see Hanza gaining a large full-service deal, as we believe Hanza's ability to add value is at its highest for this type of deal. Typically, higher value adds to customers allows for higher margins for Hanza.

Hanza has initiated a long-term share savings program targeting 13 employees, including cluster managers. The employees buy shares for their own money, and given that Hanza reaches its

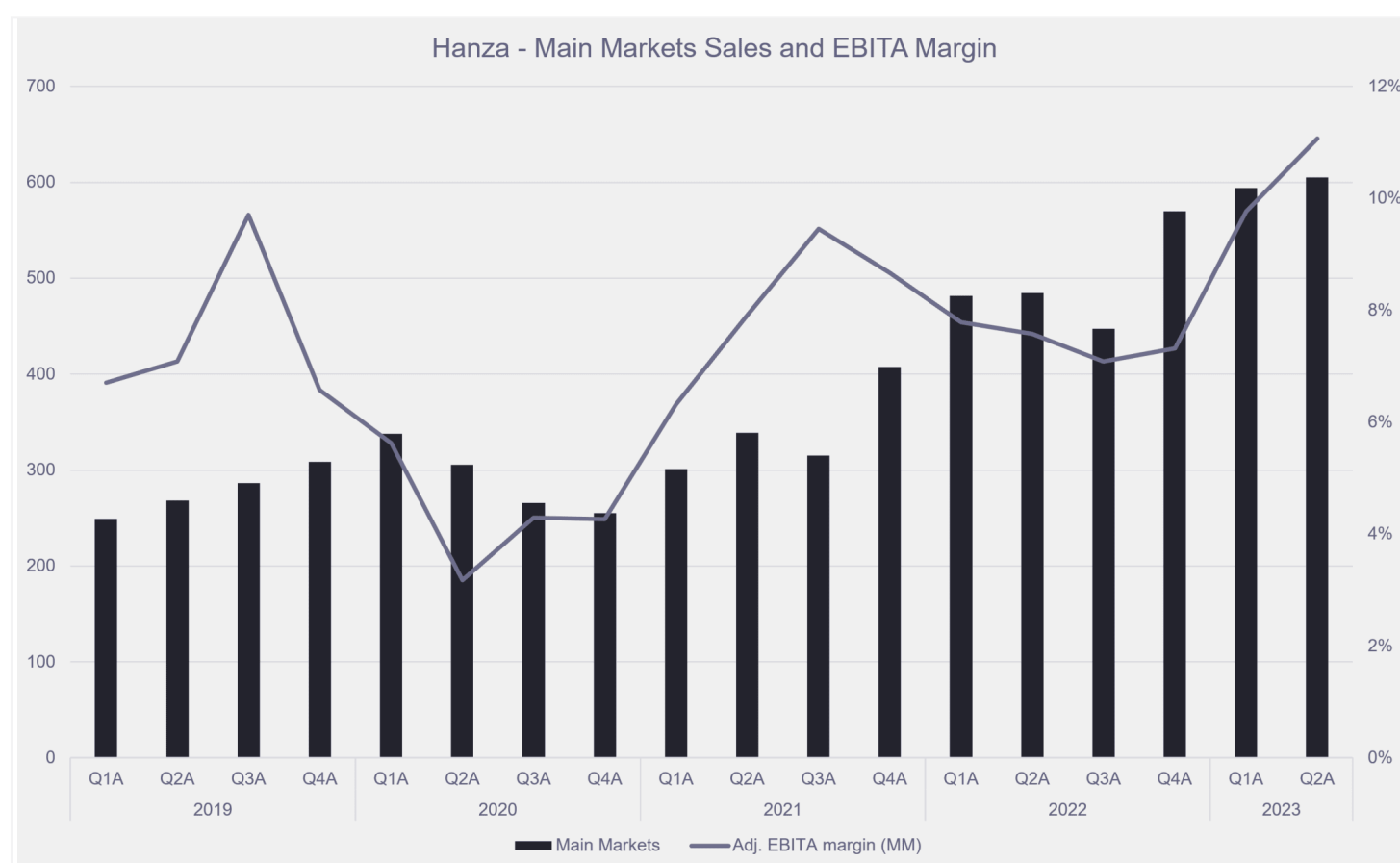
2025 targets, they are awarded additional shares. The program was subscribed to 97%. We prefer a share-based program over an option program, as it aligns management's interests closer to the shareholders. Also, Hanza's group management has increased its holdings (related to an earlier option program) and now owns 2.13% of the company.

Main Markets

While we knew that the Swedish cluster can perform in line with this level, the strong segment EBITA margin of 11.1% implies a significant improvement in the German cluster. Also, according to management, the improvement is mostly related to the German cluster. As mentioned in our last Update, we believe it is encouraging to see the German cluster – whose margins were hurt by a zero-margin acquisition – improving, strengthening our view of management's ability to execute M&A.

Management states that Hanza typically sees significant advantages when a cluster has sales of about SEK1bn and above – which only Sweden (Main Markets) and Baltics (Other Markets) have so far. This is achieved by operational cooperation (where employees can be relocated within the cluster, for example) and shared service centres. The statement implies that Sweden is likely currently running with EBITA margins substantially above 10%, probably in the 13-16% range.

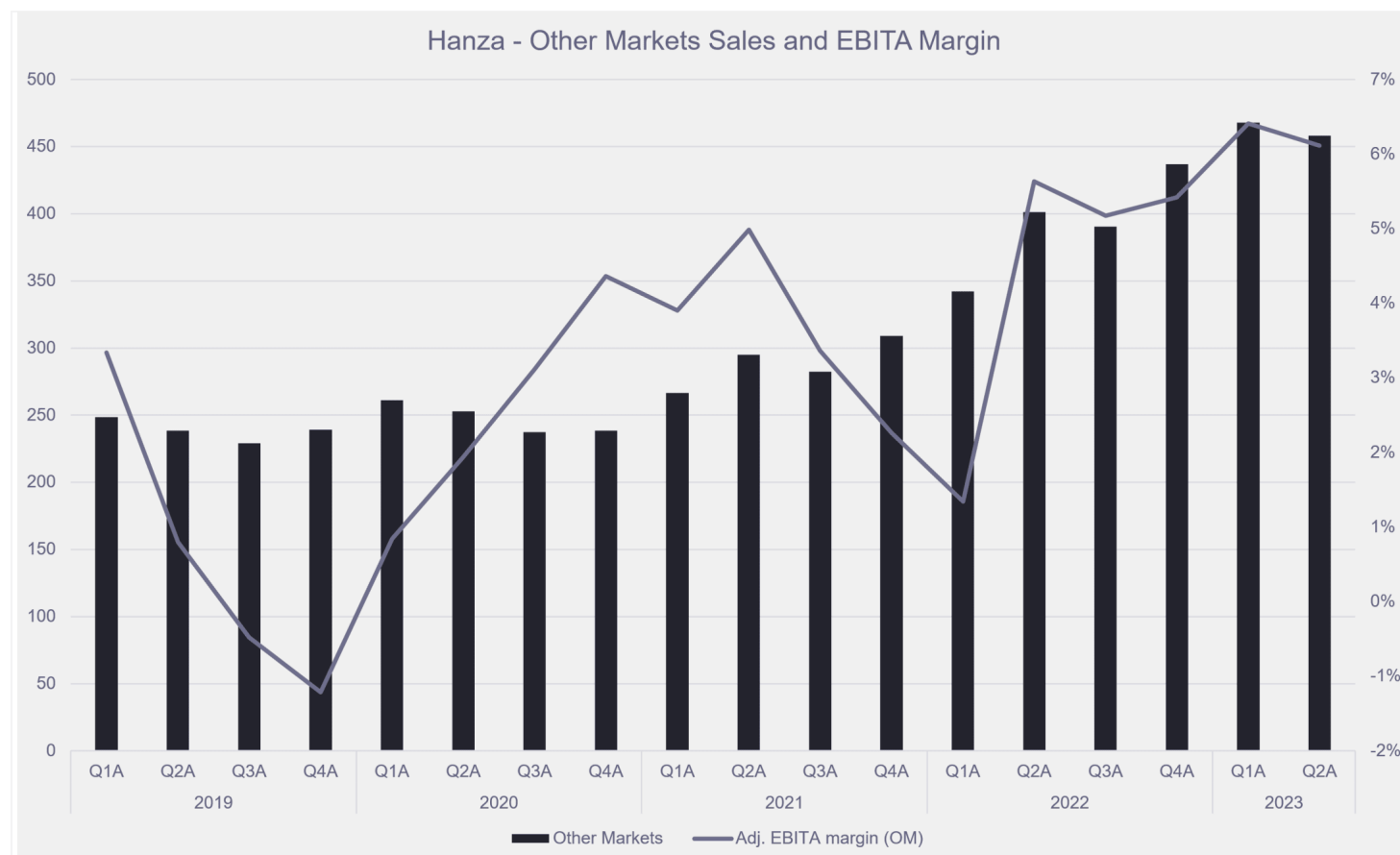
In June, Hanza acquired a property of just over 11 000 square meters with approximately 28 000 square meters of land in conjunction with its facilities in Töcksfors (Swedish cluster). The purchase allows Hanza to expand its production capacity modularly and rapidly if needed.



Other Markets

Other Markets sales and margins was hurt due to a component shortage related to a specific customer. Management expects the situation regarding components to improve further during 2023. Capacity expansions in Poland, Czechia and China also hurt the margin. Assuming a reduced component shortage and expansion programs being finished, we expect gradual improvements over the coming quarters.

In the long run, we believe Other Markets should be able to achieve margins in line with Main Markets, although our Base Case assumptions are somewhat more defensive currently.



Financial Forecasts

We leave our sales forecasts largely flat. Hanza continues to see strong demand from most of its customers, and we expect organic growth of ~15% for H2 2023 and ~8% for 2024.

We raise our EBITA and EBIT forecasts by 8-9% for 2023 and 2024. The increase is driven by us expecting higher margins in Main Markets. While we do not extrapolate the excellent 11.1% seen in this quarter, we forecast 10% from now on. The investments in Töcksfors might have a slightly negative impact, while we, on the other hand, believe there is greater potential in the German cluster.

We cut our EPS forecast by ~3% for 2023 and 2024, as we previously underestimated the financial costs. Strong growth and increasing interest rates have increased Hanza's factoring costs, which effect we previously underestimated. Our previous forecasts were based mainly on ordinary interest-bearing debt. While factoring has a cost, customers appreciate attractive payment terms, and Hanza can compensate for that in other ways.

Estimate Revisions	FYE 2023	Old	Change	FYE 2024	Old	Change
Net sales	4 268.3	4 291.0	(0.5%)	4 628.3	4 634.3	(0.1%)
Y/Y Growth (%)	20.3%	20.9%		8.4%	8.0%	
Main Markets	2 382.3	2 349.0	1.4%	2 572.9	2 537.0	1.4%
Y/Y Growth (%)	20.1%	18.4%		8.0%	8.0%	
EBITA (MM)	243.3	205.2	18.6%	257.3	220.7	16.6%
EBITA margin	5.7%	4.8%		5.7%	7.6%	
Other Markets	1 886.0	1 942.0	(2.9%)	2 055.4	2 097.3	(2.0%)
Y/Y Growth (%)	20.1%	23.6%		9.0%	8.0%	
EBITA (OM)	117.6	125.4	(6.2%)	144.0	147.0	(2.0%)
EBITA margin	6.2%	6.5%		22.4%	17.2%	
EBITA	355.0	326.1	8.9%	395.3	361.7	9.3%
EBITA Margin (%)	8.3%	7.6%		8.5%	7.8%	
EBIT	339.1	311.3	8.9%	381.6	349.4	9.2%
EBIT Margin (%)	7.9%	7.3%		8.2%	7.5%	
Diluted EPS	6.0	6.2	(2.1%)	7.0	7.2	(2.7%)

Source: Hanza & Redeye Research

On our revised forecasts, we expected Hanza to reach its SEK5bn in sales and 8% EBITA margin target for 2025. We expect SEK5bn in sales and 8.4% in EBITA margin. Sales growth and margin expansion have been strong since Hanza published its targets, and despite us expecting slower growth and margin expansion going forward, we believe Hanza can reach its 2025 targets.

Income Statement	FYA 2022	Q1A 2023	Q2A 2023	Q3E 2023	Q4E 2023	FYE 2023	FYE 2024	FYE 2025
Net sales	3 549	1 065	1 068	981	1 162	4 268	4 628	4 999
Y/Y Growth (%)	41.1%	29.3%	20.5%	17.0%	16.1%	20.3%	8.4%	8.0%
Main Markets	1 984	594	605	528	655	2 382	2 573	2 779
Y/Y Growth (%)	45.6%	23.3%	24.9%	18.0%	15.0%	20.1%	8.0%	8.0%
EBITA (MM)	148	58	67	53	66	243	257	278
EBITA margin	7.4%	9.8%	11.1%	10.0%	10.0%	10.2%	10.0%	10.0%
Other Markets	1 571	468	458	453	507	1 886	2 055	2 220
Y/Y Growth (%)	36.3%	36.8%	14.1%	16.0%	16.0%	20.1%	9.0%	8.0%
EBITA (OM)	71	30	28	27	32	118	144	160
EBITA margin	4.5%	6.4%	6.1%	6.0%	6.4%	6.2%	7.0%	7.2%
EBITA	212	88	92	78	96	355	395	432
EBITA Margin (%)	6.0%	8.3%	8.6%	8.0%	8.3%	8.3%	8.5%	8.6%
EBIT	193	84	88	74	93	339	382	420
EBIT Margin (%)	5.4%	7.9%	8.2%	7.6%	8.0%	7.9%	8.2%	8.4%
Diluted EPS	3.1	1.5	1.5	1.3	1.7	6.0	7.0	7.8

Source: Hanza & Redeye Research

Valuation

Following raised forecasts, we raise our Base Case to SEK 92 (80). Our new Bear and Bull Cases are SEK58 (50) and SEK122 (107).

Peer Valuation

Manufacturing Company	EV (SEKm)	EV/SALES			EV/EBIT (x)			Sales growth			EBIT margin		
		23E	24E	25E	23E	24E	25E	23E	24E	25E	23E	24E	25E
Incap	3 337	1.3	1.1	0.9	9	7	6	-11%	11%	10%	13%	14%	14%
Kitron	9 451	1.0	0.9	0.8	12	11	10	35%	9%	9%	8%	8%	8%
Nolato	12 987	1.2	1.1	1.0	15	12	10	-3%	8%	6%	8%	10%	10%
Scanfil	8 282	0.8	0.7	0.7	12	11	10	8%	3%	3%	7%	7%	7%
Inission	1 563	0.7	0.7	0.6	13	12	10	10%	5%	5%	6%	6%	6%
NCAB	11 622	2.6	2.3	2.1	19	17	15	2%	6%	7%	14%	14%	14%
Hanza	3 932	0.9	0.8	0.8	11	10	9	20%	8%	8%	8%	9%	9%
Average	7 874	1.2	1.1	1.0	13	11	10	9%	7%	7%	9%	10%	10%
Median	8 867	1.2	1.1	1.0	14	12	11	12%	7%	6%	9%	9%	9%

Source: Redeye, Company reports, FactSet

Despite the strong share price performance, Hanza is still trading at a slight discount to the average, although often bigger, manufacturing service companies, thanks to its strong earnings growth. We believe the discount will decrease further given that Hanza continues its strong operational performance.

Investment thesis

Case

Riding the Back-Shoring Trend with its Unique Cluster Strategy

With its 'All you need is one' cluster-based strategy, Hanza, and its experienced management take a unique approach that differentiates it from manufacturing service companies. By gathering several manufacturing technologies in a single location, Hanza can reduce costs, lead times, and environmental footprint. Having almost every cluster in the end market or in close-by low-cost countries, Hanza is set to benefit from the ongoing back-shoring trend. Quarterly reports with strong operational performance, particularly improvements in immature clusters, are the main catalysts.

Evidence

Proven Track-Record in Mature Clusters

The Main Markets segment, including the mature Swedish and Finnish clusters as well as the newly established German cluster, has an EBITA margin of about 8% - implying sector-leading margins in the mature Swedish and Finnish clusters. As the other clusters mature, we expect their margins to approach Swedish levels gradually. Since late 2021, Hanza has seen a surge in organic sales growth following the pandemic. While a rebound from the pandemic has a positive effect, we believe the strong numbers also result from increasing interest in back-shoring.

Challenge

Cyclical Exposure Through Customers' Volume Fluctuations

While Hanza seldom loses customers, its revenues depend on the customers' volumes. During the pandemic in 2020, organic sales fell by about 10%, putting pressure on margins. Thus, Hanza is, to some extent, exposed to market cycles. However, following recent acquisitions and organic customer intake, we believe the diversification between sectors has improved. In addition, the back-shoring trend should help Hanza attract new customers in economic downturns.

Challenge

Lack of transferability

Hanza's success in the Nordics may not result from its 'All you need is one' cluster strategy but rather follow from smart acquisitions and a management team with close connections to several Nordic product companies. If so, it may struggle to achieve solid profitability outside of the Nordics. However, it has already established a successful presence outside the Nordics, such as in Tartu, Estonia.

Valuation

Fair Value SEK 92

Our DCF model shows a fair value of SEK 92, which is also supported by a peer valuation. While Hanza has been trading at a discount to peers historically, considering its improvements regarding organic sales growth and margins, we believe Hanza should trade on par with peers.

Quality Rating

People: 4

Hanza receives a high rating for people, as both management and owners have favorable characteristics. CEO Erik Stenfors has vast experience of the manufacturing service industry, including being the founder and CEO of both Note and Hanza. Hanza's largest shareholder is Gerald Engström, the founder and majority owner of Systemair. As a result, Hanza also has the

support of a product company veteran.

Business: 3

Lacking clear differentiators, competition in the manufacturing service industry is typically tough. While Hanza has a unique take on the industry, we believe it is still difficult for it to increase prices for example. All the same, Hanza is a close and important partner for several of its customers. Moreover, it has decent diversification across both sectors and customers. Overall, Hanza receives an average rating for Business.

Financials: 3

While Hanza's near-term financial performance is strong, the long-term track-record has been weak, which lowers the Financials rating. Its solid financial position is positive, while the low-margin nature of its business is negative for the rating. In summary, Hanza receives an average rating for Financials. Several consecutive years of solid performance would lift the rating, though.

Financials

Income statement

SEKm	2022	2023E	2024E	2025E	2026E
Revenues	3,549	4,268	4,628	4,999	5,299
Cost of Revenue	2,171	2,587	2,870	3,099	3,285
Operating Expenses	1,063	1,210	1,237	1,334	1,402
EBITDA	316	472	522	565	612
Depreciation	57	64	74	81	94
Amortizations	19	16	14	12	10
EBIT	193	339	382	420	455
Shares in Associates	-	-	-	-	-
Interest Expenses	(50)	(55)	(51)	(51)	(51)
Net Financial Items	50	55	51	51	51
EBT	143	284	331	369	404
Income Tax Expenses	(22)	(47)	(56)	(63)	(69)
Net Income	121	237	274	306	336

Balance sheet

Assets

Non-current assets

SEKm	2022	2023E	2024E	2025E	2026E
Property, Plant and Equipment (Net)	551	761	885	1,023	1,162
Goodwill	388	400	400	400	400
Intangible Assets	90	78	64	52	42
Right-of-Use Assets	180	170	170	170	170
Other Non-Current Assets	17	6	6	6	6
Total Non-Current Assets	1,226	1,415	1,525	1,652	1,781

Current assets

SEKm	2022	2023E	2024E	2025E	2026E
Inventories	937	1,069	1,157	1,250	1,325
Accounts Receivable	151	171	185	200	212
Other Current Assets	91	128	139	150	159
Cash Equivalents	137	179	248	321	420
Total Current Assets	1,316	1,547	1,729	1,920	2,115
Total Assets	2,541	2,963	3,254	3,572	3,896

Equity and Liabilities**Equity**

SEKm	2022	2023E	2024E	2025E	2026E
Non Controlling Interest	-	-	-	-	-
Shareholder's Equity	898	1,166	1,381	1,618	1,877

Non-current liabilities

SEKm	2022	2023E	2024E	2025E	2026E
Long Term Debt	-	-	-	-	-
Long Term Lease Liabilities	348	335	335	335	335
Other Non-Current Lease Liabilities	151	171	171	171	171
Total Non-Current Liabilities	499	506	506	506	506

Current liabilities

SEKm	2022	2023E	2024E	2025E	2026E
Short Term Debt	307	318	318	318	318
Short Term Lease Liabilities	41	45	45	45	45
Accounts Payable	488	556	602	650	689
Other Current Liabilities	310	372	403	435	461
Total Current Liabilities	1,145	1,291	1,367	1,448	1,513
Total Liabilities and Equity	2,541	2,963	3,254	3,572	3,896

Cash flow

SEKm	2022	2023E	2024E	2025E	2026E
Operating Cash Flow	145	350	379	414	461
Investing Cash Flow	(184)	(260)	(198)	(220)	(233)
Financing Cash Flow	120	(53)	(111)	(121)	(129)

Rating 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 longterm 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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