

Hanza: Strong Outlook for 2024

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Redeye retains its positive stance towards Hanza following a solid Q3 report, with the strong margin in Main Markets and positive 2024 outlook being the highlights.



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Excellent Margins in Main Markets – Again

Sales increased by 14% y/y, slightly below our forecast of 17%. Underlying organic sales growth was 10% y/y. Main Markets grew faster than expected, while Other Markets was softer. EBITA was SEK89m (50.2), corresponding to an EBITA margin of 9.3% (6.0). The outcome beat our forecast of SEK79m by 13%, driven by a strong development in Main Markets. Like in Q2 2023, Main Markets reached an impressive EBITA margin. In Q3, it was 12.4% (7.1), up from 11.1% in Q2. The improvement y/y is mostly related to the German cluster but also implies strong operational performance in the other clusters (Sweden & Finland).

Positive Outlook for 2024

Management sees continued growth from its customer base during 2024, especially in Other Markets, which would be welcomed considering its recent softer development. However, we have seen several companies guiding for a strong market, which has then experienced rapid shifts downward, making us somewhat cautious about such statements in general. On the other hand, management points out that most of the products Hanza manufactures have long lead times, providing Hanza with above-average visibility into future demand. While the demand picture could change in Q4 or in 2024, it is a clear positive sign for 2024.

New Base Case SEK82 (92)

We lower our Base Case to SEK 82 (92), as we increase our WACC because of the increased risk-free rate. We leave our sales and margin forecasts largely flat. While the macroeconomic outlook is rather soft, considering Hanza large exposure to defensive sectors, structural drivers for regionalized manufacturing, and management’s positive outlook for demand from current customers during 2024, we expect an organic growth of c10% in 2024.

Key financials

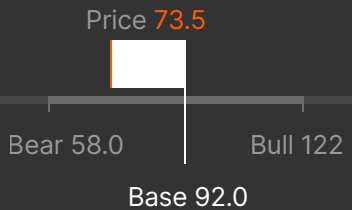
SEKm	2022	2023E	2024E	2025E	2026E
Revenues	3,549	4,191	4,598	4,966	5,264
Revenue Growth	41.1%	18.1%	9.7%	8.0%	6.0%
EBITDA	316	483	527	574	624
EBIT	193	349	383	424	465
EBIT Margin	5.4%	8.3%	8.3%	8.5%	8.8%
Net Income	121	232	269	303	337
EV/Revenue	0.6	0.7	0.6	0.6	0.5
EV/EBIT	11.0	8.7	7.8	6.9	6.0



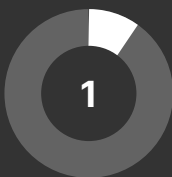
REDEYE QUALITY RATING



FAIR VALUE RANGE



TIMELINESS



KEY STATS

Market Cap	2.9 BSEK
Entprs. Value (EV)	3.0 BSEK
Net Debt (2023e)	139.0 MSEK
30 Day Avg Vol	89 K
Shares Outstanding	40.1M
Price / Earnings	23.1
PEG	N/A
Dividend Yield	1.0%

Data from 2023-11-08 06:46

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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Impressive Main Markets – Again

	Q3E 2023	Q3A 2023	Diff	Q3A 2022	Q2A 2023
Net sales	981.0	955.0	(2.7%)	838.4	1 068.0
Y/Y Grow th (%)	17.0%	13.9%		40.3%	20.5%
Main Markets	528.1	547.0	3.6%	447.5	605.0
Y/Y Grow th (%)	18.0%	22.2%		42.0%	24.9%
EBITA (MM)	52.8	68.0	28.8%	31.7	67.0
EBITA margin	10.0%	12.4%		7.1%	11.1%
Other Markets	453.0	405.0	(10.6%)	390.5	458.0
Y/Y Grow th (%)	16.0%	3.7%		38.3%	14.1%
EBITA (OM)	27.2	23.0	(15.4%)	20.2	28.0
EBITA margin	6.0%	5.7%		5.2%	6.1%
EBITA	78.5	89.0	13.4%	50.2	92.0
EBITA Margin (%)	8.0%	9.3%		6.0%	8.6%
Source: Hanza & Redeye Research					

Underlying sales (adjusted for last year's invoicing of exceptionally high energy and material costs) grew 10% organically y/y and was 3% below our forecast. Main Markets beat our forecast by 4%, and underlying sales grew organically by 16% y/y. Other Markets came in c11% short relative to our expectations, with underlying organic sales growth of 1% y/y. While the organic growth rate has declined during 2023, we still believe 10% is a solid level – especially in the softening macroeconomic environment.

Management sees continued growth from its customer base during 2024, especially in Other Markets, which would be welcomed considering its recent softer development. However, we have seen several companies guiding for a strong market, which has then experienced rapid shifts downward, making us somewhat cautious about such statements in general. On the other hand, management points out that most of the products Hanza manufactures have long lead times, providing Hanza with above-average visibility into future demand. While we believe the statement is surprisingly positive considering the softer overall macro environment – where Hanza's exposure to more defensive sectors such as agriculture, defence, and energy likely is a positive driver – a further worsening of macroeconomics could also hurt Hanza.

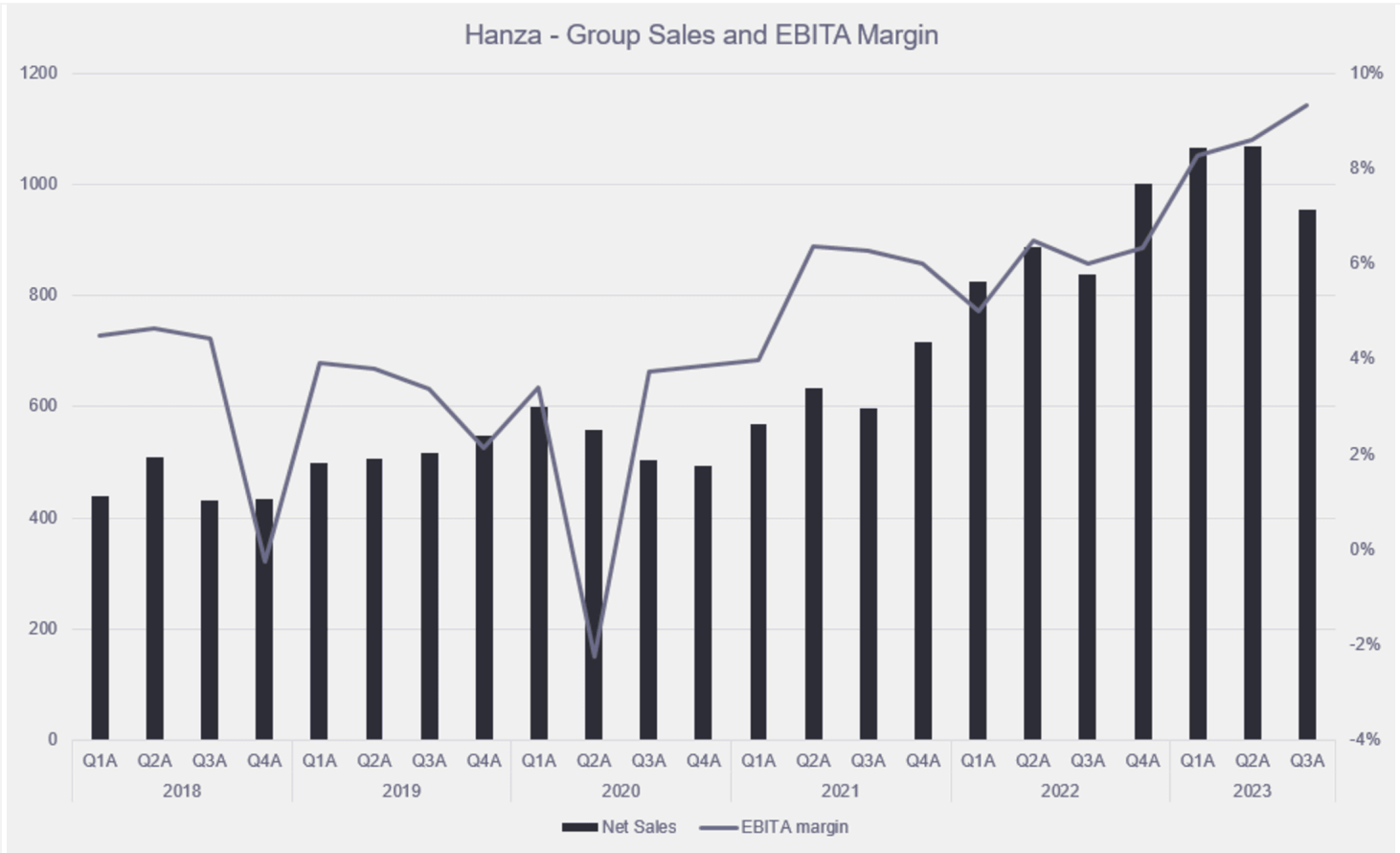
On the other hand, the interest in regionalized production remains high, which seems reasonable considering the increasing geopolitical turmoil in many areas, for example. The back sourcing or regionalization is mostly about new production for the European/American markets being manufactured in those regions rather than production moving back from Asia, although that happens sometimes as well.

EBITA was SEK89m (50.2), corresponding to an EBITA margin of 9.3% (6.0). The outcome beat our forecast of SEK79m by 13%, driven by a strong development in Main Markets. EBITA in Main Markets beat our forecast by 29%, while Other Markets came in short by 15%. On the group level, we note that Hanza beat its >8% EBITA margin target for the third consecutive quarter. The solid EBITA increase also translated into a strong EPS growth of 68% y/y.

In its ESG update in the Q3 call presentation, we noted that Hanza had reduced its energy use per SEKm from 15.3MWh in 2021 to 9.81MWh in 2023 YTD. While energy prices have been relatively low so far in 2023, they were extremely high in 2022 and might return to such a level near-term. Thus, whether you as an investor are interested in ESG in itself or not, Hanza's improved energy efficiency makes the company less vulnerable to potential future energy price shocks. Management states that investment in new modern equipment has generated significant savings.

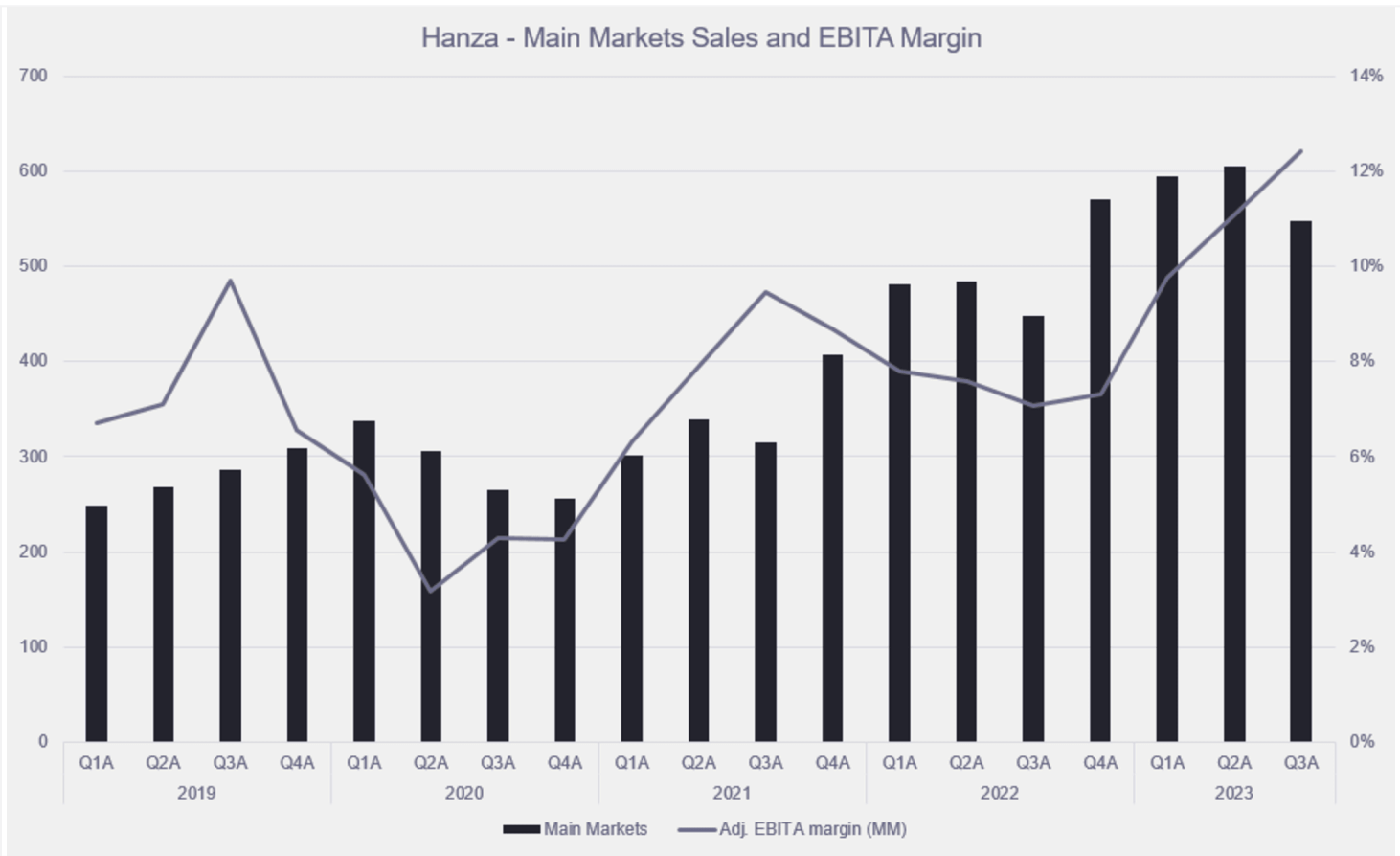
Regarding M&A, Hanza sees improved market conditions. The price expectations from potential sellers are returning to realistic levels, which should increase the likelihood of Hanza closing an acquisition. Management points out that the current M&A focuses on existing technologies and geographies – thus Sweden, Finland, Germany, The Baltics, Central Europe, and China. As Hanza sees significant scale advantages as the clusters reach about SEK1bn in sales – this is achieved by operational cooperation (where employees can be relocated within the cluster, for example) and shared service centres – we believe the smaller clusters are most attractive to expand. We believe Germany, Finland, and Central Europe are the most likely clusters for M&A, although we

believe all clusters are open for expansion by M&A. The solid improvement seen in the most recent acquisition, Beyers (discussed below), exemplifies a successful cluster-expanding acquisition.



Main Market

Like in Q2 2023, Main Markets reached an impressive EBITA margin. In Q3, it was 12.4% (7.1), up from 11.1% in Q2. The improvement y/y is mostly related to the German cluster but also implies strong operational performance in the other clusters (Sweden & Finland). 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. Main Markets had an FX-adjusted underlying sales growth of 16% y/y. Despite the 11-12% EBITA margin seen in the two most recent quarters, we expect a level of 10% going forward – still a very solid level for this kind of business.

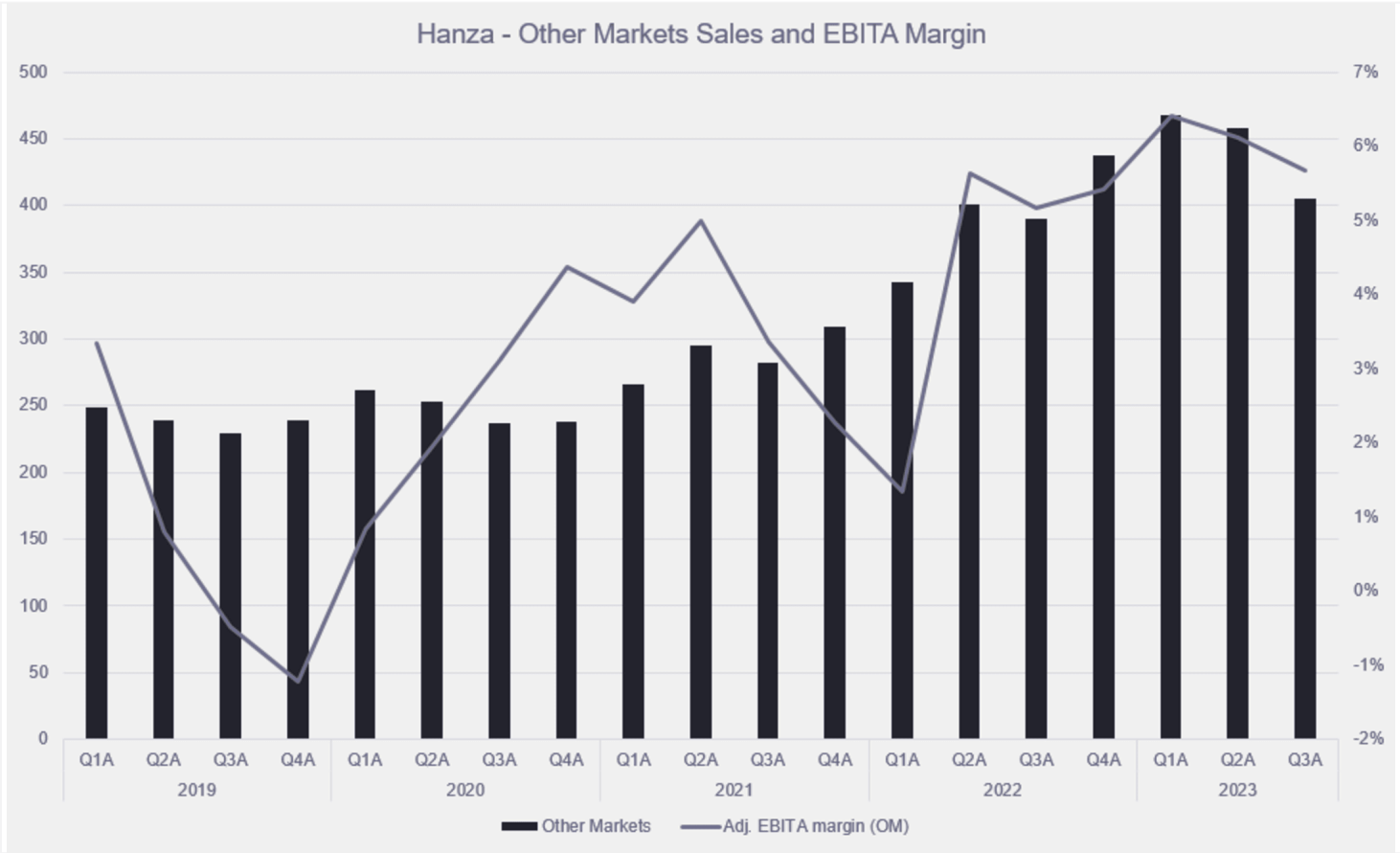


Other Markets

Other Markets had an underlying FX-adjusted sales growth of 1%. While increasing somewhat y/y to 5.7% (5.2), the EBITA margin declined slightly relative to 6.1% in Q2. Our forecast was 6.0%, and the EBITA outcome was 15% below our expectations. However, as stated earlier, management

sees a strong demand from its current customers in 2024, especially regarding Other Markets. Increased sales resulting in higher utilization rates and larger clusters should result in a higher margin, all else equal. Thus, we continue to expect further margin improvements in Other Markets.

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 – expecting EBITA margins of 8% from 2026.



Financial Forecasts

We leave our sales forecasts largely flat. While the macroeconomic outlook is rather soft, considering Hanza’s large exposure to defensive sectors, structural drivers for regionalized manufacturing, and management’s positive outlook for demand from current customers during 2024, we expect organic growth of c10% in 2024.

Although Main Markets beat our margin forecast and Other Markets missed it, we leave our assumptions roughly unchanged. We expect Main Markets to fluctuate at about 8-12% in EBITA margins, making 10% a fair long-term assumption. For Other Markets, we still expect a gradual improvement towards the lower end of Main Markets’ 8-12% range. We assume Other Markets will reach 8% in 2026.

Estimate Revisions	FYE 2023	Old	Change	FYE 2024	Old	Change
Net sales	4 191.2	4 268.3	(1.8%)	4 598.1	4 628.3	(0.7%)
Y/Y Growth (%)	18.1%	20.3%		9.7%	8.4%	
Main Markets	2 401.3	2 382.3	0.8%	2 593.4	2 572.9	0.8%
Y/Y Growth (%)	21.1%	20.1%		8.0%	8.0%	
EBITA (MM)	261.8	243.3	7.6%	264.5	257.3	2.8%
EBITA margin	10.9%	10.2%		10.2%	10.0%	
Other Markets	1 790.0	1 886.0	(5.1%)	2 004.7	2 055.4	(2.5%)
Y/Y Growth (%)	13.9%	20.1%		12.0%	9.0%	
EBITA (OM)	109.5	117.6	(6.9%)	138.7	144.0	(3.7%)
EBITA margin	6.1%	6.2%		6.9%	7.0%	
EBITA	364.8	355.0	2.8%	397.2	395.3	0.5%
EBITA Margin (%)	8.7%	8.3%		8.6%	8.5%	
EBIT	348.9	339.1	2.9%	383.5	381.6	0.5%
EBIT Margin (%)	8.3%	7.9%		8.3%	8.2%	
Diluted EPS	5.9	6.0	(1.9%)	6.9	7.0	(1.9%)

Source: Hanza & Redeye Research

We expected Hanza to roughly reach its SEK5bn in sales and 8% EBITA margin target for 2025. We expect SEK4.97bn in sales and 8.8% in EBITA margin. Sales growth and margin expansion have been strong since Hanza published its targets, and we believe Hanza can reach its 2025 targets – which, unlike our forecasts, also allows for M&A.

Income Statement	FYA 2022	Q1A 2023	Q2A 2023	Q3A 2023	Q4E 2023	FYE 2023	FYE 2024	FYE 2025	FYE 2026
Net sales	3 549	1 065	1 068	955	1 114	4 191	4 598	4 966	5 264
Y/Y Growth (%)	41.1%	29.3%	20.5%	13.9%	11.3%	18.1%	9.7%	8.0%	6.0%
Main Markets	1 984	594	605	547	655	2 401	2 593	2 801	2 969
Y/Y Growth (%)	45.6%	23.3%	24.9%	22.2%	15.0%	21.1%	8.0%	8.0%	6.0%
EBITA (MM)	148	58	67	68	69	262	265	280	297
EBITA margin	7.4%	9.8%	11.1%	12.4%	10.5%	10.9%	10.2%	10.0%	10.0%
Other Markets	1 571	468	458	405	459	1 790	2 005	2 165	2 295
Y/Y Growth (%)	36.3%	36.8%	14.1%	3.7%	5.0%	13.9%	12.0%	8.0%	6.0%
EBITA (OM)	71	30	28	23	28	109	139	162	184
EBITA margin	4.5%	6.4%	6.1%	5.7%	6.2%	6.1%	6.9%	7.5%	8.0%
EBITA	212	88	92	89	96	365	397	436	474
EBITA Margin (%)	6.0%	8.3%	8.6%	9.3%	8.6%	8.7%	8.6%	8.8%	9.0%
EBIT	193	84	88	85	92	349	383	424	465
EBIT Margin (%)	5.4%	7.9%	8.2%	8.9%	8.2%	8.3%	8.3%	8.5%	8.8%
Diluted EPS	3.1	1.5	1.5	1.2	1.6	5.9	6.9	7.7	8.6
Source: Hanza & Redeye Research									

Valuation

We lower our Base Case to SEK 82 (92), as we increase our WACC because of the increased risk-free rate. Our assumptions regarding sales and margins remain unchanged.

Peer Valuation

Manufacturing	EV	EV/SALES			EV/EBIT (x)			Sales growth			EBIT margin		
Company	(SEKm)	23E	24E	25E	23E	24E	25E	23E	24E	25E	23E	24E	25E
Incap	2 044	0.8	0.6	0.5	6	4	3	-11%	11%	10%	13%	14%	14%
Kitron	7 553	0.8	0.7	0.6	10	9	8	35%	9%	9%	8%	8%	8%
Nolato	14 452	1.4	1.2	1.1	17	13	11	-3%	8%	6%	8%	10%	10%
Scanfil	6 116	0.6	0.5	0.5	9	8	7	8%	3%	3%	7%	7%	7%
Inission	1 309	0.6	0.6	0.5	11	10	8	10%	5%	5%	6%	6%	6%
NCAB	10 958	2.4	2.2	2.0	18	16	14	2%	6%	7%	14%	14%	14%
Hanza	3 433	0.8	0.7	0.7	9	8	8	18%	10%	8%	9%	9%	9%
Average	7 072	1.1	1.0	0.9	11	10	8	8%	7%	7%	9%	10%	10%
Median	6 835	1.1	1.0	0.9	12	10	9	11%	7%	6%	9%	9%	9%

Source: Redeye, Company reports, FactSet

Despite the recent strong operational performance, Hanza is still trading at a slight discount to the average, although often bigger, manufacturing service companies. 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 82

Our DCF model shows a fair value of SEK 82, 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	4,191	4,598	4,966	5,264
Cost of Revenue	2,171	2,453	2,851	3,079	3,264
Operating Expenses	1,063	1,255	1,220	1,313	1,376
EBITDA	316	483	527	574	624
Depreciation	57	64	72	79	92
Amortizations	19	16	14	12	10
EBIT	193	349	383	424	465
Shares in Associates	-	-	-	-	-
Interest Expenses	(50)	(72)	(59)	(59)	(59)
Net Financial Items	50	72	59	59	59
EBT	143	277	324	365	406
Income Tax Expenses	(22)	(45)	(55)	(62)	(69)
Net Income	121	232	269	303	337

Balance sheet

Assets

Non-current assets

SEKm	2022	2023E	2024E	2025E	2026E
Property, Plant and Equipment (Net)	551	737	861	1,000	1,140
Goodwill	388	394	394	394	394
Intangible Assets	90	78	64	52	43
Right-of-Use Assets	180	188	188	188	188
Other Non-Current Assets	17	14	14	14	14
Total Non-Current Assets	1,226	1,411	1,521	1,649	1,778

Current assets

SEKm	2022	2023E	2024E	2025E	2026E
Inventories	937	1,051	1,150	1,241	1,316
Accounts Receivable	151	168	184	199	211
Other Current Assets	91	126	138	149	158
Cash Equivalents	137	174	234	305	406
Total Current Assets	1,316	1,519	1,706	1,894	2,090
Total Assets	2,541	2,930	3,227	3,543	3,868

Equity and Liabilities**Equity**

SEKm	2022	2023E	2024E	2025E	2026E
Non Controlling Interest	-	-	-	-	-
Shareholder's Equity	898	1,142	1,353	1,589	1,850

Non-current liabilities

SEKm	2022	2023E	2024E	2025E	2026E
Long Term Debt	-	-	-	-	-
Long Term Lease Liabilities	348	338	338	338	338
Other Non-Current Lease Liabilities	151	156	156	156	156
Total Non-Current Liabilities	499	494	494	494	494

Current liabilities

SEKm	2022	2023E	2024E	2025E	2026E
Short Term Debt	307	328	328	328	328
Short Term Lease Liabilities	41	54	54	54	54
Accounts Payable	488	546	598	646	684
Other Current Liabilities	310	366	400	432	458
Total Current Liabilities	1,145	1,294	1,380	1,460	1,524
Total Liabilities and Equity	2,541	2,930	3,227	3,543	3,868

Cash flow

SEKm	2022	2023E	2024E	2025E	2026E
Operating Cash Flow	145	322	372	415	466
Investing Cash Flow	(184)	(284)	(196)	(219)	(232)
Financing Cash Flow	120	(2)	(116)	(125)	(134)

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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