

Nederman Holding

Sweden | Industrial Goods | MCAP SEKm 4 217.5

Buy

Target Price
Current Price
Upside

SEK 149.0
SEK 117.5
26.8%

New trends in revenue generation will improve margins

Nederman Holding is a developer of products and solutions for advanced air purification in heavy process industries. According to their annual report for 2019, Nederman has a relevant market of SEKbn 46.7 with an expected CAGR of 6.0% 2019-2025E. Having a current revenue of SEKbn 4.3, Nederman inherits a 9.2% market share. With an estimated revenue CAGR of 9.2% in 2020-2024E they are expected to gain increased market share in the future. In the short term, this will be achieved through organic growth as recent investments pay off, and recurring revenue becomes an increasingly bigger part of Nederman's business through their new digital solutions. In the long term, however, Nederman is looking to combine organic growth with further acquisitions in order to reap the benefits of economy of scale. Using a discounted cash flow valuation with a WACC of 9.1%, a potential price per share of SEK 149.0 is implied, indicating an upside of 26.8%.

The Monitoring & Control Technology division will increase recurring revenue through a new level of aftermarket opportunities provided by their digital solutions. As a result, it will play an increasingly larger role in revenue generation which will improve Nederman's EBITA margin since their digital systems division had an EBITA margin of 15.9% in 2019A compared to that of the whole company, which was 9.1%. This unprecedented technology will also strengthen Nederman's position as one of the market leaders in industrial air filtration for heavy process industries, allowing them to gain further market shares.

As recent acquisitions are completely integrated, Nederman is expected to grow organically at a CAGR of 9.2% during 2020-2024E. The reorganization of 2018A has a considerable effect on these estimates as the reduced overlapping responsibilities and structural costs increase the focus and profitability of the company. Another growth driver in 2020-2024E is the integration of Gasmot which was acquired in 2019A for EURm 56.0. Gasmot presented revenue of EURm 23.0 in 2019A and will further advance Nederman's Monitoring & Control Technology division.

Based on the growth prospects of 2020-2024E, Nederman is undervalued at EV/EBIT 17.2x compared to their peers. With an expected EBIT margin increase from 8.0% to 11.2% and a revenue CAGR of 9.2% during 2020-2024E, Nederman is expected to show an EBIT CAGR of 16.8%, thus outperforming the peer median EBIT CAGR of 5.3% for the same period. As a result, Nederman's EV/EBIT of 17.2x indicates mispricing as it is roughly the same as the peer median of 17.0x.

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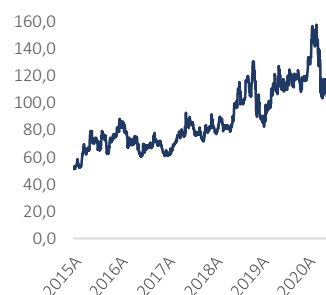
Market Data

Listing venue	Stockholm Mid Cap
Price (SEK)	117.5
Outstanding shares (m)	35.1
Market Cap (SEKm)	4 217.5
Net Debt (SEKm)	1 610.1
Enterprise Value (SEKm)	5 827.6

Key Financials(SEKm)	2019A	2020E	2021E
Sales	4307.7	4 478.6	4 972.1
Sales Growth y/y	21.2%	4.0%	11.0%
Gross Profit	1 591.3	1 701.9	1 889.4
Gross Margin (%)	36.9%	38.0%	38.0%
EBIT	343.2	361.8	449.4
EBIT Margin (%)	8.0%	8.1%	9.0%
NOPAT	267.7	282.2	350.5
Free Cash Flow	270.4	262.7	313.0
Net Income	225.8	247.8	311.4
Profit Margin	5.2%	5.5%	6.3%

Major Shareholders

Investment AB Latour	30.0%
Ernstström Finans	10.0%
IF Skadeförsäkring AB	9.9%
Fjärde AP Fonden	8.1%
Swedbank Robur fonder	8.1%
Tredje AP fonden	3.6%
Lannebo MicroCap	3.6%
Lannebo Microcap II	2.4%
Handelsbankens Nordiska Småbolag	2.0%
Total	77.7%

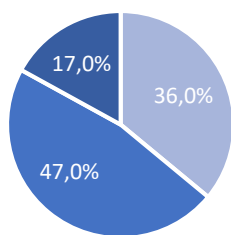


Investment thesis

Recurring revenue increases as sales trends change

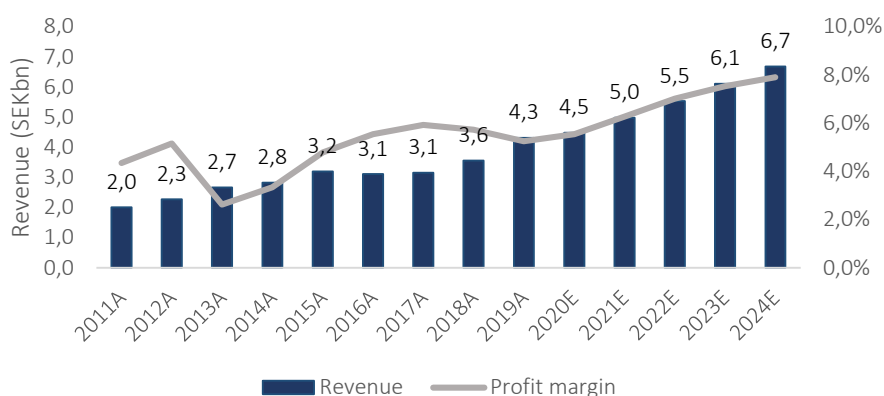
Historically Nederman’s standard products have constituted ~40.0% of sales. In 2020-2024E however, standard products are expected to decrease to a mere ~25% as complete and complex filtration systems along with included monitoring and control technology is estimated to make up a continuously bigger part of the revenue. In difference to standard products, these systems include a bigger commitment between the customer and Nederman. Thanks to the inclusion of the new digital solutions, this commitment means real-time information for Nederman on the need for service and replacement. It also allows the customer to purchase a subscription service where they leave the operation of the systems to Nederman, who in turn optimizes efficiency and reduces power consumption. As a result, recurring revenue is expected to increase in 2020-2024E as revenue from aftermarket activities should become a greater part of Nederman’s business. Because the EBITA margin of their Monitoring & Control Technology division is 15.9% compared to that of the whole company which is 9.1%, this development is also expected to improve the overall EBITA margin.

Salesgroup Revenue 201



- Standalone products
- Solutions
- Service and aftermarket

Revenue and Profit margin



Recent strategic acquisitions allow Nederman to meet the growing demand for extensive air purification systems.

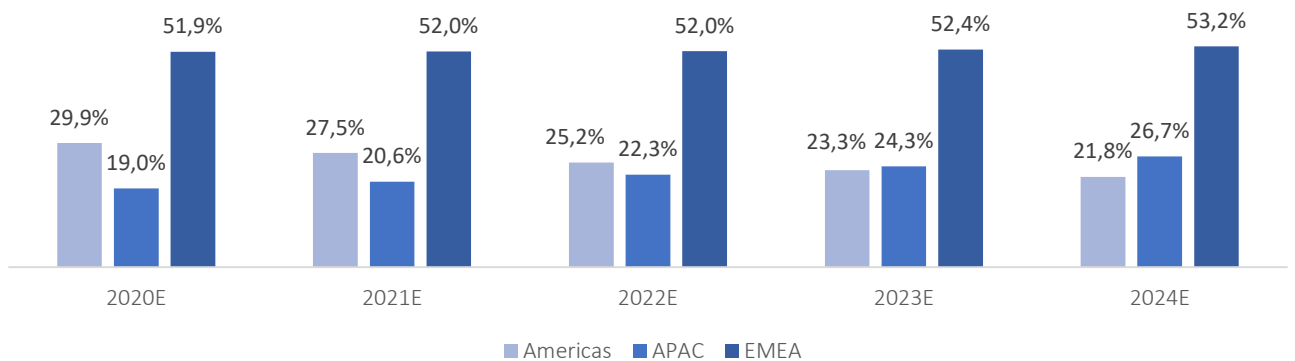
Nederman has, in recent years, made multiple strategic acquisitions. These acquisitions have resulted in the organization gaining wider geographical market reach while also expanding Nederman’s product offering. In order to integrate these companies as efficiently as possible, Nederman completed a reorganization in 2018A which divided the company and its acquisitions into divisions based on the product range. This reduced structural costs and overlapping responsibilities which has since paid off since all of their acquisitions were completely integrated in 2019A which played a major part in the organic growth in revenue of 21.0%.

There is a clear trend toward industrial companies becoming more conscious about the environmental impact of their production, leading to them requiring more extensive and complex filtration and air purifications systems. Thanks to Nederman’s wide knowledge and product offering through their acquisitions as well as their improved organization structure, they are able to meet and take full advantage of this demand. Extensive and complete air purification systems not only take longer time to complete, but it incorporates all of Nederman’s product divisions in the created system. This generates increased revenue and allows for an expected CAGR in 2020-2024E of 9.2%. Another benefit of this development is that, unlike Nederman’s standard products, these big projects, as well as their aftermarket business, will continue to generate revenue during the Covid-19 pandemic. However, fewer new projects will be initiated during this time.

Nederman's unprecedented product offering should allow them to gain increased market share in APAC and EMEA.

Strong geographical presence through recent acquisitions has culminated in Nederman currently being the market leader in EMEA, second biggest in the Americas and top 5 in APAC. Nederman's growth is dependent on competition and the development of the industrial sector in each market. As the majority of listed competitors are more or less directed toward other markets or submarkets of air purification, Nederman's unmatched product offering for heavy process industries should further enable them to gain market share in APAC and EMEA. In the Americas, however, the increased market share should be difficult to acquire due to saturation as a result of extensive competition, especially the American market. Because of this, it is expected to be their slowest developing market with an estimated CAGR of 1% in 2020-2024E. Nederman's revenue from the APAC markets, on the other hand, has grown substantially during 2016-2019A and is expected to keep growing at an estimated CAGR for 2020-2024E of 19.3% as many of the APAC markets have strong industrial growth. Lastly, EMEA made up 50% of revenue in 2019A, and this should continue being the case for Nederman in the years ahead as their estimated CAGR in this market during 2020-2024E is 10.2%.

Regional Revenue



The financial effects of Covid-19 and future risks.

According to their Q1 report for 2020E, the pandemic had little effect on Nederman's financials during their first quarter. Nederman explains that this is a result of them stacking up on critical components and identifying alternative suppliers before the pandemic started. These measures won't last long; however, they expect to see a negative impact on their business during Q2. As a result, Nederman won't be paying dividends in the short-term to protect liquidity. As of 2019A, Nederman had a net debt/EBITDA ratio of 3.2x, an interest coverage ratio of 8.1x and SEKm 445.3 in cash. Since they made multiple acquisitions in 2018A and need to secure their business during the pandemic, Nederman will probably not see any acquisitions during 2020E.

Nederman's revenue growth in 2020E is expected to decrease to 4.0% from the 21.0% growth of last year as uncertainty regarding the supply of components and the amount of new projects is expected to affect Nederman's second, third and possibly even fourth quarter. As the air filtration systems provided by Nederman are a necessity for heavy industry companies and the trend of reduced environmental impact is getting increasingly larger, the projects that are not initiated during 2020E will most likely just be postponed, not lost. As a result, the effects of the Covid-19 pandemic should be relatively insignificant when considered over the span of 2020-2024E, especially since aftermarket activities and big projects that are already initiated will continue to generate revenue during this time.

Valuation

Using DCF valuation and a WACC of 9.1% a price per share of 149.0 is calculated. The WACC comes from a cost of debt of 2.0% and a cost of equity of 9.7% with an added size premium of 1.5%. Cost of equity is based on a risk-free rate of 2.0%, an expected stock market return of 9.0% and a beta of 1.1. The weight of equity is 72.4% while the weight of debt is 27.6%. During the estimation period net working capital/revenue is 6.4% and capex/revenue is 2.2%, whereas NOPAT/revenue is approximately 7.6% and D&A/revenue is 2.1%. With this outlook Nederman's estimated free cash flow will be as shown in table 1 and 2 (appendix).

PPS	Sensitivity Analysis		WACC				
	147.0	6.0%	7.0%	8.0%	9.0%	10.0%	11.0%
Terminal Growth Rate	0.0%	201.5	164.6	137.0	115.6	98.5	84.6
	0.5%	220.3	177.7	146.6	122.8	104.1	89.0
	1.0%	242.8	193.0	157.5	131.0	110.4	93.9
	1.5%	270.4	211.1	170.2	140.2	117.4	99.4
	2.0%	304.8	232.8	184.9	150.8	125.2	105.4
	2.5%	349.1	259.4	202.3	163.0	134.1	112.1
	3.0%	408.2	292.5	223.3	177.2	144.3	119.7
	3.5%	490.8	335.2	248.8	194.0	156.1	128.3
	4.0%	614.8	392.1	280.8	214.1	169.8	138.1

Nederman should see a revenue growth as presented in table 3 (appendix), resulting in a CAGR of 9.2% in 2020-2024E. This estimate takes into consideration the effects of Covid-19, Nederman's developed product offering, including its monitoring & control technology, dominant market position and new company structure which are presented in the investment thesis.

Company name	Market Data			Valuation	Margins		Total revenue	
	Market Cap	Net Debt	Enterprise value		EV/EBIT	EBITDA	EBIT	2019A
Absolent Group (SEKm)	3 973.7	151.7	4 125.3	51.2x	13.0%	7.6%	1 038.0	1 108.0
Donaldson Company Inc (USDm)	5 769.4	408.7	6 178.1	17.0x	17.0%	13.0%	2 845.0	2 691.0
Systemair (SEKm)	8 808.8	1 995.5	10 804.3	17.0x	11.0%	7.0%	8 327.0	8 915.0
CECO Environmental (USDm)	215.9	29.9	245.8	14.1x	8.1%	5.2%	341.9	336.3
Nederman (SEKm)	4 217.5	1 610.1	5 827.6	17.2x	9.8%	8.0%	4307.7	4 478.6

As Nederman's EBIT margin and revenue increases in 2020-2024E, so should their EV/EBIT multiple. In regards to the peer median EV/EBIT multiple of 17.0x, Nederman is currently undervalued at EV/EBIT 17.2x. As the Monitoring & Control Technology division becomes an increasingly bigger part of revenue, Nederman's EBIT margin is estimated to increase from 8.0% in 2019A to 11.2% by 2024E. In conjunction with that, revenue is expected to grow with a CAGR of 9.2% during 2020-2024E. As a result, EBIT will grow with a CAGR of 16.8%. In comparison, the median EBIT CAGR of their peers, based on historic growth, is 5.3% while the median revenue CAGR is 4.8% during the same period. By these estimates, Nederman's EV/EBIT should increase in accordance with the estimated growth, further justifying an upside in stock price of 26.8%.

Appendix

Table 1

Capex, Nwc & Free Cash Flow (SEKm)	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Nwc(MSEK)	377.0	369.7	290.9	274.9	286.6	318.2	353.8	390.3	427.3
<i>Change, y-o-y(%)</i>	0.4%	-1.9%	-21.3%	-5.5%	4.3%	11.0%	11.2%	10.3%	9.5%
Nwc/COGS(%)	-18.9%	-19.0%	-13.1%	-10.1%	10.3%	10.3%	10.3%	10.3%	10.3%
Nwc/Revenue(%)	12.1%	11.7%	8.2%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%
Capex	45.9	53.4	62.5	92.9	98.5	109.4	121.6	134.2	146.9
<i>Change, y-o-y(%)</i>	-30.5%	16.3%	17.0%	48.6%	6.1%	11.0%	11.2%	10.3%	9.5%
Capex/COGS(%)	-2.3%	-2.7%	-2.8%	-3.4%	-3.5%	-3.5%	-3.5%	-3.5%	-3.5%
Capex/Revenue(%)	1.5%	1.7%	1.8%	2.2%	2.2%	2.2%	2.2%	2.2%	2.2%
Free Cash Flow	195.6	223.5	310.2	270.4	262.7	313.0	392.4	471.7	550.2
<i>Change, y-o-y(%)</i>		14.3%	38.8%	-12.8%	-2.9%	19.2%	25.4%	20.2%	16.6%

Table 2

DCF(MSEK)	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	TV
Revenue	3 107.3	3 148.5	3 553.9	4307.7	4 478.6	4 972.1	5 527.7	6 098.7	6 677.1	
EBIT	250.3	278.1	294.9	343.2	361.8	449.4	553.5	651.4	744.9	
Tax	-59.6	-73.8	-64.8	-81.5	-74.0	-93.0	-115.8	-137.2	-157.5	
NOPAT	195.2	216.9	230.0	267.7	282.2	350.5	431.7	508.1	581.0	
D&A	47.7	52.7	63.9	79.6	90.7	103.4	117.8	134.3	153.1	
Free Cash Flow	195.6	223.5	310.2	270.4	262.7	313.0	392.4	471.7	550.2	7 870.2
Discount Period					1	2	3	4	5	5
WACC					9.1%	9.1%	9.1%	9.1%	9.1%	9.1%
Present value of Free Cash Flow					240.7	262.8	301.9	332.6	355.5	5 084.5

Table 3

Nederman Holding (SEKm)	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Total revenue	3 107.3	3 148.5	3 553.9	4307.7	4 478.6	4 972.1	5 527.7	6 098.7	6 677.1
<i>Revenue growth (%)</i>	-2.8%	1.3%	12.9%	21.2%	4.0%	11.0%	11.2%	10.3%	9.5%
COGS	-1 996.3	-1 948.6	-2 227.0	-2 716.4	-2 776.8	-3 082.7	-3 427.2	-3 781.2	-4 139.8
Gross profit	1 111.0	1 199.9	1 326.9	1 591.3	1 701.9	1 889.4	2 100.5	2 317.5	2 537.3
<i>Gross margin (%)</i>	35.8%	38.1%	37.3%	36.9%	38.0%	38.0%	38.0%	38.0%	38.0%
Cost of sales	-648.1	-662.7	-735.2	-828.8	-884.9	-944.8	-1 008.8	-1 077.1	-1 150.0
Administration costs	-209.0	-222.2	-253.0	-342.8	-379.0	-419.1	-463.3	-512.3	-566.4
Research and development	-7.8	-14.2	-44.3	-65.2	-65.0	-65.0	-65.0	-65.0	-65.0
Other external costs	4.2	-22.7	0.5	-26.7	-11.2	-11.1	-10.0	-11.8	-11.0
EBIT	250.3	278.1	294.9	343.2	361.8	449.4	553.5	651.4	744.9
<i>EBIT margin (%)</i>	8.1%	8.8%	8.3%	8.0%	8.1%	9.0%	10.0%	10.7%	11.2%
Net financial expenses	-18.6	-18.0	-26.9	-35.9	-40.0	-45.0	-50.0	-55.0	-60.0
EBT	231.7	260.1	268.0	307.3	321.8	404.4	503.5	596.4	684.9
Tax	-59.6	-73.8	-64.8	-81.5	-74.0	-93.0	-115.8	-137.2	-157.5
Net income	172.1	186.3	203.2	225.8	247.8	311.4	387.7	459.2	527.4
<i>Profit margin</i>	5.5%	5.9%	5.7%	5.2%	5.5%	6.3%	7.0%	7.5%	7.9%