

Swedencare

Sweden | Consumer goods | MCAP 1,4bn

Buy

Target Price SEK 109.00
Current Price SEK 87.00
Upside 25,0%

Plaqueoff, the tail that wags the dog of Swedencare

Swedencare is a company active in the premium pet care segment developing, distributing and selling pet food additives. The main products are aligned within animal oral care with the blockbuster merchandise being the Plaqueoff powder that stands for 70% of sales and has grown 26% yearly since 2016. Plaqueoff reduces animal plaque, tartar, and bad breath. Swedencare is expecting to have a CAGR of roughly 26% to the year 2021.

Upside of 25% in 2020 using a peer average multiple, despite Swedencare being best in class

Swedencare has an upside to peers of 25% using a peer valuation and target multiple of EV/EBIT 36,9 for 2020 whereas Swedencare is trading at a multiple of 27,8. Peer comparison was used to capture a fair valuation compared to market players. The discount indicates a target price of 109SEK.

A streamlined distribution network with centers in 6 countries provide strong cost-efficiency

A key driver to the current success in Swedencare has been the strong distribution channels in the major markets. What the distribution channels have contributed with is higher incremental margin as an effect of the increased margins with boosted sales by cutting out the middleman and going straight to consumers and retailers. The effects can be seen in correlations with previous acquisitions through an increase in EBIT-margin from 20% in 2017 to today's 29%. The final effects lead to the net income growing faster than sales and despite a weaker Q4, 2020 is on track to lead to earnings growth of 24% as opposed to sales growth of 20%.

Market exclusivity lost with patent loss

Swedencare's main challenge for the coming 2 years will be the patent loss of the primary product seller Plaqueoff which stands for 70% of total sales. The patent loss will most likely lead to lesser results as gross margins are likely to be compressed as more competition will enter the niche segment within pet oral care. Swedencare however, are prepared for patent loss with a strong company brand and loyal customer base. Please see Appendix Table 2 for more additional information on customer satisfaction.

Strong financials with Net Debt/EBITDA -1,15x ripe for acquisitions

Swedencare has a solid balance sheet with net cash of 45,7mSEK as per the end of Q3. Resulting in that the company has a Net Debt to EBITDA of -1,15 which enables future acquisitions, with the possibility of raising funds to 124mSEK counting with increasing debt to reach a Net Debt to EBITDA of 2. With the funds opens for the possibility of acquiring new distribution centers or broadening the product portfolio by buying new products. Swedencare has recently acquired a distribution center in Greece and Spain to bolster the region's sales. Future acquisitions of distribution centers in new regions could facilitate stronger sales channels and create cost synergies.

Tom Eriksson
Equity Research Analyst

Market Data

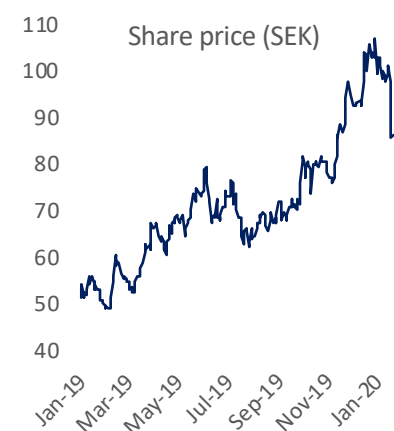
Listing Venue	First North Stockholm
Price (SEK)	87,00
No. of outstanding shares (m)	15,8
Market Cap (m)	1374,6
Net Debt (m)	-45,7
Enterprise Value (m)	1328,9

Key Financials (SEK)

	18A	19A	20E	21E
Sales (m)	99	128	153	177
Sales Growth y/y	16%	26%	19%	15%
Gross Profit	74	93	115	132
Gross Margin (%)	74%	73%	75%	75%
EBITDA (m)	31	40	57	68
EBIT (m)	29,4	37,2	47,8	57,8
EBIT – Margin (%)	30%	29%	31%	33%
Net Income	23,3	30,2	37,4	45,3
Profit Margin (%)	24%	24%	21%	21%

Key Ratios (SEK)

	18A	19A	20E	21E
EV/EBITDA	23,3	33,3	25,3	21,0
EV/EBIT	24,2	35,7	27,8	23,0
Net Debt/EBITDA	-0,64	-0,9	-0,7	-0,6
P/E	31,6	45	36,7	30,4
EPS	1,5	1,9	2,4	2,4



Major Shareholders

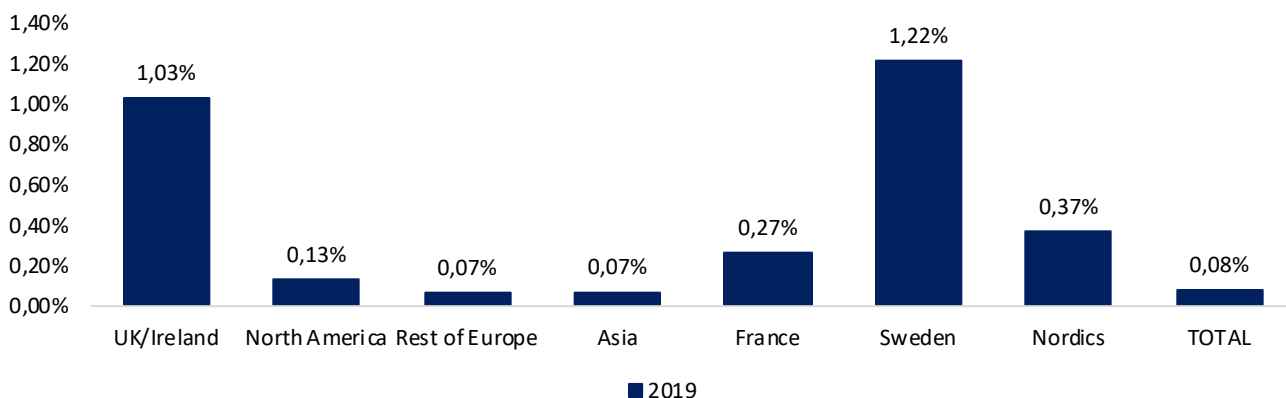
Håkan Svanberg & Co	29,5%
JCC Group Invest	9,8%
DNCA Investments	7,4%
Mastan	7,0%
AMF	4,8%
Total insider	51,95%

Investment thesis

Positive macro trend with CAGR of 6,8% in the pet care sector speaks for Swedencare

Pet ownership is going through a change with an upsurge in humanization of pets by seeing pets as family members, which looking forward will benefit Swedencare. The trend has led to a rise in expenditures to take care of pets. In the US, for instance, pet owners on average spend \$126.19 a month a CAGR of 12% since 2009.¹ The most reoccurring health issue among pets is dental hygiene, with 80% of dogs and 70% of cats developing gum diseases. The underlying CAGR over the next 5 years is expected to be 6.8% with the Asian-Pacific market being the front runner with a growth of 9.3% of the markets followed by Europe at 4,2% and North American at 2,3%. Swedencare has been able to capitalize on the growth, more vigorously than competitors so far with a CAGR of 54% by having a product that is less time consuming while still having similar effects as the most sold products from competitors. Furthermore, market segmentation for dental products such as Plaqueoff powder and other additives take roughly 8% of the total market, with major players mainly focuses on the remaining 92% as the products are more wear and tear. Giving Swedencare more of a niche market with less exposure to bigger companies. Currently sizing out Swedencares market through taking

Chart 2: Regional percentage of cats and dogs Swedencare's product reach

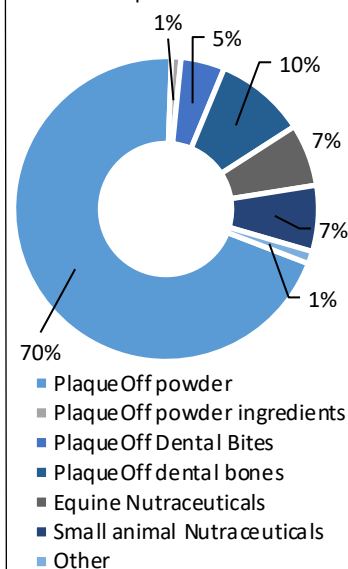


total product sales and periodize usage for a year the total dogs and cats with Swedencare products are 680 000. Out of the total dogs and cats in the world, sales equates to 0,08%. The company has the strongest penetration in the UK, France, and Nordics. However, a relatively small penetration in North America, Asia and the Rest of Europe indicate a continued potential for growth, and with a penetration of 0,5% in these markets, sales would increase 78% with 100Msek. In conclusion, Swedencare has a tailwind looking forward through a positive macro trend.

Maintaining high organic growth in main driver Plaqueoff is key factor for continued the growth

Swedencares plaqueoff will continue to lead the line with continued growth going forward, with Swedencare has broadened the product portfolio through new development and acquisitions. Currently, the majority of sales stem from Plaqueoff powder that currently stands for 70% of total sales. Plaqueoff is through well-developed production able to have a high gross margin of 85% which has been a factor of incremental growth in earning due to company gross margins being 74% therefore with increased sales of the Plaqueoff the earnings growth succeeds sales. Plaqueoff will continue to grow as the product is seen as a market leader in effectivity for dental care with plaque reduction of 35% and is the only powder approved by the Veterinary Oral Health Council. The preceding will lead to a boost in earnings growth due to sales increase and gross margin improvement resulting in 3% CAGR to the year 2021.

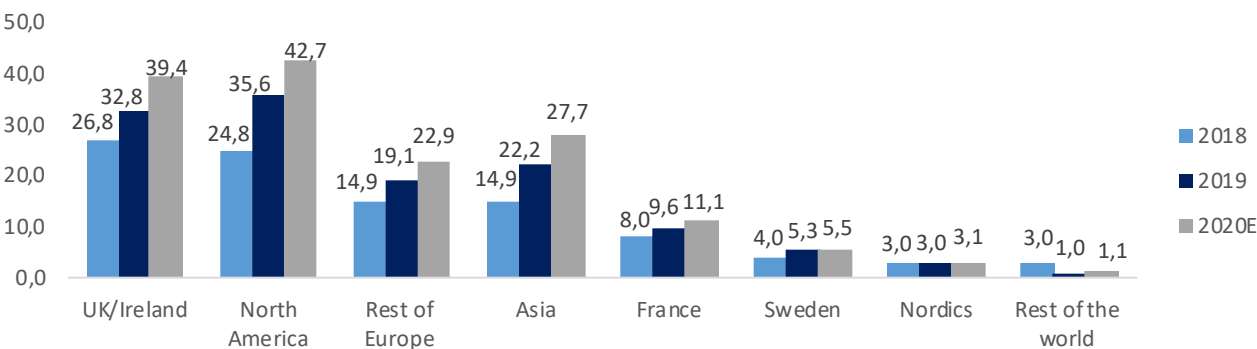
Chart 2: Percentage of sales each Swedencare product stands of total



Westernization in Asian markets to create further growth opportunity in the region

Looking forward the Asian-Pacific region will be the fast-growing market for Swedencare. The Asian-Pacific region is continuing to show momentum with record deliveries with 16,7mSEK in sales for Q1 to Q3 leveling the whole year of 2018. The past 3 years have seen annual growth in sales of 37% which can be replicated in the future. Since, Asia as a market has been tough to penetrate for other nutraceutical companies, as consumer culture is different due to brand awareness not being as important as in the West, were instead function and service is key. Swedencare has been able to combat the difference by increasing exposure at resellers by educating on the products through store visits. Furthermore, Swedencare aims to further increase exposure by launching market-specific products and increase partnership with distribution centers to create a more personal relationship. The estimated potential of the market would lead to an earnings boost of 6% CAGR to the year 2021.

Chart 2: Swedencare’s geographical distribution (MSEK)



Swedencare’s products spotlighted with Amazon partnerships in Europe, expected to increase sales CAGR by 6%

Swedencare has through a partnership with Amazon in European countries increased product exposure. During Q3 Swedencare signed a direct agreement with Amazon in Italy over a distribution line through Amazon warehouses where stock is refilled weekly, resulting in a sales growth of 0.5mSEK in the region a 100% increase. Further agreement have been reached during the start of Q4 by Amazon UK, France, and the USA have initiated a promotional campaign of Swedencare products by labeling select products under Amazon Choice. Currently, Plaqueoff is topping the lists in overall pet care selling products in both the UK and France from previously being around 40. When putting the ranking increase in the Amazons pet care section to a sales estimator the boost in sales that the agreement is expected to produce results in an accumulated earnings boost of 6%.

Despite small size, Swedencare’s World Wide distribution centers allows them to compete with the big players

Swedencare has through a widespread distribution network, with in-house sales, distribution and logistics teams in major markets been able to exceed the growth of companies with the same scale. During the second and third quarter, additional channels have been added through acquisitions in Greece and Spain, both of which have so far affected the income statement negatively as adapting to market through streamlining and retail connections have not been implemented yet. From the fourth quarter and forward the increase in margins will be seen from the acquisitions due to market adaption. Furthermore, Swedencare has a strong balance sheet that allows for further acquisitions to create more operational cost control in more regions and increasing sell channels additionally. In conclusion with continued streamlining in current distribution centers, Swedencare will have an elevating effect on margins.

Valuation

The peer analysis indicates an upside of 25% for the year 2020

The valuation is based on a peer analysis within the pet care and food segment. The focus when picking peers is by choosing competitors that have gone through a period of high growth, so the peers chosen have either gone through similar growth stories or are in a slower-growing mature state. The challenges when picking out peers are finding ones that are of a relative size. Companies that are direct competitors with similar products are smaller in size and are not listed, not giving any basis for comparison. The companies chosen are therefor operating within the pet care segment that have sales in the dental care and have a market capitalization higher than Swedencare.

Table 1: Swedencare vs peers' valuation and performance

Peer valuation	Mcap Tmsek	Ev/Ebit		CAGR (19-21e) EBIT	EBIT margin	
		2019E	2020E		2019E	2020E
Zoetis	575,9	28,1	32,0	5%	37,4%	39,0%
Elanco	97,3	69,0	24,9	11%	19,6%	21,4%
Dechra	32,7	80,4	23,8	14%	26,4%	26,2%
Fresh Pet	17,8	N/A	66,8	102%	1,1%	9,4%
Mean	180,9	59,2	36,9	33%	21%	24%
Diff avg	179,4	-40%	-25%	-7%	10,3%	10,1%
Swedencare	1,5	35,7	27,8	26%	31,4%	34,1%

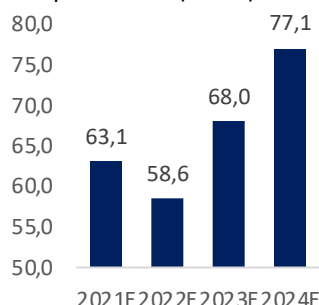
Swedencare's revenue is expected to grow 17% CAGR based on increased sales through Amazon partnership and the Asian market growth. The EBIT is expected to grow 26% CAGR succeeding revenue growth due to driving factors of increased gross margins through increased sales from Plaqueoff and cost optimizing through streamlined distribution channels.

Based on the preceding drivers Swedencare is trading at an EV/EBIT of 27,8x 2020E, implying a discount of 25% to peers, moreover, looking at future growth the median peer has an EBIT growth of 12% opposed to Swedencare at 26% which further would justify a premium valuation. However, with the market capitalization of peers being at a value above Swedencare along with the future patent loss multiple higher than peers is not warranted. The peer means EV/EBIT of 36,9 will hence be the target multiple leading to a target price of 109SEK a total shareholder return of 25%.

Risks

Potential risk is Swedencare's dependency on PlaqueOff powder, where the patent expires in 2021 for the product's major markets, possibly resulting in lower gross margins as a result. When adjusted to the sectors average gross margin of 65%, Swedencare's EBIT would take a 10% drop from 2021 to 2022 and from there on having a CAGR of 16% to the year 2024. Whereas with retained gross margins of 75% the CAGR after the patent loss would generate a 26% CAGR. Further uncertainties are with the history of M&A, as the strong cash position could lead to a risk of unbeneficial acquisitions of new products and distribution centers bought to inflated multiples.

Chart 3: Swedencare's future EBIT result with contracted Gross margins resulted by patent loss (MSEK)



Msek	Historical							Estimates	
Fiscal year	2017	2018	2019	q1 2019	q2 2019	q3 2019	2019E q4	2019	2020E 2021E
Net sales	85,5	99,1	30,6	30,4	31,8	34,1	126,8	153,3	176,6
Others operating income	0,2	0,3	0,0	0,1	0,0	0,0	0,1	0,3	0,4
Revenue	85,7	99,4	30,6	30,5	31,8	34,1	126,9	153,6	177,0
COGS	21,9	25,6	7,3	8,6	8,4	9,6	33,8	38,3	44,2
Gross profit	63,7	73,8	23,3	21,8	23,4	24,5	93,0	115,0	132,5
OPEX									
Personnel costs	21,7	23,5	6,6	7,0	6,6	8,2	28,4	29,5	31,3
Other external costs	18,5	20,5	5,8	5,7	5,5	8,1	25,1	27,6	31,8
EBITDA	22,8	30,6	11,4	9,4	11,8	8,2	39,9	57,0	68,4
Other operating expenses	0,8	-0,8	-0,6	-0,2	-0,5	0,9	-0,3	0,9	1,0
Depreciation	6,1	1,1	0,7	0,7	0,8	0,7	3,0	3,8	4,4
EBIT	16,7	29,4	10,7	8,6	11,0	6,6	37,2	52,3	63,0
Interest Income	0,0	0,0							
Financial Expenses	0,5	0,3	0,1	0,1	0,0	0,1	0,3	0,4	0,5
EBT	16,2	29,1	10,6	8,6	11,0	6,5	37,0	51,9	62,5
Tax expenses	4,4	5,8	2,1	1,8	2,1	0,8	6,8	10,9	13,1
Net income	11,8	23,3	8,5	6,8	8,9	5,7	30,2	41,0	49,4

Outstanding shares 15,6 15,6 15,8 15,8 15,8 15,8 15,8 15,8 15,8 15,8

EPS 0,76 1,49 0,54 0,43 0,56 0,36 1,91 2,37 2,87

Growth rates & margins

Revenue growth	59%	16%	-85%	-1%	5%	7%	28%	21%	15%
Gross margin	74%	74%	76%	72%	74%	74%	73%	75%	75%
EBIT growth	47%	76%	-80%	-19%	27%	-40%	27%	28%	21%
Ebit margin	20%	30%	35%	28%	35%	19%	29%	31%	33%
Profit margin	14%	24%	28%	22%	28%	17%	24%	24%	26%
Net income growth	21%	97%	-79%	-20%	31%	-36%	29%	24%	21%

Table 2: Swedencare vs competing products

Brand	Company	Rating out of 5	Number of reviews	Ranking Dog Oral Care Supplies Amazon
Plaqueoff powder	Swedencare	4,5	2,826	#1
Plaqueout	Multi-Mite	4,4	139	#10
Plaquepro	Pet Purest	4,3	332	#54
All natural plaque clean	The Healthy Dog co	4,2	36	#19
Plaque Banish	My waggy tails	4,2	13	#79
Plaque X	Paw Origins	4,4	1140	#8

Sources:

- <https://www.bls.gov/opub/btn/volume-2/spending-on-pets.htm>

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