

# Transtema

Sector: Communication Services

## Strong Momentum in Several Areas

Redeye strengthens its positive view on Transtema following a Q2 report with strong organic and acquired growth and solid margins. Also, the acquisition and deal completed during this summer strengthen Transtema's growth prospects.

### Solid Beat

Sales beat our forecast by 10%, following stronger than expected organic (9.4% y/y) and acquired growth. EBITA was SEK 49m (36.5), beating our estimated 18%. While declining somewhat from the very strong levels seen in Q2 2021, the EBITA margin reached a solid 7.9%, beating our forecast of 7.3%. Also, in conjunction with the report, Transtema raised its EBITA margin target to >7% (>5%). Considering the average EBITA margin of 7-8% since 2021, we believe the new target is more appropriate, but it also implies that management believes a level above 7% is sustainable.

### Future Growth Areas Gaining Momentum

During the summer, Transtema has strengthened its presence within both EV-charging and proptech, following the acquisition of North Projects and the deal with Proptivity. While we expect both to have a limited impact on sales near-term, we are encouraged to see Transtema adding new revenue streams, providing growth opportunities and diversification.

### New Base Case SEK 50 (48)

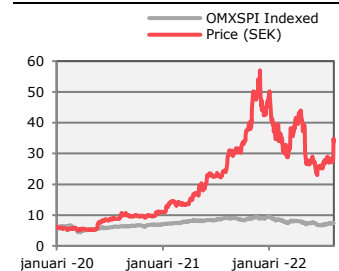
We raise our forecasts and Base Case slightly. The solid organic development and the robust momentum in Tessta combined with the acquisition and deal mentioned above, Q2 strengthens our outlook for Transtema and its share.

Key Financials (SEKm)	2020	2021	2022E	2023E	2024E
Sales	1405	1690	2210	2373	2445
Sales growth	-6%	20%	31%	7%	3%
EBITA	42	137	157	184	188
EBITA Margin (%)	3.0%	8.1%	7.1%	7.8%	7.7%
EV/Revenue			0.7	0.6	0.5
EV/EBITA			9.5	7.3	6.3

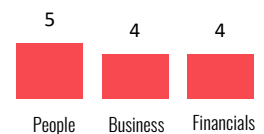
### FAIR VALUE RANGE

BEAR	BASE	BULL
26	50	63

### TRANS VERSUS OMXS30



### REDEYE RATING



### KEY STATS

Ticker	TRANS
Market	Small Cap
Share Price (SEK)	33.88
Market Cap (SEKm)	1322
Net Debt (SEKm)	44
Free Float (%)	65%
Avg. daily volume ('000)	3 220

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## Strong Organic and Acquired Growth

	Q2E 2022	Q2A 2022	Diff	Q2A 2021	Q1A 2022
<b>Revenues</b>	<b>566.6</b>	<b>623.9</b>	<b>10.1%</b>	<b>448.1</b>	<b>444.6</b>
Y/Y Growth (%)	26%	39%		30%	15%
<b>EBITA</b>	<b>41.6</b>	<b>49.0</b>	<b>17.9%</b>	<b>36.5</b>	<b>20.4</b>
EBITA Margin (%)	7.3%	7.9%		8.2%	4.6%
<b>EPS</b>	<b>0.66</b>	<b>0.89</b>	<b>34.0%</b>	<b>0.50</b>	<b>0.29</b>

Source: Transtema & Redeye Research

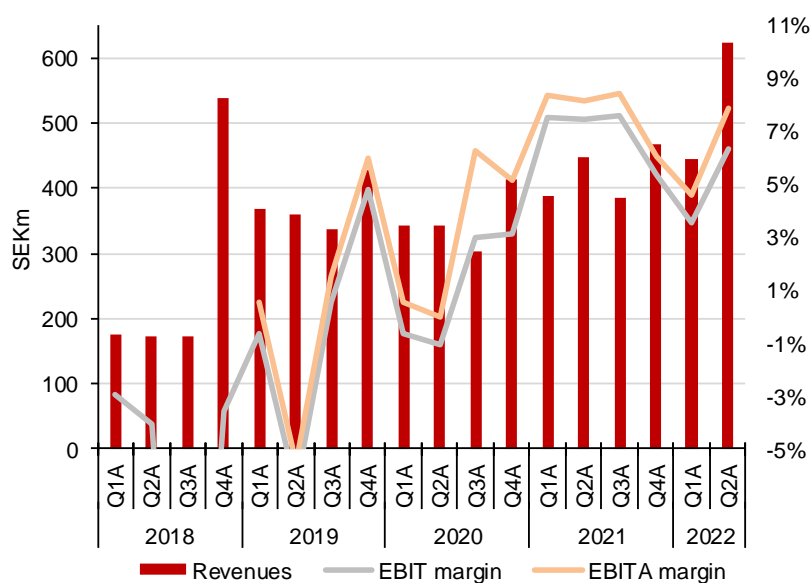
Sales beat our forecasts by 10%, following strong organic growth of 9.4%. Our forecast was 3% organic growth. Besides the stronger-than-expected organic growth, the contribution from the recently acquired Tessta was higher than we expected. While price increases had a slightly positive impact on organic growth, higher volumes were the main driver. For a company like Transtema, mostly active in mature markets, we believe the 9.4% organic growth is impressive. While Transtema had an even higher organic growth in 2021, that was due to some large contracts. We believe this is more broad-based.

EBITA was SEK 49m (36.5) (including SEK 2m in a positive one-off), beating our estimates by 18%. The EBITA margin was 7.9% (8.2), corresponding to a significant increase from 6.4% (adjusted) in Q1. While increasing energy and fuel costs still had a negative effect, the impact is smaller in Q2 relative to Q1 as Transtema has managed to pass on some costs, and considering that Transtema has some very large customers, particularly Telia, some lead time for cost compensation is expected.

According to management, Tessta has solidly started 2022 with a substantial increase in sales y/y, relative to Covid-19 affected levels last year. The numbers in Q2 support the statement. Interestingly, some Swedish customers are already using Tessta for its Norwegian operations. As Transtema has a few large customers with operations in both countries, we assume some part or parts of Telia are among those.

The order backlog is strong and considering the recent EV-charging-related acquisition and the deal with Proptivity, Transtema has taken several steps that should drive growth and make Transtema a more diversified business over the next years.

## Revenues, EBITA- and EBIT margin



After a softer Q1, hurt by fuel costs and M&A costs, the EBITA margin had a solid rebound in Q2, in line with the strong levels seen in 2021. This should, which also seems to be the case considering the massive positive share price reaction on the Q2 report, suppress worries that 2021 was a one-hit-wonder. The raised EBITA target to >7% supports that view as well.

### Raised EBITA Margin Target

In conjunction with the report, Transtema raised its EBITA margin target to >7% (>5). While we believe >5% has been very defensive following the strong margin levels seen since 2021, we are encouraged to see management aiming for a level in line with our forecasts. We forecast about 7-8% EBITA for both the short- and long-term. As for the >5% target, we believe this should be viewed as a lower bound for full-year margins (some quarters could probably see lower levels occasionally), given the business performs reasonably in line with management's ambitions. However, >7% is a high level for the industry. Among listed Nordic peers, the average EBITA margin is ~4%, with some companies with ~7% and a few that are barely profitable.

### Proptech-deal with Significant Potential

(From our Note June 17)

In mid-June Transtema announced a deal with Proptivity, regarding installing, operating, and maintenance of indoor 5G solutions in Sweden. The deal spans 15 years (with an option to extend for years 2 at a time), and the expected value for the operation and maintenance parts is estimated to be SEK 150m. While Transtema cannot estimate the installation part at this point, Ericsson and Proptivity plan to invest SEK 3bn within five years in the Nordics and Baltics. Thus, if Proptivity, with its partner Ericsson, is successful, the potential is vast, only counting Sweden. However, we would not rule out Transtema being involved in other markets as well, Norway especially.

While Proptivity is a recently founded business and its technology is new, it is backed by real estate and infrastructure investors Stronghold Invest and Niam, and the deal and roll-out plan with Ericsson suggest Proptivity's offering is competitive. Proptivity's offering enables operator-independent 5G solutions for indoor environments, typically shopping malls. 5G has

a limited indoor reach compared to 4G, making outdoor solutions targeting indoor areas, malls, for example, inefficient. With Proptivity's solutions, the real estate owner makes one investment that every operator can use, enabling high-speed internet to visitors and tenants.

The deal is a solid data point that strengthens our view on Transtema's proptech initiatives and has the potential to make a substantial sales contribution over the next years. Also, the deal improves Transtema's diversification, reducing its dependence on Telia and copper. While the deal value is unclear at this point, the deal with Proptivity is at least important from a strategic perspective.

## Strengthening within EV-Charging

*(From our Note July 4)*

Last Friday, Transtema announced the acquisitions of North Projects, a company founded in 2016, focusing on infrastructure for EV-Charging, including installation, operations, service & maintenance, and payment/cloud solutions. North Projects' current CEO and former main owner, Marcus Andersson, will remain in charge of operations.

In 2021, the company had sales of SEK ~30m (~1.5% of Transtema's sales) and based on historical profitability levels; we believe its margins are about zero. While North Projects' current sales and profit contribution is limited, EV-Charging is one of Transtema's potential growth areas, and likely the most interesting one. Several drivers are pushing the use of electric vehicles in Sweden (in July, 32% of all new cars were BEVs), including:

- Substantial price increases in fossil fuels like petrol and diesel
- Bonus/Malus putting heavy taxes on new petrol/diesel cars and subsidizing BEVs

Also, recently the European Union voted to ban new petrol- and diesel cars 2035. Thus, we believe there are a lot of factors suggesting that the EV-Charging market will become huge. In addition, a quick read in any motor journal tells that the current EV-charging infrastructure is insufficient.

North Projects adds know-how and resources that Transtema can scale within its nationwide organization. While North Projects have mostly served smaller B2B customers and tenant owners' associations, as a part of Transtema Group, the company is backed by a large nationwide organization with financial power.

We believe the combined offering strengthens Transtema's EV-Charging offering, which should be especially interesting to larger B2B customers with offices all over Sweden and large rental housing owners with multi-city presence. In other words, a customer that needs service and maintenance (installation as well but the recurring revenue from service and maintenance is the most interesting) of many EV-Chargers in different geographical areas.

While the purchasing price is not disclosed, as Transtema previously has stated, it passed on highly-priced EV-Charging-related potential acquisition targets, we believe the price is at least reasonable. We believe the solid match between the companies and the fact that Transtema has known North Projects' management for years also support our view.

## Financial Forecasts

We raise our sales and EBITA forecasts for 2022E and 2023E by about 6%, mainly due to strong organic growth and impressive development in the recently acquired Tessta. We do not expect any material contribution from the Proptivity deal in 2022. We assume a gradual ramp-up starting in 2023 at levels far below the potential deal value at this early point.

Estimate Revisions	FYE 2022	Old	Change	FYE 2023	Old	Change
<b>Revenues</b>	<b>2 210.1</b>	<b>2 100.7</b>	<b>5.2%</b>	<b>2 373.3</b>	<b>2 245.4</b>	<b>5.7%</b>
Y/Y Growth (%)	57.3%	49.5%		7.4%	6.9%	
<b>EBITA</b>	<b>156.8</b>	<b>146.1</b>	<b>7.3%</b>	<b>184.1</b>	<b>174.7</b>	<b>5.4%</b>
EBITA Margin (%)	7.1%	7.0%		7.8%	7.8%	
EPS	2.15	2.29	(6.3%)	2.70	2.84	(4.9%)

Source: Transtema & Redeye Research

In 2022 and onwards, we expect a few percent organic growth per annum and EBITA margins somewhat below 8%. However, we do not assume any material investments in or sales from new areas such as EV-charging, despite the acquisition of North Projects, which is currently a small part of Transtema. If Transtema is successful in its greenfield investment, we would likely see lower margins short-term in exchange for higher growth and possibly margins long-term.

Income Statement	2021	2022Q1	2022Q2	2022Q3	2022Q4	2022	2023	2024
<b>Revenues</b>	<b>1 690</b>	<b>445</b>	<b>624</b>	<b>529</b>	<b>613</b>	<b>2 210</b>	<b>2 373</b>	<b>2 445</b>
Y/Y Growth (%)	20.3%	14.6%	39.2%	36.7%	31.2%	30.8%	7.4%	3.0%
Cost of Revenues	(578)	(170)	(302)	(242)	(281)	(995)	(1 066)	(1 105)
<b>Gross Profit</b>	<b>1 112</b>	<b>274</b>	<b>322</b>	<b>286</b>	<b>332</b>	<b>1 215</b>	<b>1 307</b>	<b>1 340</b>
Gross Profit Margin (%)	65.8%	61.7%	51.6%	54.2%	54.2%	55.0%	55.1%	54.8%
Other external costs	(215)	(61)	(65)	(63)	(65)	(254)	(261)	(266)
Personnel expenses	(697)	(176)	(194)	(162)	(200)	(731)	(780)	(800)
Other operation income	3	1	6	1	1	8	2	2
<b>EBITDA</b>	<b>202</b>	<b>38</b>	<b>70</b>	<b>62</b>	<b>68</b>	<b>239</b>	<b>268</b>	<b>275</b>
EBITDA Margin (%)	12.0%	8.7%	11.2%	11.8%	11.1%	10.8%	11.3%	11.3%
Depreciation	(65)	(18)	(21)	(21)	(21)	(82)	(87)	(88)
<b>EBITA</b>	<b>137</b>	<b>20</b>	<b>49</b>	<b>41</b>	<b>47</b>	<b>157</b>	<b>181</b>	<b>188</b>
EBITA Margin (%)	8.1%	4.6%	7.9%	7.7%	7.6%	7.1%	7.6%	7.7%
Amortization	(13)	(5)	(9)	(9)	(9)	(32)	(38)	(38)
<b>EBIT</b>	<b>124</b>	<b>16</b>	<b>40</b>	<b>32</b>	<b>37</b>	<b>125</b>	<b>144</b>	<b>150</b>
EBIT Margin (%)	7.4%	3.5%	6.4%	6.0%	6.1%	5.6%	6.1%	6.1%
Interest Expenses	(10)	(3)	(9)	(3)	(3)	(18)	(12)	(12)
<b>EBT</b>	<b>114</b>	<b>14</b>	<b>42</b>	<b>29</b>	<b>34</b>	<b>106</b>	<b>132</b>	<b>138</b>
Income Tax Expenses	(23)	(3)	(9)	(6)	(7)	(22)	(27)	(28)
Effective Tax Rate (%)	20.6%	20.6%	21.8%	20.6%	20.6%	20.6%	20.6%	20.6%
Non-Controlling Interests	1	0	0	-	-	1	-	-
<b>Net Income</b>	<b>91</b>	<b>11</b>	<b>36</b>	<b>23</b>	<b>27</b>	<b>85</b>	<b>105</b>	<b>110</b>
Net Income Margin (%)	5.4%	2.5%	5.7%	4.3%	4.5%	3.8%	4.4%	4.5%

Source: Transtema & Redeye Research

## Investment Case

### Transtema 2.0

Following a few years with frequent acquisitions and focus mainly on Fiber-To-The-Home (FTTH) construction which ended badly, Transtema has reshaped its business, concentrating on the stable operations and maintenance market. Recent country-wide contracts with Telia and 3GIS, combined with impressive margin development in the last three quarters, indicate that the renewed strategy is a success. In addition to so far generating solid profits, the new focus has several advantages. ~70% of Transtema's revenues are recurring and, thus, independent of investments in new FTTH/B, which significantly increases the predictability and duration of its revenues. In the mean time, Transtema has improved its working capital substantially, now hitting negative net levels. We believe the market has not yet fully priced in Transtema's transformation to a stable and profitable company.

### Scale Advantages

While Transtema is a personnel-dependent service business without substantial intangible assets, we believe the company has durable competitive advantages. Considering the importance of reliable communication networks and the limited acceptance for downtime, reaching all populated Sweden fast is vital – especially for large country-wide contracts.

Established in 85 locations and with ~900 technicians, Transtema reaches all populated Sweden in an hour. Establishing a similar organization is a substantial investment and a significant deal, like Transtema's Telia and 3GIS (Telenor and 3) deals, is probably necessary to justify running operations in all of Sweden. Thus, we believe market characteristics limit the risk of new players entering the market, which should support Transtema's long-term profitability. Also, we believe Transtema's nationwide organization can handle increasing volumes at limited cost increases, paving the way for higher margins if signing new substantial deals.

### Demand for Availability and Reliability

Several structural trends, like digital health services, autonomous driving, the internet of things, and decentralized working, are driving demand for increased availability and reliability of communication networks. The acceptance for downtime is gradually decreasing as internet access is becoming increasingly vital for consumers and businesses alike and, going forward, unacceptable in some cases. We believe Transtema's services' rising importance will drive growth and reduce price pressure, as we assume network owners favor quality and comprehensive Service Level Agreements (SLA).

## Counter-Thesis

### Significant Customer Concentration

While including several different areas and contracts, Telia represents ~65% of Transtema's revenues. We believe that is a significant customer concentration, which increases the risk in Transtema's operation. However, Transtema is simultaneously a vital supplier to Telia's Swedish operations. While substantial customer concentration tends to cause price pressure, considering the importance of reliable networks, we believe it is in Telia's interest not to squeeze its suppliers. Especially not the larger ones, like Transtema with its nationwide capabilities.

### Exposure to Legacy Technology

During the next 5-10 years, copper will gradually be phased out. Considering that Transtema generates ~35% of its sales from copper-related contracts, we expect a negative sales growth impact of about 5% annually. However, as copper is phased out, the fiber market expands, and 5G opens new growth opportunities. While there are several opportunities to compensate the lost copper business, it is usually harder to gain new business than defending current contracts. Also, technical shifts are a natural part of the communication network market and, thus, something businesses in the sector must handle.

## Valuation

### Bear Case 26 SEK

- Sales CAGR of ~2% 2020-2030
- No future M&A
- Terminal growth of 2%
- Average EBITA margin of ~5% 2021-2030
- Terminal EBITA margin of ~4%

### Base Case 50 SEK

- Sales CAGR of ~3% 2020-2030
- No future M&A
- Terminal growth of 2%
- Average EBITA margin of ~7.8% 2021-2030
- Terminal EBITA margin of ~7.5%

### Bull Case 63 SEK

- Sales CAGR of ~4% 2020-2030
- No future M&A
- Terminal growth of 2%
- Average EBITA margin of ~9% 2021-2030
- Terminal EBITA margin of ~8.5%

We increase our Base Case slightly to SEK 50 (48) following raised forecasts.

Also, note that Transtema has few institutional investors despite a market cap approaching SEK 1.5bn. The transformed Transtema has many features that we believe institutional investors find attractive, such as non-cyclical recurring revenue streams and a genuine commitment to ESG.

## Peer Valuation

Transtema is trading at a discount to peers for 2023E. Also, its margins are the highest, and it has a solid track record since its transformation. Thus, we believe a premium is motivated, and our Base Case of SEK 50 equals ~10x EBITA 2023E.

Company	EV	Sales			EV/SALES			EV/EBITA (x)			Sales growth			EBITA margin		
	(SEK)	20A	21A	22E	23E	21A	22E	23E	21A	22E	23E	21A	22E	23E		
Eitel	1 253	8 242	0.2	0.2	0.2	9.4	5.8	4.6	-16%	-1%	1%	1.6%	2.6%	3.3%		
Bravida	20 170	21 724	0.9	0.9	0.8	14.4	12.9	12.1	3%	7%	4%	6.5%	6.7%	6.8%		
Caverion	7 847	2 140	0.3	0.3	0.3	14.3	11.3	9.5	-1%	6%	4%	2.4%	2.8%	3.2%		
Enersense	1 002	235	0.4	0.4	0.4	16.6	8.1	7.0	59%	6%	3%	2.4%	4.6%	5.2%		
Netel	1 798	2 420	0.7	0.6	0.5	10.3	7.2	6.3	n/a	32%	13%	7.2%	7.8%	7.9%		
<b>Median</b>	<b>4 550</b>	<b>5 191</b>	<b>0.4</b>	<b>0.3</b>	<b>0.3</b>	<b>14.4</b>	<b>9.7</b>	<b>8.2</b>	<b>1%</b>	<b>6%</b>	<b>4%</b>	<b>2.4%</b>	<b>3.7%</b>	<b>4.2%</b>		
<b>Average</b>	<b>7 568</b>	<b>8 085</b>	<b>0.5</b>	<b>0.4</b>	<b>0.4</b>	<b>13.7</b>	<b>9.5</b>	<b>8.3</b>	<b>11%</b>	<b>5%</b>	<b>3%</b>	<b>3.2%</b>	<b>4.2%</b>	<b>4.6%</b>		
<b>Transtema</b>	<b>1 492</b>	<b>1 405</b>	<b>0.8</b>	<b>0.7</b>	<b>0.6</b>	<b>9.5</b>	<b>9.5</b>	<b>7.3</b>	<b>20%</b>	<b>31%</b>	<b>7%</b>	<b>8.1%</b>	<b>7.1%</b>	<b>7.8%</b>		

Source: Redeye, FactSet

## 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 points. The maximum score for a valuation key is 5 points.

### Rating changes in the report: None

#### **People: 5**

Transtema receives the highest rating for People for several reasons. First, we believe management has relevant experience and a solid understanding of the market. Second, following operational and financial issues, its management has reshaped the business to profitability. Third, insiders, such as former CEO and current chairman Magnus Johansson, own a substantial share of Transtema. Fourth, we believe that management's communication is balanced and realistic.

#### **Business: 4**

Transtema receives a high rating for Business for several reasons. First, the group gets most of its revenue from operations, services, and maintenance, and ~70% is recurring. Second, the limited acceptance for downtime makes Transtema's services vital to its customers. Third, Transtema has established nationwide operations with ~900 technicians and a presence in ~85 locations, implying significant investments for new entrants

#### **Financials: 3**

Transtema receives an average rating for Financials. Recent improvements in organic growth, margins, and cash flow increase the rating, while weak performance a few years ago is working oppositely. Given that Transtema can preserve its recent improvements in margins, which we find likely, Transtema is heading for a higher rating over the coming years.



## 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

### Important information

Redeye AB ("Redeye" or "the Company") is a specialist financial advisory boutique that focuses on small and mid-cap growth companies in the Nordic region. We focus on the technology and life science sectors. We provide services within Corporate Broking, Corporate Finance, equity research and investor relations. Our strengths are our award-winning research department, experienced advisers, a unique investor network, and the powerful distribution channel redeye.se. Redeye was founded in 1999 and since 2007 has been subject to the supervision of the Swedish Financial Supervisory Authority.

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### Redeye Rating (2022-08-13)

Rating	People	Business	Financials
5	32	15	4
3-4	157	139	48
0-2	5	40	142
<b>total</b>	<b>194</b>	<b>194</b>	<b>194</b>

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### CONFLICT OF INTERESTS

Fredrik Nilsson owns shares in the company : No

Jacob Svensson 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.