

COMPANY UPDATE

Kontron

Buy

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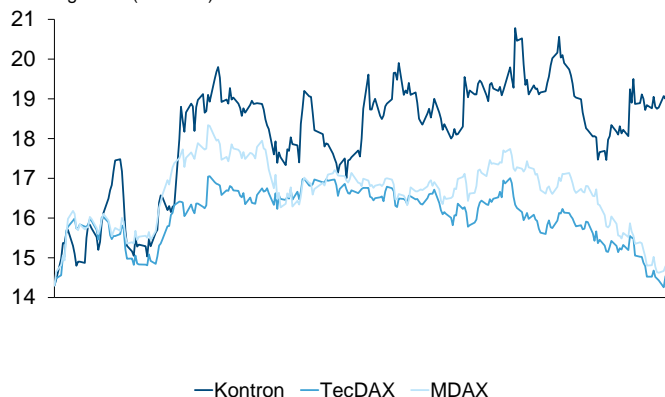
Share price (EUR) close as of 03/11/2023	20.3	Reuters	KTN.DE	Free float	65.7%
Number of shares (mn)	64.3	Bloomberg	KTN GY	Shareholders	Ennoconn (27.3%)
Market capitalization (EUR mn)	1,303.2	Div. Ex-date	29/05/23	Management	(6.4%)
Enterprise value (EUR mn)	1,169.2	Target price	26.5	Homepage:	www.kontron.com

Key figures Overview

EUR mn	2022	2023e	2024e	2025e
Net sales	1,096.1	1,240.3	1,467.7	1,633.5
EBITDA	70.0	137.7	163.3	193.2
EBIT	-2.0	92.7	112.7	142.9
EBT	-10.7	85.4	107.2	137.6
Net profit	232.5	73.6	89.3	110.6
EPS (EUR)	3.65	1.16	1.43	1.77
CEPS (EUR)	4.70	1.87	2.24	2.55
BVPS (EUR)	9.96	9.88	10.73	11.79
Dividend/Share (EUR)	1.00	0.58	0.71	0.88
EV/EBITDA (x)	11.17	8.49	6.64	5.35
P/E (x)	4.19	17.39	14.22	11.48
P/CE (x)	3.25	10.84	9.03	7.93
Dividend yield (%)	6.54	2.86	3.50	4.34
EBITDA margin (%)	6.25	10.91	10.94	11.64
Operating margin (%)	-0.18	7.34	7.55	8.61
Net profit margin (%)	-1.15	5.82	6.10	6.80

Trading data & Statistics

Daily averages	5 days	30 days	last year
Volume	148,518	89,192	76,951
Trading value (EUR mn)	2.9	1.7	1.4



Price performance:	1M	3M	6M	12M
in EUR	11.9%	-2.5%	15.4%	41.7%

Financial Strength

	2022	2023e	2024e	2025e
ROE (%)	44.18	11.66	13.62	15.44
ROCE (%)	-0.48	16.29	18.80	23.22
Equity ratio (%)	44.12	46.95	50.35	50.73
Net debt (EUR mn)	-192.94	-123.30	-210.65	-263.36
Gearing (%)	-30.35	-19.52	-30.63	-34.76

Outperformance continues

The strong order intake in 3Q23 significantly improved visibility towards 1H/FY24 and again witnessed Kontron outperforming its peers with its niche-market focus. We confirm our Buy call and lift our target price to EUR 26.5, from EUR 25.

Book-to-Bill (B2B) in 3Q23 was at 1.19x and YTD at 1.23x, significantly above its peers Advantech and HMS, which have posted a B2B significantly below 1 in 3Q23 and YTD.

Revenue and profitability continued to climb in 3Q23, despite some dilutive effects from two out of five announced acquisitions in the course of 2H23. There has been a first indication that industrial digitalization demand could start picking up again in 2Q24e.

FY23 guidance was increased on the net profit level to at least EUR 72mn (from EUR 66mn), still looking to maintain a conservative touch. Revenue is guided at above EUR 1.2bn, EBITDA at 11%.

We gained more confidence that Kontron can weather the current economic slowdown and regard its valuation at 8.5x and 17.4x for FY23 or 5.3x and 11.6x for FY25 on EV/EBITDA and P/E, respectively, as attractive. These ratios imply discounts to peers of 30-60%. Decreasing inflation/long-term yields should bring support as well.

Change in estimates following 3Q23

We remain slightly above Kontron's FY23 guidance of EUR 1.2bn in revenue, 11% or EUR 132mn in EBITDA and EUR 72mn in net profit. Despite the favorable order intake, assumptions for FY24 and beyond remain unchanged, which we believe represents a reasonable view at this time, subject to adjustments once the pending acquisition targets materialize and growth for IOT solutions resumes.

The impact from the first consolidated acquisitions of the Cellular automotive module unit from Telit and Comlab in 3Q23 were minor on revenue (about EUR 30-40mn) and dilutive on the profitability level (EBIT margins at low single-digit%, at best). Somewhat more prominent was the impact from the acquisitions on order intake, as their entire order books of some 30-40% of annual revenue (our guess), hence about EUR 40-55mn, were included fully in 3Q23. On the other hand, the cancellation of a EUR 15mn order related to a US client going Chapter 11 reduced the organic order intake in 3Q23. Consequently, we assume an order intake of some EUR 320-335mn, better displaying the market demand for Kontron's products. Such an intake still reflects a B2B of 1.07-1.12 for 3Q23 or 1.18-1.2x YTD and confirms Kontron's outperformance vs. its peers. Taking Advantech as one of Kontron's closest peers, we see that it displayed a B2B of 0.82x in 3Q23 and 0.8x YTD. HMS Networks even slipped to B2B of 0.62x and 0.83x, respectively.

For 4Q23, we could again expect some tailwind on order intake / book upon the expected closing of Hartmann, Altimate and BSQUARE. The latter might take a bit longer, though. We estimate the combined revenue of the three mentioned companies at about EUR 50-60mn p.a. Hence, order intake could be boosted by some EUR 20-30mn, as a best guess.

In general, we should expect 4Q to contribute about 30% of annual revenue. It is difficult to assess how profitability will develop this year, in contrast to previous quarters, as this is the first year after the IT services disposal to Vinci, so there is little cross-read from past years. We have assumed a flat EBITDA margin q/q.

Our estimates remain shy of Kontron's FY25 guidance of EUR 2bn in revenue and a 13% EBITDA margin. While the latter should be in the cards without further acquisitions, some EUR 200-300mn in acquired revenue will be necessary to reach the targeted level.

Change in estimates

Cons., IFRS (EUR, mn)	2023e			2024e			2025e		
	Now	Before	Change	Now	Before	Change	Now	Before	Change
Net Sales	1,240.3	1,241.5	-0.1%	1,467.7	1,471.5	-0.3%	1,633.5	1,640.2	-0.4%
EBITDA	137.7	136.4	0.9%	163.290	165.4	-1.2%	193.2	195.7	-1.3%
EBITDA margin	11.1%	11.0%	1.0%	11.1%	11.2%	-1.0%	11.8%	11.9%	-0.9%
EBIT	92.7	91.4	1.4%	112.7	114.7	-1.8%	142.9	145.4	-1.7%
EBIT margin	7.5%	7.4%	1.5%	7.7%	7.8%	-1.5%	8.7%	8.9%	-1.3%
Net profit	73.6	72.5	1.4%	89.3	91.0	-1.9%	110.6	112.6	-1.8%
Net margin	5.9%	5.8%	1.5%	6.1%	6.2%	-1.6%	6.8%	6.9%	-1.4%
EPS	1.16	1.14	1.8%	1.43	1.44	-1.2%	1.77	1.79	-1.1%
DPS	0.58	0.57	1.8%	0.71	0.72	-1.4%	0.88	0.89	-1.1%

Source: Erste Group Research

Valuation

We have to a major extent kept our previous assumptions in our DCF. Adjustments relate to the TV EBIT margin, which we increased to 8%, from 7.5% previously, as we gain more confidence in Kontron's strength in the current economic slowdown, which should play out well once overall market demand resumes growth again. Something positive to mention in this regard is that robotic supplier Kuka raised orders for 2Q24 to the pre-slowdown level, indicating that industrial IoT demand is not too far from picking up again.

Support for the share price should come from the announced SBB program '2023 II'. Kontron has earmarked EUR 70mn, or 4mn shares, which translates to up to 6.36% of shares outstanding, for a buyback until October 1, 2024. Kontron has been very active since the start of the buyback on October 2, 2023, buying back 555k shares with a total volume of over EUR 10mn (by October 27). The maximum share price for the SBB is EUR 23.

Target price composition

	DCF	Multiple	Weight	12-month target		upside to target		Recommendation
				price	act. share price	price		
Kontron	26.5	34.4	100/0	26.5	20.3	30.6%		Buy

Source: Reuters, Erste Group Research

Multiple comparison

Peers IOT	MarketC (EURmn)	P/E			EV/EBITDA			EV/EBIT		
		2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
ADVANTECH CO LTD	8,567	27.2x	25.0x	22.2x	21.2x	18.8x	16.8x	22.9x	20.4x	18.0x
CURTISS-WRIGHT CORP	7,251	22.3x	20.2x	18.3x	14.7x	13.7x	12.6x	18.2x	16.5x	15.3x
EUROTECH SPA	75	28.1x	8.6x	6.2x	11.8x	5.6x	3.9x	36.7x	9.1x	5.6x
U-BLOX HOLDING AG	669	11.4x	15.3x	11.7x	5.3x	6.3x	5.3x	8.6x	11.6x	8.9x
SECO SPA	482	23.4x	16.5x	11.2x	10.4x	8.2x	6.3x	15.6x	11.8x	8.4x
ENNOCONN CORP	905	13.4x	12.0x	10.0x	8.0x	7.3x	6.3x	11.2x	9.7x	7.9x
MERCURY SYSTEMS INC	2,015	28.0x	20.2x	18.6x	15.2x	-	12.0x	161.0x	37.2x	33.4x
PTC INC	16,312	58.5x	30.2x	24.8x	-	22.4x	19.7x	-	22.0x	19.9x
HMS NETWORKS AB	1,523	30.0x	36.0x	30.7x	20.7x	24.0x	20.8x	24.1x	28.7x	24.4x
QUECTEL	1,700	70.4x	20.4x	15.4x	30.2x	14.2x	11.3x	59.0x	23.4x	17.2x
MEDIAN		27.6x	20.2x	16.8x	14.7x	13.7x	11.7x	22.9x	18.5x	16.3x
Kontron	1303.2	17.4x	14.2x	11.5x	8.5x	6.6x	5.3x	12.6x	9.6x	7.2x
prem. / disc median		-37%	-29.7%	-31.9%	-42.1%	-51.7%	-54.2%	-45%	-47.9%	-55.5%

Peers IOT	Share price	P/B			ROE			Dividend yield		
		2023e	2024e	2025e	2023e	2024e	2025e	2023e	2024e	2025e
ADVANTECH CO LTD	10	6.2x	5.7x	5.4x	23.5%	24.3%	26.1%	2.8%	3.0%	3.3%
CURTISS-WRIGHT CORP	190	3.4x	3.1x	2.9x	16.6%	16.9%	17.5%	0.4%	0.4%	0.4%
EUROTECH SPA	2	0.7x	0.6x	0.6x	2.5%	7.7%	9.3%	-	-	-
U-BLOX HOLDING AG	92	1.4x	1.3x	1.2x	12.4%	7.4%	10.1%	2.5%	2.0%	2.6%
SECO SPA	4	1.7x	1.5x	1.3x	7.8%	9.8%	12.7%	0.0%	0.0%	-
ENNOCONN CORP	7	1.6x	1.4x	1.1x	9.7%	9.8%	12.3%	4.1%	3.9%	4.5%
MERCURY SYSTEMS INC	35	1.3x	1.3x	1.3x	1.1%	3.2%	6.9%	-	-	-
PTC INC	137	-	5.4x	4.5x	-	17.0%	15.6%	-	0.0%	0.0%
HMS NETWORKS AB	32.5	8.8x	7.7x	6.7x	32.6%	22.9%	23.3%	1.2%	1.1%	1.2%
QUECTEL	6.4	3.1x	2.8x	2.3x	5.7%	14.6%	16.8%	0.6%	1.1%	1.9%
MEDIAN		1.7x	2.2x	1.8x	9.7%	12.2%	14.1%	1.2%	1.1%	1.9%
Kontron	20.3	2.1x	1.9x	1.7x	11.7%	13.6%	15.4%	2.9%	3.5%	4.3%
prem. / disc median		23.1%	-12.2%	-5.8%	19.9%	11.7%	9.5%	140.8%	215.8%	125.1%

Per Kontron share (EUR) 2023e	29.2
Per Kontron share (EUR) 2024e	31.4
Per Kontron share (EUR) 2025e	32.6
Period weight	30% 60% 10%
NPV as of Nov 2023 EUR	30.8
Cost of Equity	12.3%
NPV as of Nov 2024 EUR	34.6

Source: Bloomberg, Erste Group Research

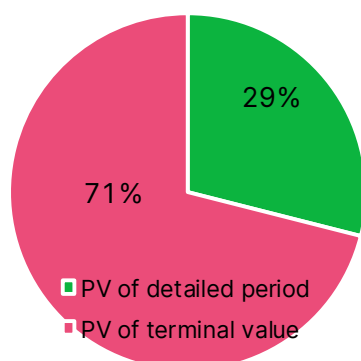
WACC calculation

	2024e	2025e	2026e	2027e	2028e	NY / TV
Risk free rate	3.2%	3.2%	3.2%	3.2%	3.2%	3.0%
Equity risk premium	6.1%	6.1%	6.1%	6.1%	6.1%	5.9%
Beta	1.5	1.5	1.5	1.5	1.5	1.3
Cost of equity	12.3%	12.3%	12.3%	12.3%	12.3%	10.7%
Cost of debt	5.7%	5.7%	5.7%	5.7%	5.7%	5.5%
Effective tax rate	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
After-tax cost of debt	4.3%	4.3%	4.3%	4.3%	4.3%	4.1%
Equity weight	100%	100%	100%	100%	100%	90%
WACC	12.3%	12.3%	12.3%	12.3%	12.3%	10.0%

DCF valuation

(EUR mn)	2024e	2025e	2026e	2027e	2028e	NY / TV
<i>Sales growth</i>	18.3%	11.3%	9.5%	6.3%	6.3%	3.0%
EBIT	112.7	142.9	165.1	181.7	196.9	166.4
<i>EBIT margin</i>	7.7%	8.7%	9.2%	9.6%	9.8%	8.0%
<i>Tax rate</i>	15.0%	18.0%	22.0%	23.0%	23.0%	25.0%
Taxes on EBIT	-16.9	-25.7	-36.3	-41.8	-45.3	-41.6
NOPLAT	95.8	117.2	128.7	139.9	151.6	124.8
+ Depreciation	50.6	50.3	50.5	51.1	52.0	52.0
<i>Capital expenditures / Depreciation</i>	86.9%	95.1%	101.0%	103.6%	105.8%	100.0%
+/- Change in working capital	-40.7	25.9	-19.8	-11.6	-8.4	-4.2
<i>Chg. working capital / chg. Sales</i>	-17.9%	15.6%	-12.8%	-10.4%	-7.0%	-7.0%
- Capital expenditures	-44.0	-47.8	-51.0	-52.9	-55.0	-52.0
Free cash flow to the firm	61.7	145.6	108.5	126.5	140.3	120.6
<i>Terminal value growth</i>						3.0%
Terminal value						1,774.6
Discounted free cash flow - Dec 31 2023	54.9	115.4	76.6	79.6	78.6	994.3
Enterprise value - Dec 31 2023	1,399.4					
Minorities	3.3					
Non-operating assets	0.0					
Net debt	-123.3					
Other effects	0.0					
Equity value - Dec 31 2023	1,519.4					
Diluted number of shares outstanding (mn)	63.9					
Cost of equity	12.3%					
12M target price per share (EUR)	26.5					
Current share price (EUR)	20.3					
<i>Up/Downside</i>	30.6%					

Enterprise value breakdown



Sensitivity (per share)

		Terminal value EBIT margin				
		7.0%	7.5%	8.0%	8.5%	9.0%
9.0%		26.7	28.0	29.3	30.7	32.0
9.5%		25.4	26.6	27.8	29.0	30.2
10.0%		24.2	25.3	26.5	27.6	28.7
10.5%		23.2	24.3	25.3	26.4	27.4
11.0%		22.3	23.3	24.3	25.3	26.3
		Terminal value growth				
		2.00%	2.50%	3.00%	3.50%	4.00%
9.0%		26.3	27.7	29.3	31.3	33.6
9.5%		25.1	26.4	27.8	29.4	31.4
10.0%		24.1	25.2	26.5	27.9	29.5
10.5%		23.3	24.2	25.3	26.5	28.0
11.0%		22.5	23.3	24.3	25.4	26.6

Group Research

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Company description

Kontron, headquartered in Linz, Austria, and listed on the Frankfurt stock exchange is a member of the TECDAX and the MDAX. Kontron was S&T previously and was renamed Kontron after the sale of the IT services business. Now Kontron is a IOT pureplay and one of the leading global providers of embedded IoT solutions in Europe, but also active in North America and Asia. With more than half of its 4500 employees being engineers, Kontron supplies a diversified customer base of over 3000 clients. S&T operates in three divisions: Europe, Global, which also reflects the North American and Asian businesses, and Software and Services.

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