Incap

Extensive report

6/15/2023 7:52

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Inderes corporate customer

This report is a summary translation of the report "Voittoputki takana, painekoe edessä" published on 6/15/2023 at 7:49 am

inderes.

Winning streak behind, pressure test ahead

We reiterate our Accumulate recommendation with a EUR 12.00 target price for Incap. The company that has grown exponentially in recent years faces an acid test toward the end of the year, as the volume of the customer that dominates its revenue decreases. We consider the situation to be temporary and expect Incap's strengths, in particular high cost efficiency, to keep the company on a growth path in the longer term. Despite the share's highish risk level, both in the short and long term, we find Incap's valuation to be low (2024e: P/E 13x, EV/EBIT 7x), so looking beyond the challenges of this year the share's risk adjusted expected return is sufficient in our opinion.

High-performance contract manufacturer

Incap is an electronic manufacturing service provider that primarily specializes in high mix / low volume applications. It creates added value for its customers 1) by allowing more efficient resource allocation for OEMs to core business activities such as product development, sales and marketing, and 2) by bringing flexibility to OEMs through outsourced production both to capacity and cost management. Incap has built its organization model based on decentralized and quickest possible decision-making, which in turn has resulted in a light organization structure, low overhead expenses, swift operational responsiveness, and a cost-conscious culture. In addition, a significant share of the company's production is in low-cost countries (particularly India). We believe that these factors are the key strengths of the company. The main risks are a single very large customer (in 2022 the largest customer generated 67% of Incap's revenue), the inherent variations in investment-driven demand and potentially tightening competition.

Interesting value creation opportunities in the long

Incap's customer risk partly realized in the spring, when the company's largest customer decided to lower its inventory levels due to slowing growth. In practice, this means Incap's sales will suffer in the rest of the year. However, the electrification of the world and the resulting increase in electronics, as well as growing outsourcing rates of industrial OEMs drive the demand for contract manufacturers upward in the longer term even faster than GDP growth. In addition, the fragmented structure of the industry, together with Incap's current balance sheet position, provides a solid foundation for inorganic growth. Considering this, we feel Incap's potential for value creation in the coming years is good, but visibility of when short-term challenges will be resolved is poor. Our estimates for the company's result for the current year are at the bottom end of Incap's guidance range. In our neutral scenario, we now expect Incap to return to growth next spring or summer and growth in the coming years will be clearly slower than the acceleration in 2021-2022. We expect profitability to remain very strong relative to the industry at 13-15% adjusted EBIT level, based on the company-specific strengths mentioned above.

Highish risk profile but low price compensates

Incap's P/E ratios for 2023 and 2024 based on our estimates are 13x and 10x, while the corresponding EV/EBIT ratios are 9x and 7x. Absolute multiples are justifiably higher than historical levels, and they are also below the neutral range we estimate for the company at least next year. We therefore consider the valuation of Incap, that has impressive qualitative features, attractive and the expected return good, as long as the inventory adjustment of the largest customer is temporary. However, due to the customer structure, the risk profile of the share is highish in both the short and medium term.

Recommendation

Accumulate
(prev. accumulate)

12.00 EUR
(Prev. 12.00 EUR)

Share price:
9.96 EUR

Key indicators

	2022	2023e	2024e	2025e
Revenue	263,8	236,3	265,2	291,7
growth-%	55 %	-10 %	12 %	10 %
EBIT adj.	40,0	31,2	37,5	41,9
EBIT-% adj.	15,2 %	13,2 %	14,1 %	14,4 %
Net Income	27,6	22,8	28,3	31,8
EPS (adj.)	0,98	0,79	0,97	1,10

P/E (adj.)	17,5	12,6	10,3	9,1
P/B	5,7	2,6	2,2	1,8
Dividend yield-%	0,0 %	1,5 %	2,0 %	2,5 %
EV/EBIT (adj.)	12,8	8,5	6,6	5,5
EV/EBITDA	12,0	7,5	5,9	4,9
EV/S	1,9	1,1	0,9	0,8

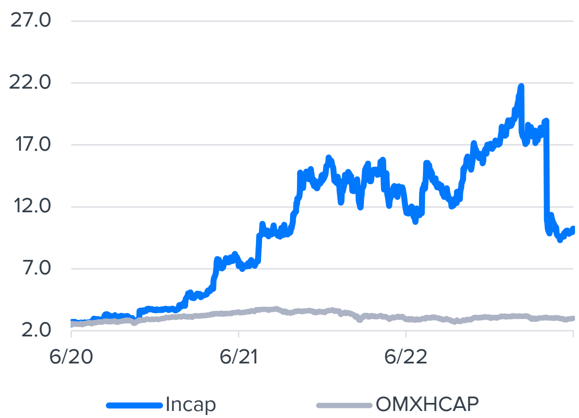
Source: Inderes

Guidance

(Intact)

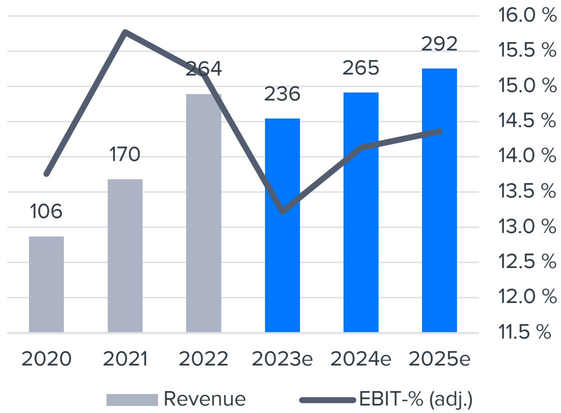
Incap estimates that its revenue and operating profit (EBIT) for 2023 will be lower than in 2022.

Share price development



Source: Millistream Market Data AB

Net sales and adjusted EBIT-%



Source: Inderes

EPS and EPS

Source: Inderes

Value drivers

- Organic growth in the electronics market, supported by global megatrends and increased outsourcing rate
- Light organization and cost structure enable a high profitability level
- Quick decision-making supports new customer procurement
- Accelerating growth with acquisitions

Risk factors

- Mutually challenging value chain position upholds a brutal competitive situation
- Cyclical nature of customer industries
- Tightening competitive situation
- Company's cost efficiency deteriorating
- A very large single customer that drives group sales and profitability short term

Valuation	2023e	2024e	2025e
Share price	9,960	9,960	9,960
Number of shares, millions	29,3	29,3	29,3
Market cap	291	291	291
EV	267	248	229
P/E (adj.)	12,6	10,3	9,1
P/E	12,8	10,3	9,1
P/FCF	7,5	12,4	12,1
P/B	2,6	2,2	1,8
P/S	1,2	1,1	1,0
EV/Sales	1,1	0,9	0,8
EV/EBITDA	7,5	5,9	4,9
EV/EBIT (adj.)	8,5	6,6	5,5
Payout ratio (%)	19,2 %	20,7 %	23,0 %
Dividend yield-%	1,5 %	2,0 %	2,5 %

Source: Inderes

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Incap in brief

Incap is a contract manufacturer for the electronics industry, which acts as a strategic partner for global OEM companies with focus on high-tech.

1985
Year of establishment

1997
IPO

264 MEUR (+55.3 % vs. 2021)
Revenue 2022

40.0% 2017-2022
Average ROIC in 2017-2022

40 MEUR (15.1% of revenue)
Adjusted EBIT 2022

2,817
Personnel at the end of 2022

65%
Revenue share of green energy products in 2022
In terms of EU taxonomy eligibility

Change in business model
2012-2015

Large structural arrangements create the base for a sustainable profitability turnaround

The organizational model is based on decentralized decision-making and the strategy is sharpened

A kind of business reboot and finding a profitable growth path

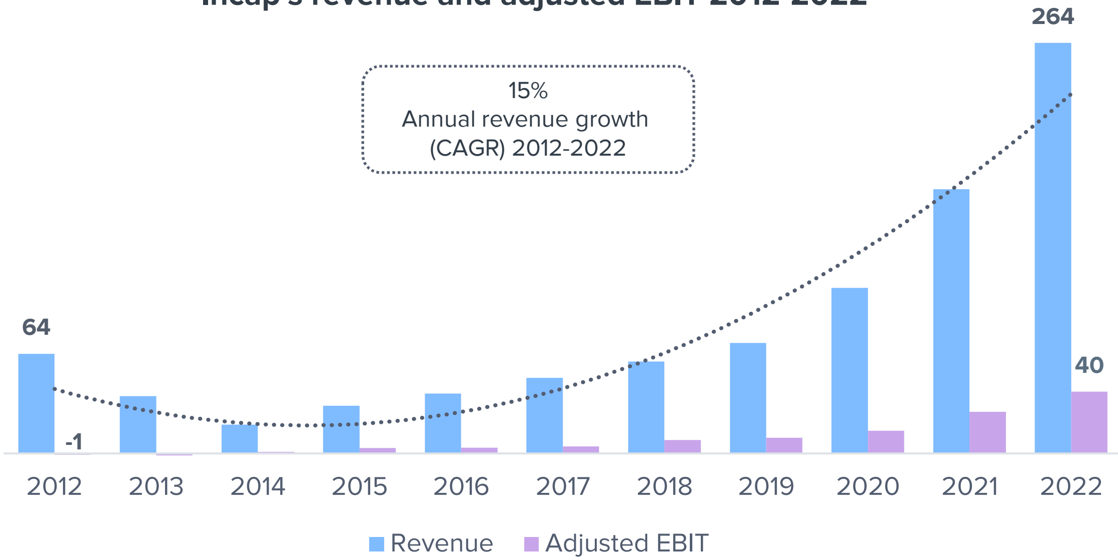
Rapid growth in market share
2016-2023

Organic growth rate remains excellent on the wing of the largest customer and profitability level is brought to the top of the industry

A successful AWS arrangement slightly reduces the level of risk and improves the purchasing power of the supply side

Indian plant investments strengthen conditions for longer-term growth

Incap's revenue and adjusted EBIT 2012-2022



Source: Incap / Inderes

Company description and business model 1/8

Contract manufacturer in industrial electronics

Incap is a contract manufacturer in the electronics industry, specializing in the production of high mix/low volume industrial electronics applications with high technical requirements and a significant emphasis on the production of green transition technologies (cf. 65% of revenue in the EU taxonomy classification of green transition products in 2022). At operations level, this means that Incap has the necessary ability to manufacture the entire product or sub-assembly for the customer, typically OEM companies. Therefore, Incap in practice creates value for its customers through two routes: 1) by allowing more efficient resource allocation for OEMS to core business activities such as product development, sales and marketing, and 2) by bringing flexibility points (incl. responsiveness) through outsourced production to manage both capacity and costs.

Incap's end products include inverters, various control systems and measuring instruments. Although Incap's strategic focus is fundamentally on industrial electronics, we believe that the company is not overlooking the potential of small batch consumer electronics, as long as they are sufficiently attractive. As a concrete example of such opportunities, we see light vehicles such as electric scooters and their charging infrastructure, which we believe has provided the company with excellent business paths in recent years. However, mass-produced consumer products (e.g. phones and computers) are not Incap's focus area.

Incap's small headquarters is in Helsinki. The company has four manufacturing units located in Estonia, Slovakia, Great Britain, and India. A group-level purchasing unit is in turn operated from Hong Kong.

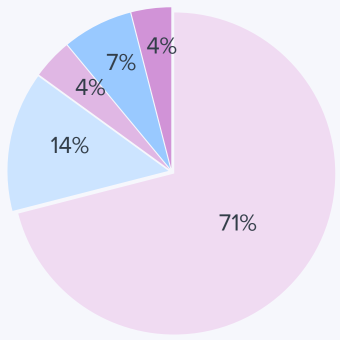
Europe and large customers

In 2022 Incap's revenue was EUR 264 million and operating profitability was at an excellent level of 15% considering the industry. Geographically, the company's business is dominated by Europe, with around 71% of its business coming from the region last year, based on the end customer locations. The second largest market is North America with 14% of revenue, while Australia, Africa and Asia together account for 15%. Although the equipment manufacturers we assess as Incap customers are global players, their main markets are primarily within Europe. Based on Incap's production, the revenue mix would be very different, as the Indian plants are by far the company's largest production unit. In other words, Incap operates with a strong export-driven business model.

Incap's customer portfolio is highly concentrated, since the largest customer accounted for 67% of revenue in 2022 (2021: 61%). According to Inderes' estimate based on public sources, the largest customer is Victron Energy, but Incap has not published its customers. The largest customer has also grown significantly faster than the rest of the Group in recent years and has been a significant factor behind Incap's rocket-like growth.

- More than 30 years of operational history and high-level technology expertise
- Strategic focus on high mix / low volume applications for industrial electronics
- Production plants in countries with low cost structures and a light organizational structure increase overall competitiveness
- In addition to efficient PCB assembly, also capabilities for larger comprehensive deliveries

Geographical revenue distribution 2022



Source: Incap, Inderes

Company description and business model 2/8

The four largest customers accounted for 74% of revenue (69% in 2021), so the other large customers are not particularly significant in relation to the size of the group. Last year, the company had 22 (21 in 2021) customers who brought in more than EUR 1 million. Overall, we estimate that the number of customers is several dozen. We estimate that Incap's key accounts are long-term and, in many cases, strategic partnerships. Thus, in principle, there is little customer turnover in the portfolio.

Although concentrated customer portfolios are not significantly abnormal in the industry and the loss of large customers is rare due to high switching costs, we believe that the highly concentrated customer structure raises Incap's risk profile quite clearly relative to peers. In particular, the direction of the largest customer's (i.e. Victron Energy) business in practice largely determines Incap's direction in the short term, so the risk of volatility is ever-present. This risk also materialized in spring 2023, when Incap had to issue a profit warning as Victron Energy wanted to reduce its stocks due to slower than expected growth.

We believe that Victron Energy is the largest customer

We estimate that Victron Energy, a Dutch power electronics manufacturer founded in 1975, is Incap's largest customer. Incap does not report its customers. The company designs and sells inverters, chargers and other power transmission related products. The company has 110 employees, 45 of whom are R&D engineers. The company has grown to become a major player in its field and its products are sold globally.

Victron Energy's goal is to provide its customers with reliable and sustainable solutions that enable them to generate and use electricity in the most efficient and environmentally friendly way possible. The products are widely used in a variety of applications and are popular with boaters, recreational vehicle owners, industry, and households. The company's products include inverters, chargers, batteries, solar panels, charge controllers and accessories. To our understanding, the company is known for its high quality, reliability, and innovative solutions.

One of Victron Energy's main areas of development in recent years has been renewable energy solutions, particularly solar panels and photovoltaic power plants. The company has developed several new products, such as smart charge controllers and solar panel optimizers, to help customers get the most out of solar power. Therefore, the green transition is likely to continue to be a significant demand driver for Victron Energy.

Victron Energy's growth has been spectacular

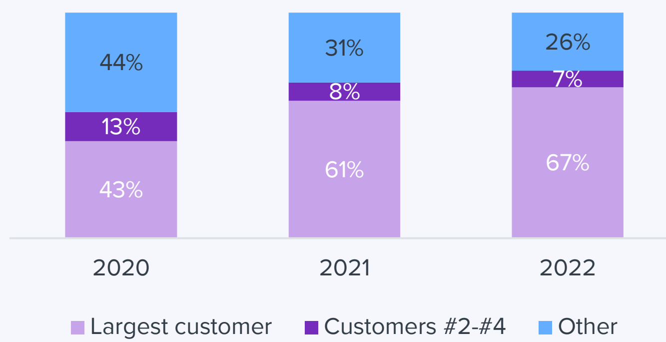
The company's revenue has grown significantly in recent years and it has expanded into several new markets around the world. Victron Energy's revenue has increased between 2013-2020 from EUR 55 million to EUR 230 million, or

Potential customers*

*Based on Inderes' estimate of potential customers. Incap does not report its customers.

Customer structure

Share of revenue in 2020-2022



Source: Incap, Inderes, companies

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roughly 23% per year (CAGR), while EBIT has increased by roughly 26% per year (CAGR) over the same period. Victron Energy appears to be a very competitive player in its sector, with excellent profitability despite strong growth. Operational efficiency has been excellent, with an average EBIT margin of 27% between 2013 and 2020. According to our assessment, the company also has a strong financial position.

We are confident that Victron Energy's business is on a solid footing in the big picture

Victron Energy's good positioning in the green trend and the company's forcible recent financial history increase confidence in Victron Energy's ability to grow profitably in the future, which is of course also critical for Incap's growth and profitability. However, as an unlisted company, the transparency of Victron Energy's business development and long-term objectives is very weak and surprises may continue to occur, both good and bad.

Another positive aspect for Incap is that the companies seem to be genuine strategic partners, as while Victron Energy is by far Incap's largest customer, Incap is Victron Energy's largest manufacturing partner. Thus, in our view, the interest in developing cooperation should be mutual, as the success of the one supports the other to some extent at least. Of course, this does not remove the fact that contract manufacturers primarily offer their customers flexibility and efficiency, and ensuring these basic conditions may also require unpleasant actions from Incap's point of view in the short term (cf. the reduction of production this year to reduce Victron Energy's inventories).

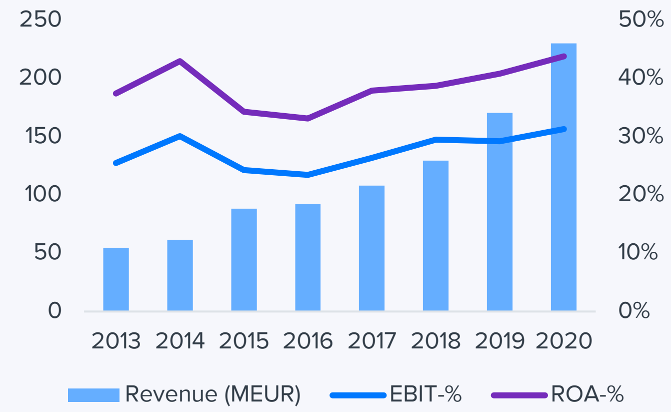
The fastest way to diversify client risk would be through acquisitions

Incap's other customers are not significantly large for a company of its size. Given the structure of the client portfolio and particularly the significant weight of Victron Energy, Incap's client base is likely to remain highly concentrated, although we believe risk diversification is high on the company's priority list. The fastest way to reduce client risk would naturally be through acquisitions, but given the scale, even after a medium-sized acquisition, Victron Energy's weight in the portfolio would be significant. Therefore, we believe investors should be prepared to tolerate higher than average individual client risk at Incap in the future.

Long-term cooperation

According to our estimates, the company aims at long-term strategic cooperation with its most significant customers, which will enable Incap to exploit its own strengths and increasing order intake, both on volume and value basis One of the key factors in creating such cooperation is, in our opinion, the customer's trust in the contract manufacturer. This makes sense because the contract manufacturer is responsible for critical functions in terms of the customer's manufacturing operations.

Development of Victron Energy's revenue and profitability



Source: Incap, Inderes, companies

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Thus, we believe that trust must be earned through high-quality and especially secure supply. In addition to strengthened customer relationships, we believe success in these elements will also increase the switching costs that the customer faces and thus create a competitive advantage for the contract manufacturer. On the other side of the coin, the same factors also slow down the acquisition of new customers.

We feel Incap has succeeded in building strategic partnerships, as customer relationships with key customers have been long-lived and we estimate that in the past few years the company has also managed to win over significant customer-specific market shares. We also believe that the newer customer portfolio that came with AWS has developed in a similar way. This, together with the enlarged geographical footprint and range of industries, provides Incap with a good basis for strengthening existing customer relationships and establishing new strategic partnerships with competitive operators and realizing the longer-term growth take-offs these generate.

Business structure

Incap does not have separate reporting segments, so revenue is presented only at group level and divided into geographical areas. In terms of production plants, we understand that Estonia and Slovakia supply mainly to Europe, while the Indian and UK units supply the majority of non-European deliveries.

However, no particular roles have been assigned for the production units, the production and service selection of all units have, in our opinion, next to actual volume production the ability to manufacture pre-series and prototype products, design support and after-sales services. There are, however, normal differences in the customer and production mix of the units, since we believe that, for example, portfolios in Estonia and Great Britain have many start-ups as customers next to established customers. In India and Slovakia, customers are mostly more mature in their life cycle. Of course, due to the specific characteristics of certain applications and the local manufacturing clusters in certain sectors, such as the certificates required to manufacture medical instruments and the automotive cluster in Eastern Europe, there are natural differences of focus between production units also when examined by industry.

Incap's organization model is based on decentralized and quickest possible decision-making, in line with which the production plants operate as independent cost centers. Thus, they are responsible for their production planning, customer acquisition, offer calculation, actual production processes and pricing, as set out in the Group Guidelines. In turn, component procurement is mainly organized through local teams within the production operations, although procurement is of course coordinated at group level through the Hong Kong supply unit as well.

Production plant network 1/2

India

- Currently three units in Tumkur (last one completed at the turn of 2022/2023)
- Investments will increase the total floor area to over 24,000 square meters
- Focus on highly cost-effective volume production, but also capabilities for pre-series and other support functions
- Extensive production portfolio, including inverters, UPS and electronics for fuel dispensing systems
- We estimate that 2022 revenue was over EUR 160 million

Estonia

- The production plant in Kuressaare serves both established and start-up companies whose primary target market is in Europe
- Efficient ramp-up of new products through special competence in a wide range of services
- The total floor area of the plant is about 7,300 square meters
- The production portfolio focuses on technologically advanced partial or turnkey deliveries
- We estimate that 2022 revenue was some EUR 35 million

Source: Incap, Inderes

Company description and business model 5/8

The procurement model also worked very well during the component shortages of 2021-2022, as Incap did not experience any visible disruption in revenue and profit from component shortages. Support functions concentrated to the top level are largely limited to IT and financial administration services.

As a result of these choices, Incap's organization structure is very thin. This in turn has led to remarkably low overheads, agile operational responsiveness and excellent cost awareness. We consider these elements, and thus the overall efficient operating model, to be Incap's key competitive assets, which together with the very low personnel costs of Indian production enable the company to achieve industry-leading profitability. The company has also achieved these characteristics in its growth in recent years. In our view, this is a good indication that the model has a certain degree of sustainability, although we do not consider it justified to talk about a real sustainable source of competitive advantage in this respect, given the replicable elements of the model.

PCB assembly is the core competence

Incap's business model consists of a few core processes and functions with which the company aims to both create and establish its position in the customer's value chain. As typical for contract manufacturers, the core competence of Incap's operations is PCB assembly (PCBA). In PCBA, various electronic components are set up and attached to a circuit board, as the name suggests, in order to achieve a whole that matches the requirements of the end product. We believe that the current lines of Incap's production plants are quite modern, and thus we believe that the actual PCB know-how is competitive.

Despite the fundamental nature of PCBA, the added value it creates is not, according to our estimates, that large as an individual/independent function. Considering this, we believe that competitive PCB skills should be seen more as a hygiene factor than an ability that brings a relative advantage, and thus as a basic requirement for operations with higher added value, such as Box Build assembly, lifecycle services for the whole product portfolio and other tailored sub-processes. In Box Build assembly, in particular, Incap's share in the value chain of the end application is wide, as the company is responsible for manufacturing the entire product (incl. materials acquisition, wiring and harness works, and product testing) and delivering it to the OEMs' distribution channel. Managing a wide value chain segment in turn means not only higher value added but also better customer retention than in PCBA alone and a stronger customer relationship.

Production plant network 2/2

Great Britain

- The unit in Newcastle has comprehensive resources for turnkey product supply (including cable and wire harness assembly)
- The total floor area of the plant is about 4,400 square meters and supply flows are both local and global
- Long experience, especially in defense, security and aerospace customers
- We estimate that 2022 revenue was some EUR 25 million

Slovakia

- The Namestovo plant is in practice a mirror image of the British unit
- The total floor area of the plant is about 5,200 square meters and Europe is the final destination of the supply flows
- A special feature of the production plant is a hall fully dedicated for automotive business
- We believe volume production (excl. automotive) is primarily in applications for niche segments
- We estimate that 2022 revenue was over EUR 35 million

Source: Incap, Inderes

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Lifecycle and other tailored services include, e.g., support functions for product and production planning, various test operations, and, according to our estimates, repair work on a small scale. Although the actual manufacturing activity is at the core of Incap's business model and the current revenue share of services is estimated to be small, it is logical to have service capability when considering longer-term overall offering. Through services, the company will be able to help both small operators in the early stages of their life cycle and offer larger equipment manufacturers packages that complement manufacturing operations, thereby providing sensible growth paths from early-stage support functions and prototypes to later stage volume production.

The production lines of contract manufacturers are typically standardized and we do not believe that it is possible to improve relative competitiveness nor obtain a competitive lead through mere equipment investments. However, despite reasonable automation levels, Incap's production processes still have a lot of personnel intensive phases and the people who control these phases are variable pieces. High personnel intensity and the importance of seamless process flow thus set quite high standards for expertise among the personnel. Thus, recruiting and retaining staff are important elements in building long-term competitiveness.

Hard order backlog is not that far-reaching

Fluctuations in contract manufacturer demand can be strong, as customers typically use contract manufacturers as buffers for variations in their own end-use demand. We estimate that under normal pre-pandemic conditions (i.e. no prolonged visibility of the component situation), Incap received both actual orders and non-binding demand forecasts from its customers for a period of 3-6 months. During the component shortage, the window stretched to 12-24 months, but recently the visibility has started to shorten as the component shortage has already eased to some extent. However, given the lessons learned from the pandemic on supply security risks, we believe it is possible that the demand forecast window will be permanently set, e.g., at a longer 6-9 month range.

However, the range of so-called hard orders in this pile is only a few months, which makes the order backlog structurally relatively short. As a result, Incap's visibility on business trends is relatively short, although we estimate that, especially for customers at the more mature end of the customer portfolio, business trends are reasonably predictable,

Customer process

Planning and development

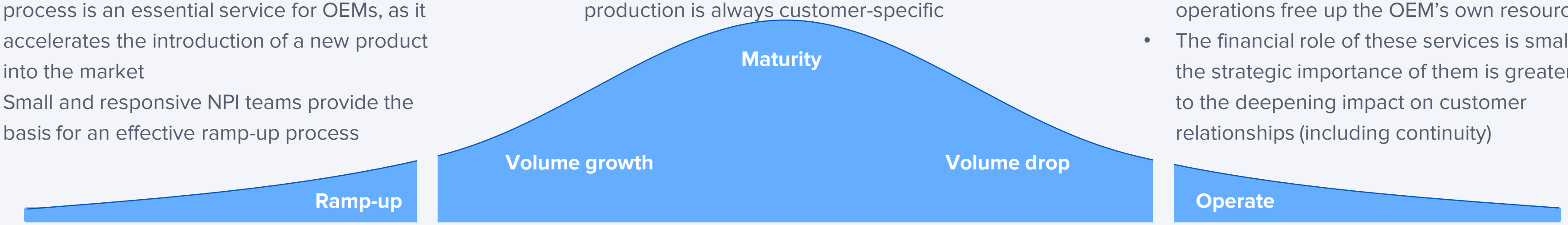
- Prototypes of new products manufactured through planning and validation work and low volume are at the heart of customer ramp-ups
- A powerful New Product Introduction (NPI) process is an essential service for OEMs, as it accelerates the introduction of a new product into the market
- Small and responsive NPI teams provide the basis for an effective ramp-up process

Production

- The greater the customer value created, the larger share of the value chain of the entire product is handled by the contract manufacturer
- The time from prototypes to actual volume production is always customer-specific

After sales

- The aftermarket capability in high tech is a logical part of the service portfolio covering the entire life cycle of electronic products
- As with other operations, maintenance operations free up the OEM’s own resources
- The financial role of these services is small, but the strategic importance of them is greater due to the deepening impact on customer relationships (including continuity)



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barring exceptional circumstances such as in recent years. Regardless of the structure of the hard order backlog, required components are acquired in a frontloaded manner before the forecasts are converted to orders. However, Incap does not take any real risk in its component procurement, as customers are in principle committed to buying the components purchased at cost price if they cancel

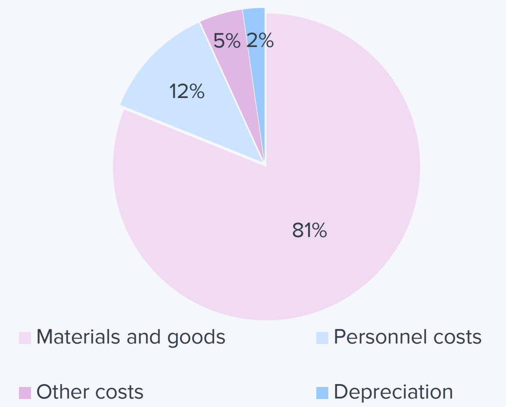
a product order after placing the component order. Due to the periodic availability bottlenecks of components (e.g. the situation in 2022), their market prices can fluctuate strongly, which in turn can put pressure on working capital management. However, the cost-based pricing model applied by Incap and typical for contract manufacturers enables fast transfer of increased material costs to customers. This should not, however, be classified as actual pricing power, since, as the pricing model works both ways, drops in material costs are also transferred to benefit the customers. For Incap, it is therefore important to have a sufficient and preferably stable margin after materials, so that after reducing the costs that are purely in the company's own hands, a margin in line with the targets can be reached.

In addition, the short structure of the order backlog may to some extent make it difficult to manage the order/supply chain in circumstances where confirmed hard orders deviate significantly from the demand forecasts given. This is based on the fact that in the short term, capacity flexibility is limited, especially when hard orders are below demand forecasts. In the opposite situation, we believe that the flexibility of capacity is under certain conditions quite good, as it is possible, e.g., to increase production shifts. It is therefore important to maintain and create operational flexibility points within the current business model.

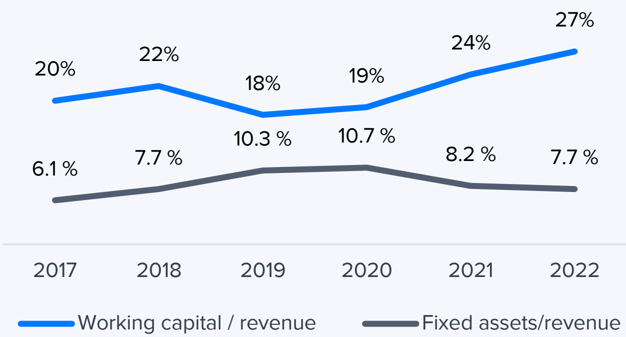
Cost structure limits growth scalability

The share of fixed costs in Incap's expense structure is very small, as due to the basic nature of electronics manufacturing and the company's operating culture, most costs are variable material costs. We estimate that about 85-90% of total company costs are variable, while fixed costs account for about 10-15%. The low level of fixed costs is explained by two factors in particular: 1) the company does not have a conventional matrix organization, but a light organization structure based on local decision-making, and 2) contrary to OEMs, the operating model of contract manufacturers does not require large R&D resources, fixed-salary personnel they tie up nor other fixed cost clusters. Because the company's operating culture is highly cost-conscious and this has been maintained even at high growth rates, we believe that the cost structure will continue to be similar in future. As a result of the light cost structure, Incap's realizable economies of scale are limited, with little scaling of revenue growth beyond a certain base level, although an increase in the revenue share of the highly profitable Indian plant (probably due to low personnel costs) may provide a slight boost to the company in the short term.

Cost structure 2022



Capital commitment



Source: Incap, Inderes

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The light cost structure gives the company flexibility against declining volume levels. Overall, we feel the light cost structure and sensible flexibility points create an excellent base for Incap to reach a high margin level even in a declining revenue environment. This, in turn, is favorable for the overall risk profile.

Limited capital requirements

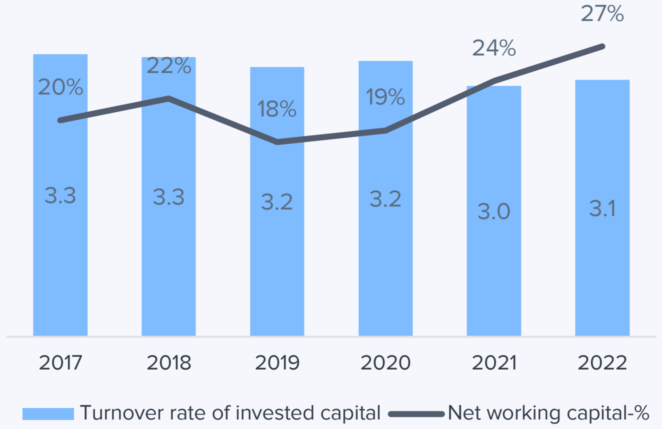
In 2022, fixed capital (incl. IFRS 16 assets) accounted for around 7% of revenue, which can be considered a moderate level. In relation to the balance sheet total, the share of fixed capital was 12%, indicating a low capital requirement for the business. The low fixed capital requirement is explained in particular by the nature of contract manufacturing, which is personnel intensive and clearly lighter in terms of hardware than conventional process and engineering industry. Reflecting this, fixed investment in equipment in the industry has typically been able to keep pace with growing demand in a fairly linear fashion, if only within the constraints of factory wall and floor space. Correspondingly, this gives contract manufacturers certain leeway in capacity investments relative to the relevant demand outlook (cf. front-loaded investments in the process industry). The dynamics have therefore both improved the use of capital by contract manufacturers and helped companies to avoid unfortunate and margin-hurting overcapacity situations.

The net working capital typically committed to Incap's operations is 18-27%. During the last year, the company's trade receivables and trade payables rotation periods were optimal for financing working capital (trade receivables < trade payables). This has been an excellent performance given the generally challenging value chain position of contract manufacturers, although the low level of receivables at the end of 2022 may not be fully sustainable. Overall, however, the working capital ratio has been on the rise as component shortages in particular have inflated inventories. Moreover, we estimate that the increase in the Indian plant's share of revenue may have a slight working capital bias as large volumes are shipped from India to Europe.

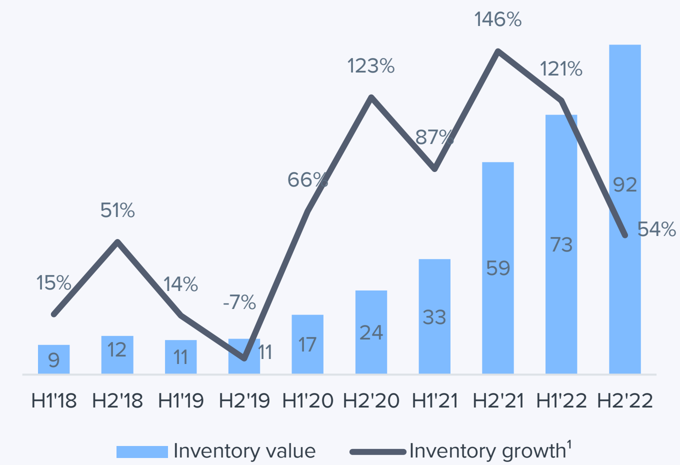
On the whole, Incap's operations are moderately working capital intensive, because with the actual figures of the last few years, Incap has gained an EBITDA increase of EUR 0.15 million from a growth of EUR 1 million and the corresponding working capital commitment has been EUR 0.25 million. Thus, during the last few years of Incap's particularly strong organic growth, the company has not generated much cash flow from operations, despite a very strong result, and the result has been tied up in inventories. However, the silver lining of this year's volume drop is that cash flow should improve on its own. Therefore, we are not worried, although Incap's earnings and cash flow have told a different story in recent years.

Overall, in a normal growth environment, moderate capital commitment is a positive factor, as capital efficiency provides an excellent basis for a high return on invested capital and hence for creating shareholder value.

Development of capital commitment

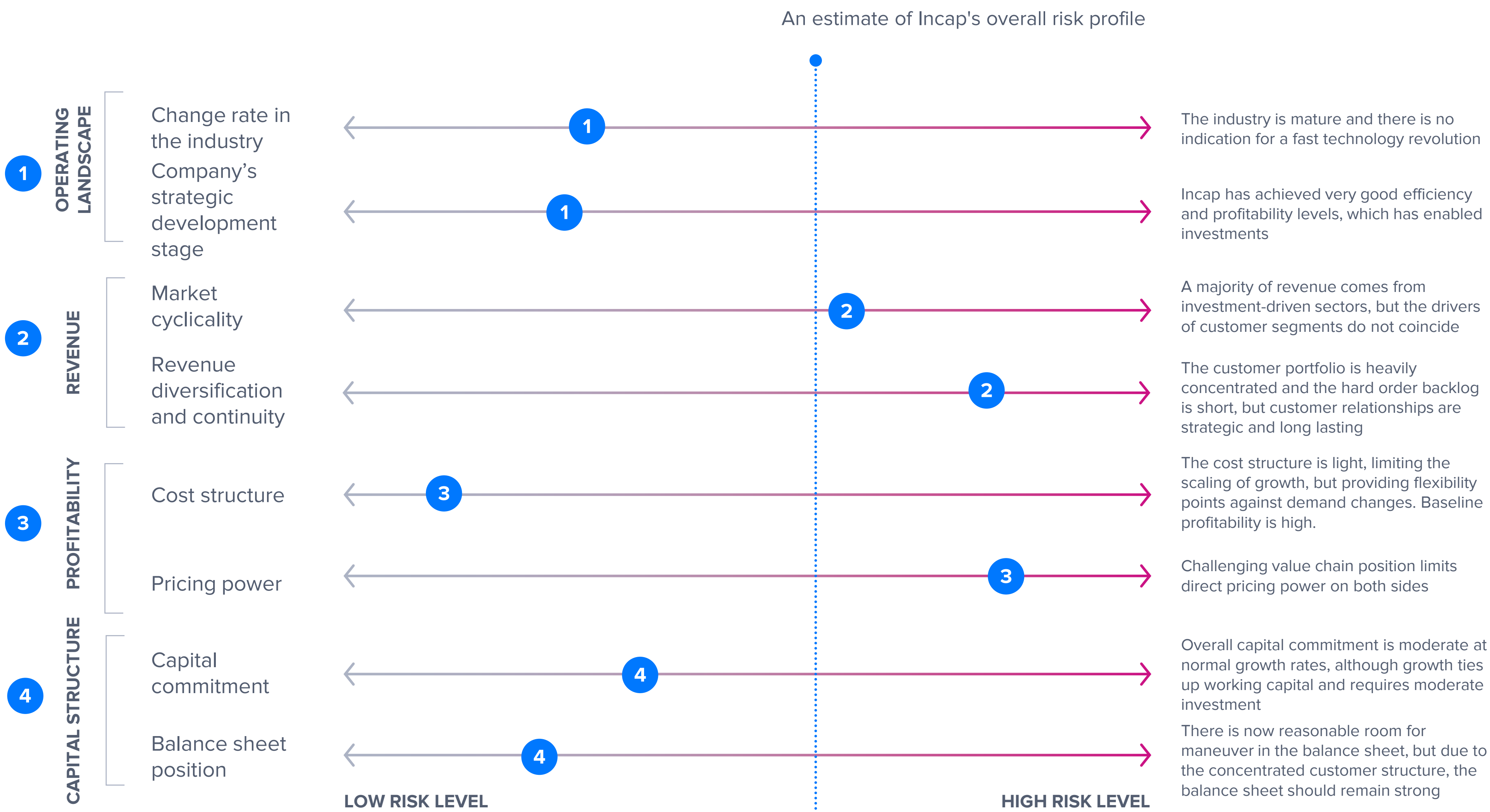


Inventory development



Source: Incap, Inderes
[1]Growth year-on-year

Risk profile of the business model



Source: Inderes

Industry and competitive landscape 1/6

Huge overall market

According to estimates by various research companies, the combined turnover of the global electronics industry in 2022 will be around USD 2,200 billion. The whole market can be divided into four parts based on the business models of the companies operating in it: equipment manufacturers (OEMs), outsourced design and manufacturing (ODMs), contract manufacturers (EMSs) and component distributors (technical wholesalers and resellers). These operating models differ in the types of underlying value chains and who owns the intellectual property rights of the end product. Since Incap itself is a contract manufacturer, the company does not have independent and fully customer-independent product development. Thus, the company does not own the rights to the applications it manufactures. However, different operating models, excluding distributors, compete to some extent with each other (e.g., manufacture / buy decision), which is why we believe that it makes sense to look at the entire electronics market as the relevant starting point for Incap's target market.

Contract manufacturing market is estimated to be worth around USD 550 billion. Therefore, the field is huge compared to Incap's own size class and we see it as limiting any possibilities in the foreseeable future.

Asia reigns supreme in size

Geographically, Asia is the number one market. The largest Asian companies in the industry, such as Hon Hai (Foxconn), Pegatron and Compal, account for around half of the global industry's turnover. The market for European electronics manufacturers is much smaller and more fragmented, with the 30 largest European companies accounting for only around 2%-3% of total industry turnover. Asia's dominant share is driven by the historically lower cost level of the region than in developed economies which has attracted equipment manufacturers and their subcontracting chains to the region to maintain their cost competitiveness. Within Asia, however, the cost dynamic has been shifting over the last decade, since strong cost increases, particularly in China, have resulted in new production and relocation of old production to more advantageous regions, like India and Vietnam. In addition to rising cost levels, this shift has been fueled by trade and geopolitical tensions in China, the risks of concentration in supply chains brought to the surface by the COVID pandemic, and increased awareness among equipment manufacturers of the total cost of supply chains. In Eastern Europe, labor costs are roughly 30-40% less than in Western regions, although wage inflation has also been high there.

With the personnel intensity of operations and constant price pressure, we believe that actual volume production will continue to focus on low-cost areas. In line with this, we believe the primary role of Western production plants is to focus on narrower and higher requirement level niche segments, fast deliveries and product development series.

Industry's earnings models

OEM

- OEMs who own the brand and intellectual property rights of the end products
- Core operations include product development, design and sales
- Good value chain position and pricing capacity
- EMS customers

ODM

- OEMs whose end products are re-branded under the OEM
- Own the intellectual property rights themselves
- Core operations include product development, design and manufacturing
- Can utilize the resources of EMS companies

EMS

- Contract manufacturers who do not own the intellectual property rights of the products they manufacture
- Core activities include manufacturing and related support activities (e.g. material procurement)
- Provide OEM companies with direct cost and capacity benefits

Distributors

- Wholesalers or retailers who focus on selling components and technical support
- No own design/ manufacturing, competition is driven by the principal portfolio
- At global level, the number of distributors is massive

Source: Inderes, Incap CMD, in4ma

Industry and competitive landscape 2/6

On the other hand, production chains moving progressively closer to equipment manufacturers' product development and end markets, the need for decentralization of production chains and the continuous development of production technologies (e.g. automation) should support the strategic roles and competitiveness of Western units, also in view of volume production.

Four segments on the market

The market can be divided into four segments: consumer electronics, industrial electronics, electronic components, and public sector electronics (e.g. defense). In consumer electronics, the technical requirements for applications are generally not very high, but the delivery volumes are large (low mix / high volume). The successful contract manufacturers in this segment are huge in size and have vast production resources. In consumer electronics, the product cycles are also short – about 2-3 years – and competition is price-driven and harrowing.

Incap is positioned in the industrial electronics sector, where product specifications are generally high and delivery volumes are on average much smaller than in consumer electronics (high mix / low volume). In industrial electronics, product cycles can be up to 20-30 years, making the contract manufacturer a strategically important partner for the OEM and highlighting the role of own product development expertise and after-sales customer service. This in turn makes the competition in industrial electronics healthier and creates attractive business opportunities also for smaller players.

Although volumes are mainly lower in industrial electronics and higher in consumer electronics, there are exceptions within segments. Incap also has some consumer products in its portfolio and their potential should not be overlooked.

The growth picture is excellent

The growth of the market is driven particularly by the electrification of the world. This in turn will be driven by rising living standards, digitalization, an aging population, and the green transition. Supported by these factors, the total market has grown by some 4-5% per year according to different research companies. The growth rate is expected to remain healthy in the coming years, although in the short term the deteriorating economic situation, inflation, and rising interest rates could worsen the situation. On the other hand, the green transition, and thus the longer-term growth in investment, can be a potential driver. Geographically, growth is estimated to be fastest in Asia, which is expected to reach 4-6% annual growth. In Europe and North America, however, market growth is estimated to remain at 2-3%, in line with the slower development of the general economy.

In addition to global drivers, another market driver in recent years has been increasing outsourcing among OEMs. The industrial logic of this is very clear, as outsourcing of production frees up OEMs' resources for their core operations, while generating direct cost savings. Outsourced production also enables OEM companies to better manage their capacity and cash flow as investments can be transferred and growing demand can be met by utilizing contract manufactures' resources. In addition, reflecting this dynamic, OEMs can achieve certain cost-related flexibility in their typically rather fixed cost structures. As a result, the aggregate level growth of contract manufacturers has increased in recent years more rapidly than in the electronics market as a whole. We believe that the situation will continue as is, reflecting the overall benefits mentioned above.

In industrial electronics, the outsourcing rate has been clearly lower than in consumer electronics, as smaller and more demanding delivery batches raise the threshold for large-scale outsourcing. However, we estimate that, with the benefits offered by contract manufacturers, reducing own manufacturing resources will become more popular among industrial electronics OEMs and especially among new companies entering the market (i.e. no large-scale production investments). Considering this we believe that growing demand will increasingly be directed toward contracting manufacturers that have demonstrated both their quality level and delivery reliability. This evolution creates preconditions for capable contract manufacturers to strengthen their own value chain positions, as we estimate that the focus of demand will gradually shift from pure PCBA to total deliveries with higher added value. Currently, we understand that the outsourcing rate for industrial electronics is around 35%, so even a small increase in the outsourcing rate would provide contract manufacturers with many new business opportunities in a large market.

Source: Inderes

Industry and competitive landscape 3/6

Incap has a strong position

Considering the long-term growth and profitability potential of industrial electronics, we consider Incap's positioning sensible. In addition, Incap is a relatively small player relative to the total market and, therefore, is not dependent on the growth rate at market level. On the other hand, the company does not operate in a vacuum. Thus, as the overall market grows, larger players than Incap may leave very attractive niche segments in their fringe areas. Of course, a slowdown in market growth would most likely result from hiccups in the general economy and would have some effect on Incap's own production volumes and thus on the result lines through the business challenges faced by customers .

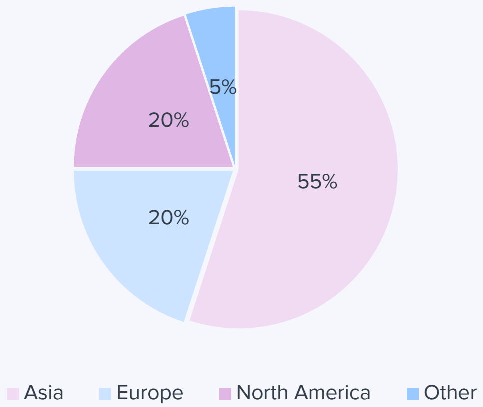
We believe that Incap's production plant network is well structured, as it can provide its global and potential global customers with a logical route from prototypes produced close to product development, to cost-effective volume production located next to the end market. In particular, the Indian production plants, located in the world's largest democracy, are a major asset for the company, thanks to the massive size of the local market, the favorable location (i.e. benefiting from lower China risks) and the admirable performance. In view of these factors, the existing ability to invest and the operating model that allows for comprehensive deliveries, we feel Incap's position relative to the target market and the forces that shape it can justifiably be seen as strong.

Plenty of competition

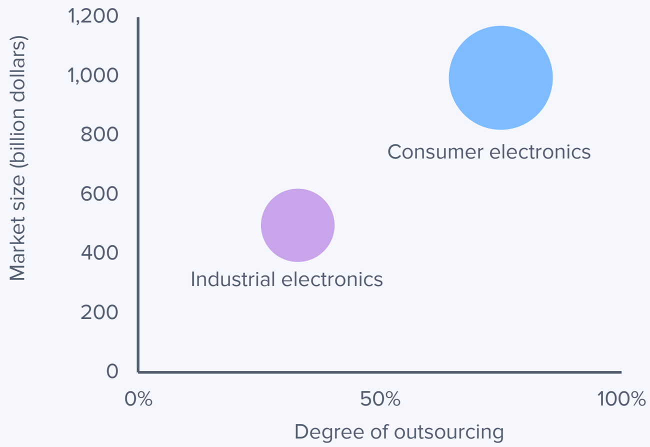
Due to the earnings logic of the industry, contract manufacturers' value chain positions and thus limited pricing power, the basic nature of the competitive landscape is harsh. Despite this, customer retention has typically been good in the industry. We believe this is particularly supported by the fact that the costs of switching contract manufacturers can be high, so customers try to stick to the same suppliers for as long as possible. In line with this, OEMs only change contract manufacturers for weighty reasons, like constantly extended delivery times. High switching costs also have a downside, as they make it more difficult to attract new customers.

Despite the global structure of operations, the local nature of customer relationships has remained strong. We, therefore, estimate that Incap has a large number of customers from northern Europe, Great Britain and the Baltic States, while the customer portfolios of Central European manufacturers consist more clearly of local target market players. Accordingly, Incap's competitive landscape varies regionally and battles are partly fought with different companies in Europe and Asia. In addition to regional factors, the competitive situation is also influenced by the underlying industry (i.e. the positioning of competitors) and the size and solution needs of the customer.

Geographical distribution of the market



Degree of outsourcing on the market



Source: Custer Consulting Group, In4ma, Inderes

Industry and competitive landscape 4/6

Three-tiered battle

Contract manufacturers are typically divided into three groups based on revenue. The largest companies (revenue > 1,000 MEUR) operate extensively across the electronics industry segments, and another common denominator for these players is massive production resources, especially in low-cost regions. Due to their large size, these players have typically operated in the low mix/high volume segments and are thus not very relevant competitors to Incap. However, these companies cannot be completely ignored, as their large-scale operations inevitably extend to customer sectors that are important to Incap. Within their financial resources, large companies have a huge investment capacity and thus the potential to change the prevailing dynamics of the competitive landscape, but we do not see this as an acute threat to Incap.

The annual revenue of the second-tier companies is EUR 200-1,000 million. These companies typically operate with global operating models but concentrate on one or more market segments. Mass production of consumer electronics is largely outside the capabilities of these players, but flexibility and agility are still sufficient to bring competitiveness to smaller manufacturing batches and tailor-made customer service. We believe that a large part of the main competitors come from this segment. We feel the current/future competitors worth mentioning among medium-sized companies are, e.g., Finnish Scanfil, Norwegian Kitron, German BMK Electronics and Katek, Swedish Note and Hanza, and Swiss Enics and Cicor.

The third tier includes players with annual revenue of under EUR 200 million. The resources of companies in this size-class are somewhat narrower than those of medium-sized manufacturers, which means that their service offering may also be smaller. In addition, the share of the biggest customers of the entire portfolio of these companies can be extremely high. The main competitive advantages of the smaller-end companies focus on agility and flexibility, specialized products, and fast lead times. Among these companies Incap competes, e.g., with Swedish Inission, French Lacroix, Finnish Kyrel and Darekon, and British JJS Manufacturing and SMS Electronics. Incap also competes with a number of small local operators specialized in prototype and small series production and with OEMs' own productions.

Consolidation shapes the competitive landscape

The industry as a whole is very fragmented, with over 2,000 contract manufacturers in Europe alone. The number is even higher in Asia, although in terms of turnover, the sector is more concentrated in Asia with large players. In recent years, the large number of players and efforts to improve value chain positions have driven the consolidation of the sector. We expect this will continue to affect the structure of the competitive landscape reflecting the industrial logic of the underlying drivers (e.g. the pursuit of economies of scale in purchasing). For Incap, the structure of the industry is favorable, as it provides ample opportunities for M&A activity.

Incap is among the leaders in the industry

Incap's profitability level is among the highest in the industry, which we believe is a tangible reflection of both its successful strategic positioning and its focus on its core strengths, as well as the tailwind from the largest customer's strong growth. However, the high profitability does not come from relative pricing power, since Incap's sales margin is at a normal level for the industry. Therefore, maintaining the correct positioning and, especially, maintaining the operational efficiency is a necessary measure in an environment characterized by constant price pressure. Against this background, we do not consider it likely that Incap will be able to substantially (>2 percentage points) increase its margin level in the coming years, despite a gradually improving sales mix, sourcing power supported by a larger size and an increasing relative share of Indian production.

Due to the low capital intensity of the industry, it is possible to generate higher returns than the COE requirement with relatively thin profit margins. With better profitability than its competitors and efficient use of capital, Incap's ROI has been excellent in recent years and quite clearly higher than for its competitors. Thus, based on the figures, we believe Incap is one of the highest quality players in the industry.

Source: Inderes

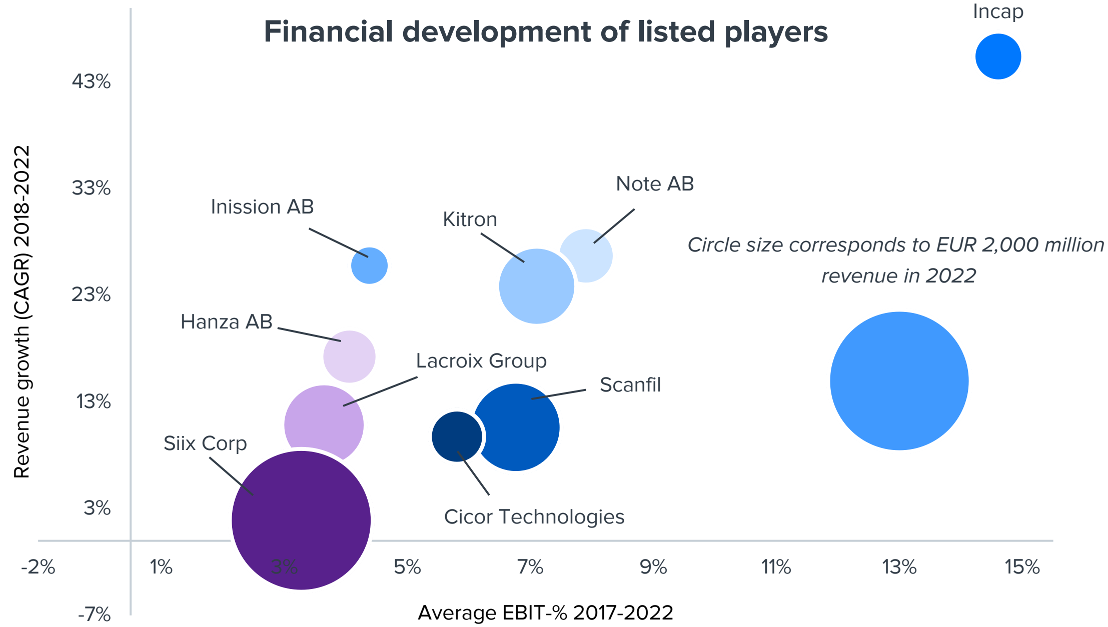
Industry and competitive landscape 5/6

Selected contract manufacturers

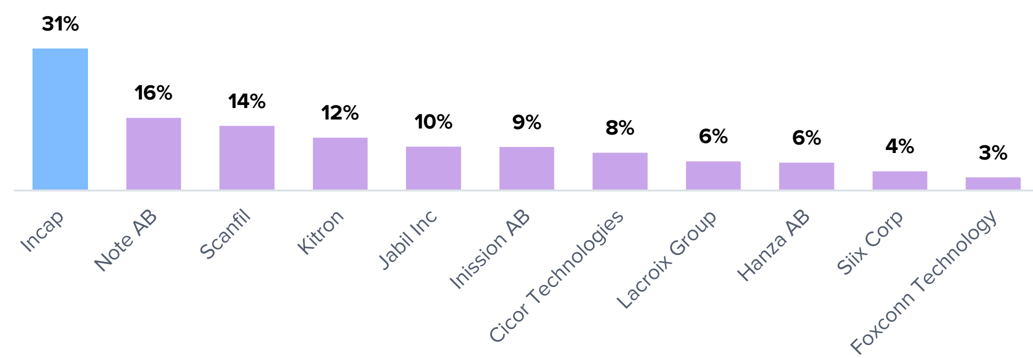
Contract manufacturers operating with high production and financial resources with a strong presence in consumer electronics

Strong players with resources for large service packages and focus almost entirely on industrial electronics applications

Companies with a slightly narrower service offering that are flexible and agile



Average ROIC 2018-2022



Source: Inderes
Source: Refinitiv, Inderes, companies

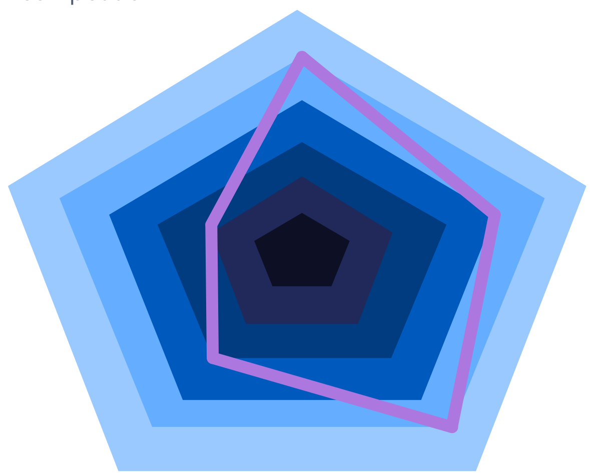
Industry and competitive landscape 6/6

Current competitive situation (significant*)

- The number of contract manufacturers is very large globally and value chain positions are fundamentally challenging
- Cost structures of OEMs are reasonably rigid, increasing their price sensitivity and partially tightening competition
- A healthy long-term growth picture lowers the tightness of competition

Threat of substituting products (minor*)

- Contract manufacturers do not have own products and the threat of substituting products manifests through customer portfolios
- We do not believe that a drop in the degree of outsourcing is a relevant threat, considering the overall benefits offered by contract manufacturers
- There are also no change catalysts in sight that would quickly replace existing production technologies



Negotiating power of suppliers (moderate*)

- Component production is rather concentrated, which limits the bargaining power of distributors and, consequently, also contract manufacturers
- Producers also have little differentiation capacity
- The supply chains of contract manufacturers are decentralized and dependence on a single supplier is moderate
- There is a risk of further integration of component suppliers, and this has also been realized in recent years

Threat of new competitors (low*)

- Ramp-up of operations does not require massively heavy capital investment and the industry growth picture is healthy
- Due to the switching costs for OEMs and the operating dynamics new customer procurement is slow, which reduces the risk of completely new competitors
- Achieving competitive technology and process expertise requires a sufficient scale

Buyers' bargaining power (significant*)

- OEMs supply chains are typically more decentralized than contract manufacturers' customer portfolios (i.e. the OEM is more important for contract manufacturers than vice versa)
- There is a low risk of contract manufacturers' backward integration, while OEMs also have their own production
- Contract manufacturers' differentiation capacity is limited to service level, but the cost of switching can be high
- In industrial electronics, the price sensitivity of OEMs is lower than in consumer electronics

*Inderes' view of the threats caused by industry power for Incap on the scale no threat, minor, low, moderate, significant and high.

Source: Inderes

Strategy 1/5

Value proposition in quality and supply reliability

We believe that Incap's long operational history has created a reputation as a reliable contract manufacturer. We do not believe that it is possible to build long operational history and good reputation without creating lasting customer value. In turn, we consider the consistent redemption of the value proposition given to be the most essential elements of this. We believe that the value proposition of Incap's strategy is to be both a reliable and competitive manufacturing partner that strengthens its value chain position over time with an extensive, high-quality and secure supply.

Cost-efficiency is key

Reflecting the company's operating model and results of recent years, we believe it is clear that high cost efficiency is key to implementing the strategy. Through cost-efficient operations, Incap is able to improve its overall competitiveness and open up important parts of value chains for strategic partnerships. At the same time, cost-efficiency creates a strong basis for making excellent profitability and creating shareholder value.

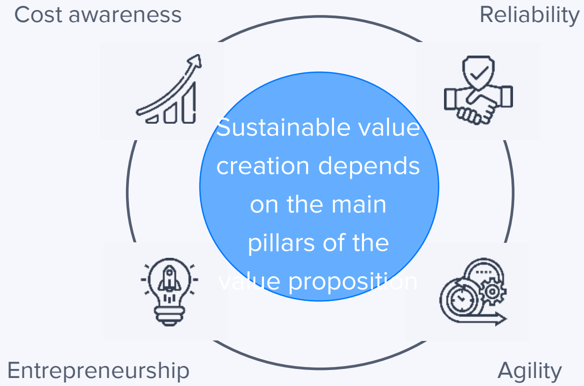
Cost efficiency, and especially maintaining it, also plays a key role in terms of competitive dynamic. Incap's current cost-efficiency enables the company to achieve good profitability levels in an environment of chronic price pressure, even if sales prices had to be cut in a negative scenario. Due to the nature of the industry, sufficient price competitiveness is an essential hygiene factor, which means that continuous focus on efficiency will be a key strategic and, to some level, tactical priority for the company in the future as well. However, it is not necessary to seek the label of the lowest-priced manufacturer in the competitive landscape, nor do we expect the company to do this.

Grabbing for strategic partners

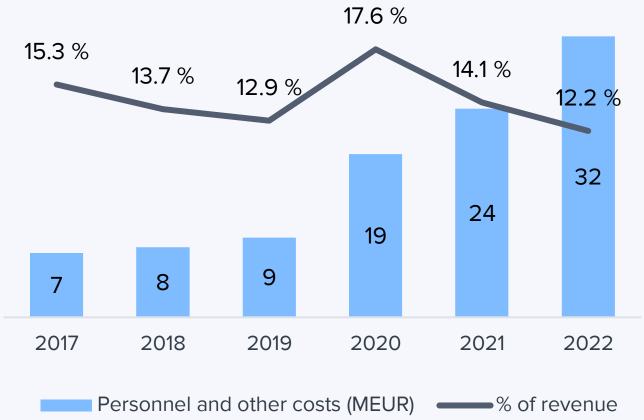
We estimate that with high cost efficiency and awareness Incap aims to build a platform for long-term customer relationships and thus for establishing strategic partnerships. This is logical, as we estimate that long customer relationships have typically led to 1) a higher customer-specific outsourcing rate and/or a higher share of the customer's outsourced production activities, 2) entirely new applications, and 3) the sum of these leading to higher order volumes. Thus, investing in and succeeding with long-term customer relationships is an important fuel for growing the business in the longer term.

By entering into strategic partnerships, Incap aims to position itself as an important production resource for the customer and, as mentioned above, to control as large a part of the value chain of the end product as possible. In addition, the industrial logic behind strategic partnerships is to increase the cost of switching from one contract manufacturer to another and to strengthen one's own competitive advantage.

The core of the strategy



Personnel costs and other costs



Source: Incap, Inderes

Strategy 2/5

We believe that in the big picture the euro-denominated starting level of the strategic partnership is not a key issue for Incap, we believe that the expected longer-term growth potential of the customer relationship and possible reference points are more important for the company. Considering this, we expect that the company considers a customer with a lower initial order flow from a completely new industry/with attractive growth potential to be strategically more important than a somewhat larger player that operates in a more mature market and is in a more mature development phase. In addition, it is also essential to avoid investing in small customers who do not have the capacity to grow and scale up.

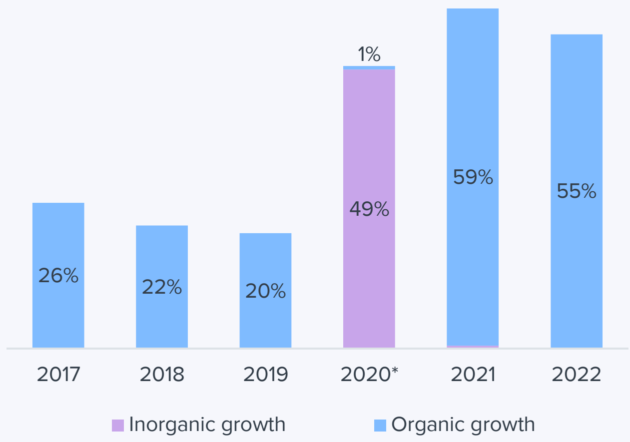
In line with the structure of Incap's customer portfolio, the establishment of new strategic partnerships also has a risk management function. However, due to the logic of the industry (e.g. time span from prototypes to volume production), new strategic partnerships are the result of very long-term work and we estimate that the progress of new customer relationships to a size class that affects the structure of the portfolio can take years. Of course, this dynamic is not universal and in the right circumstances (e.g. rapid development of the customer's business) new strategically important customers can become economically relevant relatively quickly.

Growth in sight

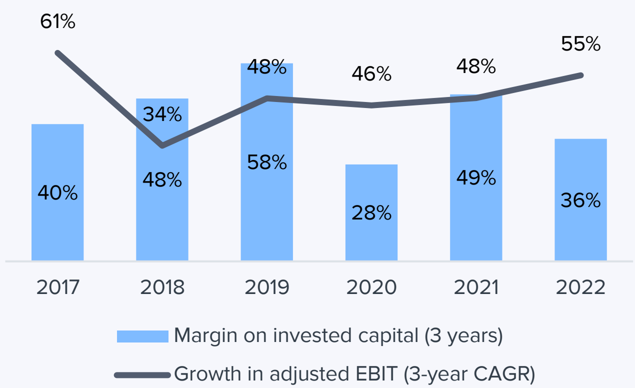
By implementing its strategy, Incap unsurprisingly targets profitable business growth (RONIC > WACC). We believe the cornerstones of this work are the preservation and strengthening of long-term customer relationships, progressing new customer procurement, maintenance of efficiency levels and M&A transactions. In recent years, the company has established a strong operational performance. As far as we know, the company has not encountered any negative surprises in the integration of AWS, and there are no significant development projects underway for a company of its size. Considering this, Incap should have full capacity to focus on implementing its strategy and creating shareholder value.

Incap seeks organic growth through both established and new customers. We estimate that the key customers in Incap's portfolio are competitive companies in their respective operations, which together with Incap's own strengths provides a solid basis for growing with these customers. Own core strengths, the expanded plant network though the AWS acquisition and the relatively small size on a global scale – we estimate that the share of the largest customers' production chain is still relatively small – also create reasonable conditions for customer-specific market share gains.

Structure of revenue growth



Return on new invested capital[1]



Source: Incap, Inderes
[1]Capital invested and EBIT growth over the last 3 years

Strategy 3/5

Such gains can also be a small risk-management success if they mean, for example, entering into entirely new applications within the customer.

Incap also has many small companies in early stages of development in its portfolio. With right positioning and innovative solutions, the businesses of such companies can grow very rapidly. Considering the strong service ability created by the operating model that allows for large comprehensive deliveries and fast decision making, we believe Incap's position in realizing the longer-term opportunities these customers bring is good. However, in the short term, the direction of the delivery flows is dominated by progression of the larger customers due to the concentrated structure of the customer portfolio.

In terms of new customer acquisition, we expect the focus to be on strategic partnerships. In addition to the time typically taken by volume-production ramp-up, one should also consider the switching costs faced by OEMs when discussing new customers. Since these costs can rise to a relatively high level, OEMs restructure their production and supply chains relatively rarely. Thus, success in customer acquisition does not directly guarantee visible organic growth in the short term but will be more clearly visible only in the medium and long term.

Acquisitions as complementary elements

Incap tries to boost organic growth through acquisitions. In its current form history, the company made its first inorganic move with the AWS arrangement in January 2020. In terms of strategic value, the AWS acquisition was significant, as it resulted in Incap nearly doubling its size class, expanding its geographical footprint into new areas, and strengthening both the production plant network and total offering. In addition, the arrangement took Incap into new industries and balanced the customer portfolio, although the faster growth of the largest customer group after the acquisition has of course taken its toll. AWS' cultural fit was also excellent, of which the integration work without major problems and realized procurement synergies are concrete proof.

Even though the sensibility of future acquisitions is always case-specific and affected, e.g., by the price and the nature of the acquired business, our view of Incap's desire to grow inorganically is positive. Our view is supported by the following factors:

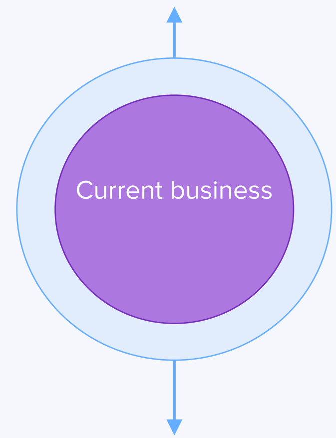
Cash flow profiles for acquisitions are positive from the start and the arrangements will result in significantly faster results than organic investments.

Acquisitions automatically expand the customer base while opening up new geographic/industrial areas. In addition, these extensions and openings can bring different cross-selling opportunities. Acquisitions can also be seen as strategic measures to gradually reduce the overall risk level.

Anatomy of organic growth

Current customers

- For long-term growth, winning new product generations for existing customer applications is very important (i.e. focus on high retention)
- Growth in customer-specific market shares is most valuable when the value chain position expands
- The combination of good customer relationships and own competitiveness also provides the basis for winning new applications



New customers

- We believe the aim of new customer acquisition is to scale different industry expertise
- Small early-stage customer relationships must have viable longer-term growth potential
- We believe companies operating in applications nearing the end of their life cycle/shrinking business operations are not, in principle, optimal new customers for Incap

Source: Incap, Inderes

Strategy 4/5

Cheap acquisitions (valuation multiples lower than own multiples and reversed ROIC > WACC) generate shareholder value already in the short term, which also results in good long-term value creation potential. Moreover, arrangements made at low deal prices provide a safety margin against the weaker-than-expected development of the acquired business and/or possible deterioration.

The structure of the industry is very fragmented. This provides Incap with a large critical mass to implement the acquisition driven strategy.

In our view, acquisitions do not offer massive cost synergies in the industry, mainly due to the moderate weight of fixed costs in the portfolio. The logic of the M&A must therefore be based on something other than the achievement of large spending synergies.

The approach is quality-oriented

We expect the company to follow a rather conservative model in terms of gauging potential targets, and we do not see Incap as being at all interested in turnaround companies operating at a loss or with very low profitability. We believe that such a quality-oriented approach is justified considering the usual risks associated with M&A transactions and their management.

In addition to the actual quality of the business, we believe that the company is very meticulous in screening the acquisition targets when it comes cultural fit. We believe Incap's independent production units are managed in a very entrepreneurial way, which means that the top level of the organization structure is rather light and decision-making is mainly at local level. Therefore, we consider that Incap is particularly interested in players who are managed in accordance with the company's own principles. In addition to calculating the risks associated with the integration phase, we believe that such selectivity is also sensible in terms of efficiency, since buying players with heavier administrative operations and centralized decision-making would inevitably result in rigidity in Incap's own structures.

Geographically, we believe the focus will be primarily on Central Europe and North America due to familiar market dynamics. These are huge blocks in absolute size, where the outsourcing rate has clear room for improvement. Reflecting these factors, we estimate that there are a reasonable number of targets that meet Incap's criteria and are of sufficient size (turnover > 25 MEUR), especially in Central Europe.

However, we do not expect the company to build a production plant in a completely new region, but rather use the capacity of the existing production plant network (especially in Infia). We estimate that the total cost of a greenfield plant would be approximately EUR 10-15 million, depending on size, which would not be a particularly high investment relative to Incap's balance sheet. However, such a plant would initially rely solely on existing customers, which would mean that the time gap between the investment and positive cash flow would be quite long. We therefore consider an acquisition of the same size to be a more reasonable option, under certain conditions.

Acquisitions

1

Cultural fit

- The company to be purchased must fit perfectly to Incap's entrepreneurial and flexible operating culture (e.g. independently operating production units)
- Recognizing cultural suitability requires time, but investing in assessment and especially in nurturing reduces the risks associated with the integration phase

2

Financial performance

- Incap's resources for various turnaround exercises or seeking considerable operational synergies are limited, so the company to be acquired must operate at a healthy earnings level
- An approach that fosters operational quality can lead to higher valuation multiples but on the other hand, the risks of the acquisition strategy are lower than in the opposite situation

3

Strategic logic

- For smaller transactions, we estimate that the underlying logic relies on quick but limited synergies (e.g. procurement and capacity).
- In larger ones, the logic is to gain access to new industries and their customers
- We feel the common strategic denominator of different sized M&A transactions is the strengthening of the geographical footprint and construction of cross-selling routes.

Source: Incap, Inderes

Strategy 5/5 – SWOT

Strengths

- An operating model that is highly cost-effective and enables fast decision-making
- A global and efficient production plant network (especially the Indian factory)
- High basic profitability and return on capital
- Strong balance sheet

Weaknesses

- Under normal conditions, the order backlog structure is short
- Dependence on major customers and especially the largest customer
- Direct pricing power is limited and the value chain position is challenging
- New customer gains are slowly reflected in the current size class

Opportunities

- Long-term growth drivers are healthy
- The degree of outsourcing in industrial electronics is low
- A strong balance sheet and industry structure enable value-creating acquisitions
- OEMs reducing their China risk and transferring supply chains closer to the end customer (i.e. localization)

Threats

- Loss of a key customer / customer's own business challenges
- Cost-efficiency erosion and decision-making becoming more rigid
- Failure in acquisitions
- In the longer term, structural changes in the competitive field

Source: Inderes

Financial position

Balance sheet offers leeway

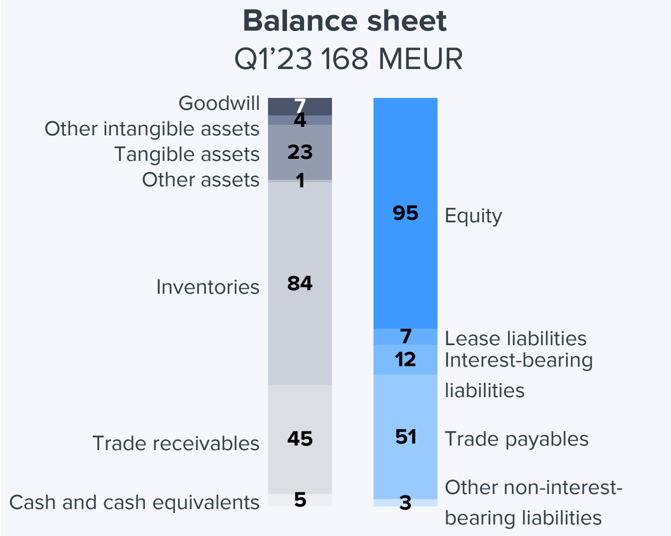
At the end of 2022, Incap had an equity ratio of 54% and a net gearing of 16%. At the end of 2022, the company had about EUR 8 million in cash, which together with undrawn credit lines is reasonably sufficient to run the business in a flexible manner. However, due to rapid growth, the strong earnings performance has not been reflected in the cash flow and for larger growth projects, the company would have to arrange external financing and/or wait for the inventory to be liquidated. In our view, there are no significant write-down risks in the balance sheet for a company of Incap's size (incl. the very small amount of goodwill).

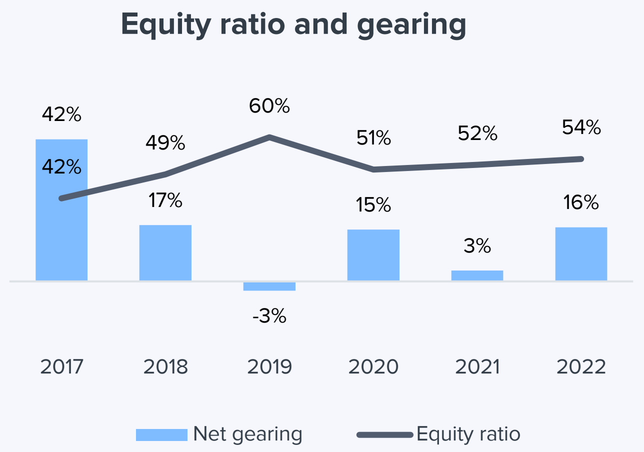
A strong capital structure and a good profitability and growth profile underpin Incap's structural debt capacity and financial flexibility. However, we would not be surprised if, in the eyes of external lenders, the concentrated customer structure partly limits the benefits of these strengths. Given the M&A arm of the company's growth strategy, we believe Incap is interested in running its machinery with a more aggressive lever than the current situation, but with a capital structure that maintains a sufficient overall sense of security. We estimate that such a balance sheet, in terms of net gearing, could mean a level of around 20-40%, or a 1x-2x range in the net debt/ EBITDA ratio. At these levels, the company would have reasonable leverage to improve its return on equity.

Reflecting the year-end balance sheet and the debt parameters we consider to be in the comfort zone, we estimate that Incap would have around EUR 50-75 million of free debt capacity for inorganic growth within its balance sheet. By applying the 6x-8x EV/EBITDA ratio (current valuation at the top end of the range) that we find typical for an unlisted contract manufacturer, this would mean the ability to purchase operational earnings growth of about EUR 6-12 million (or 10-20%) with debt alone. Recently, we believe that there is a certain mismatch between the price and quality of acquisition targets that meet Incap's criteria, which has contributed to a slowdown in acquisition-driven growth. However, we expect the company to wait patiently for the right opportunity to move forward on the inorganic front with a reasonable risk/return ratio.

Cash flow is normally lower than the result

Considering Incap's organic growth picture and the working capital needs it requires, the cash flow ratio (cash flow from operations/EBITDA) is generally under 100%. However, this is normal for contract manufacturers and Incap's cash-flow profile is in no way different from normal. In our view, the company's fixed capital expenditure needs for the coming years are moderate, which together with high operating profitability should provide the basis for comfortable free cash flow generation at a time when even rocket-like growth is unlikely to continue. Looking further ahead, good cash flow is also a prerequisite for profit distribution, although, as mentioned earlier, we hope that the dividend will remain a minor side stream in Incap's capital allocation.





Source: Incap, Inderes

Estimates 1/4

Estimate model

We estimate Incap's revenue development in the short and medium term based on underlying market growth, estimated customer-specific market share changes, and new customer acquisition based on relative competitiveness. Our longer-term estimates, in turn, are largely based on the combination of the expected growth of the electronics industry and Incap's own core strengths. We model short- and medium-term profitability line by line for different cost items. In the long term, we anticipate profitability through the margin levels we assess to be sustainable.

We have not included M&A transactions that we find likely in the medium term at the latest in our estimates. This is because it is impractical to assess the exact timing, size and other characteristics of the transactions (e.g. purchase price, financial structure and quality of the company being acquired).

Customer risk partially realized at the beginning of Q2

Incap got off to a positive start in 2023, as the demand outlook remained strong in the winter and the company had much-needed capacity coming online in India during Q1. The macroeconomic picture has also developed reasonably well, as the recession expected in much of the West last year has so far remained mild, thanks to a buoyant labor market and calming energy markets, among other factors. Reflecting this situation, Incap guided in February that its revenue and EBIT for the current year would be higher than last year.

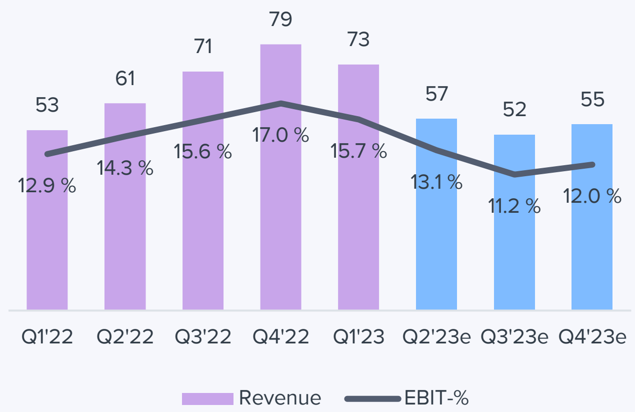
However, the picture changed significantly in April, as Incap's largest customer (who we estimate is Victron Energy) decided to reduce its inventory levels after its growth was slower than expected due to changes in market dynamics and a downturn in some markets. In addition, the improved availability of components has enabled the company to reduce inventories. Incap has been supplying Victron Energy, particularly from India, so the destocking particularly affects the company's most profitable plants in India. However, the situation has no impact on other factories, as Incap has estimated that its other customers will continue to grow this year.

As a result, Incap's biggest single risk (i.e. client risk) was partially realized and this forced Incap to issue a profit warning in April before the Q1 results were published. Incap now estimates that its revenue and operating profit (EBIT) for 2023 will be lower than in 2022. Given the percentage ranges behind Incap's verbal guidance, this means in practice a 1-20% decline in both revenue and EBIT year-on-year.

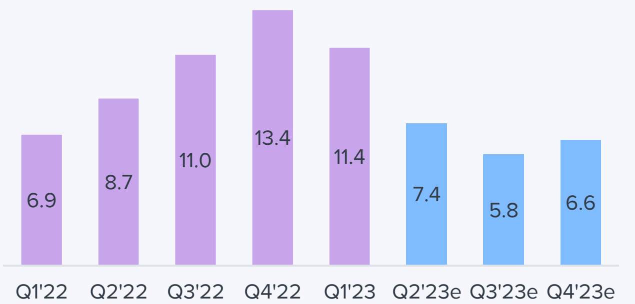
Q1 was still good

As Victron Energy's need to reduce inventories was only realized in Q2, Q1 went well for Incap. In Q1, Incap's revenue increased by 36% to EUR 73 million. The strong growth was driven by strong demand and improved delivery capacity through capacity investments. In Q1, Incap's adjusted operating profit increased by 64% compared to the satisfactory comparison period and amounted to EUR 11.4 million. The company's profitability (adj. EBIT-%) remained at a strong level of 15.8% due to high volumes and a favorable product mix. Incap's EPS increased to EUR 0.29 in Q1, reflecting the EBIT growth rate.

Revenue and EBIT-%



Adjusted EBIT



Source: Incap, Inderes

Estimates 2/4

We estimate that the company's cash flow was positive in Q1, although we expect it to be somewhat below earnings due to the working capital commitment. Thus, Q1 was still going very well for Incap before the acid test in the following quarters.

Long bullish streak snapped this year

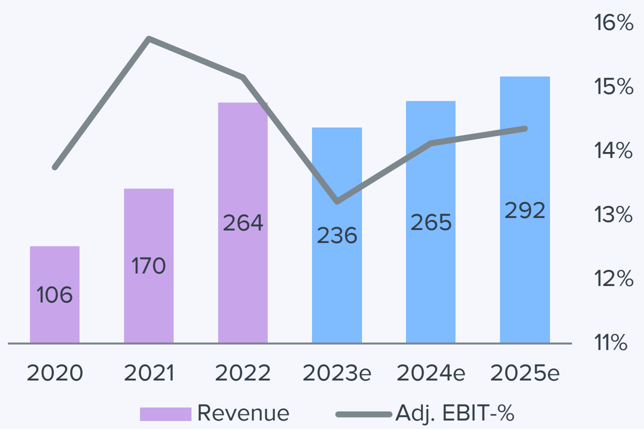
We estimate that the gradual reduction in Victron Energy's deliveries has started during Q2. However, we understand that Victron Energy has not stopped buying altogether. Reflecting a long strategic partnership, the companies have devised a plan whereby, in order to reduce Victron Energy's inventories, Incap will manufacture products for Victron Energy at a slower pace than Victron Energy's sales. We think the plan is good for Incap, as it is important for the company to keep production running to maintain its competence and competitiveness, and the gradual reduction of inventories rather than a total stop will reduce the scale of the company's short-term earnings decline. On the other hand, the duration of the need to reduce inventories is still open and will depend on the development of sales, especially at Victron Energy, where there is considerable uncertainty. Given Victron Energy's large share of revenue, other customers can only make up for this to a limited extent. Incap will also be virtually unable to find new customers for its Indian factories this year, given the typical new sales cycle in the sector.

Given the narrow scope of Incap's guidance, Victron Energy's dominant revenue share, and Victron Energy's apparently limited visibility into its own business, we do not believe that Incap's meeting its guidance is a certainty at this stage of the year. However, Incap has traditionally been setting its guidance ranges conservatively, so we believe that the company has included safety margins in the guidance.

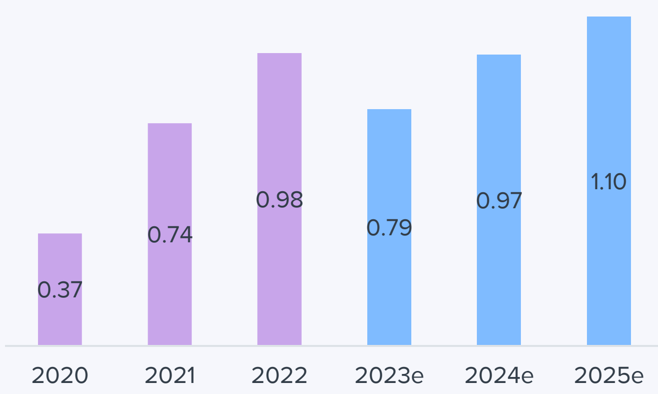
Looking at this overall picture, we expect Incap's revenue to decline by 10% this year to EUR 236 million. We expect Q2 to still be reasonable for the company, but H2 revenue and earnings levels will fall sharply due to declining deliveries to Victron Energy. Our estimates now reflect an increase of around 20% in other customers in a favorable demand environment and a 25% drop in Incap's Victron Energy sales for the current year due to the destocking. We have not made any material changes to our revenue estimates for the current year, but we have slightly adjusted the quarterly breakdown of revenue.

Excluding Incap's one-off items and minor PPA depreciation, we estimate EBIT to be EUR 31 million this year, which corresponds to an earnings drop of around 20% at the lower end of the company's guidance range. We have not made any material estimate changes for this year. Operating profit will be particularly burdened by the decline in revenue, but thanks to its low and flexible cost structure, we expect Incap to deliver a strong adjusted EBIT margin of 13% this year, in line with the industry context. In our view, defending profitability will require the company to abandon its temporary workforce in India and otherwise actively manage costs. We estimate that the drop in profitability will come entirely from the most profitable plant in India, while we expect the other plants to improve their profitability through volume growth. In our view, the weakest point in terms of profitability lies ahead in late summer.

Revenue and profitability



Adjusted EPS



Source: Incap, Inderes

Estimates 3/4

We estimate that Incap will be able to avoid inventory write-downs, as the company only buys stock against a hard order from a customer. Thus, the fall in the inventory values should not affect the company's profitability.

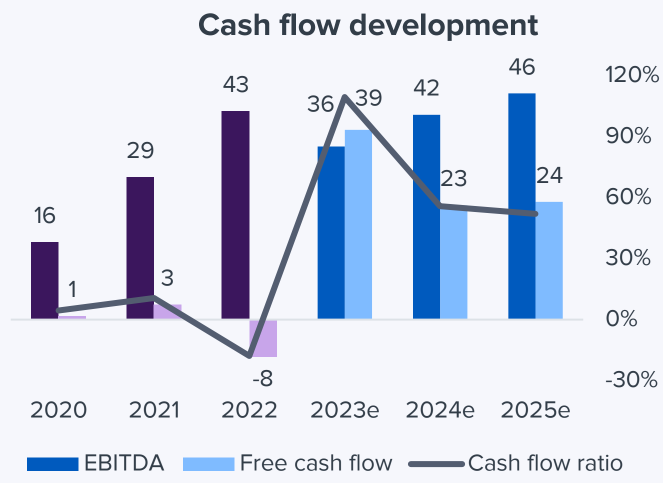
After low financing costs and a normal tax rate of around 24%, we expect Incap to achieve adjusted EPS of 0.79 this year. The silver lining in the revenue drop is cash flow, which we expect to improve significantly as capital is freed up from the substantial increase in inventory, which has grown at a rocket-like rate in recent years, as volumes fall and the component situation improves. We estimate that Incap's free cash flow will be close to EUR 40 million this year as working capital will be released. We expect the company's investments this year to be a moderate EUR 4 million, consisting of the tail end of the investment in the third plant in India and small investments in other plants. At the end of this year, we estimate that Incap's balance sheet will be clearly net debt-free if there are no acquisitions before then.

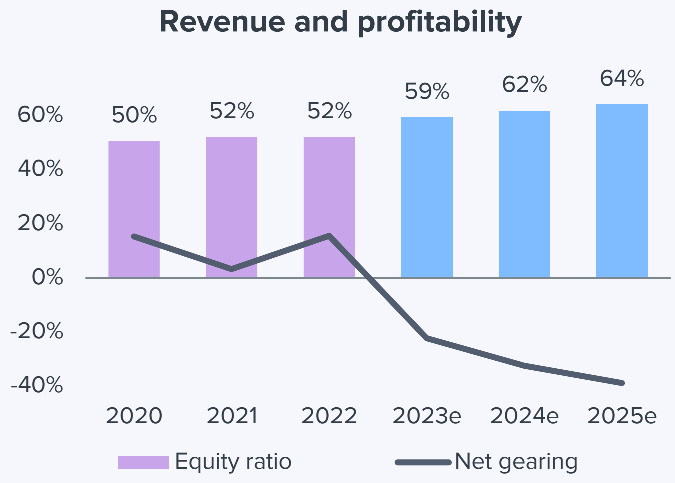
Back on growth track from next year onwards

Our estimates for 2024-2026 are based on a scenario in which macroeconomic growth remains sluggish, especially in 2024, but economies avoid a clear and prolonged recession. However, there are still risks with a recession still being possible, especially for 2024, as the overall impact on economies of the 2022-2023 rate hikes in Western countries to fight inflation becomes clearer. Underpinned by the green transition, we expect investments in clean energy and energy efficiency in particular to remain active, but the pace of the green trend may also depend partly on economic and financial market conditions.

For the estimated largest customer, our forecasts are based on a scenario in which Victron Energy's revenue continues to grow at a much slower pace than in recent years. We estimate that this would allow Incap's deliveries to Victron Energy to return to growth in spring/summer 2024 and the most intensive phase of the destocking to take place in H2'23. Of course, the predictability of this situation is still very weak and we stress that, given Victron Energy's large share of sales, the progress of this customer's deliveries will determine to a large extent the organic growth outlook for Incap's overall sales. We forecast that Incap's other customers will continue to grow in 2024-2026, but this is of course somewhat subject to economic developments.

Reflecting this baseline scenario, we expect Incap to grow organically by 8-12% between 2024 and 2026. Growth is driven by Victron Energy's delivery turnaround in H1'24, steady but slowing growth from 2022 onwards for other customers and moderate organic market share gains and Incap's good delivery performance. In terms of operational results, we expect Incap to achieve an adjusted EBIT margin of 14-15% in the coming years, as volume growth, revenue share growth from efficient production facilities in India, and a low cost structure will bring profitability close to the company's recent historical levels and potential. On the lower lines of the income statement, we expect financing costs to be low and the tax rate to remain stable at around 24%. Our medium-term estimates are virtually unchanged.





Source: Incap, Inderes

Estimates 4/4

Incap's EPS will reach around 2022 levels in 2024 and grow by an average of around 12% p.a. thereafter until 2026.

We expect cash flow from operations to remain slightly below earnings as growth continues to tie up some working capital, but with a more moderate growth rate in 2020-2022, Incap's cash flow will be significantly stronger than in these years. In terms of organic investment needs, we estimate that the next few years will see moderate purchases of individual new production lines for various factories until the full capacity completed in India in 2023 is sold. The net profit and the clearly positive free cash flow also strengthen the company's balance sheet and push net debt into clearly negative territory. We expect Incap to pay only modest dividends, as we expect the company to save its capital for acquisitions.

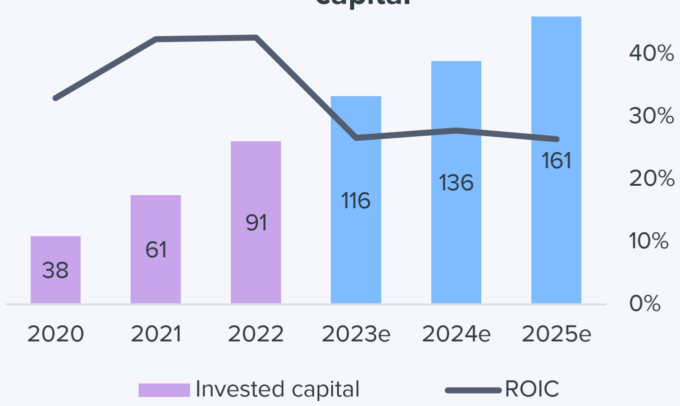
In practice, however, Incap's balance sheet is unlikely to strengthen to the levels we forecast and acquisitions are very likely in the medium term. Based on our projections for 2023-2026, we estimate that Incap would have the firepower to make acquisitions of EUR 40-100 million with the debt capacity of its current balance sheet. This estimate is based on a 1x-2x net debt/ EBITDA ratio, which we consider to be a reasonable level for Incap given its structure. Debt capacity naturally increases towards the end of the period and, in addition to debt capacity, Incap could of course use equity and its own stock to finance acquisitions.

The long-term outlook is also positive

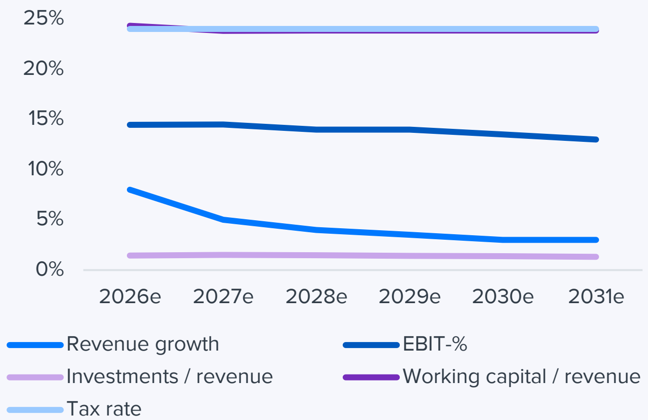
We expect Incap to implement its growth strategy in a consistent and value-creating manner even after 2026. In our longer-term estimate, we expect the company to continue to grow in a healthy way thanks to the forces that support existing customers, the entire electronics industry and contract manufacturers' businesses. Considering this overall picture, we expect the company's revenue to grow by some 2-5% per year in the long term, which is in line with the estimated growth of the global electronics industry over the same period. Considering our organic growth forecasts, the share of the largest customer of Incap's revenue is unlikely to decline significantly over the entire forecast horizon, so without acquisitions customer risk remains high even in the long term. Thus, our forecasts are subordinate to Victron Energy's ability to maintain growth in its own businesses, and we believe it would be difficult for Incap to grow materially in the long term on its current structure without growth in this account.

In the long term, we expect Incap's adjusted EBIT margin to remain at a strong level of 13-15%. The key long-term profitability drivers are revenue growth, a gradually improving production mix, mild economies of scale, for example in procurement, and a low cost structure. The main risks relate to the largest customer base and the success in maintaining the operating model and allocating capital. We note that there is some tail risk, especially for the terminal period, as Incap's profitability at the terminal is significantly above the industry average. We believe the company's strengths are sustainable, so we have not made any material changes to our estimates for the terminal period.

Development of return on invested capital



Long-term estimate parameters



Source: Incap, Inderes

Income statement and estimate revisions

Income statement	H1'21	H2'21	2021	H1'22	H2'22	2022	H1'23e	H2'23e	2023e	2024e	2025e	2026e
Revenue	**71,3**	**98,5**	**170**	**115**	**149**	**264**	**129**	**107**	**236**	**265**	**292**	**315**
Incap	71,3	98,5	170	115	149	264	129	107	236	265	292	315
EBITDA	**11,3**	**17,9**	**29,3**	**17,2**	**25,6**	**42,8**	**20,9**	**14,7**	**35,5**	**41,8**	**46,1**	**50,2**
Depreciation	-1,6	-1,7	-3,3	-1,8	-2,0	-3,8	-2,2	-2,4	-4,6	-4,6	-4,5	-4,6
EBIT (excl. NRI)	**10,2**	**16,6**	**26,8**	**15,6**	**24,4**	**40,0**	**18,8**	**12,4**	**31,2**	**37,5**	**41,9**	**45,9**
EBIT	**9,8**	**16,2**	**26,0**	**15,4**	**23,6**	**39,0**	**18,7**	**12,3**	**30,9**	**37,2**	**41,6**	**45,6**
Net financial items	-0,3	0,1	-0,3	-0,8	-1,5	-2,3	-0,7	-0,3	-1,0	0,0	0,3	0,6
PTP	**9,4**	**16,3**	**25,7**	**14,6**	**22,1**	**36,7**	**18,0**	**12,0**	**30,0**	**37,2**	**41,9**	**46,2**
Taxes	-1,6	-3,0	-4,7	-3,4	-5,7	-9,0	-4,3	-2,9	-7,1	-8,9	-10,1	-11,1
Minority interest	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Net earnings	**7,8**	**13,3**	**21,1**	**11,2**	**16,4**	**27,6**	**13,7**	**9,1**	**22,8**	**28,3**	**31,8**	**35,1**
EPS (adj.)	**0,28**	**0,46**	**0,74**	**0,39**	**0,59**	**0,98**	**0,47**	**0,31**	**0,79**	**0,97**	**1,10**	**1,21**
EPS (rep.)	**0,27**	**0,45**	**0,72**	**0,38**	**0,57**	**0,94**	**0,47**	**0,31**	**0,78**	**0,97**	**1,09**	**1,20**

Key figures	H1'21	H2'21	2021	H1'22	H2'22	2022	H1'23e	H2'23e	2023e	2024e	2025e	2026e
Revenue growth-%	52,2 %	65,1 %	59,4 %	60,6 %	51,6 %	55,4 %	12,9 %	-28,3 %	-10,4 %	12,2 %	10,0 %	8,0 %
Adjusted EBIT growth-%	83,5 %	82,3 %	82,8 %	53,1 %	47,1 %	49,4 %	20,9 %	-49,2 %	-21,9 %	19,9 %	11,8 %	9,5 %
EBITDA-%	15,9 %	18,2 %	17,2 %	15,0 %	17,2 %	16,2 %	16,1 %	13,7 %	15,0 %	15,8 %	15,8 %	15,9 %
Adjusted EBIT-%	14,3 %	16,8 %	15,8 %	13,6 %	16,4 %	15,2 %	14,6 %	11,6 %	13,2 %	14,1 %	14,4 %	14,6 %
Net earnings-%	10,9 %	13,5 %	12,4 %	9,8 %	11,0 %	10,5 %	10,6 %	8,5 %	9,7 %	10,7 %	10,9 %	11,1 %

Lähde: Inderes

Estimate revisions	2023e	2023e	Change	2024e	2024e	Change	2025e	2025e	Change
MEUR / EUR	**Old**	**New**	**%**	**Vanha**	**Uusi**	**%**	**Vanha**	**Uusi**	**%**
Revenue	237	236	0 %	265	265	0 %	292	292	0 %
EBIT	30,8	30,9	0 %	38,0	37,2	-2 %	42,5	41,6	-2 %
PTP	29,8	30,0	1 %	38,0	37,2	-2 %	42,9	41,9	-2 %
EPS (excl. NRIs)	0,79	0,79	1 %	0,99	0,97	-2 %	1,12	1,10	-2 %
DPS	0,15	0,15	0 %	0,20	0,20	0 %	0,25	0,25	0 %

Source: Inderes

Balance sheet

Assets	2021	2022	2023e	2024e	2025e
Non-current assets	**23**	**33**	**32**	**31**	**31**
Goodwill	8	7	7	7	7
Intangible assets	0	4	4	3	3
Tangible assets	14	20	20	20	20
Associated companies	0	0	0	0	0
Other investments	0	0	0	0	0
Other non-current assets	0	1	1	1	1
Deferred tax assets	1	0	0	0	0
Current assets	**102**	**136**	**154**	**186**	**219**
Inventories	59	92	71	78	85
Other current assets	0	0	0	0	0
Receivables	34	36	45	50	58
Cash and equivalents	9	8	39	58	76
Balance sheet total	**130**	**168**	**186**	**217**	**250**

Source: Inderes

Liabilities & equity	2021	2022	2023e	2024e	2025e
Equity	**63**	**87**	**110**	**134**	**160**
Share capital	1	1	1	1	1
Retained earnings	42	70	93	116	142
Hybrid bonds	0	0	0	0	0
Revaluation reserve	-2	-5	-5	-5	-5
Other equity	22	22	22	22	22
Minorities	0	0	0	0	0
Non-current liabilities	**6**	**13**	**13**	**13**	**13**
Deferred tax liabilities	1	1	1	1	1
Provisions	2	2	2	2	2
Long term debt	4	11	10	10	10
Convertibles	0	0	0	0	0
Other long term liabilities	0	0	0	0	0
Current liabilities	**60**	**68**	**64**	**71**	**77**
Short term debt	7	11	4	4	4
Payables	53	57	59	66	73
Other current liabilities	0	1	1	1	1
Balance sheet total	**130**	**168**	**186**	**217**	**250**

Valuation 1/4

Earnings-based multiples work best

We favor earnings-based multiples in examining Incap's pricing and valuation. In our opinion, the most usable earnings multiples are the net earnings-based P/E ratio, and EV/EBITDA and EV/EBIT ratios that take the company's balance sheet structure better into consideration. As absolute multiples we apply the estimated neutral multiples that are based on our view of the company's growth and profitability levels, the ability to generate capital and the risk profile, as well as partly on the company's actual pricing on the stock market. In addition to the absolute multiples, we have utilized the framework of a relatively extensive peer group consisting of companies with similar business models. We examine Incap's pricing mainly for the first two estimate years. In addition, we utilize the DCF model that considers the long term.

Factors to be considered in valuation

We believe the following factors affect Incap's valuation:

- **The cost-effective operating model** is almost unparalleled and the company's profitability level is among the highest in the industry. Cost efficiency, and especially maintaining it, is also a fundamental pillar of strong relative competitiveness.
- **Track record of profitable organic growth** and maintaining efficiency levels is strong and longer-term growth outlooks is also good.
- **Long-term organic growth potential** is good thanks to electrification, digitalization, rising outsourcing rates and strong own competitiveness. Reflecting Incap's high return on invested capital, and in particular its RONIC, success in organic growth creates a lot of value.
- **We believe that acquisitions offer** a nice option to accelerate value creation as the company has a patient approach, even though the track record so far relies on one successful acquisition. Currently, Incap has borrowing power to carry out a relatively large acquisition.
- **In practice, the largest customer** determines direction of Incap's financials in the short and probably also the medium term, which raises the risk profile of the share as the risk of volatility is ever-present. We are not afraid as such that Incap will lose the customer, but it is still problematic for investors that Incap's growth and result depend on a single and poorly predictable driver.
- **Demand drivers are investment-driven**, which exposes Incap to cyclical fluctuations in the economy. However, the customer portfolio consists of companies operating in various industrial sectors and at different stages of development, which creates some kind of stability / cyclic resilience in demand.

Valuation	2023e	2024e	2025e
Share price	9,960	9,960	9,960
Number of shares, million:	29,3	29,3	29,3
Market cap	291	291	291
EV	267	248	229
P/E (adj.)	12,6	10,3	9,1
P/E	12,8	10,3	9,1
P/FCF	7,5	12,4	12,1
P/B	2,6	2,2	1,8
P/S	1,2	1,1	1,0
EV/Sales	1,1	0,9	0,8
EV/EBITDA	7,5	5,9	4,9
EV/EBIT (adj.)	8,5	6,6	5,5
Payout ratio (%)	19,2 %	20,7 %	23,0 %
Dividend yield-%	1,5 %	2,0 %	2,5 %

Source: Inderes

Source: Inderes

Valuation 2/4

- **The challenging value chain position** between material suppliers and end customers makes the price pressure chronic. Competition is also tight and may tighten further once the post-pandemic component problem is resolved.

Considering the factors that support and depress the acceptable valuation, we believe that Incap should be priced with a P/E ratio of 10x-14x and correspondingly an EV/EBIT ratio of 8x-11x in the current stock market environment, where the nominal interest rate is clearly positive. These valuation levels are also roughly in line with Incap's median levels for the last five years. Over time, these levels are not fixed, but have inherent flexibility to consider both operational and strategic development steps and changes in risk levels (e.g. possible expansion / concentration of the customer base). The earnings growth rate and interest rate levels also play an important role when creating the acceptable valuation.

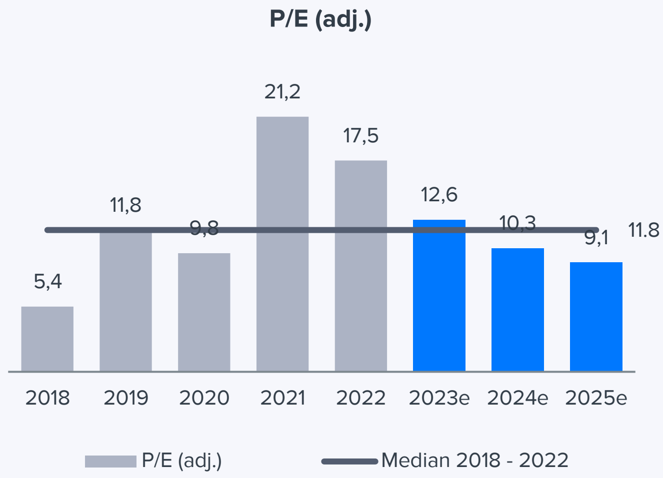
Absolute multiples are modest

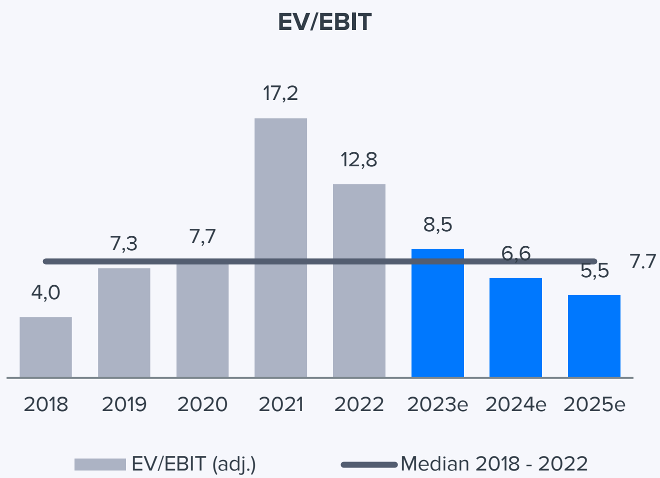
Incap’s adjusted P/E ratios for 2023 and 2024 based on our estimates are 13x and 10x while the corresponding EV/EBIT ratios are 9x and 7x. These multiples are close to the bottom end of the neutral multiple ranges we estimate for the company for this year, and below or at the bottom end of the range for next year. Relative to historical levels, the multiples for this year are at the 5-year median levels and next year's multiples are quite clearly below them. We believe this is a reasonable starting point, despite the downward trend in earnings for the next 3-5 quarters and the prevailing highish interest rates, given Incap's strong track-record in recent years and the growth potential offered by the competitive free capacity. Therefore, we find the multiple-based pricing of the share attractive, provided that the problems remain temporary and Incap returns to profitable growth next year. In addition, the investors have an option that the P/E-based valuation would decrease by 10-20% if Incap managed to put its balance sheet to work with a debt-driven acquisition. However, the attractiveness of the valuation purely depends on the direction of the earnings trend next year and we see no upside in the share if Incap's result would not grow next year.

We expect Incap's dividend yield in the next few years to be low or even zero, as the company saves its capital for implementing the inorganic branch of its growth strategy. We are positive about the choice as such, but the return for investors will largely consist of the change in share price and dividend yield does not support the short-term expected return.

We think the relative valuation should be neutral

The number of listed contract manufacturers is large, so a large group of similar companies to Incap in terms of business models and value chain positions are available for relative examination of the valuation level. However, it is worth noting that the peer group is not perfect, as some of the companies are very large EMS houses. In addition, the profitability profiles, business structures, strategic positions and risk levels of the companies are not fully comparable.





Source: Inderes

Valuation 3/4

Some of the relevant peers are also unlisted companies (e.g. JJS Manufacturing) or, e.g., have no public forecasts, which makes the peer group deficient. Despite these points, we find the relative valuation to be sufficiently useful, although we only apply it as a secondary support to the other methods we use.

Some of the peers we have chosen are significantly larger manufacturers than Incap, but the majority are relevant to the size of the company. In particular, we consider Nordic manufacturers to be excellent indicators, because similar geographical and industrial positions mean that they are also often direct competitors to each other, in our opinion. In addition, acquisitions are central to the strategies of all Nordic manufacturers, which we believe indicates that there is some competition also on the front of potential acquisition targets.

Compared to the peer group, Incap is priced with a slight discount with the multiples for this year and especially next year. In our opinion, Incap's strong track-record and almost superior base profitability compared to the peer group, would speak for a premium for the company, but the opposite driver is the customer structure, which is much more focused than for the peers on average. Considering everything, we feel that pricing Incap roughly in line with the peer group in an earnings-based scenario would be a sensible outset. We, therefore, consider the share's relative earnings-based valuation moderate, especially when looking at next year.

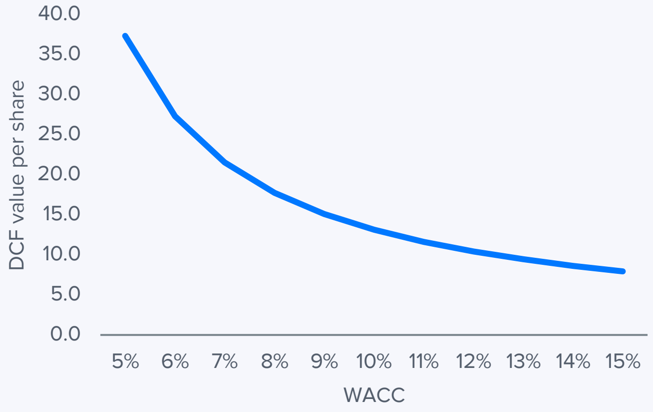
In volume-based terms, Incap is still priced at a premium of about 50% relative to the peer group. We believe that this is justified considering the high basic profitability relative to the company's industry. We note, however, that maintaining the premium on the current scale will require the company to continue reaching double-digit profitability margins and there could be a clear downside in the share price if profitability would fail even temporarily to a single-digit level.

Cash flow based valuation

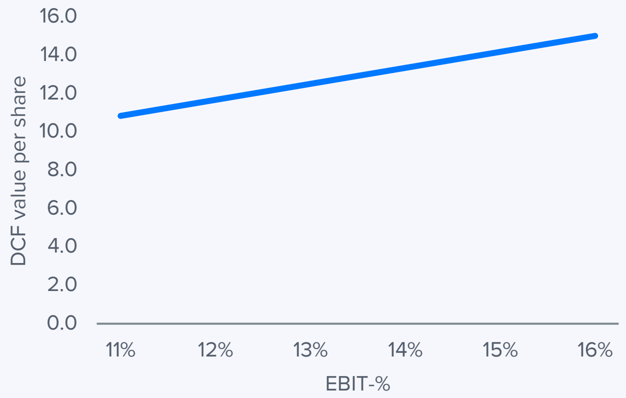
We also give weight to the cash flow based model (DCF) in our valuation despite it being rather sensitive especially to the required return and the variables of the terminal period. In light of this we feel the model provides sufficiently relevant support for other methods used, and in particular for examining the longer-term potential for value creation. Our DCF model indicates a share value of EUR 13 per share. The DCF, therefore, provides a positive signal of the share's valuation.

In our model, the company's revenue growth stabilizes at 3% in the long term, while we expect operational profitability to stabilize at 13-15% reflecting the dynamics of the industry. Therefore, the model has some tail risk, especially in terms of profitability. In our model, the weight of the terminal period is a very tolerable 50%.

Sensitivity of DCF value per share to required return



Sensitivity of DCF value per share to EBIT-%



Source: Inderes

Valuation 4/4

The cost of capital (WACC) we use is 9.7% and the cost of equity is 10.4%, reflecting the highish risk profile of the share (risk category 3). We clearly raised our required return in April after a partial materialization of the customer risk, but in this update, we have not changed our required return. Therefore, there could also be an upside in the DCF through a decrease in the required return if the company is able to offset its customer risks in the longer term. We have applied a risk-free interest rate of 2.5% and similarly a market risk premium of 4.75%.

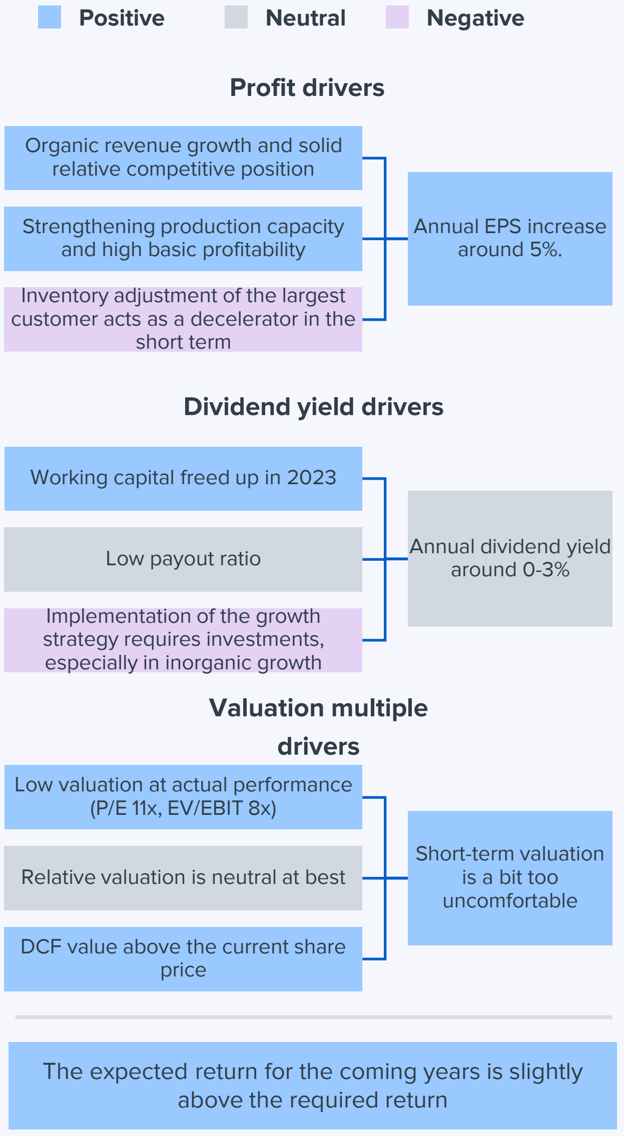
Expected return is attractive

We also feel that with actual earnings, Incap's valuation is low (P/E 10x), but the earnings trend points downwards starting from Q2 according to our estimates for the next 3-5 quarters. Thus, within 12 months, earnings growth will not support the share much, and the dividend yield is at zero or low as the company is saving (sensibly) its capital for growth investments. Thus, in the short term, the upside in the share must come especially through a higher valuation. In the current interest rate environment, relying on a higher valuation is partly risky, but we believe that visibility to improved volumes from Victron Energy (largest customer according to our estimates) and/or the problems proving temporary could be a positive company-specific driver for the valuation. In this scenario, market focus would shift from the short-term challenge to Incap's longer-term growth and profitability potential, as well as strong relative competitiveness, which we estimate would support the valuation.

In the medium term, we do expect Incap to return to earnings growth and, thus, the earnings growth outlook creates an attractive expected return starting from the current valuation especially beyond the more difficult period that lasts for roughly a next year. We also believe that this good earnings growth potential supports looking beyond the short-term challenges. Realization of short- and medium-term expected returns naturally requires that the result does not dip clearly more than our expectations in the next year or so, and that the company returns to earnings growth in the coming years. The main risks behind our positive views are based on a single large customer, fluctuations in investment demand and the company's ability to maintain high efficiency.

In addition, a driver for the share even in the short term could be M&A transactions, if Incap could put its balance sheet to work at an affordable, sufficiently high-quality, even slightly synergistic target that especially lowers the customer risk level. However, we do not rely on successes in acquisitions, although the AWS transaction and a patient approach to acquisitions have supported confidence in the company's M&A strategy.

TSR drivers 2022-2026e

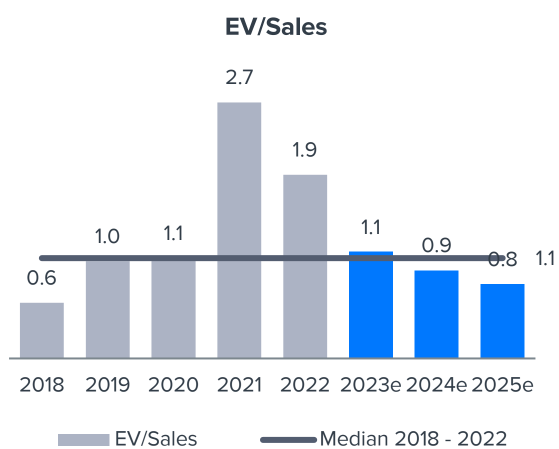


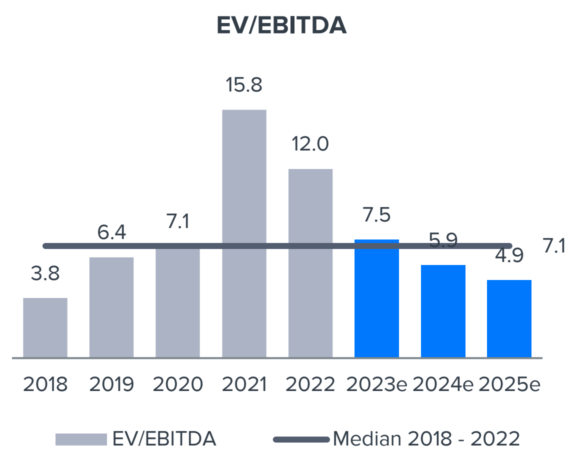
Source: Inderes

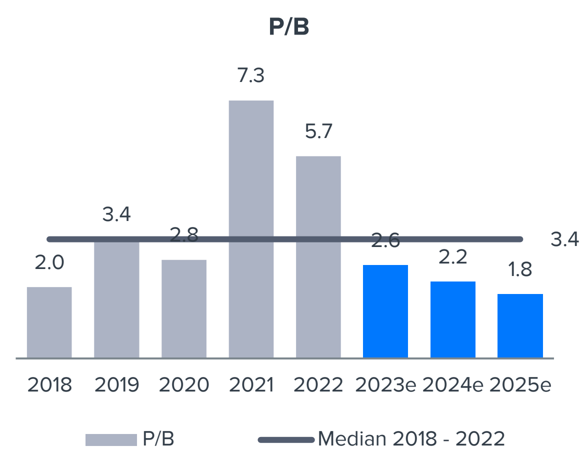
Valuation table

Valuation	2018	2019	2020	2021	2022	2023e	2024e	2025e	2026e
Share price	1,45	3,38	3,69	15,70	17,10	**9,96**	**9,96**	**9,96**	**9,96**
Number of shares, millions	21,9	21,9	29,1	29,2	29,3	**29,3**	**29,3**	**29,3**	**29,3**
Market cap	32	74	107	459	500	**291**	**291**	**291**	**291**
EV	35	73	113	461	514	**267**	**248**	**229**	**208**
P/E (adj.)	5,4	11,8	9,8	21,2	17,5	**12,6**	**10,3**	**9,1**	**8,3**
P/E	5,4	11,8	11,6	21,8	18,1	**12,8**	**10,3**	**9,1**	**8,3**
P/FCF	13,7	11,4	neg.	>100	neg.	**7,5**	**12,4**	**12,1**	**10,5**
P/B	2,0	3,4	2,8	7,3	5,7	**2,6**	**2,2**	**1,8**	**1,6**
P/S	0,5	1,0	1,0	2,7	1,9	**1,2**	**1,1**	**1,0**	**0,9**
EV/Sales	0,6	1,0	1,1	2,7	1,9	**1,1**	**0,9**	**0,8**	**0,7**
EV/EBITDA	3,8	6,4	7,1	15,8	12,0	**7,5**	**5,9**	**4,9**	**4,1**
EV/EBIT (adj.)	4,0	7,3	7,7	17,2	12,8	**8,5**	**6,6**	**5,5**	**4,5**
Payout ratio (%)	0,0 %	0,0 %	0,0 %	0,0 %	0,0 %	**19,2 %**	**20,7 %**	**23,0 %**	**25,0 %**
Dividend yield-%	0,0 %	0,0 %	0,0 %	0,0 %	0,0 %	**1,5 %**	**2,0 %**	**2,5 %**	**3,0 %**

Source: Inderes







Peer group valuation

Peer group valuation	Market cap	EV	EV/EBIT		EV/EBITDA		EV/S		P/E		Dividend yield-%		P/B
Company	**MEUR**	**MEUR**	**2023e**	**2024e**	**2023e**	**2024e**	**2023e**	**2024e**	**2023e**	**2024e**	**2023e**	**2024e**	**2023e**
Cicor Technologies	151	257	13,8	12,2	6,5	5,9	0,7	0,6	23,5	16,3			1,2
Integrated Micro-Electronics	186	447	29,6	17,5	10,7	6,8	0,3	0,3		11,3			0,5
Data Modul	215	233	6,5	5,3	5,8	4,9	0,6	0,6	10,8	9,7	0,2	0,2	1,4
Hanza	307	354	12,6	9,0	5,0	4,3	0,4	0,4	16,1	14,1	1,4	1,6	1,1
Kitron	751	890	12,8	16,9	10,3	9,6	1,1	1,0	13,7	13,2	1,7	2,4	4,7
Lacroix Group SA	161	330	11,6	9,5	6,4	5,7	0,4	0,4	11,1	8,1	3,1	4,2	0,9
Jabil	12123	13767	8,8	8,5	5,6	5,5	0,4	0,4	11,8	10,8	0,3	0,3	4,5
Scanfil	642	734	12,0	11,7	9,1	9,0	0,8	0,8	13,7	13,3	2,3	2,5	2,5
Fabrinet	4360	3869	14,6	14,3	12,7	12,4	1,6	1,5	17,1	16,7			3,2
Hana Microelectronics	1030	948	18,2	14,3	9,5	8,1	1,3	1,1	18,7	15,0	2,4	3,4	1,5
SVI	502	583	12,8	11,2	10,9	9,8	0,8	0,7	12,6	11,0	2,6	3,0	2,4
TT Electronics	348	514	8,8	8,0	6,6	6,0	0,7	0,7	9,1	8,1	4,0	4,4	1,0
Katek Se	210	247	13,7	8,2	6,1	4,6	0,3	0,3	23,8	12,0			1,3
Nolato AB	1257	1351	18,5	14,3	11,2	9,4	1,5	1,4	22,1	16,9	3,8	3,5	2,6
Celestica	1501	2065	5,7	5,4	4,4	4,2	0,3	0,3	6,7	6,1			1,0
Incap (Inderes)	**291**	**267**	**8,5**	**6,6**	**7,5**	**5,9**	**1,1**	**0,9**	**12,6**	**10,3**	**1,5**	**2,0**	**2,6**
Average			**13,3**	**11,1**	**8,1**	**7,1**	**0,7**	**0,7**	**15,0**	**12,2**	**2,2**	**2,5**	**2,0**
Median			**12,8**	**11,2**	**6,6**	**6,3**	**0,7**	**0,6**	**13,7**	**12,0**	**2,4**	**2,7**	**1,4**
Diff-% to median			***-33 %***	***-41 %***	***15 %***	***-6 %***	***66 %***	***48 %***	***-8 %***	***-14 %***	***-37 %***	***-27 %***	***87 %***

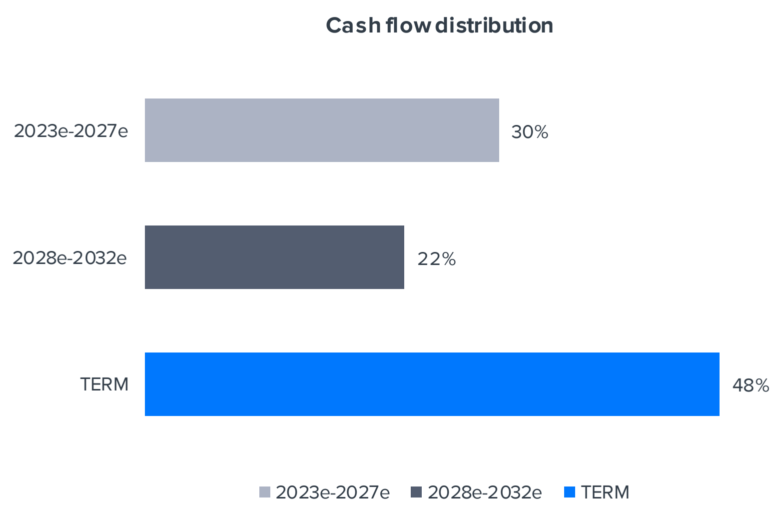
Source: Refinitiv / Inderes

DCF calculation

DCF model	2022	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e	2031e	2032e	TERM
Revenue growth-%	55,4 %	-10,4 %	12,2 %	10,0 %	8,0 %	5,0 %	4,0 %	3,5 %	3,0 %	3,0 %	2,0 %	2,0 %
EBIT-% (adj.)	14,8 %	13,1 %	14,0 %	14,3 %	14,5 %	14,5 %	14,0 %	14,0 %	13,5 %	13,0 %	13,0 %	13,0 %
EBIT (operating profit)	**39,0**	**30,9**	**37,2**	**41,6**	**45,6**	**48,0**	**48,2**	**49,9**	**49,5**	**49,1**	**50,1**	
+ Depreciation	3,8	4,6	4,8	4,8	4,7	4,8	5,1	5,1	5,3	5,3	4,8	
- Paid taxes	-8,8	-7,1	-8,9	-10,1	-11,1	-11,7	-11,9	-12,4	-12,4	-12,3	-12,6	
- Tax, financial expenses	-0,6	-0,3	-0,2	-0,2	-0,2	-0,2	-0,2	-0,2	-0,2	-0,2	-0,2	
+ Tax, financial income	0,0	0,0	0,2	0,2	0,3	0,4	0,5	0,6	0,6	0,7	0,7	
- Change in working capital	-30,7	14,8	-5,6	-7,7	-7,2	-2,2	-3,2	-2,9	-2,6	-2,6	-1,8	
Operating cash flow	**2,8**	**42,9**	**27,5**	**28,7**	**32,2**	**39,0**	**38,5**	**40,1**	**40,3**	**40,0**	**41,1**	
+ Change in other long-term liabilities	0,3	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
- Gross CAPEX	-9,7	-4,0	-4,0	-4,5	-4,5	-5,0	-5,0	-5,0	-5,0	-5,0	-5,6	
Free operating cash flow	**-6,7**	**38,9**	**23,5**	**24,2**	**27,7**	**34,0**	**33,5**	**35,1**	**35,3**	**35,0**	**35,5**	
+/- Other	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
FCFF	-6,7	38,9	23,5	24,2	27,7	34,0	33,5	35,1	35,3	35,0	35,5	468
Discounted FCFF		**37,0**	**20,3**	**19,1**	**19,9**	**22,3**	**20,0**	**19,1**	**17,5**	**15,8**	**14,6**	**193**
Sum of FCFF present value		398	361	341	322	302	280	260	241	223	207	193
Enterprise value DCF		**398**										
- Interest bearing debt		-21,2										
+ Cash and cash equivalents		7,6										
-Minorities		0,0										
-Dividend/capital return		0,0										
Equity value DCF		**385**										
Equity value DCF per share		**13,1**										

WACC	
Tax-% (WACC)	25,0 %
Target debt ratio (D/(D+E)	10,0 %
Cost of debt	5,0 %
Equity Beta	1,40
Market risk premium	4,75 %
Liquidity premium	1,25 %
Risk free interest rate	2,5 %
Cost of equity	**10,4 %**
Weighted average cost of capital (WACC)	**9,7 %**

Source: Inderes



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Reduce The 12-month risk-adjusted expected shareholder return of the share is weak

Sell The 12-month risk-adjusted expected shareholder return of the share is very weak

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Date	Recommendation	Target	Share price
12/05/2020	Accumulate	2,60 €	2,40 €
25/05/2020	Accumulate	2,80 €	2,57 €
27/08/2020	Accumulate	4,00 €	3,71 €
17/09/2020	Accumulate	4,00 €	3,60 €
27/10/2020	Accumulate	3,50 €	3,02 €
12/11/2020	Accumulate	3,80 €	3,40 €
26/11/2020	Accumulate	4,00 €	3,60 €
25/02/2021	Accumulate	5,40 €	4,88 €
28/04/2021	Accumulate	7,60 €	7,05 €
29/07/2021	Accumulate	9,20 €	8,58 €
16/09/2021	Accumulate	11,00 €	10,12 €
28/10/2021	Reduce	14,00 €	14,78 €
25/02/2022	Accumulate	14,40 €	13,42 €
23/03/2022	Reduce	14,80 €	15,08 €
27/04/2022	Reduce	14,80 €	14,00 €
Analyst changes			
28/07/2022	Accumulate	16,00 €	14,66 €
19/10/2022	Accumulate	17,00 €	15,08 €
28/10/2022	Reduce	17,00 €	16,06 €
18/11/2022	Reduce	17,00 €	16,18 €
23/02/2023	Reduce	17,00 €	18,04 €
19/04/2023	Accumulate	12,00 €	10,92 €
27/04/2023	Accumulate	12,00 €	10,36 €
15/06/2023	Accumulate	12,00 €	9,96 €

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