

Epiroc AB Class A

CORE HOLDING*

Recommended since 05.07.21

20.07.2022



Country SE	Market capitalization (bn) SEK	198.6	Perf. since reco. (%)	
Sector Industrial Goods & Services	Free float	74.1%	Epiroc AB Class A	-13.0
Factset EPI.A-SE	Closing price SEK	170.45	Sector	-15.4
ISIN SE0015658109	ESG Risk score*	22.1	Medium risk	

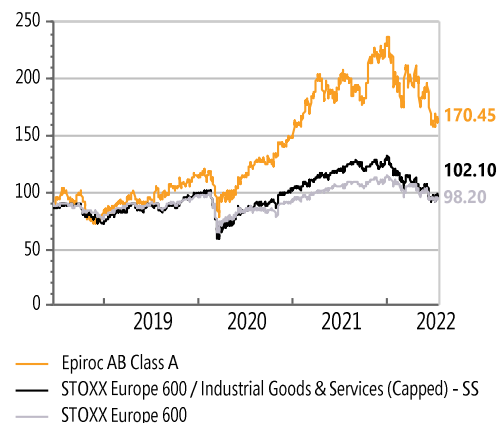
*From 2015, B&Cie separates its investment recommendations into Core Holdings (higher organic growth potential, high free cash flow, ROCE in excess of the cost of capital and balance sheet efficiency throughout the cycle) and Satellite Recommendations, which do not meet the above criteria but are likely to outperform in the short-to-medium term.

Profile

Epiroc is one of two major companies producing underground mining equipment. It has operated as a standalone group since 2018 after being spun off from Atlas Copco, founded in 1873. Epiroc has a workforce of 15,500 and operations in 150 countries, generating annual sales of roughly SEK 40bn (c. €4bn). Over the medium term, equipment sold by Epiroc is likely to become 100% electrified. Group sales are split between underground mining/excavation machinery (77%) and infrastructure equipment, e.g. tunnelling (23%).

Market - competition - positions - barriers to entry

The underground mining/excavation equipment market totalled SEK 210bn in 2020. In this sector, Sandvik and Epiroc operate in a specialised segment, forming a virtual duopoly. Sandvik has several business divisions, but its sales associated with this sector amount to SEK 40bn, hence close to those of Epiroc. Innovation acts as a major barrier into this market and will be further reinforced by development of driverless electric vehicles, together with ongoing digitalisation. 75% of Epiroc's manufacturing costs are outsourced, its added value thus being derived chiefly from design and assembly.



Source: Factset

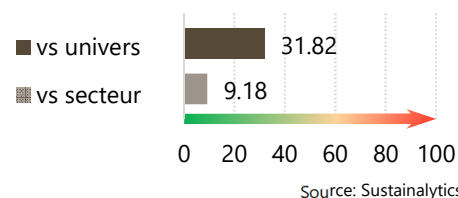
Investment case

- Epiroc is a leader and pure player in an industry that stands to benefit from a quickening of the investment cycle in the mining industry in the aftermath of low capex levels over the last few years and in connection with demand for metals, ores and minerals required for the energy transition. Epiroc is targeting 6%-8% growth over a cycle, but this range does not include the growth boost that the above-mentioned factor would justify and which analysts have not yet factored in either at this stage. Our valuation does incorporate this extra potential, factoring in an assumption of a faster rate of medium-term growth.
- The average quality grade of minerals and ores has worsened noticeably over the last 15 years, which should lead to increased investment per tonne of product extracted under more challenging conditions. Electrification and sophistication (driverless vehicles, digitalisation) in Epiroc's offering should result in a higher average price per vehicle in the medium term; this should feed through to boost the company's margins, on top of operating leverage gains associated with sales growth.
- Lastly, more than two-thirds of Epiroc's sales revenues are recurring: aftermarket and spare parts. This business model provides some degree of visibility, resilient profit margins and solid cash-flow-generating capabilities across the cycle, translating into a high RoCE.
- FY2021 and H1-2022 results showed a strong rebound in orders intake and sales. We nevertheless onboard a moderate recession scenario for 2023, leading to a sharp reduction in growth and a c. 2 pt% impact on Ebit margin.

ESG - risks and key points

- Epiroc is rated as "Medium Risk" on the basis of an assessment of ESG criteria. This rating stems from Epiroc's exposure to material ESG risks being judged to be moderate, coupled with its strong risk management; moreover, Epiroc has not been involved in any major controversies.
- Epiroc's ESG reporting is of a high standard, with a compliance unit set up to oversee these issues and a whistleblower system (Speak Up) put in place. This combination of solutions delivers strong ESG-related risk management.

ESG risk vs. universe & sector (percentile)*



Source: Sustainalytics

Valuation** in SEK

Current price	Value Bordier Scenario
170	203

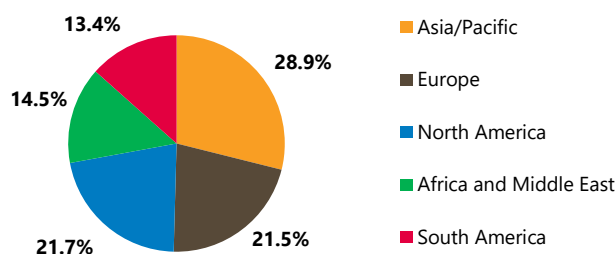
Our fundamental valuation of Epiroc factors in long-bond yields of 2.0% in Europe and our sales/margin trajectories as outlined above. The share price correction YTD discounts the sovereign yields regime change and a slowdown of growth.

** The theoretical value reflects the company's business model, our baseline growth and profit scenario and market data, exogenous to the company (risk-free rate and equity risk premium). It does not in itself constitute a target price.

"Bordier Core Holding" indicators

In millions of SEK	2020	2021	2022e	2023e	2024e
Sales revenue	36'122	39'645	45'988	46'908	50'661
Sales growth %	-12.0%	10.0%	16.0%	2.0%	8.0%
<i>o/w organic</i>	-5.0%	12.0%	6.0%	0.0%	6.0%
EBIT adjusted	7'380	8'995	9932	10076	11399
% of sales	20.4%	22.7%	21.6%	21.5%	22.5%
Net income	5'410	7'069	7747	7758	8663
Adjusted EPS	4.48	5.85	6.41	6.42	7.17
Adjusted EPS growth	-8.3%	30.6%	9.6%	0.2%	11.7%
Capex/Sales	3.1%	9.8%	3.5%	3.7%	3.7%
Free cash-flow	7'417	4'134	6328	6191	7143
FCF/Sales	20.5%	10.4%	13.8%	13.2%	14.1%
Dividend per share	2.50	3.00	3.00	3.00	3.00
Dividend yield	1.7%	1.3%	1.8%	1.8%	1.8%
ROCE - WACC	13.5%	19.7%	17.4%	13.8%	12.9%
ROE (%)	22.8%	27.4%	25.4%	22.0%	21.2%
Net debt/Ebitda	-74%	-15%	-41%	-69%	-93%

Source: Factset, Bordier estimates

Sales breakdown - 12/2021**Ratios**

	Epiroc AB Class A	Stoxx Europe 600 Sector	Market
PE (x)***		Indus. Good & Serv.	STOXX 600
2021	39.2	20.3	15.4
2022e	26.6	14.9	12.3
2023e	26.5	14.6	11.8
P/B (x)***			
2021	10.7	3.5	2.0
2022e	6.8	2.7	1.7
2023e	5.8	2.4	1.6
Beta (2Y, daily) vs market: 0.95			

***) The valuation ratios set out are provided for information only. They do not constitute the criteria based upon which Core Holdings are selected, and may present significant premi-ums representing the quality of the company's business model.

Governance and ownership structure

Since 2020: CEO Mrs Helena Hedblom.

Agenda

Q3-2022 Results: 26.10.2022

Key shareholders (if any):

Investor AB holds 23% of the voting rights.

Any special characteristics of ownership (multiple voting rights, controlling holding company, shareholders' agreements, etc.):

Two classes of share: A (one voting right per share) and B (10 voting rights per share).

Glossary**ESG Risk Score**

At B&Cie, we take particular care to ensure that the companies in which we recommend investing are sustainable. Accordingly, our selection process takes account of risks relating to environmental, social and governance (ESG) issues. This approach is underpinned by research from Sustainability, the global leader in ESG and corporate governance analysis, whose methodology aims to identify major controversies and risks and assess a company's ESG risks relative to both its sector and the investment universe as a whole. The corresponding score is expressed as a percentile: the lower the overall risk score, the lower the risk within the investment universe.

b-Digital, b-Transition & b-Well

Over and above the conventional geographical and sectoral approaches to asset management, at B&Cie we believe the world of tomorrow is being shaped by structural trends. We have identified three main megatrends: ongoing digital globalisation of the economy; economic transition, particularly in the energy sector; and the quest for wellness. We believe selecting and investing in companies that play an active role in these transformations should lead to more resilient portfolios that generate higher long-term returns. Our investment recommendations in the digital globalisation space are labelled "b-Digital", those in the economic transition space "b-Transition" and those in the wellness space "b-Well". A given recommendation may fall under more than one theme, in which case it will carry the relevant matching labels.

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