Innofactor

Extensive report

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Inderes corporate customer

This report is a summary translation of the report “Vankempi ja jatkuvampi pohja lähivuosien tuloskasvulle” published on 9/11/2023 at 8:30 am EEST

A firmer and more stable base for earnings growth

Innofactor's turnaround has progressed well for four years, driven by the pull of the Finnish business. In the short term, the market creates uncertainty, but Innofactor's good base created by the order book, recurring net sales and the public sector, provides support. Operationally focus still lies on developing a unified organization, where the foundation is in place, but it still requires evidence from outside Finland. We expect modest earnings growth this year and in the longer-term, stronger growth requires a solid Nordic business. Risk/return ratio is attractive. We reiterate our Accumulate recommendation and EUR 1.35 target price.

Transformation from projects toward continuous services and own solutions continues

Throughout its history, Innofactor has grown strongly through acquisitions in Finland and abroad by consolidating the field of IT suppliers specialized in Microsoft. After several acquisitions in 2016 the company moved to a strategic phase where the focus shifted to building a uniform Nordic organization. After a pit in 2017-18, the company's earnings turnaround has progressed well. At the same time, the share of continuous services has increased strongly in recent years (2017: 35% of net sales and 2022: 60%), which provides business continuity and lowers the risk profile.

Operational drivers in the short and longer term

In recent years, Innofactor has invested in building a unified Nordic organization, but this has been slower than we expected. Norway has performed well for a couple of years but important Swedish development has been weak for years. The company tries to create value from the synergies and efficiency of a unified Nordic organization but this still lacks evidence. In the short term, the uncertainty of customer demand hampers development, but in the longer term, the demand outlook in the sector remains good. In addition, with the strongest cloud transition over, it is important for the company to succeed in selling continuous services. In the medium term, Microsoft and its strong position in AI will create new growth opportunities and generate a competitive edge in terms of technology.

We expect moderate earnings growth and realizing the potential requires proof

Innofactor has proven that it can achieve stronger growth and turned profitability sustainably to the average level of the sector that is satisfactory for the company. In the next few years, Innofactor will continue to focus on growth, which should scale to profitability. We consider the company's long-term goals (20% growth and 20% EBITDA) achievable, but to materialize they require strong uniform performance across the Nordic organization. We expect net sales to grow organically by ~4% in the coming years (2023e: 9%), driven by billable utilization, and the EBITDA margin to be around 11%, limited by wage inflation and use of subcontracting. In addition, we consider it highly possible that the company will accelerate growth with small acquisitions, enabled by the balance sheet (net debt/EBITDA 0.9x). We feel the company has succeeded well in capital management in recent years, balancing between acquisitions, dividends and share buybacks. The key risks relate to new project or country-specific challenges emerging and acquisitions.

Risk/return ratio is attractive

The positioning of Innofactor's investment profile has strengthened in the profit generator category but stronger growth requires a continuous track record. With 2023e EV/EBIT and P/E ratios (9x and 11x), the valuation of the share is moderate. The ratios are 30% below Finnish peers, which is a very attractive level. With earnings growth (10%), dividend yield (7%) and a slight upside in multiples, the expected return of the share rises well above the equity return requirement. In addition, the DCF calculation indicates a clearly higher level than currently (EUR 1.6 per share). Thus, the valuation is actually very attractive in some respects, but the increased uncertainty in the market, however, curbs the enthusiasm about the share.

Recommendation

Accumulate

(previous Accumulate)

EUR 1.35

(previous EUR 1.35)

Share price:

1.14

Key figures

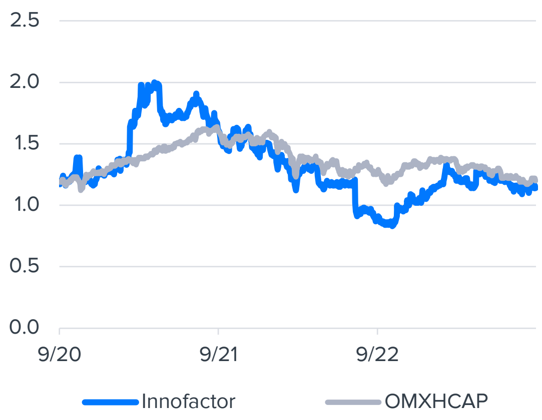
	2022	2023e	2024e	2025e
Revenue	71	80	83	86
growth-%	7%	12%	4%	3%
Käyttökate	7.8	8.3	9.4	10.1
Käyttökate-%	11.0 %	10.4 %	11.3 %	11.7 %
Net Income	3.3	3.5	4.7	5.4
EPS (adj.)	0.10	0.10	0.13	0.15
P/E (adj.)	10.7	11.2	8.5	7.4
P/B	1.5	1.6	1.5	1.3
Dividend yield-%	5.7 %	6.2 %	7.0 %	7.9 %
EV/EBIT (adj.)	10.0	9.3	7.2	6.0
EV/EBITDA	6.5	6.1	5.0	4.3
EV/S	0.7	0.6	0.6	0.5

Source: Inderes

Guidance (Unchanged)

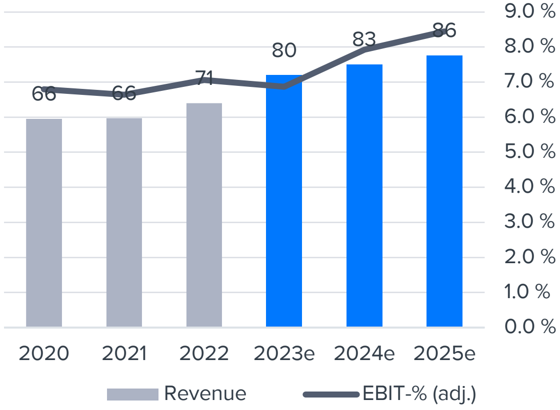
Innofactor's net sales and operating margin (EBITDA) in 2023 are estimated to increase from 2020, during which the net sales were EUR 71.1 million and operating margin was EUR 7.8 million.

Share price



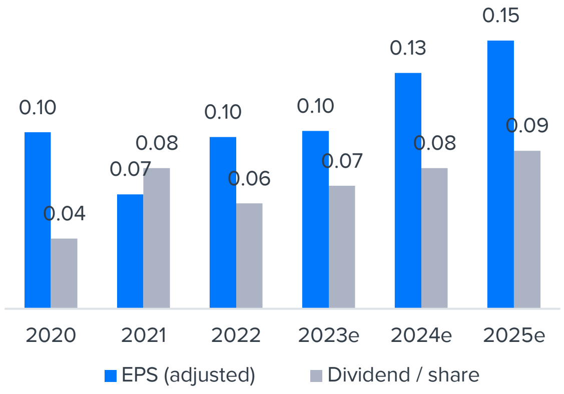
Source: Millistream Market Data AB

Revenue and EBIT-%



Source: Inderes

EPS and dividend



Source: Inderes

Value drivers

- Growth and profitability improvement in all Nordic countries, especially in Finland and Sweden
- Turnaround continuing and strengthening
- The positive trend of recovered investor confidence continuing
- Organic and acquisition-driven growth
- Increasing share of continuous business and own product business

Risk factors

- Growth strategy failing
- Failure in project management
- Failure in strengthening international business
- Delay in building a Nordic organization
- Internationalization and acquisitions raise the risk level
- Weakening of Microsoft's position, which is currently strong

Valuation	2023e	2024e	2025e
Share price	1.14	1.14	1.14
Number of shares, millions	36.3	36.3	36.3
Market cap	41	41	41
EV	51	47	43
P/E (adj.)	11.2	8.5	7.4
P/E	11.8	8.7	7.7
P/B	1.6	1.5	1.3
P/S	0.5	0.5	0.5
EV/Sales	0.6	0.6	0.5
EV/EBITDA	6.1	5.0	4.3
EV/EBIT (adj.)	9.3	7.2	6.0
Payout ratio (%)	72.9 %	61.6 %	60.7 %
Dividend yield-%	6.2 %	7.0 %	7.9 %

Source: Inderes

Contents

Innofactor in brief

Innofactor is Finland's leading software supplier focusing on Microsoft solutions and one of the leading suppliers in the Nordic countries.

2000
Year of establishment

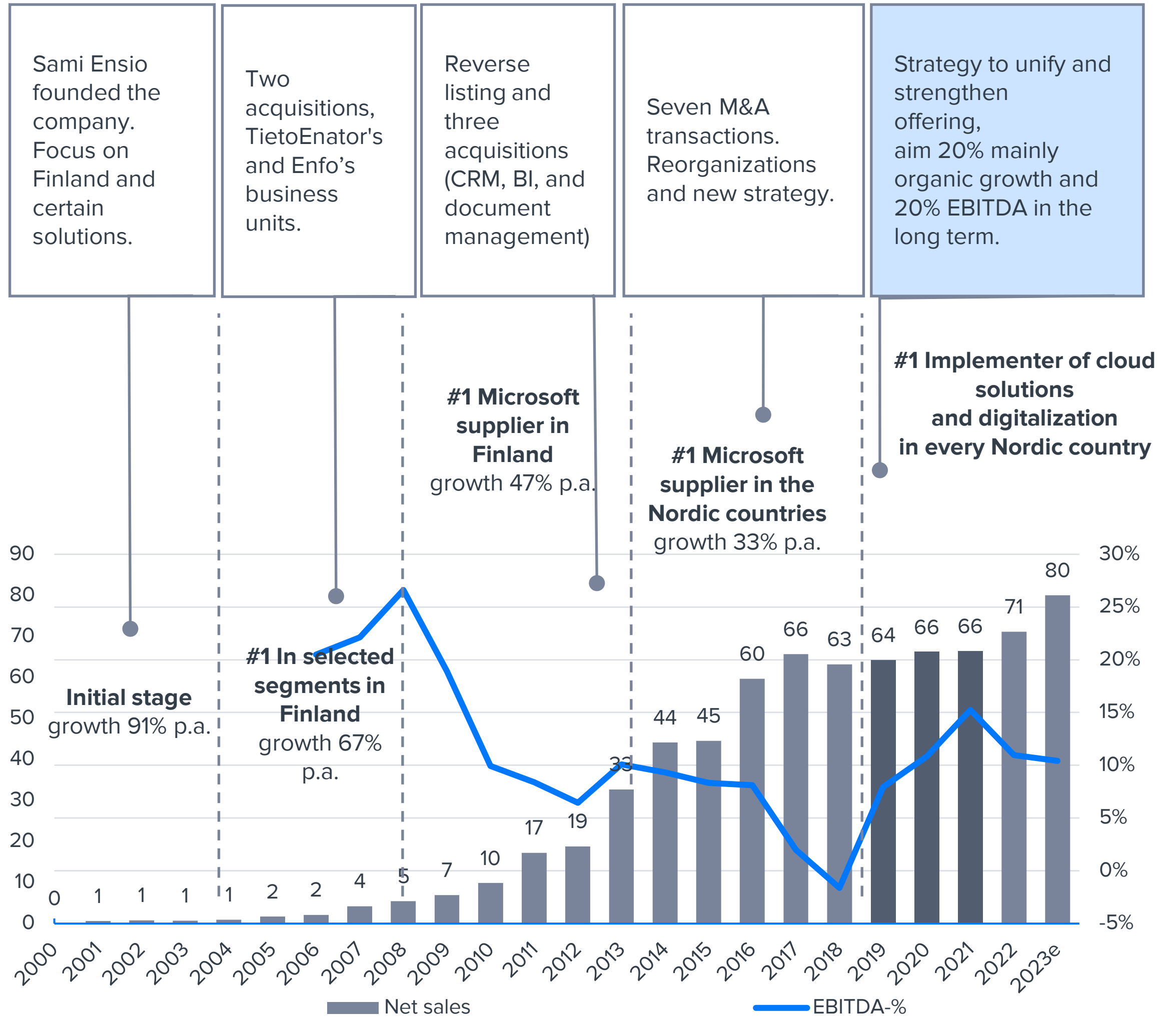
21.8%
Holding of CEO and immediate circle

71.1 MEUR **(+7.2% vs. 2021)**
Net sales 2022

66% Finland
16% Sweden
12% Norway
6% Denmark
Geographical share of net sales

7.5 MEUR **(11% of net sales)**
EBITDA (adj.) 2021

588 **(6% vs. Q2'22)**
Personnel at the end of Q2'23



Source: Innofactor / Inderes

Company description and business model 1/3

Company description

An entrepreneur-driven Microsoft expert

Innofactor established in 2000 is one of the leading software suppliers focusing on Microsoft solution in the Nordic countries. The company's business mainly consists of acting as a system integrator in IT projects, as well as developing and selling own software products and services. The company employs <600 people in Finland, Sweden, Denmark, and Norway.

Innofactor's current structure was born out of several M&A transactions. The company was listed on the Helsinki stock exchange by making a reversed listing and acquiring Westend ICT's entire stock at the end of 2010. Since then, the company has grown quickly through acquisitions and with the Lumagate acquisition in 2016 it gained an extensive Nordic platform for further expansion it was seeking. Due to operational challenges, the international growth strategy hit a pit in 2018. However, the turn for the better began in 2019 and has in the big picture continued stably especially pulled by the Finnish business. A moderate turn in internationalization began in 2021, driven by Norway, buta wider turnround is yet to come.

Innofactor's founder Sami Ensio still acts as the company's CEO and Board member and is also the company's biggest owner with a ~22% share.

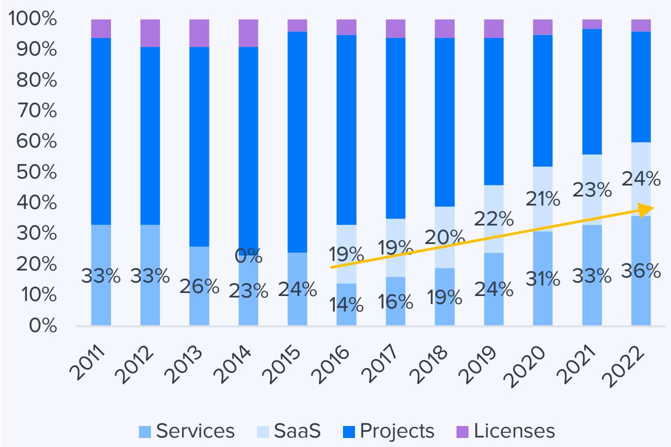
Presence in all Nordic countries

Innofactor has over 1,000 corporations, voluntary sector, and public administration organizations as its customers in Finland, Sweden, Denmark, and Norway. Innofactor's ten largest customers generated 27% of the company's net sales in 2022.

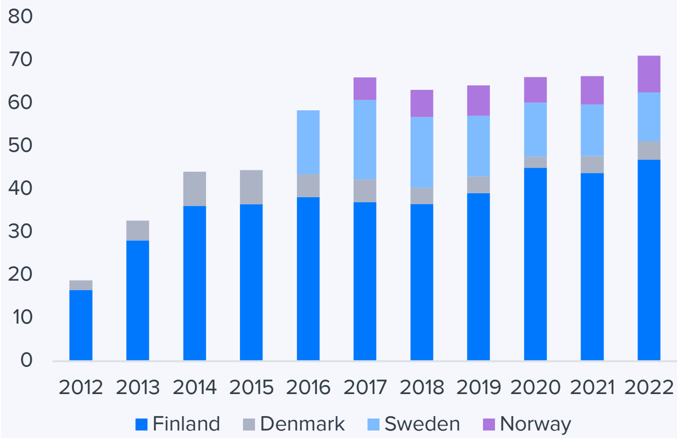
Last year, the company's net sales grew by 7% to EUR 71 million, of which organic growth was 4 percentage points. Of 2022 net sales, 53% came from corporate customers and 47% from the public sector. The company aims to increase its corporate customer share, which supports the increase in the average price and thus net sales growth and profitability. Geographically the company has historically expanded through acquisitions. Last year, 66% of net sales came from Finland, 16% from Sweden, 12% from Norway, and 6% from Denmark. Net sales from Finland, Norway and Denmark have grown in recent years, while net sales from Sweden have decreased.

After several acquisitions, in 2017 Innofactor started to build a uniform Nordic service and product offering and a Nordic organization. The company did, however, face several challenges and instead of synergies from acquisitions operational risks materialized. In 2019, the company was able to launch a brisk earnings turnaround. Now the company is in a development stage where the base abroad is still being fixed before more extensive growth. We suspect the company wants to continue strengthening and unifying its international offering and size class. We believe the synergies between the countries have so far been relatively small and the aim is to improve this by continuing to build a uniform Nordic offering. In recent years, the company has unified and concentrated its administrative tasks in particular, andnow its focus is on the offering. We believe that the Finnish business has been very profitable for years. Achieving the company's growth and profitability targets also requires sustainable growth from the other Nordic countries, a larger size class and, as a result, better profitability.

Net sales structure



Net sales geographically



Company description and business model 2/3

Business model

System integrator in the Microsoft ecosystem

Innofactor's core business is to mainly work as a system integrator in the Microsoft ecosystem. As a smallish player, Innofactor must specialize on a particular expertise area in the IT market. The company believes its competitive advantage is generated from specializing in Microsoft solutions and in future increasingly from extensive geographic presence. This choice of technology has seemed even better in recent years as Microsoft's competitiveness has strengthened. The company's solution offering is extensive and covers all key areas in Microsoft's corporate solutions, and is now especially a pioneer in AI solutions. The solutions can be delivered to the customer in Microsoft's cloud environment or in the customer's own environment. The need for Innofactor's expertise is further increased by customers' shift to Microsoft's cloud environments.

Transformation from project house to continuous services and product solutions

The business model of Innofactor is that of an IT service company that primarily delivers Microsoft technologies as projects and maintains these technologies. The company has also developed its own software product solutions to support the service business. The aim of the company in the long term is to focus on productizations that increase the scalability and continuity of the business. The company has been able to clearly increase the share of continuous net sales in the long term. In 2022, 36% of the net sales (2018: 55%) came from delivery projects, 36% (2018: 20%) from services, 24% (2018: 19%) from SaaS (e.g. Azure cloud services), and 4% (2018: 6%) from license sales. The company's goal is to increase SaaS net sales to 1/3 of net sales.

Innofactor has developed its own software products to support the Nordic service business. Own products built on Microsoft's technologies create competitive advantages in the project business and increase the scalability of the business. A large share of SaaS net sales comprises the company's own products. Thus, the company's own products and productized services already generate stable and quite large income flow. In software products, the company seeks growth especially from the Dynasty product and trade union software. In addition the solutions surrounding Virtual Datacenter and Azure and related service sales that are partly sold together are important although small so far. In own products there is growth potential especially abroad.

Extensive offering of IT services

Innofactor has an extensive life cycle offering of IT services. The offering covers planning, integration, development, and maintenance. The entire offering with all services is rarely sold at once, customers usually first buy one part (proof of concept, e.g. a project) and after this, other additional services (e.g. maintenance services).

Projects are usually relatively short depending on the size of the project. Continuous agreements typically start out as three-year agreements after which they continue as valid until further notice typically for over 10 years as it is hard and expensive for customers to change/arrange competitive bidding for maintenance of Innofactor's solutions. Thus, there is not similar cost pressure in maintenance as in well-standardized ICT services.

Business Areas

Digital services
Software Development and DevOps
App and Data Modernization
Process Digitalization
Low-code Development

Business solutions
Sales and Marketing | CRM
Customer Service Enablement
Finance and Operations | ERP
Project and Membership Management

Information and case management
Collaboration and intranets
Document and records management
Case and decision management
Contract and quality management

Data and analytics
Data Platform Modernization
Advanced Analytics and BI
Master Data Management | MDM
AI, real-time Analytics and IoT

Cloud infrastructure
Managed Services and DevOps
Cloud Transformation
Governance and Automation
Migrations

Cybersecurity
Less than
Security Assessment
Hybrid Work Security
Platform and Solution Security
Identity and Access Management | IAM

Around 50 experts

Partners

Microsoft and other technology suppliers

Subcontractors, talent resources

Operations

- Recruitment
- Sales
- Consulting and projects
- Continuous services and support
- Own software products and product development

Business Areas

- Digital services
- Business solutions
- Information and case management
- Data and analytics
- Cloud infrastructure
- Cybersecurity

Business idea

Leading supplier of cloud solutions and digitalization in the Nordic countries

INNOFACTOR®

- Modern digital organization
- More personal digital customer experience
- Secure cloud platform
- Higher operational productivity
- Modern employee experience
- Data oriented business

Objectives

- Innofactor's guidance is that net sales and EBITDA will grow from 2023
- In the long term, the aim is around 20% growth and 20% EBITDA margin.

Competition

IT generalists: accenture, tieto EVRY, CGI, digia, GOFORE, SOLTEQ, SOFIGATE

Medium sized players on the IT market: LOIHDE, siili_, futurice, Reaktor, VINCIT, INNOFACTOR®, Witted, SOLITA

Customer segments (2022)

Corporations 53%

Public administration47%

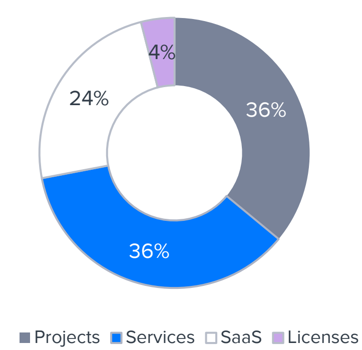
66% *16%*

12% *6%*

Cost structure

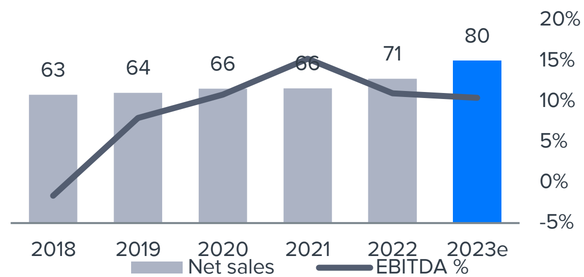
500 employees (2022)
EUR 63 million (2022)

- Personnel costs *(68% of costs)*
- Subcontractors and purchases *(16%)*
- Other operating expenses *(11%)*
- Depreciation *(5%)*



Income streams

Net sales 66 MEUR (2022)
EBITDA 8 MEUR (2022)



Source: Inderes

Company description and business model 3/3

The profitability of a customer relationship typically improves over time. In addition to administrative structures, the company has improved its cost base especially by recruiting young experts in recent years. This also helps solve the talent shortage and pressure from wage inflation.

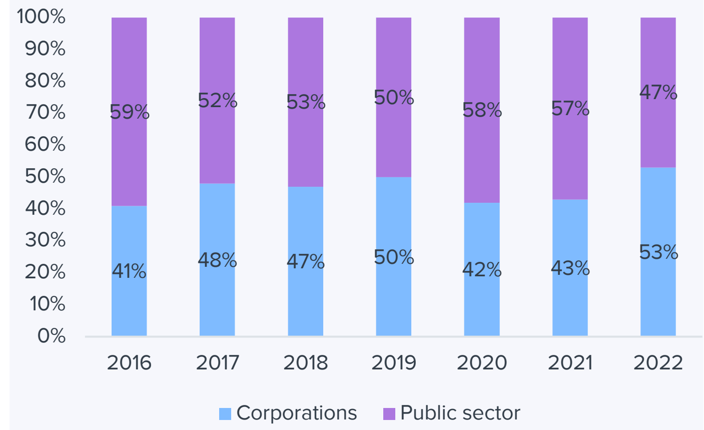
Innofactor refined its offering and structure two years ago to better reflect the current strategy. Innofactor's offering includes the following business areas: Digital Services, Business Solutions, Data and Case Management, Data and Analytics, Cloud infrastructure and Cybersecurity. Digital Services employ around 150 people and is concentrated on Finland. Business Solutionsemploy around 100 people and AI will accelerate development. Data and Case Management employs roughly 100 people and includes the company's own and most important Dynasty product. Here too, AI is key for future development. Cloud infrastructure employs around 100 people and the challenge is price competition and the transition from cloud transformation to continuous development. Data and Analytics also employs roughly 100 people and is one of the key growth areas that also gets tailwind from AI. A year ago, the company strengthened its data and analytics expertise by acquiring Invenco. Cybersecurity employs some 20 people and we suspect it has progressed slower than expected although it has been a hot area for the past few years. Innofactor is still looking for its own angle in Cybersecurity with which to stand out in the market. The company's goal has been to further strengthen these businesses, especially outside Finland. However, the company has not succeeded extensively in this in other countries so far and the benefits of the new structure are still sought.

Own products

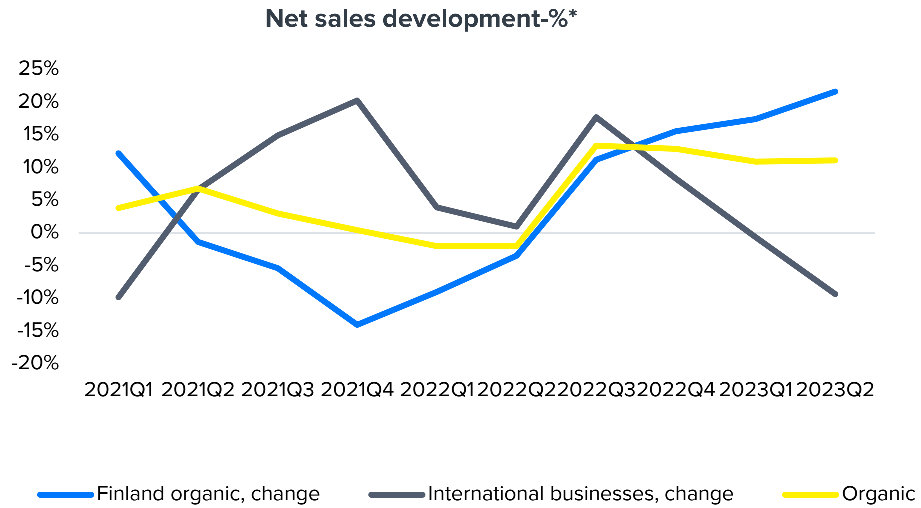
In Innofactor's current strategy the role of own software solutions grows, and the company tries to be a continuous service house built more strongly on products. The share of Innofactor's own product's license sales in net sales was ~2% last year and a considerable share of own product sales is visible in SaaS income (24%). Sales of own software products is very scalable net sales. Innofactor spent EUR 4.2 million on product development of its own software products, which represents 6% of net sales (2020: 3.5 MEUR and 5%). We estimate that R&D costs will remain at the same level over the next few years, and AI will bring efficiency to this, which means that in the future, investments will be more efficient.

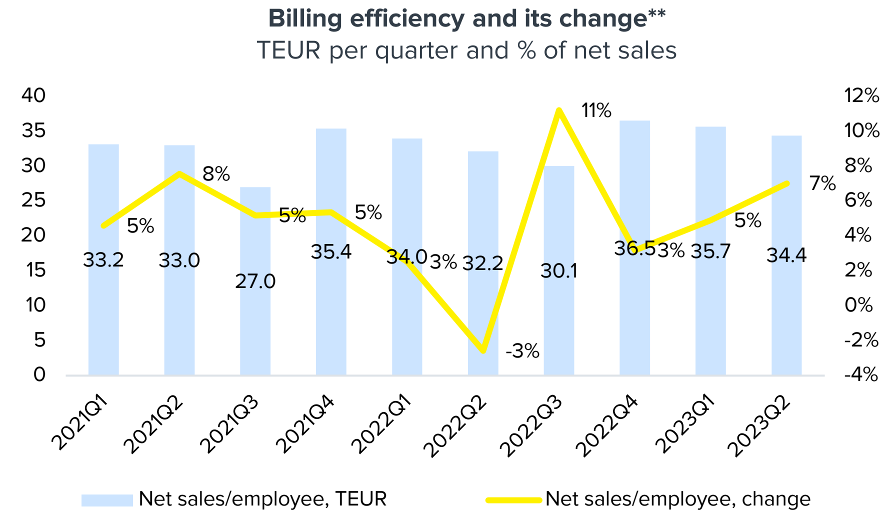
Especially the Dynasty product has been renewed in recent years and its demand is strong and profitability good. The product is currently sold mainly in Finland, but Innofactor is taking steps to expand product sales to Sweden, where the company has an important opening but the market is clearly more challenging. We believe that half of the net sales from the Dynasty product comes from software, which represents some half of SaaS's net sales, which we estimate to be just over EUR 8 million and has good margins. The second half from Dynasty (8 MEUR) is divided into services and projects that have lower margins. Some 50 people work on Dynasty's R&D, sales and implementation. We feel that the Dynasty product could independently comprise a rather large share of Innofactor's market cap, but we believe that the value is hidden within the Group and determining its value more closely is very challenging because investors have no detailed visibility into its profitability and development.

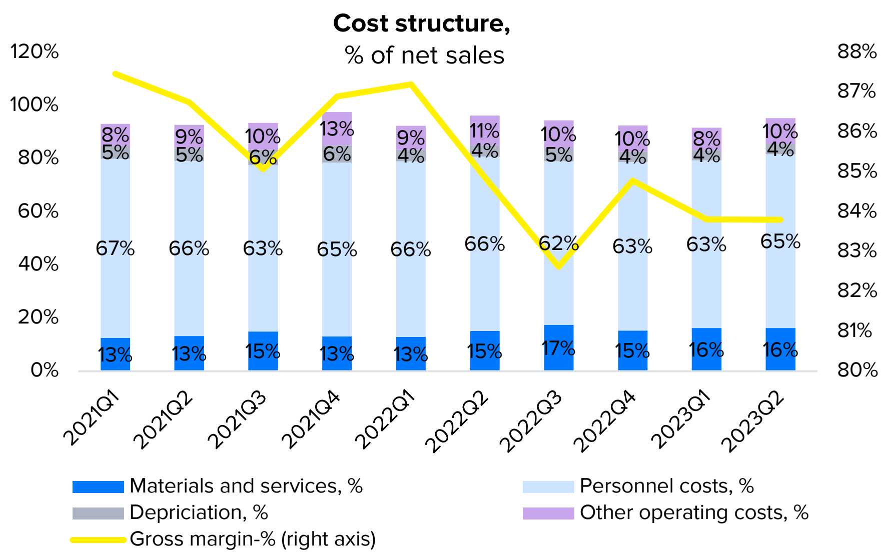
Net sales structure

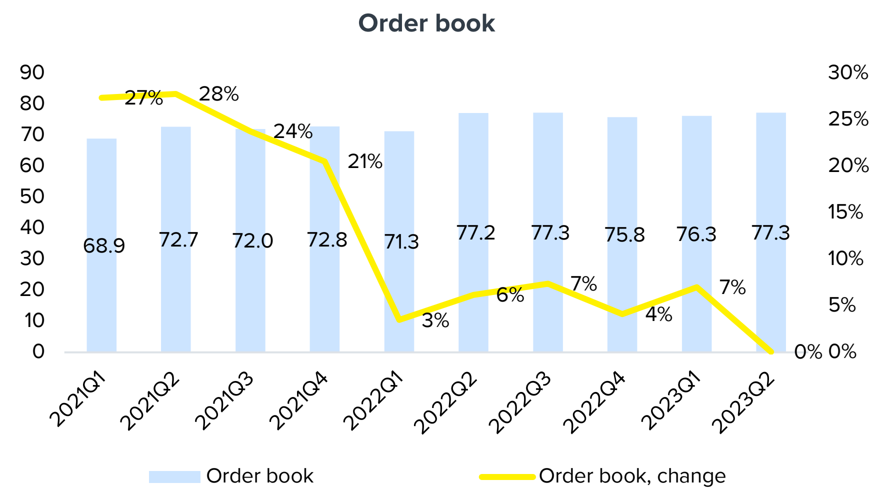


Key figures



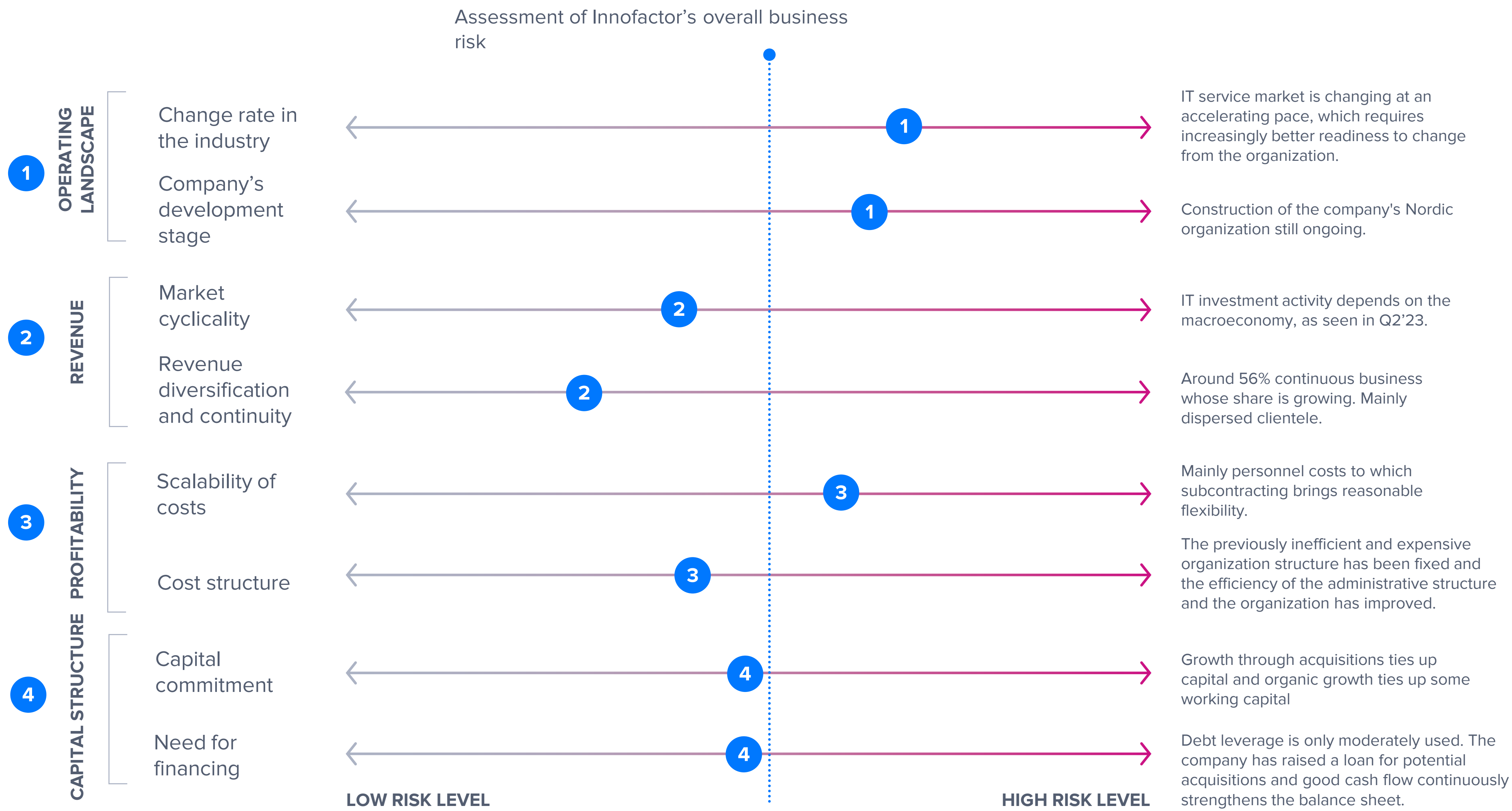






Source: Innofactor, Inderes. *Inderes' calculation of net sales growth and based on the company's net sales distribution. Includes the effects of currencies (weak SEK and NOK already for several quarters). **The indicator is a combination of the development of billable utilization, billed hourly rates and software.

Risk profile of the business model



Source: Inderes

IT service market 1/8

Large overall market

According to various research institutes, the size of the Nordic (Sweden, Norway, Finland, Denmark) IT service market was USD 25 billion in 2019. The Finnish IT service market has in turn been estimated to be divided into some EUR 3.5 billion private and some EUR 1.1 billion public sector. We believe the market has grown in recent years roughly in line with estimates, so we estimate the market size is around EUR 5.5 billion. The market is large and there is room for grow for the listed companies we monitor.

According to the definition of IT service markets, the market includes areas like IT consulting, software development services, integration and implementation services, outsourcing services, software maintenance and support, and IT infrastructure services. The definition of the IT service market and its euro-denominated size continues becoming obscure as the role of IT and technology continues rising from the engine room to the operational core in various industries because of digitalization. The operating field of IT service companies crosses paths with new parallel markets that have not conventionally been considered part of the IT markets. These include, for example, strategy consulting, transformation management and service design.

Market growth driven by digital services

According to various estimates, the conventional service areas are expected to grow by an average of 2-4% p.a. New digital services are expected to grow by up to 10% depending on the segment, although demand for them is more cyclical. Market growth is slowed down by decreasing demand for conventional infra and older generation software solutions. In addition, conventional IT systems are modernized, creating a rapidly growing area between the two.

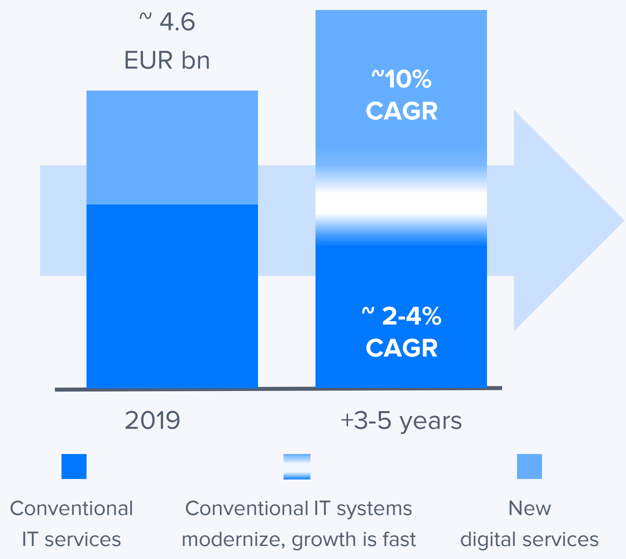
By service area, according to our research, the areas growing faster than the market are cloud services, transformation management, data & analytics, and cybersecurity. Tietoevry expects cloud services to grow by 15%, data & analytics by 15%, core software by 10%, and automation and DevOps by 20%. In our opinion, Tietoevry is one of the best players to assess market development in the Nordic countries because the company has an extensive IT offering, and it operates in most customer sectors and has strong geographical presence in all Nordic countries. By customer sector, Tietoevry reported that it expects the health care sector to grow by an average of 5-6%, public sector by 4-5%, energy sector by 3-4%, the forest industry by 6-7%, and banking and payment solutions by 4-9% in 2020-2023.

Long-term growth outlook of the market

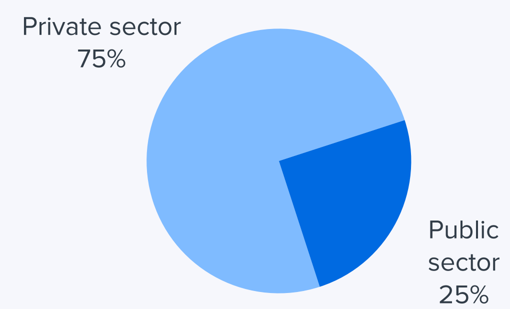
The digitalization of society requires a huge number of hands to build, integrate and maintain new applications, which means that the long-term demand fundamentals of IT consulting companies are strong.

Finnish IT market

Finnish market and growth picture



Market distribution by buyer group, 2019, % of the market



Source: IDC, Tutkihankintoja.fi

IT service market 2/8

Therefore, IT service companies offer investors a good opportunity to invest in the digitalization trend with the more limited risk profile of the service business. One can expect the market to grow more quickly than the macro economy in the long term. However, the market is cyclical, and the volume of IT services that companies buy externally can also decline and price competition intensify, as in the weaker economic situation in 2022-23.

Changing nature of IT investments divide the market

The continuously strengthening digitalization revolution launched a new era on the IT markets in the 2010s, which has redivided the market and generated new ways to operate on the market. Rapid market change requires IT companies to be able to continuously adjust their offering.

The shift on the market towards IT investments that create new business and differentiating factors that began in the 2010s continues as the quest for cost efficiency is no longer enough in the competition. This means that the IT buyer is often a business unit or product development not data administration or support function.

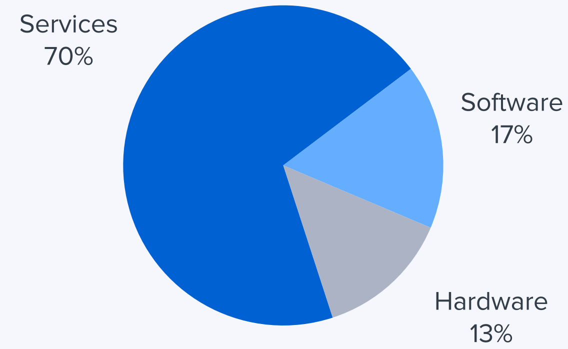
The desired expertise areas are increasingly linked to new digital services and less to background systems. The market revolution created strong growth potential for many original players of the new era (e.g. Futurice, Solita, Reaktor, Siili, Gofore and Vincit), that are profiled as developers of new digital services. Conventional players were initially slow to adapt their offering and culture to better correspond with the changing purchasing behavior and demand for service areas.

The change on the IT service markets in the 2010s can be illustrated in a simple way by dividing the market into new digital services that grow strongly and into the faltering traditional software system development. Dividing the market in two is, however, becoming irrelevant, as new digital services cannot be discussed separately from the core business systems.

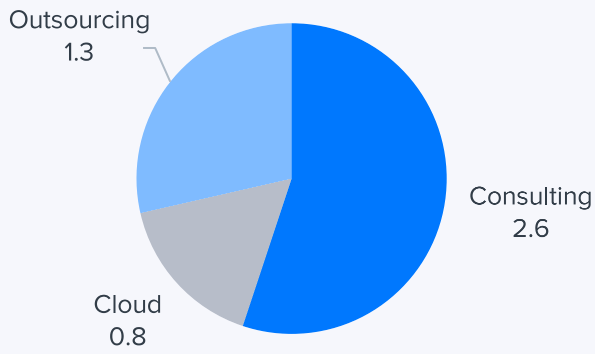
A clear trend on the market has in recent years been that IT purchases become more serious as the customer organizations have realized that you cannot get a short cut to digitalization by buying digital applications bypassing data administration. Organizations' established data systems will not disappear, but they must be modernized to work as platforms for new digital services. IT investments are directed at new functionalities that are built with interface solutions on top of existing systems. Correspondingly, this trend has restored competitive advantage to more conventional players, while many, primarily digital service developers that have succeeded mainly by acquiring talent, have been forced to reassess their strategies. As a result of increasing digital maturity in customer organizations, they have also become more demanding buyers and active in building their own software development teams.

The IT service market has undergone a considerable change over the past decade. Over the coming 10 years the change rate on the market will accelerate further and due to the complexity of technology and rapid development, it will become harder for companies to predict change. Thus, we believe that the ability of the companies in the sector to react and change will become increasingly important.

Finnish IT market,
2019, EUR billion



Finnish IT service market,
2019, EUR billion



Source: Radareco Nordic Outlook 2019

IT service market 3/8

Three different market areas

We have divided the IT service markets into three sections as follows:

Market for new digital services, that includes development of new digital services (tailored software development). This has been the strongest growing area on the market that was practically born only in 2010s. Well-known players on the markets are, e.g., Reaktor, Futurice, Nitor, Siili and Vincit, in addition to which large IT generalists have also started investing in this area but have been late to the game. The market is characterized by a low entry barrier. Witted is strongly positioned in this area.

Market for background IT systems and enterprise software, that includes ERP extensively and related systems covering primarily delivery, tailoring, integration and maintenance of firmware. Known players on this market in Finland include, e.g., Innofactor, Enfo, Solteq, Digia, Sofigate, Fellowmind, Vincit (after Bilot merger) and in particular IT generalists like Tietoevry and CGI. Market growth has been slow in this area and a high threshold to enter the market is typical. However, modernization of old systems has also created rapidly growing pockets in the market.

Market for IT platforms, that mainly covers infrastructure services (local, hybrid and cloud) and ICT outsourcing. This market has mainly been the strength of IT generalists (like Tietoevry, Fujitsu) and the threshold for entering the market is high because the market has required economies of scale and investments. As a result of the cloud revolution, a redistribution of the market is ongoing that has generated new quickly growing players (like Nordcloud) and many medium-sized IT consultants (like Gofore, Siili and Enfo) are also entering the field. This market has rapidly shrinking (local infra) and drastically growing (cloud platforms) areas.

Cross-cutting service areas of these three markets are, for example, data and analytics, integration, cybersecurity and robotic process automation.

In recent years, the most visible trend on the market has been IT players striving to win over customers already when projects are being planned, as selling one hour of design work has translated into selling multiple hours of software development work. Many players seek a stronger position in the value chain by strengthening their consulting service expertise, in which case the IT supplier manages the projects and resources and does not merely deliver them. This trend has been visible as several acquisitions on the market. In addition, many IT consultants try to expand into strategy level consulting, granted with varying degrees of success.

Another clear trend for the players in this sector is the life cycle approach, as many new players now try to build the ability to offer software maintenance. Customers' purchases continue to shift from software development projects towards continuous software development, which changes the nature of the markets.

Common for the strategies of all medium-sized and large players is also a strive towards the position of a more business critical partner for the customer. The know-how and offering of small software developers does not in this case reach deep enough into the customer's IT systems and processes. This development may accelerate market consolidation. When the market shows weakness, companies with the strongest customer relationships typically perform best, as in the weaker market environment of 2022-23.

We believe the Finnish IT service market is strongly developing in a direction where the paths of conventional and new players cross and the boundary between new and conventional IT continues to blur.

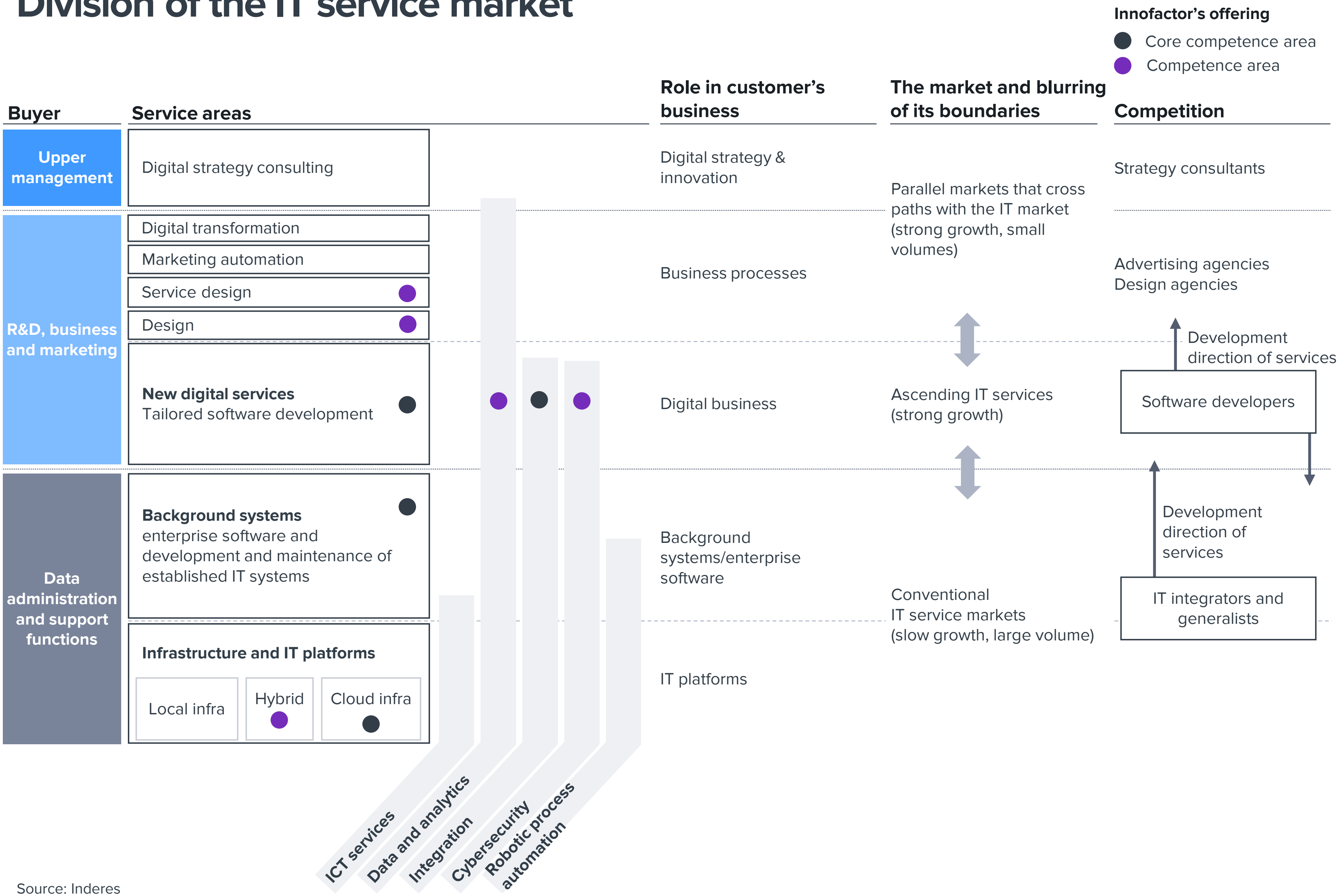
Background system expertise makes a comeback and one must know how to utilize related data

The strongest demand on IT markets has for years been in developing digital services and in software development that is still quite experimental by nature. According to our view, the market has, however, in recent years moved to a stage where one must be able to integrate new digital services and especially related data more tightly with the customer's background systems to get full business benefits from the new solutions.

Customers also have increasing needs to modernize their background systems because an old ERP system may act as a break for the development of digitalization solutions. Thus, the nature of the ERP market that has suffered from slow growth for a long time will change, and the market is clearly picking up. The importance of integration and data expertise also becomes emphasized.

In background systems and maintenance, the competitive landscape is much more stable, the entry barrier is higher and customer relationship are long lasting.

Division of the IT service market



Source: Inderes

IT service market 4/8

It is also difficult to build the capabilities required for background systems. This trend towards a life cycle approach is one challenge for pure digital service developers in the competition with generalists.

Trends in organizations' IT purchases

According to our view, the digitalization revolution will drive customers' purchasing behavior towards the following trends, where there are both winners and losers:

Data and analytics is one of the hottest trends on the market. Data is becoming a strategic competitive factor in several industries and the precondition for AI solutions. Many players have put it at the core of their strategies. The challenge for customers is to combine data from silo-like data administration throughout the organization to marketing and business management. IT companies that have a combination of understanding in analytics, machine learning, and business are the winners. Innofactor strengthened this expertise last year through an acquisition.

Cybersecurity is still a relatively small share of IT service suppliers' offerings but like data it is becoming an increasingly strong competition factor. AI development also provides tailwind for cybersecurity demand. Buyers focus increasingly on cybersecurity, and a lack of this expertise is a clear reputation risk for suppliers. The geopolitical situation has further increased demand. Several companies in the sector are currently investing in their security capabilities. Innofactor has also invested in cybersecurity and set up a separate unit for this in H1'21.

Automation and robotic process automation are also becoming more important as service areas. Automation enables increased productivity, flexibility, scalability, and improved quality, as well as a customer experience without large and expensive system projects. Several companies in the sector have developed or acquired this expertise (e.g. Digital Workforce is an industry pioneer).

The market for **artificial intelligence (AI)** has been growing rapidly in recent years and is no longer just a buzzword. Recently, the market has taken quick leaps, e.g., in the field of technologies like ChatGPT and almost all actors are trying to exploit AI.

Building **subcontractor networks** is one of the clear trends of recent years. Companies partly patch-up their recruitment needs this way and increase flexibility.

Building **nearshore** capabilities has been a clear trend in recent years. With COVID, telecommuting has enabled this more widely. However, the cost level (wages) in nearshore countries has also increased but is still lagging behind the Nordic countries and this is one way to solve the lack of experts.

The in-house trend has continued to grow as companies' digital maturity increases. Digitally capable customers want to lead and keep the development of business-critical IT systems for their value creation under their own control.

Very little direct effects **from the war in Ukraine** have been seen on companies' business, only for Tietoevry. The virtually elimination of capacity from Russia and Belarus and the reduction in Ukrainian capacity has increased demand for other European countries. Large organizations have also begun to weigh their purchasing decisions outside Europe more closely. Indirect effects have been visible everywhere.

User orientation and the customer experience continue growing. Important areas include, e.g., digital service design, design and customer experience. Know-how in these areas will become the biggest competitive factor when selecting IT suppliers. Creative, design-centered players have been the winners.

The IT market still does least of what is talked about most. The volume of services related to the most visible terms (VR, AR, IoT, NLP, etc.) is still small on a sectoral level. These are, however, likely to become considerable service areas over the next five years.

Low-code and No-Code software development has become increasingly common in recent years. The development can be seen as partly disrupting conventional "easier" software development when software development can be done with a low number of or without any codes. It contributes to technological development, which companies have to adapt to and learn to utilize, which enables spending time on developing more challenging and better solutions.

The cloud transformation divides the market, even though the biggest transition is almost over. Customers' IT operations are still moved to the cloud due to benefits, and because it is often a precondition for new digital business models. Players with strong cloud technology expertise are the winners. The losers are players in conventional local IT infrastructure. The biggest cloud transformation is almost over in the Nordic countries and now we are moving to continuous cloud service/maintenance.

Conventional reselling of software licenses moves to the cloud and software companies try to take over a larger share of the value chain when moving to SaaS models. License commissions of resellers have decreased in recent years. Players that are dependent on license reselling are the losers. Customers are the winners.

IT service market 5/8

Customer organizations becoming silo-like will be a challenge for IT company sales. In addition to data administration, the IT buyer is increasingly marketing or product development, but building of a digital business requires cooperation between these areas and the ability to manage the whole. Players that manage large entities and who can address the customer's management and marketing are the winners.

The importance of **cheaper offshore resources** as a competitive factor diminishes as it is hard to generate new digital services reliably, fast enough and cost efficiently with offshore resources. Robotic process automation and AI weakens the competitive advantage of cheap labor. In addition, the price advantage of offshore has decreased with higher wage inflation. Players whose competitive edge has been based on offshore cost efficiency are the losers. Players who can combine local presence with sufficient cost efficiency by utilizing nearshore resources are the winners.

Large, multi-year high-risk ERP implementation projects (SAP, Oracle, IBM) are no longer carried out to the same extent and the nature of the market changes. Established ERP systems will not disappear from customers, but they will remain in maintenance mode by existing IT suppliers, and they will be moved to the cloud. Companies invest in modernizing ERP systems so that they do not become a bottleneck for digitalization projects. Generalists dependent on large projects have been the losers. Smaller players that have integration expertise are the winners.

Buying IT as large projects decreases further and moves towards smaller, iterating processes and continuous development. Slowly reacting project organizations are the losers. Players that have expertise in agile production, the ability to manage the services of several suppliers, and the ability to generate continuous services are the winners.

As business-oriented purchasing becomes more common, IT companies seek new value production based and more scalable pricing models to break their business model away from poorly scalable sales of expert resources.

IT investments shift from investments that make the customers' business support processes more efficient towards core business processes or investments that improve the end product itself. Players that have conventionally served business support processes and ERP stakeholders are the losers. Developers of new digital service with technological know-how, expertise in background systems and business savvy are the winners.

Ownership of customers' IT budgets becomes blurred and moves from a CIO role more towards the role of business directors and marketing. Players that understand the customer's business and industry are the winners.

Lack of experts, wage inflation and customer prices are the nut to crack in the sector

According to our view the chronic lack of experts and stronger wage inflation than customer price increases is one of the key medium- and long-term challenges for the sector. It becomes increasingly difficult over time to solve this equation through continuously improving efficiency. In particular, at senior level, companies must be able to distinguish themselves with other factors than pay related ones. We believe these factors include, e.g., interesting customer projects and a good work environment for career development.

Companies must also be able to retain employees and minimize attrition. In recent years, the sector has tried to solve the lack of experts by increasing and building outsourcing networks.

Based on discussions we have had with various companies, wage inflation has been between 2% and 6% in 2020-2023 depending on emphasized skills. Tietoevry's wage inflation averaged 4% in 2022, which is lower than the sector's other comments. In 2023, Tietoevry expects wage inflation to be on average 4-5%. In the shorter term, the slowdown in demand curbs wage inflation, as in a weak economic environment attrition typically decreases, but at the same time high inflation creates additional pressure on pay raises. This is partly controlled by using geographically cheaper workforce, which is not, however, a sustainable solution for the problem in the long run. Gofore's collective agreement where wage increases are linked to the development of organic growth and profitability, seems to us to be one of the ways of controlling wage inflation.

The development of customer prices has for years been 0-2% based on sector comments and thus clearly more modest than wage inflation. Personnel costs represent roughly two-thirds of costs in the sector and thus comparison with wage inflation is not one-to-one, but the effect is still negative for nearly all players in the sector. As a rule of thumb, customer prices are higher in the private sector while contracts in the public sector are conventionally long and thus offer continuity and predictability which enables better management of billable utilization.

IT service market 6/8

In the medium- and long-term, wider use of junior resources would solve the lack of experts, alleviate wage inflation, and increase efficiency. Wider use of nearshore working would also solve the lack of experts in the short term and could curb wage inflation in the companies. In the medium and long term also those who can generate added value for customers and thus raise customer prices will be winners.

Features we expect from future market winners

The clearest winners on the IT markets in the past five years have been companies specialized in developing new digital services that have been particularly successful in the competition for talent. The market for digital services has now reached a clearly more mature stage and the next battle will also be outside pure talent competition. In our view, the sector's success factors change and the winners in the next five years will be:

Companies capable of continuous renewal. The IT service market is sort of in a constant transformation. Reacting to changes and recognizing them in advance is crucial for one's success. In an accelerating technological change, experts' ability to change also becomes key. Failure in this renewal exercise would directly affect current customer relationships, acquisition of new customers, relative competitive position, and thus long-term value creation potential. We believe that sustainable competitiveness in the sector must be built on constant ability to change.

We believe that companies that **are better able to combine junior resources** will grow more strongly and profitably. A god example of this is the Danish IT service company Netcompany. Wider use of junior resources in Finland would to some extent also require a change in buyers (away from the CV model to buying solutions).

Owners **of strong customer relationships** with a strategic partner role among customers, a strong sales machine and the ability to manage large IT projects and scale operations through a strong subcontractor network. Small players that hold the role of subcontractor and that have mainly focused on talent competition more than on customers are weak when the economic cycle weakens.

Companies with strong integration and background system expertise and the ability to provide maintenance and continuous services. Strong maintenance players are also strong when the market weakens. This is the weakness of many medium-sized digital service developers.

Companies that can build a dynamic organization model that has the agility to react to a rapidly developing market. Many companies in the sector suffer from inefficient, inflexible, hierarchal, and silo-like organization structures, which makes renewal difficult when the market changes.

Data and analytics are becoming an increasingly critical part of the delivery and an ability to generate added value for the customer and competitive advantage for the supplier. The role of the service area is already important but becoming even more important and also enables wider and more efficient use of AI and machine learning.

Sources of competitive advantage in the market

- Especially important now is the sales function
- Continuous ability to renew
- Ability to recruit in the medium and long term
- Life cycle offering
- Hot expert areas:
  - Transformation ability
  - Data utilization
  - Cybersecurity
- Agility and speed
- Experts' abilities (CV)

Added value in the market

- Digitalization and digital transformation
- Business approach
- Developing new business
- Data utilization

Source: Inderes

IT service market 7/8

Acquisitions and consolidation continue in the sector

Consolidation of the IT service sector was active throughout the last decade and has continued as surprisingly lively despite market uncertainty. However, we believe many companies in the sector would have preferred to continue more active inorganic growth as well and put strong balance sheets into productive work.

In the big picture, most companies in the sector have a high interest in M&A transactions. Consolidation is driven by the desire to expand the expertise portfolio, geographical expansion and increase supply capacity. We believe, however, that most companies in the sector do not have a critical need for acquisitions, and the need is driven by other issues, like strategic objectives. Growth alone is a relatively 'poor' reason for acquisitions and, in our view, the greatest benefit will come through the expansion of the expertise portfolio, which will strengthen competitiveness and generate revenue synergies. For an acquisition to be successful it is important that strategies and cultures are compatible.

Most companies in the sector have strong balance sheets and virtually all have healthy profitable businesses, which consistently generate good cash flow and further strengthen the balance sheet. Of course, it is possible to use own shares and many companies have also utilized this option. However, the valuation level of several companies is currently relatively low and the use of own shares does not offer the same opportunities for creating shareholder value.

We believe using leverage in acquisitions remains a good option, even though interest rate levels have risen considering the strong balance sheets and companies' strong cash flow. A moderate leverage would also improve equity efficiency.

Capital investors are also still active and building IT expert houses. A couple of years ago Triton acquired HiQ that was listed in Sweden In addition, several capital investors have continued consolidating smaller IT service companies.

As the market for digital service development is becoming more mature and the various areas of the IT market become integrated, a broader consolidation is likely as was seen in the Tieto and EVRY, and the KnowIT and Cybercom mergers. An interesting scenario could be to combine two players in the mid-market to better challenge large generalists like the merger of Bilot and Vincit. In our view a merger should have clear revenue synergies and factors that strengthen competitive advantages. We believe there are unlisted players on the Finnish market whose expert focus, geographical presence and customer portfolio would fit in well with listed players.

Clear expert areas that in recent years have been acquired to strengthen the offering include consulting, transformation management, data and analytics, and automation expertise utilizing robotics. Cybersecurity expertise is on the wish list, but we suspect that the valuations of the acquisition targets limit transactions. Transactions have also been carried out for delivery capacity, but especially at the moment, in an easier recruitment market, companies are more cautious about making arrangements simply based on capacity.

At Innofactor, acquisitions were a significant part of the strategy in the past. Now the role of acquisitions has diminished, but it is still part of the strategy.

	Digia	Gofore	Innofactor	Loihde	Netum	Siili	Solteq	Tietoevry	Vincit	Digital Workforce	Witted
Interest in transactions	4	4	3	4	4	4	3	4	4	5	4
Need for transactions	2	3	2	2	2	3	2	1	2	4	2
Balance sheet enables acquisitions	3	5	2	5	2	3	2	3	4	5	4
Interesting acquisition target	2	3	3	2	3	2	4	1	3	4	2

1=lowest, 5=highest.

Source: Inderes' estimates

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Comments based on latest earnings periods

Uncertainty in customer demand was realized more widely in Q2, but development was even more mixed than before. Companies with a high weight of tailored software development and the private sector suffer more in relative terms. Reported figures included mainly negative surprises, which was also seen in the form of change negotiations and profit warnings. We predict that the duality will continue in 2023, but the demand outlook will remain more subdued as a whole in 2023 in the private sector, while public sector demand is expected to remain at a good level.

Company-specific Q2 figures for the IT services sector are seen in the table on the right. Key comments about the sector in the latest quarter are:

- Organic growth decelerated clearly in Q2'23 and was 0% (Q1: 10%). The weaker development was partly affected by one working day less than in the previous year, while Q1 had one more working day than the previous year.
- In Q2, profitability decreased to 5% from 9% in Q1 (Q2'22 5%). Profitability remained below expectations for most companies in the sector.
- During the summer, driven by a weak market, there have been several change negotiations and profit warnings.
- You can read our IT service sector Q2'23 summary here, and the Q1'23 summary is available here.

Short-term outlook for the sector

Company-specific 2023 estimates for the IT services sector are seen in the table on the right. Key findings on the short-term outlook:

- In the short term, there is clear uncertainty in the market, which has already materialized for some companies as declining demand and price competition.
- Companies with more recurring revenue (longer order books), deep and strategic customer relationships, that operate in the public sector, have long contracts, ERP business, and generally those who make business-critical solutions for customers are faring best. Companies with a high emphasis on the private sector and software development are faring the weakest.
- In the big picture, it can be said that competition has shifted from experts to customers for the first time in several years. However, we expect this to be temporary.
- Declining attrition and uncertainty in customer demand are likely to curb the strongest wage inflation. We also expect wage inflation to moderate at sector level in the short term. For some companies, attrition even reduces wage inflation.
- AI has also been a hot topic, and it is particularly interesting in this market situation because it can generate cost savings for the customer and also make the work of suppliers more efficient. However, for the time being, AI still plays a small role. In the coming years it will open up new growth opportunities. However, we suspect that it is difficult for IT service companies in the big picture to stand out from each other competitively.

Q2'23	Growth, %	Q2'23 Organic growth, %	EBITA % adj. Q2'23	EBITA % adj. Q2'22
Digia	16%	9%	7.1%	5.0%
Digital Workforce*	5%	-3%	1%	-13.4%
Gofore	28%	22%	11.3%	15.0%
Innofactor	19%	11%	5.2%	4.0%
Loihde	15%	0%	-2.2%	1.8%
Netum*	11%	6%	5.7%	11.0%
Siili	7%	3%	5.2%	10.0%
Solteq	-20%	-8%	-13.7%	3.0%
Tietoevry	-6%	-6%	10.5%	11.0%
Vincit	36%	-7%	-1.7%	5.0%
Witted	25%	-4%	-1.4%	-0.4%
Average	12%	2.2%	2.3%	4.7%
Median	15%	-0.2%	5.2%	5.0%

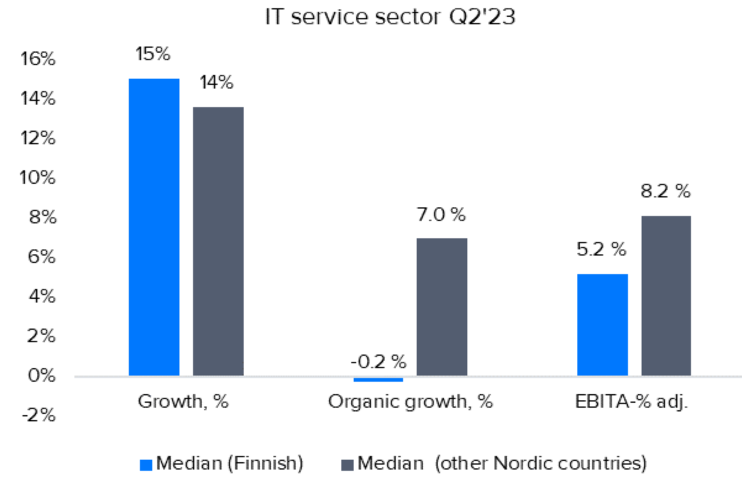
Source: Companies and Inderes.

	2023e (after Q2 report) Growth, %	Organic growth, %	EBIT % adj.
Digia	11%	7%	9.2%
Digital Workforce	3%	1%	2.1%
Gofore*	29%	24%	13.9%
Innofactor	12%	9%	6.9%
Loihde	10%	0%	1.1%
Netum*	30%	14%	8.8%
Siili	6%	2%	6.9%
Solteq	-13%	-4%	-4.0%
Tietoevry	-2%	0%	13.2%
Vincit	17%	-1%	4.1%
Witted	25%	4%	0.2%
Average	11.6%	5%	5.7%
Median	10.7%	2%	6.9%

Source: Inderes, *Gofore's estimate after net sales release in July

Nordic IT service market in Q2

Q2'23	Growth, %	Q2'23 Organic growth, %	EBITA % adj. Q2'23	EBITA % adj. Q2'22	Net sales vs. expectations	EBITA % vs. expectations
Digia	16%	9%	7.1%	5.0%	Above	Below
Digital Workforce*	5%	-3%	1%	-13.4%	Below	In line
Gofore	28%	22%	11.3%	15.0%	In line	Below
Innofactor	19%	11%	5.2%	4.0%	In line	Below
Loihde	15%	0%	-2.2%	1.8%	In line	Below
Netum*	11%	6%	5.7%	11.0%	Below	Below
Nixu						
Siili	7%	3%	5.2%	10.0%	In line	In line
Solteq	-20%	-8%	-13.7%	3.0%	Below	Below
Tietoevry	-6%	-6%	10.5%	11.0%	Below	Below
Vincit	36%	-7%	-1.7%	5.0%	In line	In line
Witted	25%	-4%	-2.6%	-0.4%	Below	Below
Avensia	-8%	-8%	-6.5%	0.6%		
Addnode	4%	1%	7.1%	10.3%		
Bouvet	14%	14%	11.0%	12.5%		
Columbus	11%	16%	2.2%	2.0%		
CombinedX	19%	7%	10.1%	7.8%		
Exsitec	13%	7%	16.3%	12.9%		
Knowit	-2%	-2%	4%	8.5%		
Netcompany	14%	14%	10%	11.9%		
NNIT	15%	11%	5.9%	-4.8%		
Webstep	16%	16%	9.2%	8.5%		
Average (Finnish)	12%	2.2%	2.3%	4.7%		
Median (Finnish)	15%	-0.2%	5.2%	5.0%		
Average (other Nordic countries)	10%	6.9%	6.9%	7.0%		
Median (other Nordic countries)	14%	7.0%	8.2%	8.5%		
Average	11%	4.3%	4.5%	5.8%		
Median	14%	4.5%	5.7%	7.8%		



	Public change negotiations	Net sales guidance cut	Guidance cut
Digia	No*	No	No
Digital Workforce	No	No	No
Gofore	No	No guidance	
Innofactor	No	No	No
Loihde	No*	Yes	No
Netum	No	Yes	Yes
Siili	Yes	Yes	Yes
Solteq	Yes	In estimates	In estimates
Tietoevry	No*	No	No
Vincit	Yes	Yes	Yes
Witted	Yes	No	No

Source: Inderes, Companies, *Part of the organization has been restructured

Sector acquisitions in the Nordic countries

Acquisitions in the IT service sector in Nordic countries

Date	Buyer	Target	Net sales	EBITDA	EBITDA %	Own workforce	EV	EV/Sales	EV/EBITDA
			MEUR	MEUR			MEUR		
07/23	Netum	Buutti Oy	9.3	1.1	12%	110	10.0	1.1x	9.1x
04/23	Azets	Solteq's Microsoft and Retail businesses	11.2	1.5	~13 %	60	15-20	1.3x-1.8x	10x-13x
02/23	DNV Group	Nixu	60.2	2.4	4%	393	98.0	1.6x	41x
01/23	Netum	Studyo	1.3	0.1		14			
01/23	Investcorp International	Eficode Oy	150.0			600			
11/22	Solteq	S2B Energia Oy				10			
11/22	Loihde	Onrego	7.1	0.5	7%	30	4.3	0.6x	~9x
11/22	Gofore	eMundo	~8	0.8	9%	96	8.0	~1x	~8x
10/22	Digia	Avalon	2.4	0.4	15%	24			
10/22	Siili	Haallas	5.8	0.9	~15 %	>50	3.75-9.0	0.6x-1.6x	4x-10x
09/22	Witted	Nexec Oy	12.8	0.7	5.8%	80	8.3-12	0.7x-0.9x	11x-16x
07/22	Vincit	Bilot (merger)	30.5	0.6	2.1%	195			
06/22	Digia	Productivity Leap Oy	5.5	1.2	22%	35			
06/22	Innofactor	Invenco Oy	6.3	0.4		50	3-7	0.5x-1.1x	8x-19x
06/22	Knowit	Marketing Clinic Oy	10.5			60	8.5-10	1.0x	
05/22	Pinja	Oiwa	2.1			25			
04/22	Digia	MOST Digital	3.0	0.0	0%	34			
01/22	Gofore	Devecto	10.7	2.0	19%	130	21-26	2.0x-2.4x	10x-13x
01/22	Solteq	Enerity Solutions Oy	2.2	0.3	~15 %	>20	4.5	2x	15x
11/21	Norvestor	Pinja	40.0			450			
11/21	HiQ	Lamia	8.3	2.7	33%	90			
10/21	NetCompany	Intrasoft International S.A.	197.0	18.0	9%	2,800	235	1.2x	13.1x
10/21	Netum	Cerion Solutions Oy	3.6	0.5		38	6-7.1	~1.8x	9x
10/21	Bilot	Motley	4.1	0.2		40	5.1	1.2x	26x
09/21	KnowIT	Capacent (management consulting)				50			
08/21	HiQ	Advicon				25			
08/21	Advania	Visolit				1,200			
05/21	eCraft (Fellowind)	Project-IT	12.0			30			
05/21	Eficode	Beecom (SUI)	10.0	1.5	15%	58	10	1.0x	6.7x
05/21	Loihde	Talent Base Oy	7.4	1.1	15%	58	10	1.4x	9x
05/21	HiQ	Scandio (GER)				100			
05/21	Knowit	Cybercom				1,200			13x
04/21	Vincit	Bonsky Digital	2.7	0.2	7%	30	2.7-3.0	1.0x-1.1x	13x-15x
03/21	TSS	Innofactor's Prime business	>2			15			
02/21	Aucerna	TietoEVRY's oil and gas business	~50			430	155	3.2x	
02/21	Solteq	Partiture Oy	2.4	1.0	40%	16		1x	2x-3x
02/21	Gofore	CCEA and Celkee Oy	5.6	1.2	21%	50		1.1x	5.1x
12/20	IBM	Nordcloud	80.0			490			
12/20	Digia	Climber (SE, FI, DK, NED)	13.8	0.7	5%	77	8-14	0.6x-1.0x	12x-20x
12/20	Siili	Supercharge (Hungary)	9.0	2.1	23%	115	17	~1.8x	~8x
08/20	Triton	Hiq	~180	~25	14%	1,500	~340	1.9x	13.6x
08/20	Bilot	CastorIT	7.3	0.9	12%	60	8.8	1.2x	10x
08/20	Gofore	Qentinel	12.0	1.7	14%	100	8.9-10.9	~0.9x	~6.4x

Competitive landscape 1/5

Competitors on three levels

Following the fragmented structure of the Finnish IT service market the competitive landscape is also fragmented. At the top level we feel the competitive field can be divided into three layers.

The first layer is international IT generalists whom according to different market sources hold a market share of close on 50%. Such global giants include, e.g., Tietoevry, CGI, Fujitsu, Accenture and CapGemini. The second layer is suppliers with revenue of around EUR 20-150 million and their combined market share is estimated to be around 30%. The third layer and thus the tail-end of the market includes smaller solution houses that employ less than 200 people.

Innofactor's competitors

Innofactor's competitors are large often international IT generalists, medium-sized IT service companies, and small players specialized in certain solutions. Examples of generalists are Tietoevry, CGI, Capgemini, Fujitsu and Accenture (Avanade). Among medium-sized IT service companies Digia, eCraft, HiQ and KnowIT can be mentioned as competitors. It is, however, hard to pick clear individual main competitors due to the fragmented sector and Innofactor's Microsoft specialization. Of individual companies, Innofactor faces Tietoevry most often in tender processes. Small software developers (like Vincit, Reaktor and Futurice) mainly operate on different markets and thus Innofactor seldom faces them in competition but with Siili the company participates in some of the same competitive biddings in the area of digital customer experience. In public administration the company faces Gofore in competition who has succeeded in public administration with a strategy based on open-source code. Next to Innofactor, also Digia and eCraft are strong in Microsoft's ERP solutions in Finland. In Microsoft's cloud-based solutions and especially in the Office365 area the company competes with the rapidly growing Sulava.

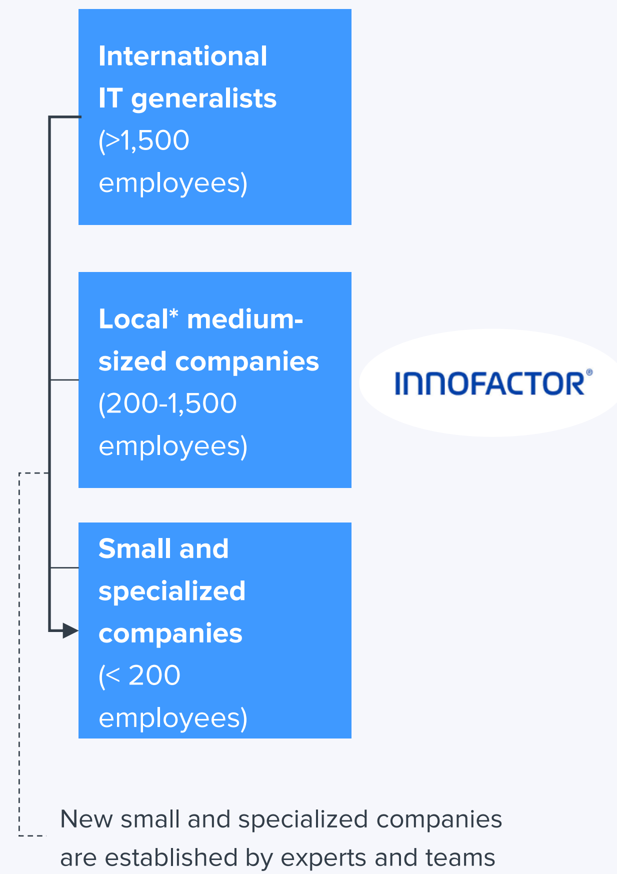
Innofactor stands out from its biggest competitors with its agility, service, productized offering, local expertise, and know-how in Microsoft solutions. Customer organizations rarely want to buy from players that are clearly bigger than themselves, so the company also has a more natural position among medium sized customers. Innofactor stands out from smaller competitors with its Microsoft expertise, productization, as well as the credibility and references of a larger player.

Various ways to combat the scale of big players

We feel the clearest strengths of large IT generalists are extensive resources and offerings, which are often strengthened with cost-efficient offshore production.

The customer and industry portfolios of these players are typically extensive. Customer and industry understanding is also often deeper than for smaller players. Strong background system expertise lies at the core of IT generalists' genetic ancestry.

Dynamics of the competitive landscape



*There are also international companies such as Siili, Gofore, Witted, Solteq, Vincit and Innofactor among medium-sized companies

Source: Inderes

Competitive landscape 2/5

In practice this means that the solutions of these companies are both very business critical and established from the customer's viewpoint. In addition, these background system deliveries are also technically very challenging and high-risk projects, which raises the threshold of market entry. The key sources of competitive advantages of IT generalists can in our opinion be summarized as large resources, the costs the customer faces if changing suppliers, and high thresholds to enter the market.

Next to agility, small companies usually need some expert spearhead to be competitive against large generalists. Smaller companies also break into customers through some other buyer than IT management by selling digitalization solutions, for example, directly to the business. Thus, smaller companies do not necessarily ever face the customer's established system supplier in competition. Large generalists and small suppliers often operate in slightly different areas. In recent years, the biggest players in the sector have, however, started strengthening their abilities in the development of new digital services, which has made the competition tighter (e.g. more overlapping).

Because the revenue model in the industry is capital light and personnel intensive the thresholds to enter the industry are also low in general. Many new payers on the IT service market have been born when experts that have left established IT generalists have founded their own companies. We believe the biggest weakness of smaller players is that they often get stuck in the value chain and must serve end customers only as a part of the value chain. Therefore, small companies are not necessarily able to offer ambitious experts interesting career paths which also makes it more difficult to grow the business and improve the company's position in the value chain. In the competition for experts the key assets of small companies are usually cultural.

Competitive advantages are constantly being built

Despite the good growth outlook in the industry there is a lot of competition as there are several suppliers on the market, and, as stated before, the thresholds to enter the market are low. We also believe that the preconditions to stand out merely with technical skills and individual point solutions are small. In the long term, we believe competitive advantage must be built based on more extensive skills that aim at strategic partnerships. This in turn requires that the company's operations offer continued dynamism, flexibility, and renewal ability. To be successful in the long term, we believe companies must be able to read the development of both technologies and customer needs and react to these changes by building their own capabilities.

Considering this, we believe that building truly sustainable competitive advantages is structurally hard. We do not, however, consider this to be a barrier for long-term value creation.

Innofactor's competitive factors

Strengthening factors

- Ability to deliver and maintain business critical systems
- Solid Microsoft expertise
- Productization of offering and own software products
- Good position in public sector in Finland
- Product offering that covers life cycle

Weakening factors

- Facing large generalists with extensive offshore resources
- Several small, agile players as challengers
- Strong competition for experts limits growth
- Excluding other technologies

Source: Inderes

Competitive landscape 3/5

Growth and profitability of the peer group

The figure on the next page examines the growth and profitability of listed and unlisted Finnish and other Nordic IT service companies. The comparison also includes some US players that operate globally and play an important role in the European market, as well as Kainos from Great Britain. For some companies we have not yet received 2022 figures.

The annual average growth of the peer group has been around 22% in 2018-2022, which is explained by market growth, the fast organic growth of many players and acquisitions. The companies that have grown most strongly have expanded both through acquisitions and organically. Strong organic growers have been, e.g., Luoto, Gofore, Sulava, Siili, Vincit, Witted, Futurice, Netum, Reaktor, Eficode, Bouvet Netcompany. Growth has been slowest for the largest players that have suffered from the market revolution (like Tietoevry, Enfo and CGI).

When examining growth, you can see that small, specialized players have clearly reached the fastest growth on the Finnish IT markets. This reflects the faltering of the demand for conventional system development, and IT demand focusing on new areas to which smaller and more agile players have been able to respond more efficiently. Over the past few years many formerly small and agile players have, however, already grown into a relatively larger size class and maintaining the growth rate is becoming more challenging, which was visible as slowing organic growth for some companies in 2019-2021. A company that stands our clearly is the Danish Netcompany that despite its nearly 5,000 experts (now 7700) was able to grow organically in its service business by ~20% p.a. and generate an EBITDA margin of over 25%. In addition, Gofore's organic profitable growth has even accelerated in recent years, even though the company has already reached a significant size class.

In terms of profitability, the average for the peer group is 11% measured by EBITDA % at an annual level in 2018-2022 (2017-2021: 12%). On average, the profitability of the companies is on a healthy level. The IFRS-16 amendment raised the EBITDA margins of companies using IFRS accounting by some 1 to 3 percentage points starting from 2019 (more moderate effect when examining averages). This weakens comparability with the period preceding 2019, and especially with companies using FAS accounting. In the IT service sector, we have considered an EBITDA level of over 10% to be a good profitability level (excluding the IFRS-16 effect). Companies should not be satisfied with single-digit profitability levels. Large generalists Tietoevry and CGI have generated good profitability despite slow growth, which is based on their strong market position and software business.

By comparing the combination of profitability and growth over the past few years, a few players stand out above the rest. The stars include Finnish companies Gofore, Solita, Sofigate and Netum, as well as Danish Netcompany, Kainos from Great Britain, Norwegian Bouvet, and Globant, Endava and Epam from the US.

Growth drivers

Long-term

- Digitalization will accelerate and grow the market
- AI creates new growth opportunities
- IT will become more of a key area of companies' business and strategy
- Increasing customer prices
- The definition of the IT service market becomes broader
- Internationalization and increasing nearshore
- Acquisitions

Short-term

- Efficient sales function
- Decrease in customer prices
- Recruitment - employee image, low attrition
- Improving efficiency through billable utilization and/or process efficiency
- Increasing subcontracting
- Acquisitions

Profitability drivers

Short-term

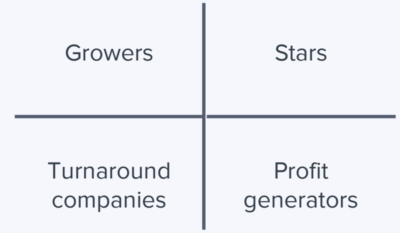
- Pressure in customer prices
- Billable utilization
- Attrition management
- Controlling wage inflation
- Improving efficiency

Competitive landscape 4/5

Competitors' financial development 5 years

Source: Inderes, companies. Figures include the IFRS 16 amendment starting from 2019, for some
*2017-2021
**Contains independent figures of Tieto and Evry first for 2017-2020
***2019-2022; revenue development for digital development and Group EBITDA used for Loihde
^EBITDA % -10.7%; ^^Vincit's and Bilot's consolidated figures

Profile of competitive field



Stars

- Forerunners with a history of profitable growth
- Mainly small and agile players that have positioned themselves and invested in growing areas of the IT service market
- The organization structures of stars are light, and they are highly business oriented

Growers

- Companies that are growing but whose investments depress profitability
- Growth has often been accelerated with acquisitions

Profit generators

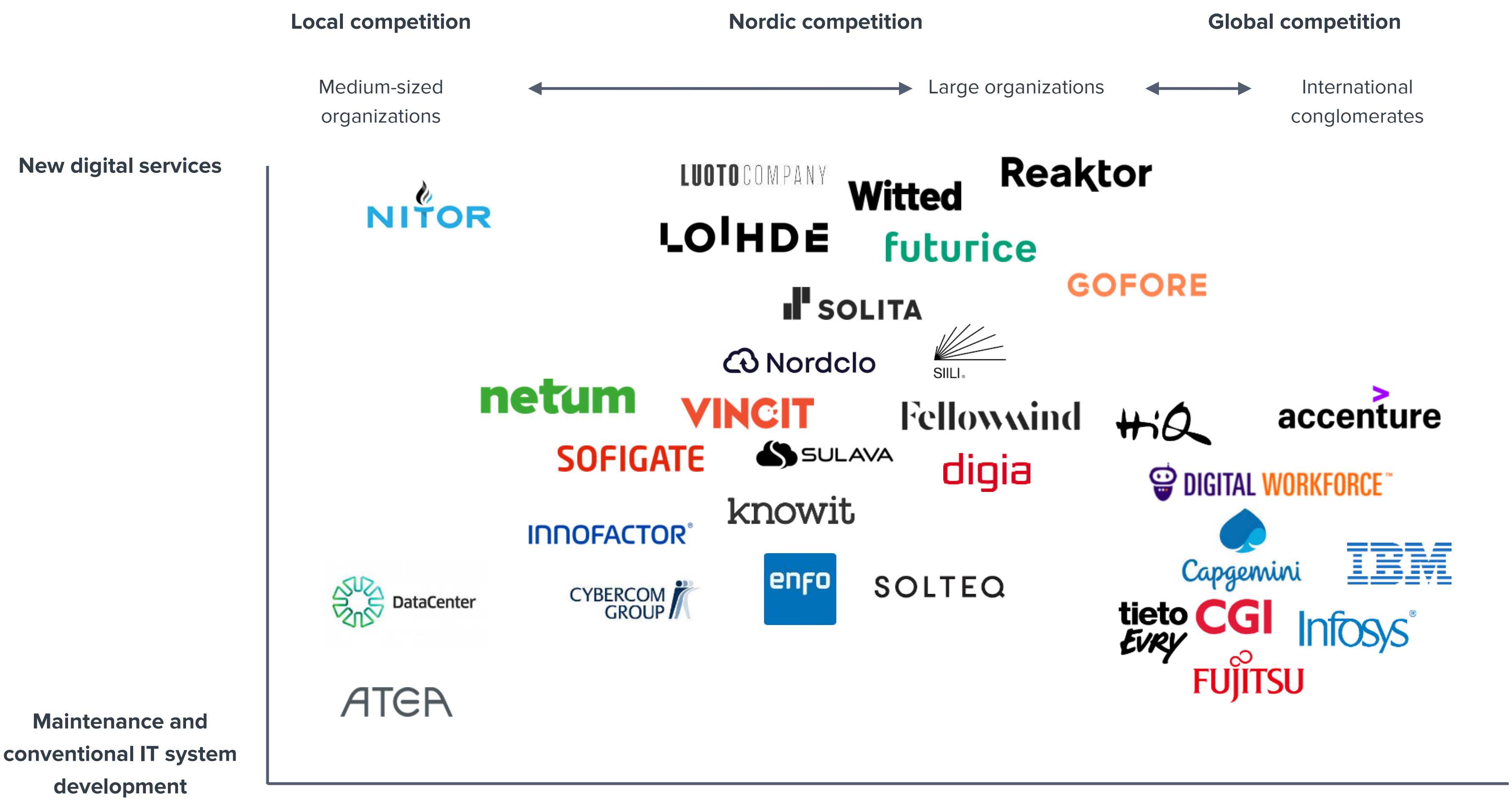
- Companies whose customers have high costs of changing supplier, for example due to tailored software solutions
- Profitability partially optimized at the expense of growth

Turnaround companies

- Mainly conventional IT companies that are in transition or have not been fully capable to adjust to the IT market revolution

Competitive landscape 5/5

Finland's market structure based on customer size and service area-specific positioning



Source: Companies, Inderes

Microsoft solutions in the IT market

Microsoft's position on the IT market is strong

Microsoft has grown clearly faster in several product areas than the rest of the IT market, which also supports Innofactor's strategic choice. We believe Microsoft's position on the IT market is very strong and we see no signs of the position of Innofactor's principal weakening. The demand for Microsoft's products has grown with the cloud transformation and as a company Microsoft has shown its ability to renew itself and has also invested in renewal through acquisitions like LinkedIn and GitHub. The latest and most significant investment is Microsoft's investment in Open AI whose product is called ChatGPT.

In its strategy, Innofactor believes Microsoft and thus also its partners will be strong in the key trends that shape the IT markets. These trends include, e.g., software moving to the cloud, mobility, IoT, machine learning, analytics, cybersecurity and data protection, and as the hottest topic, generative AI. Microsoft is in a leading position on several IT market areas, its offering is competitive, and its cloud solutions are still growing strongly.

From Innofactor's viewpoint Azure, Office 365 and Dynamics 365 have for years been Microsoft's key products. Cutting edge products are still important, but the strongest cloud transformation is almost over in the Nordic countries. In the coming years, Innofactor expects Microsoft's AI solutions to further strengthen the position of Microsoft products and thus also demand.

Innofactor also believes that Microsoft's strong product development investments will secure the competitiveness of its products in the long run. Microsoft has spent USD 10-21 billion on product development annually in 2012-2021 financial periods. The level of product development investments is clearly higher than for the main competitors. Headed by the CEO Satay Nadella, Microsoft has moved its focus especially towards digital transformation, cloud platforms, as well as data-driven business and solutions that are more compatible with its competitors' solutions. R&D costs (18% and USD 25 billion) in 2021 were raised by investments in cloud services, gaming and LinkedIn. This year, investments in AI will drive development. We believe that AI was by far the biggest topic in the annual internal Microsoft and suppliers conference s summer. Microsoft's key competitors in various corporate solutions include, e.g., IBM, Oracle, HewlettPackard, SAP (ERP), Amazon (cloud services), Google and Salesforce (CRM).

Over the past decade, Microsoft has suffered from weak PC sales but the company's development has been good when examining the corporate solution areas that are key for Innofactor. Especially in the Commercial cloud solution reporting area (e.g. Office 365, Windows Azure , Dynamics CRM) growth has been strong and the annualized net sales of Microsoft's cloud solutions in Q3.23 was already good EUR 100 billion compared to EUR 80 billion in corresponding period in the year before and the EUR 60 billion before that. On product level, Azure grew by 27% (46%), corporate side Office 365 by 14% (17%), Dynamics 365 product by 25% (35%) and LinkedIn by 8% (34%) in Q3'23.

As software solutions have moved or will move to the cloud, success in cloud solutions is key for Microsoft's competitiveness. In market research company Gartner's Magic Quadrant reports on different cloud revolution areas (BI, IaaS, CRM and ERP) and in the AI Magic Quadrant reports Microsoft is the player that is ranked in the Leaders box most often (4/5). In the bigger picture the positioning is at the level of previous years in all quadrants.

According to Gartner, the cloud infrastructure market is still, despite the strong growth, heavily concentrating in the hands of a few players that are in order AWS, Microsoft and Google. Microsoft's position has improved slightly in the cloud infrastructure market quadrant. Microsoft and Salesforce (Tableau) are still the top BI platforms, and more competitors are running behind.

The CRM report has not been updated since 2021, when Salesforce was at the top, followed by several challengers, including a slightly strengthened Microsoft.

We included two Gartner reviews as new components in this report. Firstly, cloud AI solutions that are important for software developers, where Microsoft's solutions were at the top already at the beginning of 2022 and have, according to our estimates, strengthened further thanks to the ChatGPT cooperation. The second new review included in the report is cloud ERPs, which has been an important area for Microsoft and Innofactor in recent years. This is the only one of the included areas where Microsoft has fared a little weaker and is in the Visionary box with its Dynamics-365 product, while the other 4 spearheads (Oracle 2 products, Workday, SAP) are in the leader box.

Microsoft's competitive position 1/2

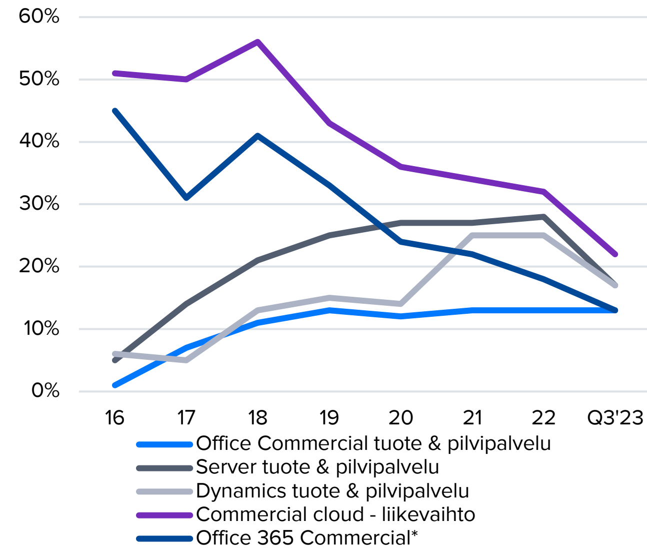
Magic Quadrant for Cloud ERP for Service-Centric Enterprises

Source: Gartner (July 2022)

Magic Quadrant for Cloud AI Developer Services

Source: Gartner (January 2022)

Development of key Microsoft product areas for Innofactor



Growth %	15	16	17	18	19	20	21	Q3'22
Office Commercial product & cloud service	-1%	1%	7%	11%	13%	12%	13%	12%
Server product & cloud service	9%	5%	14%	21%	25%	27%	27%	29%
Dynamics product & cloud service	12%	6%	5%	13%	15%	14%	25%	22%
Commercial cloud - net sales	106%	51%	50%	56%	43%	36%	34%	32%
Office 365 Commercial*	74%	45%	31%	41%	33%	24%	22%	17%

Source: Microsoft, *2015-2017 increase in user numbers, 2018-> net sales growth

Microsoft's competitive position 2/2

Gartner's Magic Quadrant for Business Intelligence Platforms

Source: Gartner (January 2023)

Gartner's Magic Quadrant for Cloud Infrastructure as a Service (IaaS)

Source: Gartner (June 2022)

Gartner's Magic Quadrant for the CRM Customer Engagement Center

Source: Gartner (May 2021)

Strategy 1/3

Nordic Microsoft expert

Innofactor has made a strategic choice to focus on technologies and solutions implemented on Microsoft's platforms or that utilize these platforms, where Microsoft's growth exceeds the average growth of the IT service and software market. A strong position in the Microsoft ecosystem makes Innofactor a desired partner for Microsoft which helps the company stay at the forefront of the development of Microsoft's solutions.

In terms of customer groups the company focuses on large and medium-sized Nordic companies and public administration organizations with high requirement levels for IT solutions. Now the company strives to increase the private sector's share, as the price point is better than in the public sector.

Strategy supports growth

Innofactor revised its strategy two years ago to support growth more strongly. In its strategy, the company has identified the business areas in which the company sees the strongest growth potential from the point of view of its business and Microsoft's solution offering. The company is divided into 6 business areas, while the previous structure included 3 areas. We believe, the best growth opportunities can be found in Business Solutions, driven by AI, in Data and Case Management driven by own products, and in Data and Analytics supported by AI. Cybersecurity is also a clear growth market, but the company is still seeking its own clear competitive advantage. Cloud Infrastructure and Digital Services are more stable areas in relative terms. The company still aims to recruit a significant number of new experts to the "new" business units.

With these measures, the company aims to achieve clearly stronger organic growth and efficiency. In the latest quarters, the company has been able to grow organically clearly better than in the past, driven by billable utilization. However, competition has shifted from talent to customers over the past year in the IT service sector. Thus, in the short term, the company must primarily succeed in sales , and not in recruitment, as in recent years. Strong inflation puts pressure on earnings levels, and thus efficiency gains have not yet been achieved, as inflation has not been transferred to customer prices in Innofactor or on the market on average.

Strengthening the Nordic base still in focus

The company's strategy continues to focus on harmonizing its operating model and offering at the Nordic level. The company's focus still lies on strengthening its international operation and building a Nordic organization while improving efficiency, which should support continued gradual improvement in profitability if successful. Success of the strategy is no longer strongly tied to finding good acquisition targets, but it depends more on the company's ability to create a uniform and efficient group from the international player it has built with acquisitions.

Harmonizing the offering can be achieved through organic growth and selected M&A transactions. We expect the wide Nordic offering will improve Innofactor's competitiveness in medium-sized and large companies with operations in several Nordic countries. At the same time, the company will be able to utilize cross selling between countries in products and expert areas more strongly. If successful, more extensive cross selling of products and expertise between countries could clearly improve Innofactor's organic growth and scalability. Cross-deliveries from Finland and Sweden to Norway and Denmark may have positive effects on the company's profitability, as it is able to utilize the relatively lower personnel costs in Finland and Sweden.

It has now taken more than 5 years to harmonize the whole and small progress has been made on the cost front, but evidence is still needed in terms of net sales. Finland has developed well, but over the years the company has been disappointed by the performance of countries outside Finland, especially Sweden. In Norway, the company has been successful in recent years. Thus utilization of the synergies between different operating countries is still in the initial stages. We also suspect there is still clear potential to be realized in internal efficiency especially through billable utilization outside Finland. In the short term, however, tight market conditions create headwinds for a stronger realization of the potential of a unified entity and offering.

Financial targets

In 2016, Innofactor published ambitious financial targets in connection with its strategy. The company targets around 20% growth and some 20% EBITDA in the long term by maintaining a positive cash flow and safeguarding financial solvency. The aim is to pay around one-half of the result as dividends considering the financial position, M&A transactions and development needs.

Strategy 2/3

Innofactor's annual growth target of some 20% that is to be achieved mainly organically is ambitious and requires success in both sales and recruitment and especially outside Finland. The company has stated that it is pursuing growth in all business areas, especially cloud solutions, data and analytics, and cybersecurity. At organizational level, organic growth has remained below sector growth in the previous 5 years, but in the past year it has been at sector level or even slightly above it. We do not expect Innofactor to continuously reach the targeted 20% growth for the entire group, but we believe that the company will be able to maintain growth above its historical figures once the demand in the IT service market improves again.

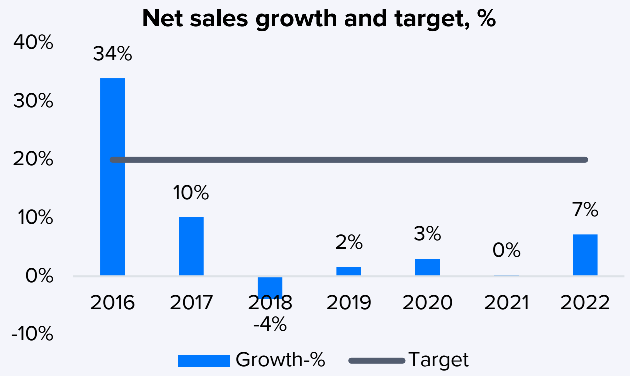
In our view, Innofactor reaching its profitability target requires the company to be highly successful in realizing the synergies between the countries, productization, own software products and sales. In Finland, we believe the company has already reached around 20% EBITDA from time to time, but the weak profitability of other countries depresses the overall picture. The average EBITDA margins of the industry are above 10% and for the best players nearly 20%. The aim is not unrealistic considering the occasional track record in Finland and the estimated profitability of the products but requires strong performance from the whole and especially other Nordic countries.

Competitive edge and scalability from own software and productization

Innofactor develops its own software products to support scalability and service sales. As a rule, the company does not develop software products for the global markets but locally to strengthen the offering to existing customers and markets where the company already has a strong presence.

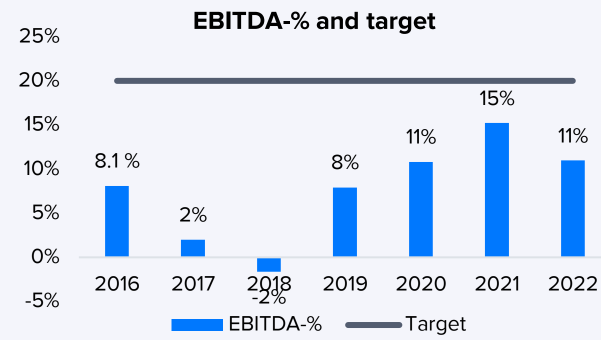
Means to achieve 20% growth target

- Focusing on industries and customer segments with the biggest growth potential and scalability
- The current organization structure and stronger focus on private sector customers support growth acceleration.
- Further increase efficiency in product and service sales. The company has managed to develop the order book strongly in Finland. There is still a lot of improvement potential in sales in other Nordic countries.
- Focusing on skills governance, recruitment, and resource optimization at a Nordic level. We believe there is still upside potential in billable utilization in the short term.



Means to achieve 20% EBITDA target

- Shift the offerings and focus of net sales more towards own products and services, which has already been happening for several years.
- Developing its own personnel so that customers are ready to pay a higher price, which we believe is difficult in the short term.
- Move to self-managing teams and reduce organizational levels. Innofactor moved towards a self-managing organization at the end of 2018. During 2020 the company's financial administration was centralized to Finland. HR and payroll have also been centralized and made more efficient.
- Improve billable utilization by minimizing unnecessary work or non-billable work. Here the company has progressed well in 2019-22 and we estimate is that in the short term the company still has clear potential especially in other Nordic countries.



Strategy 3/3

According to the company, Innofactor's own software components act as a key competitive advantage and an important factor in the customer's decision making in many project tenders. Especially when the customer organizations' activities are taken to the cloud it is critical for an IT supplier to own the tools and manage the processes to enable a smooth transition without use being disrupted. In this area, Innofactor has the expertise especially in the Azure environment, including its own Innofactor Virtual Data Center and Managed Azure services. There is great potential for growth in continuous services and the company in part has to succeed in this, as the cloud transition and implementations are slowly coming to an end. Own software also brings a considerable share of continuous maintenance income and license sales.

With own products built on Microsoft's technologies and platforms Innofactor builds continuity, competitive edge, and scalability for its business. The company's goal is to increase the share of the product business to 33% of net sales (now 28%). This is a key driver with which the company tries to improve its profitability towards the targeted 20% EBITDA level. Thus, the company can decrease the dependence of the business model on less scalable expert work, which would justify a higher valuation level for the share.

Microsoft expertise as a competitive advantage

Innofactor's key competitive advantage still comes in our understanding from focusing on and specializing in Microsoft solutions. On the other hand, the biggest weakness of the strategy focusing on Microsoft in our opinion is Innofactor's dependence on Microsoft's strategy being successful in the long term and the increasing popularity of open-source code software. Innofactor does not exclude the use of other technologies and Microsoft's strategy also changes constantly, e.g., as a result of the GitHub acquisition. The benefit of competitors that are not technology dependent like Innofactor is that they can select among several technologies to best respond to the customer's problem.

A history of strong inorganic growth

Innofactor has historically grown strongly driven by acquisitions. In practice, companies have been acquired with a structure where only a small amount of cash is paid for the target company and a more significant share with own shares. This has enabled rapid growth without Innofactor needing a strong balance sheet or large amounts of capital in advance. In addition, a large share of the deal price has typically focused on an earnout additional deal price.

The valuation levels of the deals have also without exception been lower than Innofactor's own valuation multiples on the stock exchange. These factors have lowered the risk of paying an excessive price.

However, the company has not been as successful in integrating the deals and realizing profitability synergies. The entrepreneurs of the acquired companies have mainly left Innofactor, integration has been challenging and the turnaround in members of the management group has probably slowed down operational development. Although the company has first-hand experience of the things key risks are related to and strives to minimize them, risks can never be fully managed.

Acquisitions outside Finland in future

Innofactor's strategic goal is to grow stronger outside Finland. We expect that in future the company primarily seeks acquisition targets abroad to strengthen these markets to reach similar economies of scale as in Finland and stronger synergies on a Nordic level. We also believe the business of the acquired company must be profitable and sustainable. In addition, the company has communicated its willingness to strengthen cloud expertise and cybersecurity.

When technology development, companies' strategies or focus change, businesses can also become non-strategic. Innofactor is not excluding business divestments either. In early 2021, the company sold the small non-strategic Prime business to unify its offering.

Good capital management

First and foremost, the company wants to ensure its dividend payment capability. On the other hand, the company also wants to grow inorganically, which the balance sheet enables (equity ratio of 47%, net debt/EBITDA 0.9x). The company's cash flow continuously strengthens the balance sheet and provides leeway for smaller acquisitions. We believe that as a rule the use of a small leverage in acquisitions is justified for service companies with a good cash flow profile. If no suitable acquisition targets are found, the company can return funds either through an extra dividend payment or share buybacks. We feel the company has been successful in capital management in recent years.

Summary of Innofactor's strategy

Strategic development projects

Best Nordic experts

Cloud solutions and digitalization offering

- The aim is especially to increase net sales
- Strengthening the organizational base especially in other Nordic countries
- Stronger level of productization
- AI solutions support growth and profitability

Strategic measures

- Stronger focus on solution areas that offer a large growth potential and scalability.
- Making sales of own products and services more efficient in the current clientele
- Increasing the weight of productized services
- Investing in operational efficiency
- Raising the level of expertise and thus higher pricing

- The strategy aims at a leading position in every Nordic country
- Focus of the business shifts heavily towards own products and services
- Honing Nordic activities into a uniform whole and making own processes more efficient
- Complementary acquisitions expected also in the future

Financial targets in the long term

- Around 20% annual growth with the aim to achieve most of it organically
- Around 20% EBITDA margin
- Pay around one-half of the result as dividends considering the company's financial position, possible M&A transactions, and other development needs

- Ambitious targets
- The company should continously reach >5% organic growth with the current portfolio
- Successful sales and growth in existing customers through cross selling
- Reaching the goals needs own solutions to break through strongly

Source: Inderes

Past development

Growth has been strong historically, partly at the expense of profitability

Innofactor's long-term net sales growth has been strong and driven by acquisitions. In the early 2010s, Innofactor's growth was strong (35% on average) organically and driven by acquisitions. In the second half of the 2010s, organic growth has again been weaker, and acquisitions have dominated growth.

Company growth has partly come at the expense of profitability, which has been below other companies in the sector. Before its listing, the company still reached EBITDA levels of over 20%. The company's EBITDA % adjusted for non-recurring items has been between 8% and 12% in 2011-2022, except in 2017-2018 (2% and -2%).

Last year's focus on sales generated growth

Innofactor's net sales increased by 7% to EUR 71 million in 2022. Organically, revenue grew by 4%. Innofactor invested in sales and organic growth accelerated to 13% in H2. In addition, growth in H2 was supported by the Invenco acquisition.

Geographically, Finland grew with the Invenco acquisition. According to our calculations, Norway grew strongly (~30%) and Denmark more moderately (<10%). Sweden's net sales continued to decline and the result was negative. We believe the clearly largest market Finland was still depressed by the organizational change and difficult customer contracts at the beginning of the year. The challenges in Sweden, Innofactor's second largest market, have continued for more than five years, reflecting the challenging nature of a turnaround.

The order backlog grew moderately by an average of 4% during the year and was EUR 76 million at the end of the year. We feel the bright spot in sales was the targeting of sales, which improved clearly as organic growth accelerated in H2. In the past, strong growth in the order book was not reflected as accelerated net sales growth, as orders targeted areas of already good demand.

Personnel increased by 62 to 562 during 2022. Growth was driven by the Invenco acquisition with some 50 people. Net sales per employee increased by 3%, indicating that billable utilization and/or average prices increased in 2022. We believe that there is still clear upside potential in billable utilization.

EBITDA was EUR 7.8 million or 11% of net sales (2021: adj. 7.5 MEUR or 11%). Depreciation decreased by EUR 0.5 million and financial expenses by EUR 0.2 million. Thus, adjusted EPS increased by 3 cents and amounted to EUR 0.10 in the whole year.

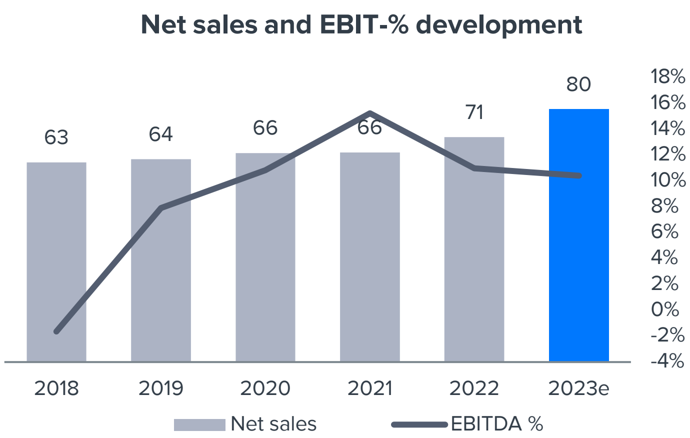
The company distribute a dividend of EUR 0.06 per share for 2022. In addition, the company launched a new share buyback program at the end of the year where a maximum of EUR 1 million will be used. The company later canceled more than 1 million shares in 2023. After that, in July 2023, the company launched a new share buyback program of up to 600,000 shares or EUR 1 million.

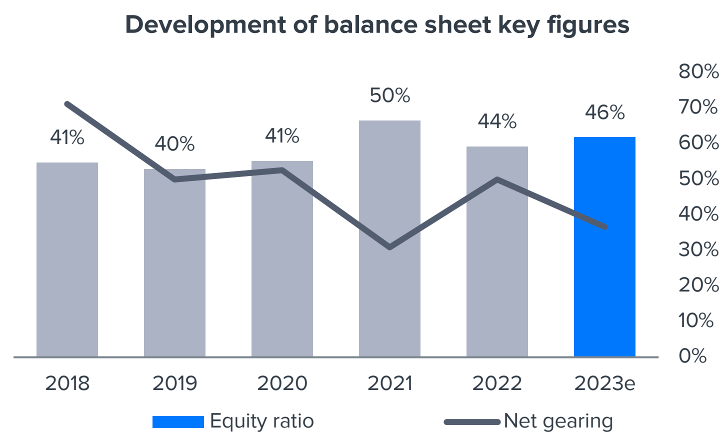
Balance sheet and financing

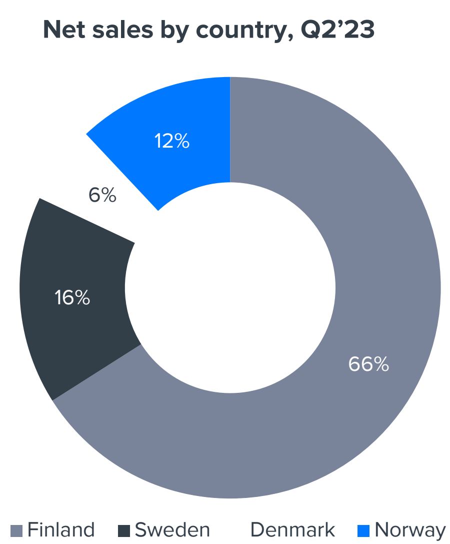
Innofactor's balance sheet weakened slightly in 2022 with the acquisition, but remained healthy at the end of Q2'23, with net debt/EBITDA of 0.9x, equity ratio of 47% and net gearing of 47% (1.3x, 52% and 27%). Strong cash flow also strengthens the balance sheet.

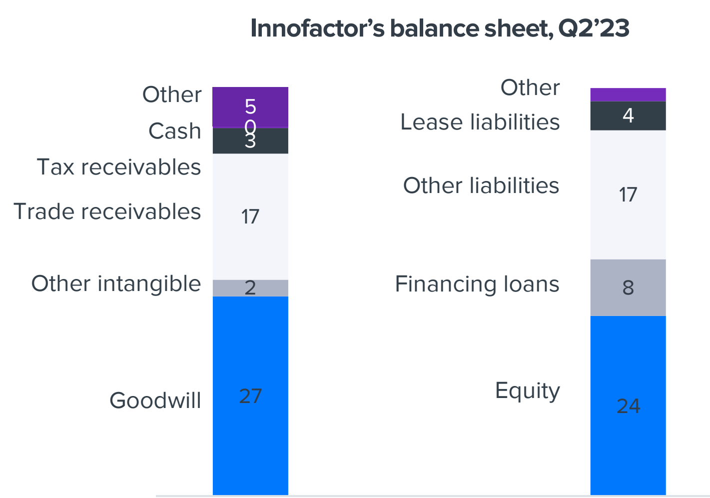
Structure wise the assets of the company's balance sheet are very typical for a service company. At the end of Q1, the company had EUR 27 million in goodwill in its balance sheet representing 49% of the balance sheet. Receivables were EUR 17 million or 31% of the balance sheet. The company also had EUR 3 million or 6% of the balance sheet in tax receivables at the end of Q2'23. Cash assets have decreased from last year, driven by the acquisition and share buybacks. In the past, the company has consolidated the market strongly using own shares and bank loans. Thus, we believe that the company can continue to grow inorganically.

Past development









Source: Inderes

Estimates 1/2

We expect earnings growth to continue

In 2023, Innofactor will continue to focus particularly on increasing net sales, with the continued aim of getting especially Sweden on a growth path. In terms of sales, focus will still be more on the private sector with better average prices. If the shift in focus towards the private sector works, it will support the net sales structure and thus also profitability. In this market situation, sales are clearly a more challenging equation, as more talent is available than in years. However, we believe the company can currently also grow through better billable utilization. By area of expertise, the company sees good growth opportunities in business-critical solutions, data and case management solutions and data & analytics. Cybersecurity is still an interesting area, but the company is seeking its own sharper competitive advantage in this area. In addition, growth and especially earnings are driven by growth in own product business.

Innofactor's guidance for 2023 is that net sales and EBITDA will increase from 2022, when net sales were EUR 71.1 million and EBITDA was EUR 7.8 million. We expect Innofactor's net sales to grow by 12% to EUR 80 million in 2023 supported by the Invenco acquisition. Organically, we expect net sales to grow by 9%, which would be a clearly better performance than the sector this year. Growth is supported by a good EUR 77 million order backlog at the end of Q2'23. The timing of a good order backlog realizing as sales and assessment of the profitability structure of the order backlog is still difficult, although the structure seems to be clearly better than in the past quarters. This view is based on the fact that organic growth (12%) has been clearly better than the development of the order book (5%) over the past year. In the short term, however, uncertainty about net sales development is elevated due to weak customer demand. In Q2, uncertainty materialized in several sectors, even relatively abruptly and clearly (more about this in the market section on page 20). However, Innofactor is supported by a good order backlog, a high share of the public sector and continuous services.

We expect the company's EBITDA to reach EUR 8.3 million (10.4% of net sales, 2022: 7.8 MEUR). Thanks to Innofactor's improved internal efficiency and own product sales, the company can continue growing faster than the number of personnel in the short term, which supports profitability. We believe, Innofactor still has a lot to improve especially outside Finland, in billing utilization and dependency ratios (productive person per administration).

The profitability improvement is slowed down by the estimated pressure in customer prices, while we expect wage inflation to ease in the short term. As regards the damages related to the additional purchase price of the Lumagate acquisition, we do not expect a solution this year. We estimate that EPS has increased by one cent to EUR 0.10. We expect the company to distribute a dividend of EUR 0.07 per share for 2023.

Innofactor's growth drivers

- Improving efficiency through billable utilization and/or process efficiency
- Own product solutions
- Recruitment – employee image, low turnover and new cities
- Increasing customer prices driven by the private sector. More downward pressure in the short term.
- Acquisitions
- Growth by area of expertise is driven by business-critical solutions, data and case management and data & analytics
- Geographically, growth would be valuable especially outside Finland

Innofactor's profitability drivers

- Billable utilization
- Improving efficiency through processes and resource allocation, already partially successful
- Own scalable product solutions
- Increasing customer prices, especially through the private sector
- Cross-delivery between countries (from Finland and Sweden to Norway and Denmark), but this is still in the initial stages
- Curbing wage inflation, has worked well by recruiting younger talent
- Attrition management
- Recruitment in lower paid areas outside the greater Helsinki region

Estimates 2/2

Medium- and long-term estimates

We expect Innofactor to reach 3-4% annual organic growth with the current structure and an EBITDA margin of some 12% in 2024-2026. Our estimates are moderate given the strong growth of the past year and the company's order backlog, but the tight market situation and the weaker historical level justify caution. In addition, the long-standing challenges in Sweden also speak for caution. Growth is below overall market growth. The company has potential to grow faster than the market but this requires a consistent positive development at the Nordic level, which still requires further evidence from the company. In addition, in the medium term, the development will be supported more strongly by the utilization of AI.

Our operational growth estimate practically assumes the level of service companies. The company should have the preconditions to reach better profitability levels than the sector thanks to own products and growth in recurring business but we keep our estimates conservative for the time being due to weaker development in Sweden.

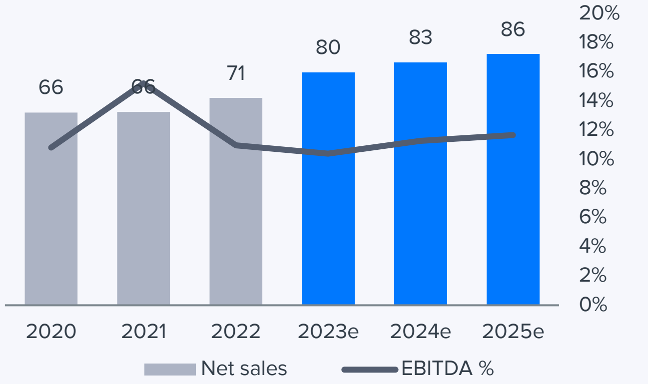
We estimate that the company's EPS will be EUR 0.13 in 2024 and rise to EUR 0.15 in 2025. We expect the company's dividend payment to grow by one cent annually in the next few years and to be EUR 0.10 in 2026. Dividend estimates correspond to a payout ratio of approximately 60%, which is in line with the company's dividend policy that aims to pay about half of the profit as dividends. This is based on the challenges of recent years to find a suitable acquisition target partly due to the market.

Innofactor still has good EUR 3 million tax receivable in its balance sheet, so the company's tax expenses do not have cash flow effect in the next few years. This will support the company's cash flow in coming years. Thus the cash flow per share will still be higher than the earnings per share in the next few years if no significant changes take place in working capital and investments.

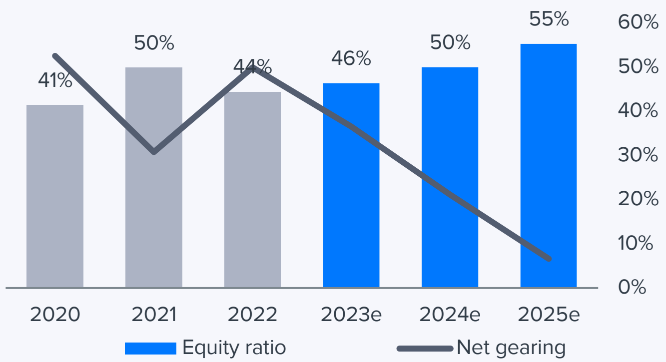
After 2026, we estimate that Innofactor's net sales will continue growing by 2.5 % until the terminal assumption. At the same time we expect profitability to gradually drop towards 10% EBITDA level in the terminal assumption. Thus, our estimates put the company clearly below its own targets.

In general, the IT service sector and Innofactor have strong cash flow and continuously strengthens the balance sheet. In our estimates, the company's balance sheet strengthens clearly in the next few years and will provide considerable leeway for acquisitions or stronger dividend distribution.

Net sales and EBITDA-% development



Development of balance sheet key figures



Quarterly estimates

Income statement	2020	2021	Q1'22	Q2'22	Q3'22	Q4'22	2022	Q1'23	Q2'23	Q3'23e	Q4'23e	2023e	2024e	2025e
Revenue	**66.2**	**66.4**	**17.0**	**16.9**	**16.7**	**20.5**	**71.1**	**20.2**	**20.1**	**17.5**	**22.2**	**80.0**	**83.4**	**86.2**
EBITDA	**7.2**	**10.1**	**2.0**	**1.4**	**1.9**	**2.5**	**7.8**	**2.5**	**1.8**	**1.4**	**2.6**	**8.3**	**9.4**	**10.1**
Depreciation	-4.7	-3.6	-0.7	-0.7	-1.0	-0.6	-3.1	-0.8	-0.8	-0.8	-0.8	-3.1	-3.0	-3.0
EBIT (excl. NRI)	**4.5**	**4.4**	**1.4**	**0.7**	**1.0**	**1.9**	**5.0**	**1.8**	**1.0**	**0.7**	**1.9**	**5.5**	**6.6**	**7.3**
EBIT	**2.5**	**6.5**	**1.3**	**0.7**	**1.0**	**1.8**	**4.8**	**1.7**	**1.0**	**0.7**	**1.9**	**5.3**	**6.4**	**7.1**
Net financial items	-0.5	-0.8	-0.2	0.0	-0.2	-0.1	-0.6	-0.4	-0.2	0.1	-0.2	-0.6	-0.5	-0.3
PTP	**2.1**	**5.7**	**1.1**	**0.6**	**0.8**	**1.7**	**4.2**	**1.3**	**0.8**	**0.8**	**1.7**	**4.6**	**5.9**	**6.8**
Taxes	-0.3	-1.2	-0.3	-0.1	-0.2	-0.4	-0.9	-0.3	-0.4	-0.2	-0.3	-1.1	-1.2	-1.4
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	0.0	0.0
Net earnings	**1.8**	**4.5**	**0.8**	**0.5**	**0.6**	**1.3**	**3.3**	**1.0**	**0.5**	**0.6**	**1.4**	**3.5**	**4.7**	**5.4**
EPS (adj.)	**0.10**	**0.07**	**0.03**	**0.02**	**0.02**	**0.04**	**0.10**	**0.03**	**0.01**	**0.02**	**0.04**	**0.10**	**0.13**	**0.15**
EPS (rep.)	**0.05**	**0.12**	**0.02**	**0.02**	**0.02**	**0.04**	**0.09**	**0.03**	**0.01**	**0.02**	**0.04**	**0.10**	**0.13**	**0.15**

Key figures	2020	2021	Q1'22	Q2'22	Q3'22	Q4'22	2022	Q1'23	Q2'23	Q3'23e	Q4'23e	2023e	2024e	2025e
Revenue growth-%	3.1 %	0.3 %	-4.7 %	-2.0 %	21.8 %	16.9 %	7.2 %	19.2 %	18.6 %	5.0 %	7.9 %	12.4 %	4.3 %	3.3 %
Adjusted EBIT growth-%		-2%	4%	-47%	-3%	214%	14%	27%	39%	-28%	5%	9%	20%	10%
EBITDA-%	10.8 %	15.2 %	12.0 %	8.1 %	11.6 %	11.9 %	11.0 %	12.3 %	8.8 %	8.2 %	11.9 %	10.4 %	11.3 %	11.7 %
Adjusted EBIT-%	6.8 %	6.6 %	8.2 %	4.4 %	6.1 %	9.1 %	7.1 %	8.8 %	5.2 %	4.2 %	8.8 %	6.9 %	7.9 %	8.4 %
Net earnings-%	2.7 %	6.8 %	5.0 %	3.2 %	3.6 %	6.5 %	4.7 %	5.1 %	2.3 %	3.5 %	6.2 %	4.4 %	5.7 %	6.2 %

Source: Inderes

Watch our video interview with the company's CEO about the Q2’23 result (subtitled in English):

Watch our video interview with the company's CEO about the Q1’23 result (subtitled in English):

Investment profile

Value creation from organic growth and own products

For investors Innofactor has historically in the early 2010s been profiled as a quickly growing IT company that acts as the consolidator of its own segment in the Nordic countries. With the Lumagate acquisition, the company moved in 2017 to a stage where after strong acquisition-driven growth the focus has shifted to building a uniform Innofactor. This change proved harder than expected and created a dip in the growth strategy. The foundation has been built in recent years and it is largely in place (structure, order backlog and profitability) in Finland. However, over the past five years, organic growth has been challenging, except for the latest quarters. Thus, the company still has something to prove in terms of sustainably better organic growth.

The new strategy focuses strongly on growth and better efficiency and, reflecting this, value creation is expected to be based more on organic growth in service sales and growth in scalable own products. We believe the company will also continue slight inorganic growth, but in the future, the key drivers will be organic growth and improving profitability.

Positioning established to profit generator category

In our view, the positioning of Innofactor's valuation is more firmly in the profit generator category. However, the investor should consider market uncertainty, which in the short term elevates the risk level. In addition, numerous historical challenges still rattle around in the back of the mind.

The company has continued a relatively good performance for four years, driven by the Finnish business. The company still aims to strengthen growth outside Finland, which should be reflected through billable utilization as a lever in profitability and scaling of own products. In the short term, there is clear uncertainty in the market, which has materialized in the sector in Q2. However, Innofactor's good order book, the high share of the public sector and continuing operations, provides support amidst the uncertainty. In the mid- and long-term, we estimate that Innofactor's markets will again perform well and grow. In addition, with AI solutions, Microsoft seems to be an even better choice of principal.

In recent years, Innofactor has unified its Nordic organization, as well as the offering and processes between the countries. Thus, the company has completed the base and achieved some internal efficiency. In our view, however, the company still has a lot of potential to utilize in the Nordic businesses through growth, at least on paper. However, this has proven a challenge for years and we are, therefore, cautious about this in our forecasts. Organic growth outside Finland is key to making the most of country-specific efficiency gains.

Ambitious long-term objectives

In our view, Innofactor's value creation in the long term will still consist of the company's ability to build a uniform Nordic player out of the acquisitions carried out in different countries. Service productization and the role of own products are also important in reaching the company's profitability target, These should be visible as stronger organic growth and better profitability. However, we do not expect the company to meet its own ambitious targets (20% growth mainly organically, 20% EBITDA margin). We do not find the expectations unrealistic either as for Finnish operations organic growth has from time to time been an estimated 15% and profitability close to the targeted 20% level.

The main macro-level risk is the weak development of the general economic situation. Key sector-specific risks are related to customer prices in the short term and to the availability of talent, wage inflation and attrition in the medium term. The main risks within the company are related to the implementation of the growth strategy, especially the turnaround in Sweden, and the construction of a unified Nordic organization becoming prolonged. The long-term risk is the company's dependence on Microsoft's success. The risks are evened out by the product business, the current stronger order book, increasing share of continuous services, and the continued development of Microsoft's product on the IT market.

Entrepreneur-driven growth company

Innofactor is strongly personified in the biggest owner, the company's founder, and CEO Sami Ensio, who owns some 22% of Innofactor. We feel the company as an investment object next to growth-seeking also reflects strong entrepreneurship and personified ownership. The entrepreneur-drive is visible in how despite several challenges the company has been developed in a disciplined manner and unyieldingly.

Investment profile

1. **Template of a Nordic player built through acquisitions**

2. **Foundation for long-term growth in place, but proof still required**

3. **Uncertainty on the market but growth fundamentals are still strong in the longer term**

4. **Own products provide continuity and scalability**

5. **Entrepreneur-driven profit generator**

Potential

- Organic and inorganic growth
- Still potential for profitability improvement
- Growth, continuity and scalability of own products
- Clear upside in acceptable valuation level
- IT service markets in general and Microsoft solutions performing strongly
- Strong and growing continuous business and own products

Risks

- Prolonged or further deterioration of economic uncertainty
- Further delay in building a Nordic organization
- Internationalization and acquisitions raise the risk level
- Weakening of Microsoft's market position
- Development of customer prices, availability of experts, attrition, and wage inflation

Source: Inderes

Valuation 1/2

Value drivers and risks of the share

Innofactor's turnaround has progressed relatively well for over 4 years. The company has shown good organic growth figures in recent quarters but more evidence is needed of continuity. The profitability potential has also proven higher than our previous estimates, and the 20% EBITDA target is now actually realistic.

We have divided the value drivers of the share into short (1-3) and long term (4-6). The key value drivers are:

1) The ability to get all countries to a continued organic growth rate of at least the level of the IT service market of 3-5%.
2) Success in strengthening the post-acquisition organization to raise the efficiency of all countries to a good level.
3) The company's ability to continue to raise profitability to a better level, closer to the long-term goal driven by own product businesses and recurring net sales.
4) Strengthening investors' confidence as the turnaround continues.
5) The ability to tie the group together with a unified offering, which would help realize the synergies between the countries.
6) Increasing acceptable valuation level especially as the focus of the business shifts to product business in line with strategic objectives.

Innofactor has clearly more continuity and scalability in its business than many peer companies involved in project business. Continuity is increasingly valued in the current market situation, where companies compete for customers and not talent for the first time in a long time.

The turn has progressed, but slower than expected in the past couple of years. Thus, work must continue to unify the organization and improve efficiency. The company's many difficulties in history are mainly due to its international operations.

We believe the key risks are:

- Declining customer demand and price pressure
- Success, especially in Sweden, where challenges have been ongoing for years Continued growth in Norway and stronger development in Denmark In addition, the good performance of the important Finnish market being interrupted
- Failure in project management
- Failure on the talent market, rising wage inflation and high expert attrition
- The failure of integrating new acquisitions (like Invenco). The company has faced challenges in several integrations
- Microsoft's market position weakening in the IT market in corporate solutions Microsoft's market position has strengthened further in recent years, but the IT market develops and changes quickly

Peer group

We can find a Nordic and Finnish peer group for Innofactor to which the valuation can be compared and supported on. Our peer group consists of Nordic IT service companies of which some also have their own software business. We have added more Nordic peers to the comparison, which improves comparability and is relevant because the company has operations in all countries. When examining the business structure next to project work Innofactor also has own scalable software business. The company should not, however, be equated with pure software companies.

In the peer group, we have used Inderes' estimates for the companies we cover, which takes into account goodwill amortization and improves comparability between Finnish IT service companies.

In general, we consider IT service companies to be a very attractive sector, due to the strong long-term demand fundamentals, capital-light business and low valuation levels. In our view, short-term uncertainty is already clearly reflected in prices and, despite "lower-than-normal" estimates, valuation levels are historically low. The valuation differences between companies have narrowed in recent years, reflecting the unification of strategy phases and/or performance outlook. Now Witted and Digital Workforce have also slowed down their growth ambitions and put more emphasis on profitability than before.

The undervaluation of Innofactor compared to the sector has increased over the last year. The company is now priced on average 30% below the 2023-2024 EV/EBIT and P/E ratios of Finnish IT service peers (good 10% one year ago). The share's valuation is almost 40% below the entire peer group. In addition, tax receivables increase the attractiveness of the valuation.

Valuation 2/2

In relative terms, the valuation is very attractive. However, short-term uncertainty of the market keeps us somewhat cautious. In our view, a small undervaluation is justified, as the company's earnings growth outlook is on par with the sector or slightly below it.

Valuation multiples

The primary valuation multiples we use for Innofactor are adjusted P/E and EV/EBIT ratios. The figures are adjusted for IFRS3 book depreciations from acquisitions(~ 0.2 MEUR p.a.). With our estimates, Innofactor's adjusted P/E ratios for 2023 and 2024 are 11x and 9x. The corresponding EV/EBIT ratios are 9x and 7x. This is an attractive level in absolute terms, given the increased confidence in earnings growth although there currently is uncertainty in the market.

In our view a slightly higher than "normal" P/E level can be accepted for the share due to the company's high tax receivables and the fact that tax expenses do not have a cash flow effect for the company. The book value of the tax receivable is currently EUR 3.4 million, which corresponds to a value of around EUR 0.09 per share. If the current value of this tax receivable would be priced conservatively, e.g., as half of the book value some 5% higher valuation multiples could be accepted for the share.

In our view, a gradually higher valuation can be accepted for the share as the turnaround continues, growth strengthens and is geographically broader and steadier. In addition, with growth and scalability of own products, a higher valuation can be accepted for the share.

Components of the expected return for the share

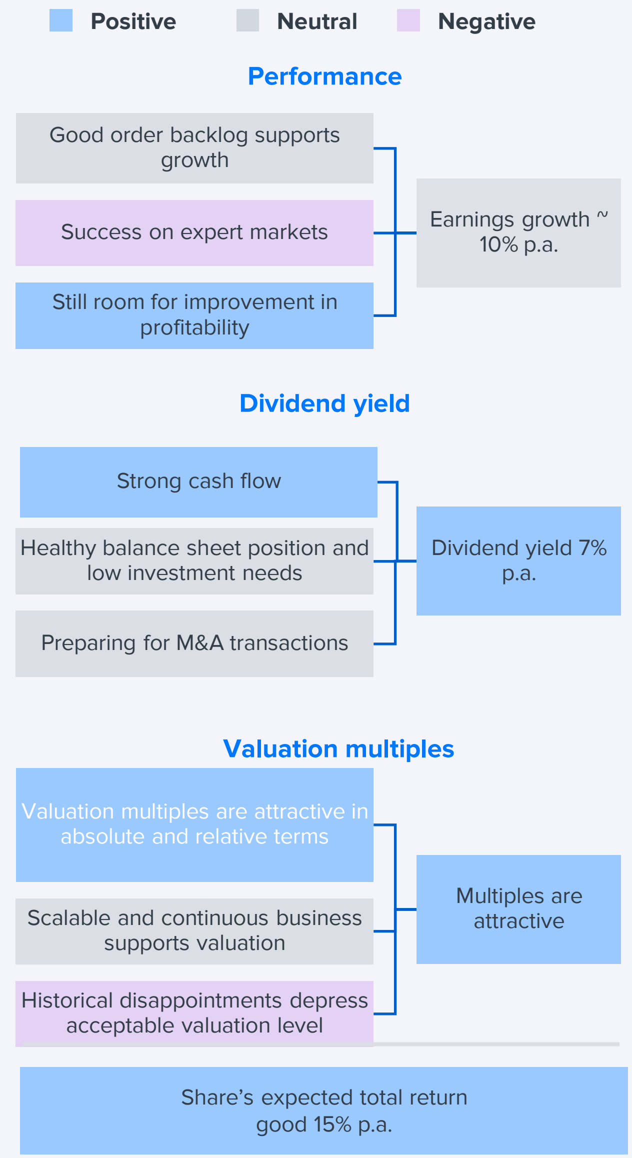
We also examine Innofactor's share from the viewpoint of earnings growth, dividend yield and accepted valuation multiples We estimate that the company has preconditions to reach annual earnings growth of ~10% in coming years driven by net sales and increased profitability. Dividend also now provides support for the valuation and with our slightly higher dividend estimates (good 60% of profit) than the dividend policy (about 50% of profit) the dividend yield is ~7% (2021-22 65% of profit). Strong cash flow provides good preconditions for relatively high profit distribution, but we believe the company will continue to also strive for inorganic growth in line with its strategy.

The share is attractively priced with 2023 multiples, considering the increased earnings growth outlook although there is uncertainty in the market. Thus the share's expected return consisting of dividend yield, earnings growth and the upside in multiples is >15% and the risk/return ratio is attractive. The key risks in the share relate to market demand and price pressure, emergence of the company's project or country challenges and acquisitions.

DCF

Our DCF model indicates a value of EUR 1.6 per share for Innofactor. In the long term (after 2026), we estimate that growth will remain at 2.5% (1.5% in terminal) and EBITDA % will stabilize at 10% level. In the model, the taxes in the income statement do not have a cash flow effect in Finland because the company can utilize profits against the tax receivables in the balance sheet. In the model, the weight of the terminal assumption is 42%, which is low and improves reliability. In the cash flow model, the average cost of capital (WACC) used is 9.4% and the cost of capital is 9.9%. Thus, considering the DCF model based on rather conservative estimates, share pricing also seems moderate at the moment.

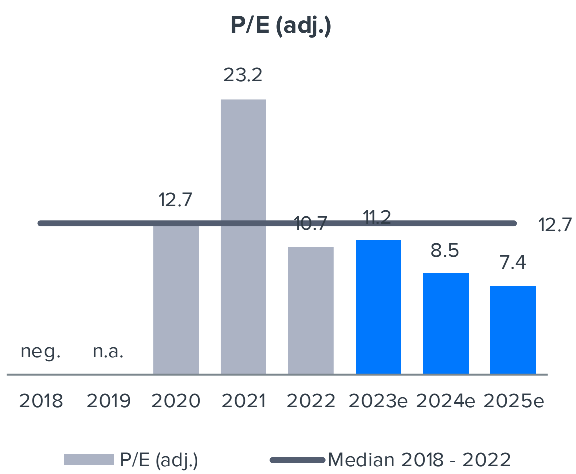
TSR drivers 2023-2025

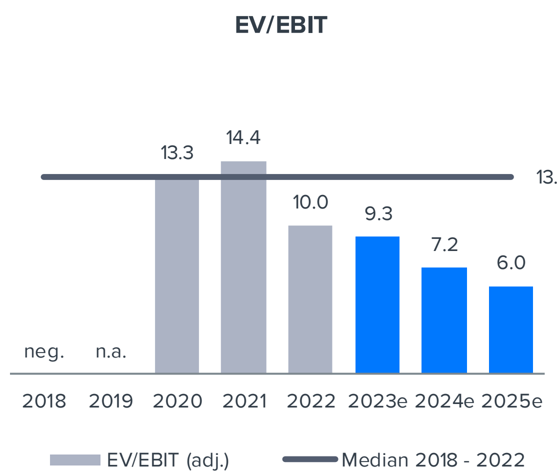


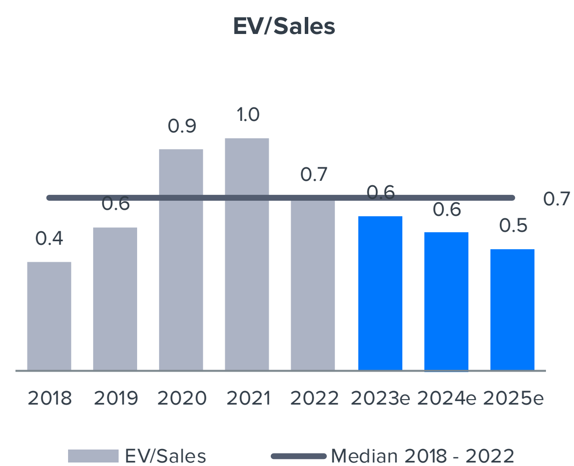
Valuation table

Valuation	2018	2019	2020	2021	2022	2023e	2024e	2025e	2026e
Share price	0.36	0.72	1.28	1.52	1.05	**1.14**	**1.14**	**1.14**	**1.14**
Number of shares, millions	36.2	36.8	37.4	36.6	36.2	**36.3**	**36.3**	**36.3**	**36.3**
Market cap	13	27	48	55	38	**41**	**41**	**41**	**41**
EV	28	38	60	63	50	**51**	**47**	**43**	**39**
P/E (adj.)	neg.	n.a.	12.7	23.2	10.7	**11.2**	**8.5**	**7.4**	**6.8**
P/E	neg.	63.3	27.1	12.3	11.5	**11.8**	**8.7**	**7.7**	**7.0**
P/B	0.6	1.2	2.0	2.2	1.5	**1.6**	**1.5**	**1.3**	**1.2**
P/S	0.2	0.4	0.7	0.8	0.5	**0.5**	**0.5**	**0.5**	**0.5**
EV/Sales	0.4	0.6	0.9	1.0	0.7	**0.6**	**0.6**	**0.5**	**0.4**
EV/EBITDA	neg.	7.4	8.4	6.3	6.5	**6.1**	**5.0**	**4.3**	**3.7**
EV/EBIT (adj.)	neg.	n.a.	13.3	14.4	10.0	**9.3**	**7.2**	**6.0**	**5.1**
Payout ratio (%)	0.0 %	0.0 %	84.9 %	65.1 %	65.4 %	**72.9 %**	**61.6 %**	**60.7 %**	**61.7 %**
Dividend yield-%	0.0 %	0.0 %	3.1 %	5.3 %	5.7 %	**6.2 %**	**7.0 %**	**7.9 %**	**8.8 %**

Source: Inderes







Peer group valuation

Company	Market cap MEUR	EV MEUR	EV/EBIT		EV/EBITDA		EV/S		P/E		Dividend yield-%	
			2023e	2024e	2023e	2024e	2023e	2024e	2023e	2024e	2023e	2024e
Digia*	151	165	9.5	8.1	7.6	6.6	0.9	0.8	11.7	10.2	3.4	3.5
Digital Workforce*	48	32	59.8	14.4	58.1	13.1	1.2	1.1	78.3	25.2		
Gofore*	322	297	11.0	8.8	10.1	8.1	1.5	1.3	14.9	13.0	2.4	2.8
Loihde*	71	53	35.9	11.9	6.7	4.4	0.4	0.4	73.9	19.1	2.4	2.6
Netum Group*	42	50	15.2	11.7	13.4	10.5	1.3	1.1	15.2	12.5	3.7	4.0
Siili Solutions*	89	81	9.4	7.0	6.6	5.3	0.6	0.6	16.6	11.2	2.7	3.4
Solteq*	20	43		17.7	4.4	4.2	0.7	0.7		45.7		3.0
Tietoevry*	2683	3311	8.8	8.0	7.6	6.9	1.2	1.1	9.7	9.0	6.6	6.8
Vincit*	58	49	11.8	7.6	10.4	7.1	0.5	0.5	19.3	11.8	4.8	5.7
Witted Megacorp*	42	35	369.8	13.8	237.5	13.1	0.5	0.5	386.6	19.7		
Addnode	807	846	25.1	18.2	13.5	11.1	1.4	1.2	36.7	25.0	1.1	1.6
Avensia AB	25	27		13.4	39.8	9.7	0.8	0.7		15.7	1.9	3.8
Bouvet	515	541	14.4	13.2	12.0	11.3	1.8	1.7	17.9	16.5	4.9	5.3
Columbus	107	133										
CombinedX	46	45	6.6	6.3	4.7	4.6	0.7	0.7	9.1	8.6		
Exsitec	159	168	20.0	15.5	13.7	11.3	2.7	2.4	27.2	20.0	3.1	2.9
Knowit	304	392	15.2	11.6	7.1	6.2	0.7	0.6	17.1	12.4	4.4	5.0
Netcompany Group	1778	2085	20.6	16.7	15.1	13.3	2.5	2.3	24.1	19.4		
NNIT	282	296	367.5	9.2	6.6	5.8	0.7	0.7	21.1	11.1	0.0	4.9
Webstep	61	77	10.6	9.2	8.5	7.5	0.9	0.8	11.4	9.7	9.1	10.3
Innofactor (Inderes)	**41**	**51**	**9.3**	**7.2**	**6.1**	**5.0**	**0.6**	**0.6**	**11.2**	**8.5**	**6.2**	**7.0**
Median Nordic companies			**15.2**	**11.7**	**10.1**	**7.5**	**0.9**	**0.8**	**17.9**	**13.0**	**3.3**	**3.8**
Diff-% to median			*-39%*	*-39%*	*-40%*	*-33%*	*-26%*	*-28%*	*-37%*	*-35%*	*90%*	*87%*
Media Finnish companies			***11.8***	***10.2***	***8.9***	***7.0***	***0.8***	***0.8***	***16.6***	***12.8***	***3.4***	***3.5***
Diff-% to median			*-22%*	*-30%*	*-31%*	*-28%*	*-21%*	*-24%*	*-33%*	*-34%*	*84%*	*104%*

Source: Refinitiv / *Inderes' adjusted estimate. NB! Market cap used by Inderes does not consider own shares held by the company.

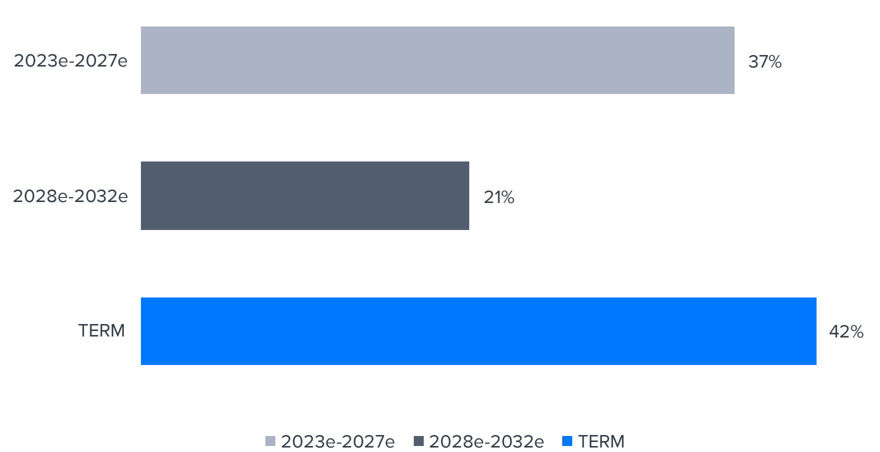
DCF calculation

DCF model	2022	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e	2031e	2032e	TERM
Revenue growth-%	7.2 %	12.4 %	4.3 %	3.3 %	3.4 %	2.5 %	2.5 %	2.5 %	2.5 %	2.5 %	1.5 %	1.5 %
EBIT-%	6.7 %	6.6 %	7.7 %	8.2 %	8.4 %	8.0 %	7.8 %	7.5 %	7.0 %	7.0 %	7.0 %	7.0 %
EBIT (operating profit)	**4.8**	**5.3**	**6.4**	**7.1**	**7.5**	**7.3**	**7.3**	**7.2**	**6.9**	**7.1**	**7.2**	
+ Depreciation	3.1	3.1	3.0	3.0	3.1	3.1	3.1	3.2	3.1	3.2	3.2	
- Paid taxes	0.2	0.0	0.0	0.0	0.0	-1.5	-1.5	-1.5	-1.4	-1.5	-1.5	
- Tax, financial expenses	-0.1	-0.2	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
+ Tax, financial income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
- Change in working capital	-0.7	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Operating cash flow	**7.3**	**8.3**	**9.3**	**10.0**	**10.6**	**8.9**	**8.9**	**8.9**	**8.6**	**8.8**	**8.9**	
+ Change in other long-term liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
- Gross CAPEX	-7.4	-2.8	-2.9	-2.9	-3.0	-3.0	-3.1	-3.2	-3.2	-3.2	-3.5	
Free operating cash flow	**-0.2**	**5.5**	**6.5**	**7.1**	**7.6**	**5.9**	**5.8**	**5.8**	**5.4**	**5.6**	**5.4**	
+/- Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
FCFF	-0.2	5.5	6.5	7.1	7.6	5.9	5.8	5.8	5.4	5.6	5.4	69.5
Discounted FCFF		**5.3**	**5.8**	**5.8**	**5.7**	**4.0**	**3.6**	**3.3**	**2.8**	**2.6**	**2.3**	**30.2**
Sum of FCFF present value		71.5	66.1	60.4	54.6	48.9	44.9	41.3	38.0	35.2	32.5	30.2
Enterprise value DCF		**71.5**										
- Interest bearing debt		-14.4										
+ Cash and cash equivalents		2.0										
-Minorities		0.0										
-Dividend/capital return		-2.2										
Equity value DCF		**56.9**										
Equity value DCF per share		**1.57**										

WACC	
Tax-% (WACC)	20.0 %
Target debt ratio (D/(D+E)	10.0 %
Cost of debt	6.0 %
Equity Beta	1.55
Market risk premium	4.75%
Liquidity premium	0.00%
Risk free interest rate	2.5 %
Cost of equity	**9.9 %**
Weighted average cost of capital (WACC)	**9.4 %**

Source: Inderes

Cash flow distribution



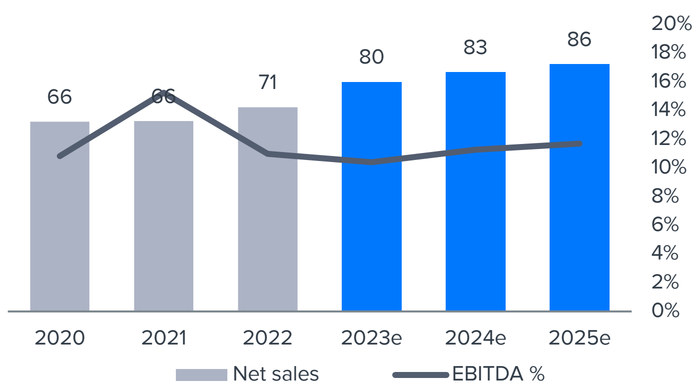
Income statement

Income statement	2020	Q1'21	Q2'21	Q3'21	Q4'21	H1'21	H2'21	2021	Q1'22	Q2'22	Q3'22	Q4'22	2022	Q1'23	Q2'23	Q3'23e	Q4'23e	2023e	2024e	2025e
Revenue	**66.2**	**17.8**	**17.3**	**13.7**	**17.6**	**35.1**	**31.3**	**66.4**	**17.0**	**16.9**	**16.7**	**20.5**	**71.1**	**20.2**	**20.1**	**17.5**	**22.2**	**80.0**	**83.4**	**86.2**
EBITDA	**7.2**	**4.7**	**2.1**	**1.7**	**1.7**	**6.8**	**3.4**	**10.1**	**2.0**	**1.4**	**1.9**	**2.5**	**7.8**	**2.5**	**1.8**	**1.4**	**2.6**	**8.3**	**9.4**	**10.1**
Depreciation	-4.7	-0.8	-0.8	-0.8	-1.1	-1.7	-1.9	-3.6	-0.7	-0.7	-1.0	-0.6	-3.1	-0.8	-0.8	-0.8	-0.8	-3.1	-3.0	-3.0
EBIT (excl. NRI)	**4.5**	**1.3**	**1.4**	**1.1**	**0.6**	**2.8**	**1.6**	**4.4**	**1.4**	**0.7**	**1.0**	**1.9**	**5.0**	**1.8**	**1.0**	**0.7**	**1.9**	**5.5**	**6.6**	**7.3**
EBIT	**2.5**	**3.8**	**1.3**	**0.9**	**0.5**	**5.1**	**1.4**	**6.5**	**1.3**	**0.7**	**1.0**	**1.8**	**4.8**	**1.7**	**1.0**	**0.7**	**1.9**	**5.3**	**6.4**	**7.1**
Net financial items	-0.5	-0.5	0.0	-0.2	-0.2	-0.4	-0.4	-0.8	-0.2	0.0	-0.2	-0.1	-0.6	-0.4	-0.2	0.1	-0.2	-0.6	-0.5	-0.3
PTP	**2.1**	**3.4**	**1.3**	**0.8**	**0.3**	**4.6**	**1.1**	**5.7**	**1.1**	**0.6**	**0.8**	**1.7**	**4.2**	**1.3**	**0.8**	**0.8**	**1.7**	**4.6**	**5.9**	**6.8**
Taxes	-0.3	-0.7	-0.3	-0.2	0.0	-1.0	-0.2	-1.2	-0.3	-0.1	-0.2	-0.4	-0.9	-0.3	-0.4	-0.2	-0.3	-1.1	-1.2	-1.4
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	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net earnings	**1.8**	**2.6**	**1.0**	**0.6**	**0.3**	**3.6**	**0.9**	**4.5**	**0.8**	**0.5**	**0.6**	**1.3**	**3.3**	**1.0**	**0.5**	**0.6**	**1.4**	**3.5**	**4.7**	**5.4**
EPS (adj.)	**0.10**	**0.00**	**0.03**	**0.02**	**0.01**	**0.04**	**0.03**	**0.07**	**0.03**	**0.02**	**0.02**	**0.04**	**0.10**	**0.03**	**0.01**	**0.02**	**0.04**	**0.10**	**0.13**	**0.15**
EPS (rep.)	**0.05**	**0.07**	**0.03**	**0.02**	**0.01**	**0.10**	**0.02**	**0.12**	**0.02**	**0.02**	**0.02**	**0.04**	**0.09**	**0.03**	**0.01**	**0.02**	**0.04**	**0.10**	**0.13**	**0.15**

Key figures	2020	Q1'21	Q2'21	Q3'21	Q4'21	H1'21	H2'21	2021	Q1'22	Q2'22	Q3'22	Q4'22	2022	Q1'23	Q2'23	Q3'23e	Q4'23e	2023e	2024e	2025e
Revenue growth-%	3.1 %	3.8 %	3.2 %	-2.2 %	-3.8 %	3.5 %	-3.1 %	0.3 %	-4.7 %	-2.0 %	21.8 %	16.9 %	7.2 %	19.2 %	18.6 %	5.0 %	7.9 %	12.4 %	4.3 %	3.3 %
Adjusted EBIT growth-%		2.5 %	5.9 %	20.9 %	-39.4 %	4.2 %	-11.0 %	-2%	4%	-47%	-3%	214%	14%	27%	39%	-28%	5%	9%	20%	10%
EBITDA-%	10.8 %	26.2 %	12.1 %	12.4 %	9.4 %	19.2 %	10.7 %	15.2 %	12.0 %	8.1 %	11.6 %	11.9 %	11.0 %	12.3 %	8.8 %	8.2 %	11.9 %	10.4 %	11.3 %	11.7 %
Adjusted EBIT-%	6.8 %	7.6 %	8.2 %	7.7 %	3.4 %	7.9 %	5.3 %	6.6 %	8.2 %	4.4 %	6.1 %	9.1 %	7.1 %	8.8 %	5.2 %	4.2 %	8.8 %	6.9 %	7.9 %	8.4 %
Net earnings-%	2.7 %	14.8 %	5.7 %	4.3 %	1.7 %	10.3 %	2.8 %	6.8 %	5.0 %	3.2 %	3.6 %	6.5 %	4.7 %	5.1 %	2.3 %	3.5 %	6.2 %	4.4 %	5.7 %	6.2 %

Source: Inderes

Net sales and EBITDA-% development



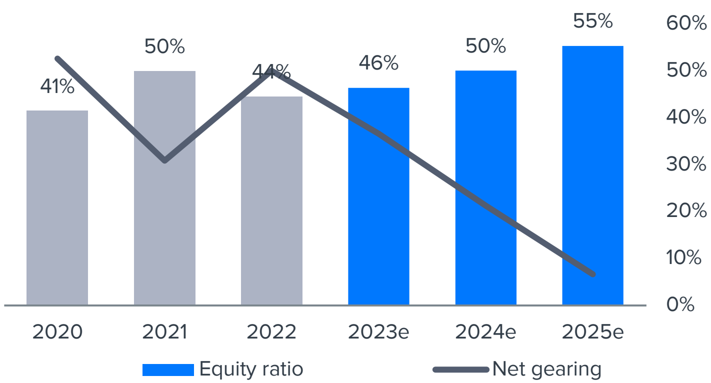
Balance sheet

Assets	2021	2022	2023e	2024e	2025e
Non-current assets	**35.7**	**39.3**	**37.9**	**36.6**	**35.1**
Goodwill	26.4	26.8	26.8	26.8	26.8
Intangible assets	0.6	2.4	2.2	2.0	1.8
Tangible assets	3.7	5.9	5.9	5.9	6.0
Associated companies	0.0	0.0	0.0	0.0	0.0
Other investments	0.0	0.0	0.0	0.0	0.0
Other non-current assets	0.1	0.1	0.1	0.1	0.1
Deferred tax assets	4.8	4.1	3.0	1.7	0.4
Current assets	**15.4**	**16.5**	**18.4**	**20.0**	**20.6**
Inventories	0.0	0.0	0.0	0.0	0.0
Other current assets	0.0	0.0	0.0	0.0	0.0
Receivables	13.4	14.5	16.8	17.5	18.1
Cash and equivalents	2.0	2.0	1.6	2.5	2.5
Balance sheet total	**51.1**	**55.8**	**56.3**	**56.6**	**55.6**

Source: Inderes

Liabilities & equity	2021	2022	2023e	2024e	2025e
Equity	**25.5**	**24.8**	**26.1**	**28.3**	**30.8**
Share capital	2.1	2.1	2.1	2.1	2.1
Retained earnings	3.1	5.3	6.6	8.8	11.3
Hybrid bonds	0.0	0.0	0.0	0.0	0.0
Revaluation reserve	0.1	0.1	0.1	0.1	0.1
Other equity	20.2	17.2	17.2	17.2	17.2
Minorities	0.0	0.0	0.0	0.0	0.0
Non-current liabilities	**7.8**	**9.2**	**10.4**	**7.9**	**4.9**
Deferred tax liabilities	1.5	1.9	1.9	1.9	1.9
Provisions	0.0	0.0	0.0	0.0	0.0
Long term debt	6.3	7.3	8.6	6.0	3.0
Convertibles	0.0	0.0	0.0	0.0	0.0
Other long term liabilities	0.0	0.0	0.0	0.0	0.0
Current liabilities	**17.8**	**21.8**	**19.8**	**20.4**	**20.0**
Short term debt	3.5	7.0	2.6	2.5	1.5
Payables	14.3	14.8	17.2	17.9	18.5
Other current liabilities	0.0	0.0	0.0	0.0	0.0
Balance sheet total	**51.1**	**55.8**	**56.3**	**56.6**	**55.6**

Development of balance sheet key figures



Summary

Income statement	2020	2021	2022	2023e	2024e
Revenue	66.2	66.4	71.1	**80.0**	**83.4**
EBITDA	7.2	10.1	7.8	**8.3**	**9.4**
EBIT	2.5	6.5	4.8	**5.3**	**6.4**
PTP	2.1	5.7	4.2	**4.6**	**5.9**
Net Income	1.8	4.5	3.3	**3.5**	**4.7**
Extraordinary items	-2.0	2.1	-0.3	**-0.2**	**-0.2**

Per share data	2020	2021	2022	2023e	2024e
EPS (reported)	0.05	0.12	0.09	**0.10**	**0.13**
EPS (adj.)	0.10	0.07	0.10	**0.10**	**0.13**
OCF / share	0.13	0.24	0.20	**0.23**	**0.26**
FCF / share	-0.01	0.21	0.00	**0.15**	**0.18**
Book value / share	0.63	0.70	0.68	**0.72**	**0.78**
Dividend / share	0.04	0.08	0.06	**0.07**	**0.08**

Balance sheet	2020	2021	2022	2023e	2024e
Balance sheet total	56.6	51.1	55.8	**56.3**	**56.6**
Equity capital	23.4	25.5	24.8	**26.1**	**28.3**
Goodwill	26.5	26.4	26.8	**26.8**	**26.8**
Net debt	12.3	7.9	12.4	**9.6**	**6.0**

Growth and profitability	2020	2021	2022	2023e	2024e
Revenue growth-%	3%	0%	7%	**12%**	**4%**
EBITDA growth-%	n.a.	n.a.	-23%	**7%**	**13%**
EBIT (adj.) growth-%	n.a.	n.a.	14%	**9%**	**20%**
EPS (adj.) growth-%	n.a.	n.a.	50%	**3%**	**33%**
EBITDA-%	10.8 %	15.2 %	11.0 %	**10.4 %**	**11.3 %**
EBIT (adj.)-%	6.8 %	6.6 %	7.1 %	**6.9 %**	**7.9 %**
EBIT-%	3.8 %	9.8 %	6.7 %	**6.6 %**	**7.7 %**
ROE-%	7.7 %	18.4 %	13.2 %	**13.7 %**	**17.4 %**
ROI-%	6.9 %	17.7 %	12.8 %	**13.8 %**	**17.4 %**
Equity ratio	41.4 %	49.9 %	44.4 %	**46.4 %**	**50.0 %**
Gearing	52.6 %	30.8 %	50.0 %	**36.6 %**	**21.2 %**

Cash flow	2020	2021	2022	2023e	2024e
EBITDA	7.2	10.1	7.8	**8.3**	**9.4**
Change in working capital	-2.0	-1.1	-0.7	**0.1**	**0.0**
Operating cash flow	5.0	8.9	7.3	**8.3**	**9.3**
CAPEX	-2.2	-1.3	-7.4	**-2.8**	**-2.9**
Free cash flow	-0.5	7.6	-0.2	**5.5**	**6.5**

Valuation multiples	2020	2021	2022	2023e	2024e
EV/S	0.9	1.0	0.7	**0.6**	**0.6**
EV/EBITDA (adj.)	8.4	6.3	6.5	**6.1**	**5.0**
EV/EBIT (adj.)	13.3	14.4	10.0	**9.3**	**7.2**
P/E (adj.)	12.7	23.2	10.7	**11.2**	**8.5**
P/B	2.0	2.2	1.5	**1.6**	**1.5**
Dividend-%	3.1 %	5.3 %	5.7 %	**6.2 %**	**7.0 %**

Source: Inderes

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Accumulate The 12-month risk-adjusted expected shareholder return of the share is attractive

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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Recommendation history (>12 mo)

Date	Recommendation	Target	Share price
10/31/2018	Reduce	0.52 €	0.50 €
1/28/2019	Reduce	0.35 €	0.40 €
3/6/2019	Reduce	0.45 €	0.47 €
5/15/2019	Reduce	0.58 €	0.60 €
6/5/2019	Sell	0.68 €	0.71 €
7/24/2019	Reduce	0.68 €	0.63 €
10/30/2019	Reduce	0.80 €	0.75 €
2/26/2020	Reduce	0.90 €	0.78 €
4/1/2020	Accumulate	0.68 €	0.66 €
5/5/2020	Accumulate	0.90 €	0.84 €
6/23/2020	Accumulate	0.95 €	0.90 €
6/24/2020	Reduce	1.30 €	1.19 €
10/28/2020	Accumulate	1.40 €	1.28 €
2/19/2021	Accumulate	1.80 €	1.43 €
4/28/2021	Accumulate	2.00 €	1.97 €
6/10/2021	Accumulate	2.00 €	1.72 €
7/23/2021	Buy	2.00 €	1.86 €
10/27/2021	Reduce	1.80 €	1.59 €
2/18/2022	Accumulate	1.50 €	1.33 €
4/27/2022	Accumulate	1.45 €	1.24 €
6/28/2022	Accumulate	1.35 €	1.17 €
7/22/2022	Reduce	1.00 €	1.02 €
10/25/2022	Reduce	1.00 €	1.00 €
2/10/2023	Accumulate	1.35 €	1.20 €
4/26/2023	Accumulate	1.45 €	1.29 €
7/20/2023	Accumulate	1.35 €	1.11 €
9/11/2023	Accumulate	1.35 €	1.14 €

Inderes connects investors and listed companies. We help over 400 listed companies to better serve their investors. Our community is home to over 70 000 active investors.

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Mikael Rautanen
2014, 2016, 2017, 2019

Sauli Vilén
2012, 2016, 2018, 2019, 2020

Antti Viljakainen
2014, 2015, 2016, 2018, 2019, 2020

Olli Koponen
2020

Joni Grönqvist
2019, 2020

Erkki Vesola
2018, 2020

Petri Gostowski
2020

Atte Riikola
2020

Research belongs
to everyone.