I-Tech

Sweden | Biotech | MCAP SEK 892.5mn

19 May 2021

Buy

Target price:	107.8
Current price:	75.0
Upside	**43.7%**

I-Tech – What else?

I-Tech is a biotech company operating in the marine paint industry. The Company sells a unique, patented substance called Selektope® that drastically reduces fuel consumption for ships by reducing marine growth on the hull. Through close customer relations and a first-mover advantage in a market with high barriers to entry, a sales CAGR of 52.5% between the years 2020A-2023E is estimated. A target multiple of EV/S 7.0x for 2023E, supported by a DCF-model, justifies a target price of SEK 107.8 and a potential upside of 43.7%.

Key takeaways

- **First-mover advantage in a market with high barriers of entry:** I-Tech has a first-mover advantage in a market with high barriers of entry. The market is characterized by regulations creating long processes to test paint components. Furthermore, an EU BPR (Biocidal Products Regulation) approval is required. Selektope® is one of only two non-metal substances with an EU BPR approval to this date but is the only one used for commercial ships.
- **Strict emission targets in the marine industry benefit I-Tech:** Regulatory requirements from authorities are expected to be a driving force for the market in the coming years. In 2020, the IMO (International Maritime Organization) introduced global requirements to lower the sulfur emissions in the shipping industry and by 2050, the industry must have halved their emissions. This implies increased fuel costs as higher quality fuel is required, and stronger incentives to choose an effective antifouling agent as marine growth of only 10.0% on the hull can increase the fuel consumption by up to 36.0% to maintain the same speed.
- **The largest paint manufactures choose Selektope®:** I-Tech sells Selektope® to Chugoku Marine Paints (CMP), Jotun and Hempel. These three customers account for 60.0% of the market for marine paint producers within antifouling. One additional customer is expected to be announced during this year, which in combination with increasing volumes from existing customers is estimated to contribute to a sales CAGR of 52.5% 2020A-2023E. Moreover, the Company collaborates with all eight potential customers on the market, which entails testing Selektope® with the intention of generating finished products. Between 2024E-2029E it is estimated that Selektope® will be sold to six customers in total, resulting in a sales CAGR of 15.8% in that period.
- **The scalable business enables margin expansion:** I-Tech's business is highly scalable which creates an opportunity for margin expansion as sales volume increases. The majority of the workforce is already in place and the Company will not need to hire more personnel to reach the estimated revenue growth. This is estimated to lead to OPEX growing with a CAGR of 9.0% 2020A-2023E, compared to the estimated sales CAGR of 52.5%, contributing to a rapidly increased EBIT-margin, from negative in 2020A to 32.4% in 2023E.

Analysts

Oscar Petersson	Equity Analyst
Joen Sundmark	Equity Analyst

Market Data

Exchange	First North Stockholm
MCAP (SEKmn)	892.5
EV (SEKmn)	865.1

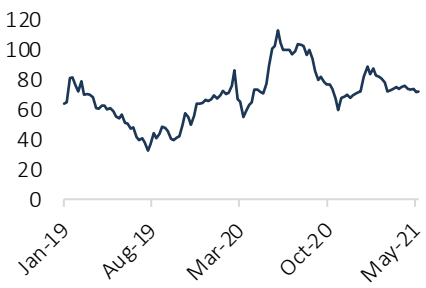
Financial Forecast	20A	21E	22E
Revenue (SEKmn)	52.8	70.9	116.9
Rev. growth y/y	16.0%	34.0%	65.0%
Gross Margin	48.0%	48.0%	53.0%
EBITDA Margin	6.8%	11.6%	27.9%
EBIT Margin	Neg.	Neg.	20.3%
Profit Margin	Neg.	Neg.	15.8%
EPS	Neg.	Neg.	1.5

Metrics & Drivers	20A	21E	22E
EV/Sales	16.4x	12.2x	7.4x
EV/EBIT	Neg.	Neg.	36.3x
P/S	16.9x	12.4x	7.5x
P/E	Neg.	Neg.	49.9x

Major Shareholders

Pomona-gruppen	11.4%
Handelsbanken Fonder	8.0%
Total Institutional	37.7%
Total Insider	15.2%
Total	52.9%

Price Development, SEK



Investment thesis

A market with high entry barriers that I-Tech so far has managed well

I-Tech started to develop Selektope® in 2000. Over 20 years later the product is still considered unique within its segment, giving the Company a first–mover advantage. Increasingly stricter content requirements and regulations for antifouling paints used by commercial ships creates a solid barrier to enter the market. To ensure that the marine paint components do not harm the environment, extensive research about the environmental effects is required. A market approval for a new biocidal active substance to be used in water means a substantial cost and it takes approximately ten years to reach the market. I-Tech experimented with the substance for 9 years before conducting the first test of Selektope® on larger vessels in 2009, and the first commercial order came from CMP in 2014. The product needs to be approved by authorities, paint manufacturers, and shipowners to enter the market. Therefore, Selektope® is currently one of merely two non-metal biocides that have received regulatory approval on all markets. The other approved substance requires 50 times more volume than Selektope® and is not in the market for commercial ships. This gives a strong threshold against other substances and an advantage for I-Tech that already has experience within the market.

Close customer relationships creates brand recognition

The Company has so far managed to acquire four customers, (where three of them have been named) and launched 14 products with three of the biggest actors on the market. This validates that Selektope® is a strong brand and holds a trustworthy product. The demonstrated positive effect strengthens incentives for more paint manufacturers to start using the product. All this gives Selektope® a clear competitive advantage and consolidates the position in the global market. I-Tech's largest customer Chukogu Marine Paints has started to brand their products including Selektope® with "Powered by Selektope®", giving I-Tech brand recognition which will be an important factor to further strengthen their position on the market.

Strong environmental and cost-efficient incentives

Shipping accounts for almost 3.0% of the world's total carbon dioxide emissions and the proportion increases every year. According to The European Environment Agency, global emissions from shipping can account for as much as 17.0% of the global emissions by the year 2050. Increased fuel consumption and emissions are a global problem within the shipping industry and in January 2020, the IMO introduced global requirements in to lower the sulfur emissions in the shipping industry. This implies increased fuel costs for the shipowners as a result of a larger proportion of finer, low-sulfur fuel. The International Bunker Industry Association estimates that this could mean a rise in annual fuel costs of USD 24.0bn from 2020 and forward[1]. The higher cost of fuel creates a higher demand for optimal hull performance to achieve cost-efficient transport. This means stronger incentives to choose an antifouling product containing Selektope®. Copper is currently the most commonly used antifouling ingredient; however, according to the Washington Department of Ecology, copper is poisonous to fish and aquatic life. Therefore, the use of copper-based coatings for recreational boats has recently been banned in the ports of San Diego and Washington. Selektope® can be used both by itself and in combination with copper and still offer properties reducing growth. It is also becoming increasingly common for ships with too much marine growth to be refused to enter new ports as foreign marine growth can damage the marine life at the new location.

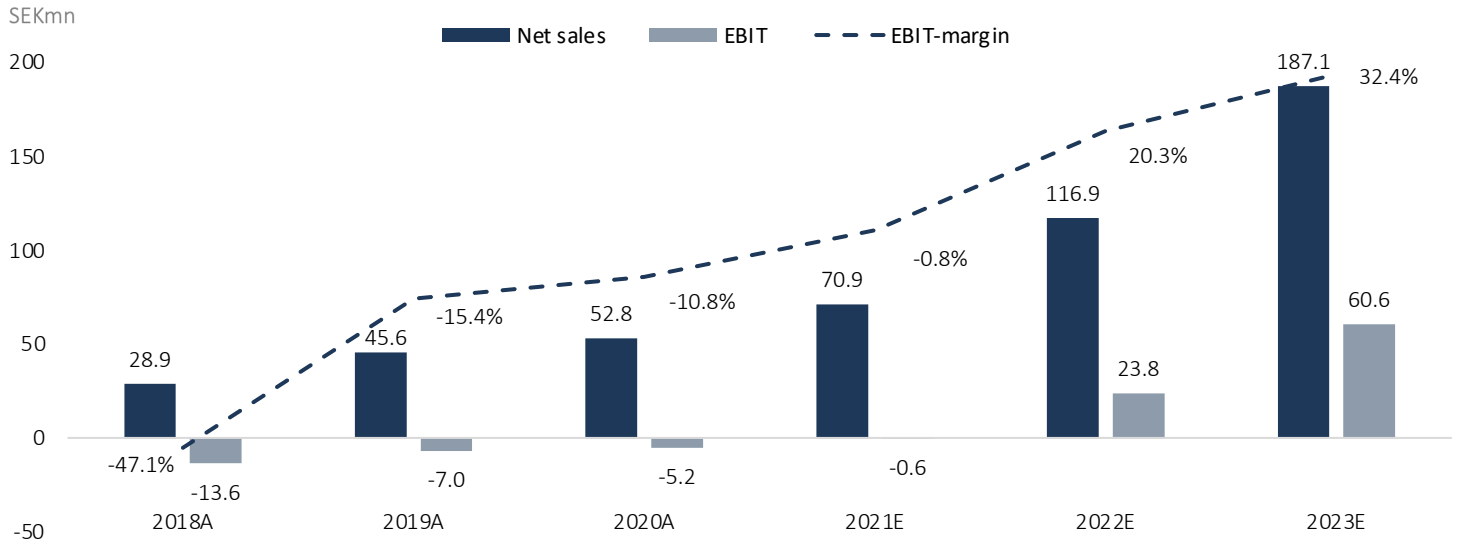
1. https://ibia.net/2017/03/29/how-much-will-2020-cost/
2. https://apps.ecology.wa.gov/publications/documents/1804003.pdf

Investment thesis

Fast-growing with rising margins while being well-capitalized

I-Tech is estimated to grow with a CAGR of 52.5% in 2020A-2023E while increasing EBIT-margins. The production of Selektope® can scale up sixfold without significantly higher costs. Additionally, OPEX is estimated to not grow much in the coming years as most of the workforce already is in place. One more employee is estimated to be hired until 2023E. Furthermore, the Company also has bypassed the largest barriers in terms of R&D and regulatory affairs. An EBIT-margin of 32.4% is therefore estimated for 2023E, increasing further to 45.1% in 2029E. The Company is also well-capitalized with SEK 40.0 million in cash which enables further expansion.

Strong net sales growth combined with an improved EBIT-margin to 2023E.



Source: I-Tech and Analyst Estimates

Additional actors and high dependency of a narrow customer base concludes risks for I-Tech

Selektope® is currently one of only two non-metal-based biocides that have received regulatory approval in the EU and certain other regions in the world. Despite that, there is still a risk that additional competing biocides receive regulatory approvals resulting in increased market competition. However, the high barriers of entry reduce the risk of this from happening within the next few years. Furthermore, the Company is currently selling Selektope® to four customers, indicating a high dependency on a narrow customer base. If the current agreements would change meaning less favorable terms for I-Tech, it is likely to negatively affect revenue and profit margins. Through continuous discussions and collaboration with paint manufacturers and shipowners, they are constantly mitigating this risk. In addition, the test process is long which would create high switching costs for customers if they decide to switch to another solution. The fact that the shipping industry is a conservative market also increases the risk. This can mean that I-Tech grows slower than we estimate as marine paint manufacturers still are heavily dependent on copper-based solutions.

Overview of the Company

Many years of research has resulted in a unique, sustainable antifouling product

I-Tech has its background from research on marine growth that started as early as 1990 at the University of Gothenburg. As a result, I-Tech was founded in 2000 and received its first patent for Selektope® the same year. 15 years later, they received their first order from CMP. I-Tech manufactures a substance that is mixed with paint. The paint will then protect the ship's hull from marine growth, which is a major problem for ships today. A ship's hull that is only covered with 10.0% marine growth requires an increased fuel consumption of 36.0%.

Selektope® is an antifouling ingredient that is organic and metal-free

The substance is primarily used in coatings for large commercial ships. It is an organic metal-free substance. Compared to copper oxide where 500-700 grams per liter of paint is required to reach comparable efficiency, Selektope® requires merely 2 grams per liter, which also makes the manufacturing process simpler. I-Tech's direct customers are paint manufacturers that blend Selektope® in their paintings. Through close collaboration with the paint manufacturers, I-Tech and the customers develop effective products containing Selektope®. The paint manufacturers then sell the products to ship owners and boat manufacturers. The product's powerful and repellent effect on marine growth keeps the ship's hull clean, which reduces friction against the water and reduces fuel consumption. The product has been approved as environmentally acceptable by the EU.

Copper is the most commonly used method today

Most of the present marine paints are based on a slow release of toxins. This technique is in most cases preventing biofouling from attaching to the hull, but the negative aspect is the substantial amount of toxin the ships release. The impact of normal paint containing toxins can have a detrimental effect on marine wildlife. The negative environmental consequences have contributed to a progressive increase of organotin compounds being banned. Selektope® is a unique product based on the application of advanced biotechnology in marine color systems. The technology's distinctive ability to operate with high efficiency even at very low concentrations provides the opportunity to reduce biocide leakage by more than 90.0%. Selektope®'s impact on the paint is non-existent in addition to the positive effects that are created. The product is together with seven other substances approved according to the comprehensive EU biocides legislation, EU-BPR, but is only one of two metal-free substances. Since Selektope® can be used both by itself and in combination with copper the reduced biocide leakage means huge environmental advantage. Copper is today the most widely used method.

How Selektope® is different

Instead of using toxic substances, Selektope® is based on a molecular structure that includes so-called phenyl and imidazole groups. When a barnacle caterpillar comes in contact with Selektope®, the caterpillar becomes hyperactive and performs about 100 bone kicks per minute. The effect is reversible, and the caterpillar quickly returns to its normal state. By this, the caterpillar simply cannot attach to a surface painted with Selektope®, while the caterpillar is not exposed to any damage. Eliminating the harmful effects other antifouling ingredients may have.

Overview of the market

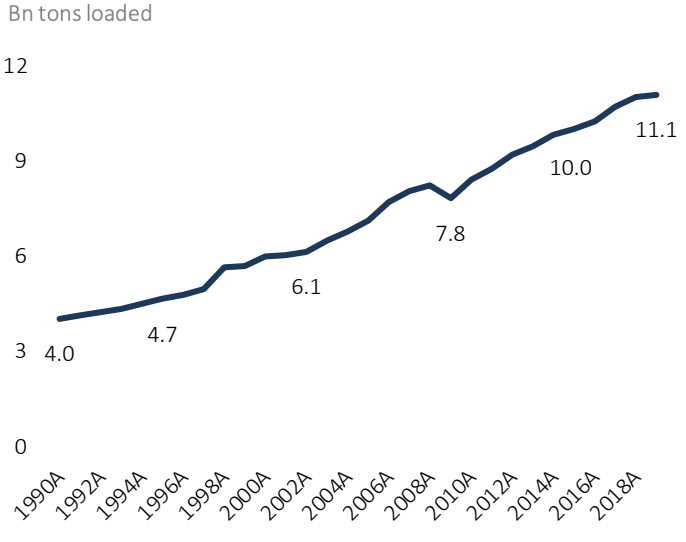
A USD 500.0mn market that I-Tech is ready to penetrate

The market for antifouling and Selektope® is currently valued at USD 500.0mn, and revenue in the global antifouling industry reaches USD 3.0 billion on an annual basis. Around 70.0% of the marine paint is consumed by large industrial- and cruise ships. There are 100 000 IMO-registered vessels and according to the Company, all are potential end-customers for I-Tech. The transport volume of seaborne trade has almost doubled since the year 2000 and is expected to continue to grow. With the right antifouling paint, carbon dioxide emissions could be reduced by 100.0 million tons each year and the total savings potential could amount to USD 20.0 billion annually. The market is usually relatively insensitive to cyclical fluctuations as the ships must be docked every 3-5 years.

Market segments

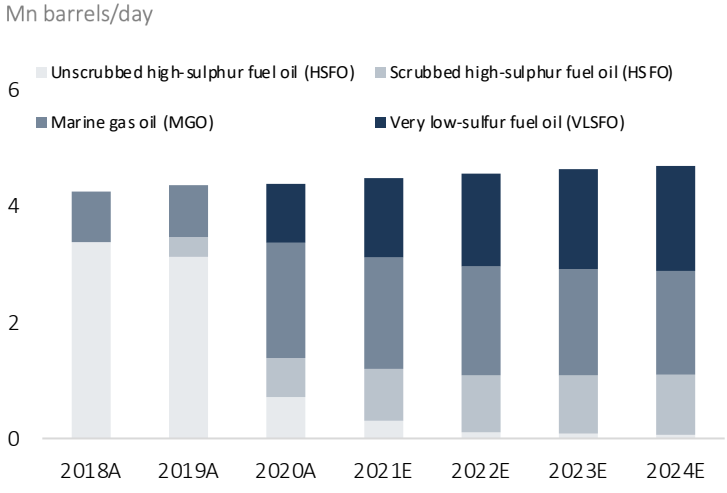
Today I-Tech is primarily active in the market for shipping, but in the future, expansion into new markets is possible, such as the market for leisure boats, fish farms, and offshore. Selektope® is already included in one of CMPs and the Greek-based paint maker Vemars products specially developed for the leisure boat market. The Company has also signed a long-term collaboration agreement with Pettit Marine Paint, one of the largest companies in the US pleasure craft antifouling market. The vast majority of antifouling paints are used by the global commercial merchant fleet, which also uses most of the 350 million tonnes of bunker oil consumed annually by the shipping industry. I-Tech estimates that the market for antifouling products will increase as shipping companies want to reduce their fuel consumption and airborne emissions, such as sulfur oxides. The environmental incentives like the new global sulfur emission regulations from IMO are also increasing the demand for other fuels implying higher costs for shipowners. More attention is successively drawn towards the negative aspects of the metal's use in boat paints harming the environment. In the US, Washington has decided to ban the use of copper-based paint for recreational boats by 2021 due to toxic impacts on aquatic life. California's department of pesticide regulation has recently also established a maximum leach rate for copper-based antifouling products.

Transport volume of seaborne trade from 1990 to 2019.



Source: Statista

Global marine bunkers product demand in 2018 with a forecast for 2019 to 2024, by fuel type.



Source: Statista

Financial forecast breakdown

Sales expected to increase from SEK 52.8mn in 2020A to SEK 187.1mn in 2023E

It is estimated that existing customers will order significant volumes of around 7.5 tons of Selektope® in 2023E. I-Tech is currently holding agreements with a strong majority of the leading companies within the antifouling paint industry, such as Hempel AS, Chugoku Marine Paints, and Jotun. This is expected to increase awareness of the product's exceptional functionality and result in an increased customer demand. The forecasted sales imply rising volumes from existing customers and entry of a new customer during 2021E. The fourth unannounced customer has contributed to about 10.0% of sales in 2019A and continued to show great interest in Selektope® by ordering significant volumes in 2020A. With a CAGR of 52.5% 2020A-2023E, I-Tech is expected to reach a market share of 4.3% (the total market for antifouling and Selektope®) on a market worth USD 500.0 million. I-Tech has consistently increased its market share since 2017A by increasing the number of products containing Selektope® from five in 2017A to 11 at the end of 2020A. For the estimated years, I-Tech is expected to continue the product integration as more ship-owners realize the multiple benefits of using environmentally friendly and cost-saving antifouling paint. Selektope® is currently integrated into 14 products, which is estimated to increase to 29 products by 2023E.

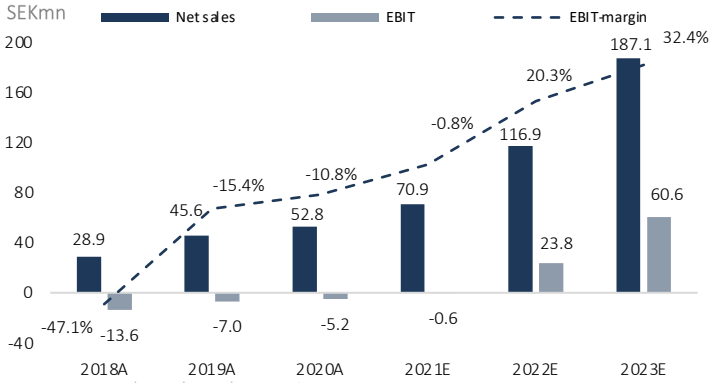
Efficiency in production is estimated to lead to a gross margin of 52.8% in 2023E

By outsourcing the production to India, I-Tech can scale up production sixfold without increasing costs significantly. Due to higher production volumes meaning reduced production costs per unit, the gross margin is expected to increase slightly in coming years. I-Tech has successfully increased the gross margin from 30.0% in 2016A to 47.7% in 2020A and it is estimated that the gross margin will reach 52.8% in 2023E.

OPEX growing slower than sales implies scalability and an EBIT-margin of 32.4% in 2023E

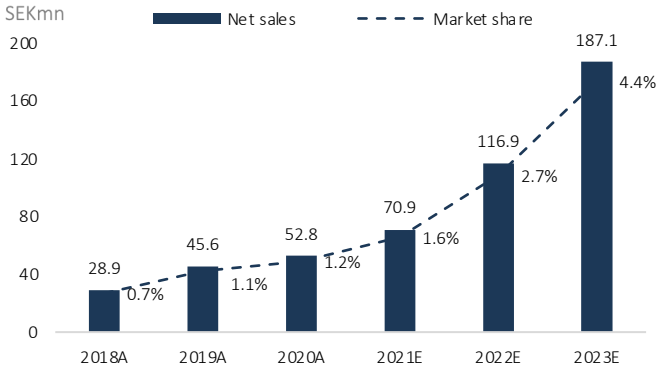
Due to the scalable business model, the workforce will not increase significantly as the company grows. I-Tech has at the beginning of 2021A expired the team with two employees and is expected to add one more employee until 2023E, which will lead to personnel costs of SEK 15.7 million in 2023E compared to 10.4 million in 2020A. The Company has in previous years shown an increased revenue per employee from 1.0 million SEK in 2015A to 5.9 million in 2020A, implying a CAGR of 41.9%. The revenue growth per employee is expected to continue to SEK 15.6 million implying a CAGR of 39.4% between 2020A and 2023E. Both external costs and other operating expenses have a steady previous trend, hence no markedly expected difference is expected. I-Tech has already bypassed the highest costs for R&D and regulatory processes, and with costs growing significantly slower than sales, it is estimated that the Company will be profitable on an EBIT level in 2022E. It is estimated that the EBIT-margin will increase rapidly to 20.3% in 2022E and 32.4% in 2023E.

Growth in net sales and improved EBIT-margin



Source: I-Tech and Analyst Estimates

Growth in net sales and increased market share.



Valuation

Applying an EV/S multiple of 7.0x in 2023E indicates a potential upside of 43.7%

Since the Company and half of the peer group is not yet profitable, an EV/S multiple is chosen for valuation. I-Tech trades at an EV/S multiple of 15.4x looking at LTM, followed by 12.2x 2021E, 7.4x 2022E, and 4.6x 2023E. In comparison with the average EV/S multiple of 15.3 over the last three years, the Company is attractively valued at an EV/S multiple of 4.6x using estimated sales for 2023E. The fact that no directly comparable listed company exists, it is recognized that our chosen peer group is not optimal. However, I-Tech has similarities to different aspects of the chosen peers, and therefore there is value in referencing them to understand where I-Tech sits against this peer group. Two Swedish biotech companies are used which arguably have similarities looking at the market cap, sales growth, and margins. Additionally, two international paint manufactures operating in markets similar to I-Tech have been selected. In comparison to peers, I-Tech has higher historical sales growth, less competition, and closer customer relations. Additionally, I-Tech is operating in a market that is characterized by high barriers of entry and has a product that will be a must-have eventually, assuming that copper will be completely banned. All of this considered, an applied target multiple of EV/S 7.0x in 2023E is justified, indicating an upside of 43.7% and a target price of SEK 107.8.

Peer valuation	Market Data (SEKmn)			Financials		Valuation (LTM)
Company Name	Market Cap	Enterprise V.	Sales CAGR 2016A-2020A	Gross margin 2020A	EBIT-margin 2020A	EV/Sales
SenzaGen AB	299.1	209.8	29.3%	70.1%	Neg.	30.4x
OrganoClick AB	1123.8	1081.5	25.0%	20.9%	Neg.	10.0x
Shinto Paint	494.5	455.2	-0.3%	19.1%	2.1%	0.2x
Sniezka	2458.4	1943.5	9.3%	42.4%	12.7%	1.5x
Average	**1094.0**	**923.0**	**15.8%**	**38.1%**	**3.7%**	**10.5x**
Median	**794.1**	**768.5**	**17.0%**	**31.5%**	**7.5%**	**5.8x**
I-Tech	842.5	815.1	46.0%	48.5%	Neg.	15.4x

Source: Bloomberg

The peer valuation is supported by a DCF using a WACC of 10.3%

In 2024E-2029E, it is estimated that I-Tech will grow with a sales CAGR of 15.8% from SEK 243.3 million to SEK 506.1 million. In these years it is estimated that Selektope® will be sold to six customers. It's also estimated that the Company will record sales from the leisure boat market. This is supported from by collaboration with Pettit Marine Paint and Chugoku Marine Paints recently releasing a product for the leisure boat market.

DCF valuation breakdown 2023E	
Forecasted value (SEKm)	558.3
Terminal value (SEKm)	849.0
Enterprise value (SEKm)	1407.3
Net debt (SEKm)	-27.8
Market cap (SEKm)	1379.5
No. Shares (m)	11.9
Value per share (SEK)	**115.9**

Source: Analyst Estimates

Management and Board

Philip Chaabane, CEO

Philip has experience in senior positions from global tech companies. Most recently, Philip came from PowerCell Sweden AB, where he was responsible for business and customer development. Philip has also held various operational roles within Volvo Aero Corporation (today GKN Aerospace). Philip holds a Master of Science in International Materials Engineering, Luleå University of Technology, and EEIGM in France.
Ownership: 153 899 shares (1.3% of outstanding shares)

Magnus Henell, CFO

Magnus has extensive experience within finance and management from various companies as well as extensive experience of M&A within the Volvo Group. When Magnus was CEO of PowerCell Sweden AB, he successfully refinanced the Company and listed it on First North at Nasdaq Stockholm. Magnus holds a Master of Business Administration from Karlstad University and the Gothenburg School of Business.
Ownership: 30 000 shares (0.3% of outstanding shares)

Cecilia Ohlauson, Head of Regulatory Affairs

Cecilia has an academic background within ecotoxicology regarding biocides and a doctorate in environmental science. Cecilia has worked for I-Tech with responsibility for regulatory work since 2008 and has similar experience in the pharmaceutical industry. She holds a doctoral degree from the University of Gothenburg and a master's degree in biology from Linnaeus University as well as a microbiology studies at Stockholm University.
Ownership: 22 020 shares (0.2% of outstanding shares)

Stefan Sedersten, Chairman of the board

With a Master of Science in Mechanical Engineering from Chalmers University of Technology, Stefan has a background in radar electronics and marine propulsion industry and has had different leading positions in purchasing, production, and research, and development. Stefan is now the CEO of Berg Propulsion Group, a leading supplier of variable pitch propellers for the maritime industry
Ownership: 451 330 shares (3.8% of outstanding shares)

Chatarina Schneider, Member of the board

With studies in chemistry at University of Linköping Chatarina has worked for more than two decades for the chemical group, AkzoNobel, and has in various leading positions led multicultural teams in business management, marketing, and sales. She has also been responsible for a business within Akzo Nobel in Asia. Chatarina Schneider is currently CEO of the chemical distributor AmphoChem AB and Pemco Additives AB.
Ownership: 6 000 shares (0.1% of outstanding shares)

Mikael Laurin, Member of the board

Mikael Laurin holds a Master of Science in Industrial Engineering and Management, Chalmers University of Technology. He has worked for several consultancy firms with a focus on supply chain management, business strategy, and management. He is today the CEO of Lean Marine. Prior to that, he worked for 11 years as the CEO for Laurin Maritime who ran a modern tank fleet for oil products and chemicals worldwide with 16 x 45k-50k deadweight tonne chemical classed vessels.
Ownership: 2 649 shares (0.0% of outstanding shares)

Source: I-Tech AB

Appendix

Income statement, SEKmn	2020	2021E	2022E	2023E
Net sales	52.8	70.9	116.9	187.1
Other income	0.8	1.1	1.1	1.0
Total revenue	**53.6**	**72.0**	**118.0**	**188.1**
COGS	(27.6)	(37.0)	(57.8)	(88.3)
Gross profit	**25.2**	**33.8**	**59.1**	**98.8**
Gross margin	47.7%	47.7%	50.6%	52.8%
Other external costs	(10.5)	(11.3)	(12.1)	(12.4)
Personnel costs	(10.5)	(14.2)	(14.3)	(15.7)
EBITDA	**3.6**	**8.2**	**32.6**	**70.4**
EBITDA margin	2.7%	11.6%	27.9%	37.6%
Depreciation (incl. Impairments)	(8.8)	(8.8)	(8.8)	(9.8)
Amortization (incl. Impairments)	(0)	(0)	(0)	(0)
EBIT	**-5.1**	**-0.6**	**23.8**	**60.6**
EBIT margin	-9.8%	-0.8%	20.3%	32.4%
Net financial items	(143.0)	(152.0)	(134.0)	(143.5)
EBT	**-6.0**	**-0.9**	**23.3**	**60.0**
Tax expense	(1.2)	(0.2)	(4.8)	(-12.4)
Net income	**-4.8**	**-0.7**	**18.5**	**47.6**
Net income margin	-9.1%	-1.0%	15.8%	25.5%

Source: I-Tech AB and Analyst Estimates

DCF

Key Cash flow items	2020A	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E
Net sales	**52.8**	**70.8**	**116.9**	**187.1**	**243.3**	**316.2**	**363.7**	**418.2**	**460.1**	**506.1**
EBIT	-5.2	-0.9	23.8	60.6	109.5	142.3	163.7	188.2	207.0	227.7
Taxes on EBIT	0.0	0.2	-4.9	-12.5	-22.6	-29.3	-33.7	-38.8	-42.6	-46.9
NOPAT	**-5.2**	**-0.7**	**18.9**	**48.1**	**86.9**	**113.0**	**129.9**	**149.4**	**164.4**	**180.8**
D&A	8.8	8.8	8.8	9.8	12.2	15.8	18.2	20.9	23.0	25.3
Capex	-0.9	-0.9	-0.9	-1.9	-9.7	-12.6	-14.5	-20.9	-23.0	-25.3
change NWC	-6.1	-0.6	-1.4	-2.1	-1.7	-2.2	-1.4	-1.6	-1.3	-1.4
FCFF	**-3.4**	**6.6**	**25.4**	**53.9**	**87.7**	**114.0**	**132.2**	**147.8**	**163.1**	**179.4**

Source: I-Tech and Analyst Estimates

Sensitivity analysis

	WACC						
Terminal Growth	7.0%	8.0%	9.0%	10.0%	11.0%	12.0%	13.0%
0.5%	177	148	126	109	95	84	74
1.0%	188	155	131	112	98	86	76
1.5%	200	164	137	117	101	88	78
2.0%	216	174	144	**122**	104	91	80
2.5%	234	185	152	127	108	94	82
3.0%	258	199	161	133	113	97	85
3.5%	288	217	171	140	118	101	87

Source: Analyst estimates

Disclaimer

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