

Railcare Group

Sector: Industrial Goods & Services

Raising the Bar

Redeye is encouraged by Railcare's new and rather aggressive financial targets of SEK1 billion in sales by 2027 and EBIT margins over 13%. Obviously, the company sees excellent business opportunities in the coming years and has the ambition to further accelerate its expansion. The Q4 report shows continued solid growth and healthy margins. We bump up our near- and mid-term projections, raising our Base case fair value ~10% to SEK33 per share.

Q4 – No big surprises

Net sales of SEK149m in Q4 were 17% higher Y/Y and just above our forecast. EBIT margins of 9% was also significantly higher Y/Y, but slightly lower than we expected. The difference is mainly explained by costs relating to train maintenance and more sales activities in business segment Machines & Technology. Transport Scandinavia is again exceeding our expectations in terms of sales and earnings thanks to continued high capacity utilization in the locomotive workshop and construction transports. The overall market outlook remains firm with no significant changes, as far as we understand.

New financial targets

In conjunction with the report, Railcare raised its financial targets quite considerably. By 2027 they now target sales of SEK1 billion (previously: SEK800m) and to maintain EBIT margins >13% (previously: >10%). There are probably several reasons for this. One is the fact that they were awarded the five-year contract for standby locomotives, starting in 2025, worth SEK80m annually. Also, we understand that Railcare sees good opportunities for new long-term transportation contracts. Moreover, the company's ambition and efforts to grow machine sales are now higher.

Raising our forecasts and valuation

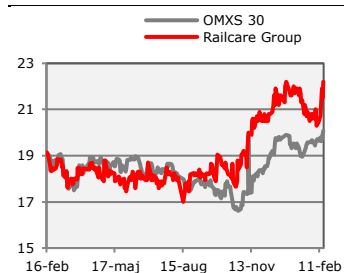
We have raised our growth projections for the near- and mid-term period on the back of Railcare's new financial targets, as they indicate more aggressive growth ambitions. Meanwhile, we leave our margin forecasts unchanged at this point. Our new Base case fair value is now around SEK33 per share (previously: SEK30), suggesting a potential of ~50% to current share price levels.

Key Financials (SEKm)	2022	2023	2024e	2025e	2026e
Net sales	497	564	618	716	826
Sales growth	13%	14%	10%	16%	15%
EBITDA	95	112	127	142	173
EBIT	52	68	75	89	103
EBIT Margin (%)	11%	12%	12%	12%	12%
Net Income	37	44	50	61	73
EV/Sales	1.2	1.1	1.1	0.9	0.8
EV/EBITDA	6.5	5.9	5.2	4.7	3.8
EV/EBIT	11.7	9.7	8.8	7.5	6.5

FAIR VALUE RANGE

BEAR	BASE	BULL
17.0	33.0	42.0

RAIL.ST VERSUS OMXS30



REDEYE RATING



KEY STATS

Ticker	RAIL.ST
Market	Nasdaq
Share Price (SEK)	22.2
Market Cap (MSEK)	536
Net Debt 24E (MSEK)	126
Free Float	60%
Avg. daily volume ('000)	12

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Q4 report - key takeaways

Railcare: Actual vs. Expectations

SEKm	Q4 2022	Q4 2023 Actual	Q4 2023e	Diff
Net sales	128.0	149.3	142.0	5%
EBIT	6.7	13.2	16.6	-20%
Pre Tax Profit	4.8	9.7	13.8	-30%
<i>Sales growth Y/Y</i>	-3%	17%	11%	
<i>EBIT margin</i>	5.2%	8.8%	11.7%	

Source: Railcare, Redeye Research

Contracting Sweden had a good quarter with some growth and stable margins but was impacted by the early winter and had to delay some planned lining and construction work until spring.

Contracting Abroad again saw very modest volumes and posted a small loss. Hopefully, the next UK control period will support a recovery but H1'24 will likely remain sluggish.

Transport Scandinavia had another very strong quarter driven by construction transports and continued high activity in the locomotive workshop. Railcare is not suffering any financial impact from the traffic interruption at Malmbanan. Locomotive maintenance has been carried out during the stop, resulting in higher costs than normal.

Machines and Technology has intensified its efforts on export sales including the participation at the trade fair AusRail in Australia. This incurred higher costs, hence the operating loss in Q4. The MPV with a pantograph is about to be completed and is planned to go into Railcare's contracting operations during 2024.

On group level sales grew by 17% Y/Y with EBIT margins of 9%. Trailing 12 months, top-line growth reached 14% while EBIT margins improved to 12%.

Segments by quarter

SEKm	Q4'21	Q1'22	Q2'22	Q3'22	Q4'22	Q1'23	Q2'23	Q3'23	Q4'23
Contracting Sweden									
Net sales	40	37	52	49	48	41	58	58	60
PTP	7	5	5	6	5	2	5	6	5
PTP margin	16%	13%	10%	13%	10%	4%	8%	10%	9%
Contracting Abroad									
Net sales	14	11	5	10	10	13	5	6	8
PTP	5 *	-1	-5	0	-3.3 *	2	-1	-1	-2
Profit margin	n.m.	neg	neg	neg	n.m.	neg	neg	neg	neg
Transport Scandinavia									
Net sales	85	43	73	88	75	68	82	97	92
PTP	14	0	11	14	4	7	9	18	13
Profit margin	16%	0%	15%	15%	5%	10%	11%	18%	14%
Machines and Technology									
Net sales	7	22	23	24	19	18	18	24	21
PTP	-1	3	2	3	1	1	1	1	-2
Profit margin	-13%	13%	7%	11%	3%	5%	8%	3%	neg
Group sales:	132	95	127	146	128	111	145	159	149
Growth Y/Y	38%	7%	40%	16%	-3%	17%	14%	9%	17%
Growth, TTM	9%	16%	30%	25%	13%	15%	10%	8%	14%
EBIT	25	9	13	24	7	13	15	27	13
EBIT-margin	19%	9%	10%	16%	5%	12%	10%	17%	9%
EBIT margin TTM	13%	12.7%	15.0%	14.1%	10.5%	11.1%	11.1%	11.3%	12.1%

* Including one-off costs of SEK3m in Q4 2022.

Source: Railcare, Redeye Research

Financial forecasts

Raising our expectations for 2024-26e

We raise our growth projections mainly on the back of Railcare's new financial targets. Certainly, it still remains to be seen how this will play out, but we believe this shows that Railcare sees great opportunities for profitable growth in the coming years and are willing to act on it. Their history and track record suggest that they walk the walk, not just talk the talk.

Railcare: Estimate changes			
SEKm	2024e	2025e	2026e
Net sales			
Old	610	680	748
New	618	716	826
% change	1%	5%	10%
EBIT			
Old	78	87	90
New	75	89	103
margin	12.1%	12.5%	12.5%

Source: Redeye Research

Main considerations and changes to our forecast:

Contracting Sweden has a solid market position and demand for contracting services as well as relining are expected to remain high. We expect some further growth and margins ~10%.

Contracting Abroad (UK) has been struggling with low volumes for a long time. We think it will improve, but our expectations are still low. We think there is a possibility that UK operations will be discontinued. It's probably a binary situation and difficult to assess.

Transport Scandinavia is one of the cornerstones in Railcare's growth strategy with an ambition to expand significantly in the coming years. This includes transports as well as services offered by the locomotive workshop. Our forecast revisions mainly relate to this segment, which historically has shown robust growth and margins over 10%.

Machines and Technology is the segment that can offer the best leverage to the groups' margins. Railcare has a unique and attractive product range mainly based on the Railvac systems and soon also the new electric MPV with pantographs. Admittedly, our predictions for this segment are very uncertain and should be viewed as guesstimates.

Forecasts per segment						
SEKm	2021	2022	2023	2024e	2025e	2026e
<u>Contracting Sweden</u>						
Net sales	131	186	217	224	230	242
Wherof leasing operators to UK	-	-	23	23	26	27
PTP	8	21	17	22	23	27
Margin	6%	11%	9%	11%	11%	12%
<u>Contracting Abroad</u>						
Net sales	48	36	32	32	36	39
PTP	4	-9	-3	-2	0	2
Margin	8%	-25%	-8%	-6%	0%	5%
<u>Transport Scandinavia</u>						
Net sales	274	279	340	367	430	494
PTP	39	28	46	40	47	54
Margin	14%	10%	14%	11%	11%	11%
<u>Machines and Technology</u>						
Net sales	37	88	81	100	130	160
PTP	1	8	1	5	13	16
Margin	2%	9%	1%	5%	10%	10%
Group net sales	438	497	564	618	716	826
EBIT	56	52	68	75	89	103
Sales growth, Y/Y	9%	13%	14%	10%	16%	15%
EBIT margin	12.8%	10.5%	12.0%	12.1%	12.5%	12.5%

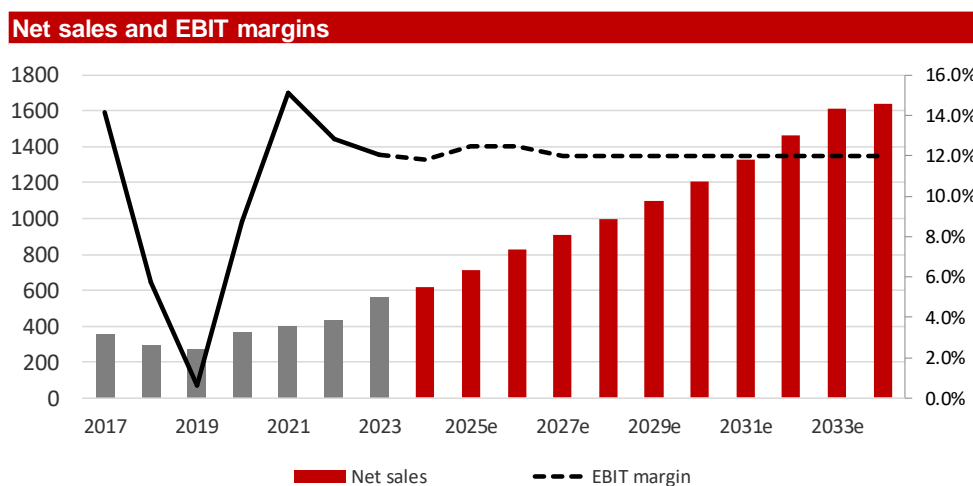
Source: Railcare, Redeye Research

Long-term assumptions, years 2027-33

No changes have been made to our long-term assumptions in terms of growth and EBIT margins. But since we have raised our sales forecasts for 2024-26, our projections for the following year's have also moved up a notch. Railcare's target is now to reach sales of SEK 1 billion by 2027 (previous target: SEK800m). We don't think it's impossible, but our forecasts imply that it will take until ~2028. As for EBIT margins we believe the 13% target is fair, but we are still slightly more cautious at this point.

- 10% annual growth
- 12% EBIT margins
- From 2033 (Terminal year): 12% EBIT margin and 2% annual growth

In the period up until 2033 we find it highly likely that Railcare will expand into new geographic markets. In our view, probably countries in northern Europe. And with machine exports to the global market. The future progression will certainly not be linear, like our model suggests. But a CAGR of 10% should be attainable, given the significant expansion opportunities available. If so, annual sales in 2033 will reach around SEK1.6bn.



Source: Railcare, Redeye Research

Valuation

Fair value:
~SEK 33 per share

Our cash flow model indicates a fair enterprise value around SEK 917m. After deducting net debt, we arrive at a fair equity value just above SEK 700m, or **SEK ~33 per share** (SEK 30 previously). This suggests a rather appealing potential of around 50% from current share price level. Assumptions for our Base case scenario and valuation are summarized in the table below.

Railcare: Base case			
Assumptions	2027-33e	DCF-value	
CAGR	10%	WACC	10.0%
EBIT margin	12%	NPV FCF 2022-32	295
ROIC (avg)	17%	NPV FCF Terminal	622
		Total (EV)	917
		Net debt	120
Terminal			
Net sales 2034 (SEKm)	1 642	Fair value	797
Growth FCF	2%	Fair value per share	33.0
EBIT margin	12%		
EV/S Exit multiple	0.9	Share price	22.2
EV/EBIT Exit multiple	7.7	Potential	49%

Source: Redeye Research

Still trading at attractive multiples

Based on our estimates Railcare is trading at more attractive multiples than we have seen historically. With a rather stable business and continued good outlook, we find this unjustified and a bit surprising. EV/EBIT is in our view the most relevant multiple since it also takes net debt into account. We are not including leasing debt in our EV/EBIT. It is however included in our EV/EBITDA multiple.

Valuation multiples						
	2021	2022	2023	2024e	2025e	2026e
P/E	13.3	13.1	12.3	10.7	8.8	7.4
EV/EBIT	11.8	11.7	9.7	8.8	7.5	5.3
EV/EBITDA	6.6	7.1	6.3	5.5	5.0	4.1
P/S	1.2	1.2	1.1	1.1	0.9	0.7
Share price	22.4	20.5	22.2	22.2	22.2	22.2

Source: Railcare, Redeye Research

Scenarios

For a company like Railcare there are of course a variety of possible scenarios. We do not see any specific binary events that would cause a significantly different development than the one outlined in our main scenario, Base case. Business operations are stable and the balance between different segments offer some diversification in terms of risks. However, two other possible scenarios are outlined below: Bull- and Bear-case. Both are quite possible, but in our view rather optimistic and pessimistic, respectively.

Bull-case

Railcare certainly could grow faster than we anticipate for an extended period of time. If they, e.g. establish operations in a new country or if machine sales really start taking off. The Railvac, Minevac, Tubevac and MPV, all have significant market potential globally. These machines have a potential for very good gross margins and with higher volumes Railcare can improve its manufacturing process. Growth driven by machine sales should also drive margins. Assumptions for our Bull case:

- CAGR 2023-32: ~13%, taking sales to SEK1.6bn in 2033.
- Sustainable EBIT margins of 12%.
- Bull case fair value around **SEK 42 per share**.

Bear-case

Although the near-term outlook is bright, market conditions could deteriorate later on. New competitors, that we don't see today could emerge and impact profitability. State budgets could see major cuts or Railcare itself could run into internal problems. Bear case assumptions:

- CAGR 2023-32: 5% taking sales to ~SEK800m in 2033.
- Sustainable EBIT margins of 10%.
- Bear case fair value around **SEK 17 per share**.

Investment Thesis

Unique position in attractive market segment

Railcare has established a solid position in the railway maintenance market, with an offer based on its own unique proprietary vacuum technology. The company has developed efficient systems to handle ballast replacement that standard excavators are unable to perform. This means maintenance work can be done at a lower cost and with less interruptions in railroad traffic. The global market potential is huge and if executed well, Railcare has decades of major growth opportunities ahead.

Successfully validated

The Railvac systems have been operating successfully in Sweden and the UK for many years and been exported to several markets overseas. It has become a well-known concept, validated by partners and clients. With the new all-electric MPV (emission-free and low noise), Railcare is adding features very appealing to niche applications like maintenance in subways, tunnels and populated areas.

Challenges

Limited progress in export sales lately

In recent years, export sales of Railvac systems have been quite few and far apart. This is reason for some concern, as we believe the company's ambition has been higher. We don't really know the reasons behind this. When it comes to Railcares' overall growth ambitions, our sense is that they have been somewhat defensive and not too eager. This may be changing considering the new financial sales target of SEK1000m by 2027, corresponding to a CAGR ~15%.

Political risk

A significant part of the group's operations is exposed to public utilities and government budgets. Currently there is good support for railroad maintenance, but there is always a risk associated with political involvement. This can certainly be applied to Railcare's own contracting business, but also to some extent when it comes to exports of machinery and equipment.

Summary Redeye Rating

The rating consists of three valuation keys, each constituting an overall assessment of several factors that are rated on a scale of 0 to 1 points. The maximum score for a valuation key is 5 points.

Rating changes in the report: No changes.

People: 3

Management is very active in daily operations and have extensive experience from the railroad industry. However, Mattias Remahl is still rather new as CEO and we really cannot evaluate him in this capacity yet. Communication and financial reports are relevant and transparent and Railcare is ticking most boxes in the People category. Furthermore, the two dominant owners are represented on the Board of directors, which also has some independent members. So a good mix on the Board.

Business: 4

Revenues and profitability have been quite volatile in the last few years, due to fluctuating demand. The customer offer based on the unique Railvac machines is a competitive advantage that should give good prospects for growth and profitability. There are still no head-on competitors in this niche segment, as far as we know. For some of Railcare's other service offerings, there is more competition. Management appears to be committed on innovation of new products and services and we also believe that Railcare will expand geographically, in due course.

Financials: 2

Profitability was poor in 2017-18, due to declining volumes, but has improved remarkably since then. Railcare decided not to make any drastic reductions in personnel during 2017-18, as they anticipated better times and need skilled staff. EBIT margins have been well over the company's own target of 10% lately and we would not be surprised if Railcare decides to raise this target. However, there is limited leverage in the major part of the company's business offering. Hence, there are also limitations in terms of what they can score in our Financial rating. Financial gearing (debt/equity) is on a reasonable level given stable and profitable operations. But there is probably limited room for major acquisitions or significant expansions into new markets.

	2023	2024e	2025e	2026e
INCOME STATEMENT				
Net sales	564	618	716	826
Cost of Revenues	230	223	258	297
Gross Profit	352	396	458	529
Operating Expenses	240	269	316	355
EBITDA	112	127	142	173
Depreciation & Amortization	44	52	53	59
EBIT	68	75	89	103
Net Financial Items	-11	-11	-10	-8
EBT	57	64	79	95
Income Tax Expenses	14	14	18	22
Non-Controlling Interest	0	0	0	0
Net Income	44	50	61	73
BALANCE SHEET				
Assets				
Current assets				
Cash & Equivalents	39	43	32	38
Inventories	36	37	50	58
Accounts Receivable	57	62	64	66
Other Current Assets	36	37	43	66
Total Current Assets	168	179	190	228
Non-current assets				
Property, Plant & Equipment, Net	405	447	489	538
Goodwill	6	6	6	6
Intangible Assets	4	3	1	0
Right-of-Use Assets	55	51	52	36
Shares in Associates	0	0	0	0
Other Long-Term Assets	5	5	5	5
Total Non-Current Assets	475	512	553	584
Total Assets	643	690	742	812
Liabilities				
Current liabilities				
Short-Term Debt	85	95	95	95
Short-Term Lease Liabilities	12	12	12	12
Accounts Payable	48	43	50	58
Other Current Liabilities	54	62	64	75
Total Current Liabilities	198	212	221	239
Non-current liabilities				
Long-Term Debt	74	74	74	74
Long-Term Lease Liabilities	37	37	37	37
Other Long-Term Liabilities	60	60	60	60
Total Non-current Liabilities	171	171	171	171
Non-Controlling Interest	0	0	0	0
Shareholder's Equity	274	307	350	402
Total Liabilities & Equity	643	690	742	812
CASH FLOW				
NOPAT	84	91	110	127
Change in Working Capital	8	-3	-13	-14
Operating Cash Flow	102	99	101	118
Capital Expenditures	-57	-68	-72	-83
Investment in Intangible Assets	-3	-6	-7	-8
Investing Cash Flow	-61	-89	-94	-91
Financing Cash Flow	-34	-7	-18	-21
Free Cash Flow	41	25	22	27

DCF Valuation Metrics	Sum FCF (SEKm)
Initial Period (2024–2026)	48
Momentum period (2026-32)	247
Stable period (2033-)	622
Firm Value	917
Net Debt (last quarter)	120
Equity Value	797
Fair Value per Share	33.0

	2023	2024e	2025e	2026e
CAPITAL STRUCTURE				
Equity Ratio	0.4	0.4	0.5	0.5
Debt to equity	0.6	0.6	0.5	0.4
Net Debt	120	126	137	131
Capital Employed	445	478	521	573
Working Capital Turnover	36.2	33.7	23.1	18.2

	2023	2024e	2025e	2026e
GROWTH				
Revenue Growth	14%	6%	16%	15%
Basic EPS Growth	18%	15%	22%	19%
Adjusted Basic EPS Growth	18%	15%	22%	19%

	2023	2024e	2025e	2026e
PROFITABILITY				
ROE	17%	17%	18%	19%
ROCE	15%	16%	17%	18%
ROIC	20%	20%	22%	23%
EBITDA Margin (%)	20%	21%	20%	21%
EBIT Margin (%)	12%	12%	12%	12%
Net Income Margin (%)	8%	8%	8%	9%

	2023	2024e	2025e	2026e
VALUATION				
Basic EPS	1.8	2.1	2.5	3.0
Adjusted Basic EPS	1.8	2.1	2.5	3.0
P/E	12.3	10.7	8.8	7.4
EV/Revenue	1.1	1.1	0.9	0.8
EV/EBITDA	5.9	5.2	4.7	3.8
EV/EBIT	9.7	8.8	7.5	6.5
P/B	2.0	1.7	1.5	1.3

SHAREHOLDER STRUCTURE	CAPITAL %	VOTES %
Nornan Invest AB	29.5%	29.5%
TREAC Aktiebolag	9.9%	9.9%
Ålandsbanken AB	5.3%	5.3%
Försäkringsbolaget Avanza Pension	3.4%	3.4%
Bernt Larsson	3.1%	3.1%

SHARE INFORMATION	RAIL.ST
Reuters code	RAIL.ST
List	Nasdaq Smallcap
Share price	22.2
Total shares, million	24.1

MANAGEMENT & BOARD	
CEO	Mattias Remahl
CFO	Lisa Borgs
Chairman	Anders Westermark

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Redeye Rating and Background Definitions

Company Quality

Company Quality is based on a set of quality checks across three categories: PEOPLE, BUSINESS, FINANCE. These are the building blocks that enable a company to deliver sustained operational outperformance and attractive long-term earnings growth.

Each category is grouped into multiple sub-categories assessed by five checks. These are based on widely accepted and tested investment criteria and used by demonstrably successful investors and investment firms. Each sub-category may also include a complementary check that provides additional information to assist with investment decision-making.

If a check is successful, it is assigned a score of one point; the total successful checks are added to give a score for each sub-category. The overall score for a category is the average of all sub-category scores, based on a scale that ranges from 0 to 5 rounded up to the nearest whole number. The overall score for each category is then used to generate the size of the bar in the Company Quality graphic.

People

At the end of the day, people drive profits. Not numbers. Understanding the motivations of people behind a business is a significant part of understanding the long-term drive of the company. It all comes down to doing business with people you trust, or at least avoiding dealing with people of questionable character.

The People rating is based on quantitative scores in seven categories:

- Passion, Execution, Capital Allocation, Communication, Compensation, Ownership, and Board.

Business

If you don't understand the competitive environment and don't have a clear sense of how the business will engage customers, create value and consistently deliver that value at a profit, you won't succeed as an investor. Knowing the business model inside out will provide you some level of certainty and reduce the risk when you buy a stock.

The Business rating is based on quantitative scores grouped into five sub-categories:

- Business Scalability, Market Structure, Value Proposition, Economic Moat, and Operational Risks.

Financials

Investing is part art, part science. Financial ratios make up most of the science. Ratios are used to evaluate the financial soundness of a business. Also, these ratios are key factors that will impact a company's financial performance and valuation. However, you only need a few to determine whether a company is financially strong or weak.

The Financial rating is based on quantitative scores that are grouped into five separate categories:

- Earnings Power, Profit Margin, Growth Rate, Financial Health, and Earnings Quality.

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CONFLICT OF INTERESTS

Henrik Alveskog owns shares in the company : No

Fredrik Nilsson owns shares in the company : No

Redeye performs services for the Company and receives compensation from the Company in connection with this.