Investors' Chronicle | Alpha

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Alpha small company research

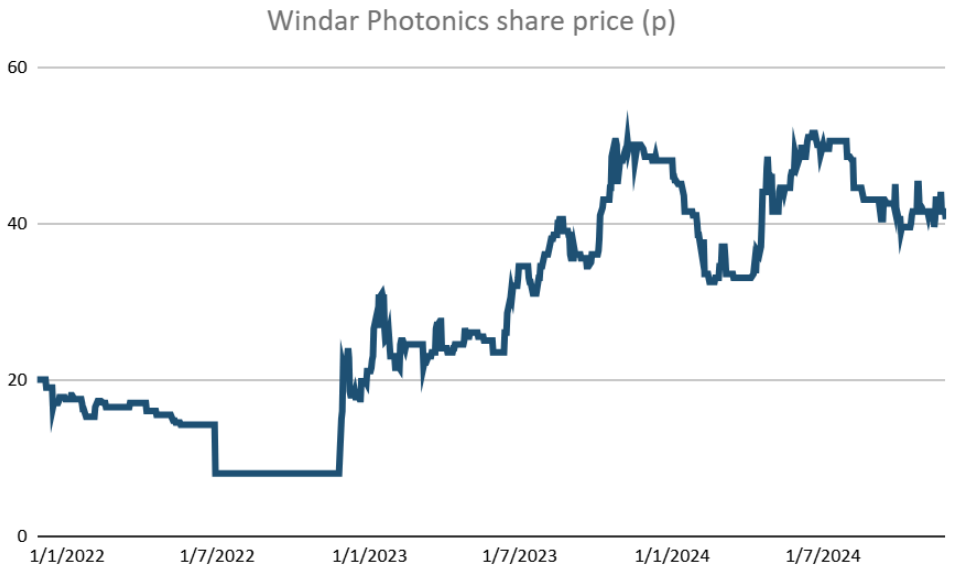
28 November 2024

A small-cap share poised to catch a fair wind

'You will be hard pressed to find a company forecast to organically increase pre-tax profit more than 10-fold, but that's the tantalising prospect offered by this niche component business.'

Simon Thompson's view:

'The wind power industry's installed capacity has grown almost 100-fold in the past two decades and there are now 340,000 large turbines generating electricity across the world. Newer turbines are becoming even larger and more efficient, so operators are using new technology to improve energy capture of their existing fleet in order to improve their return on investment. One below-the-radar company is helping them do exactly that by offering a cost effective patented solution that significantly improves a turbine's energy capture as well as extending its life. Demand is surging, so much so that this company is in very advanced talks to secure €60mn of potential orders, which will be transformational for both revenue and earnings next year. Trading on a 2025 forward price-to-earnings (PE) ratio of 6.3, the share price could double and still wouldn't fully capture the growth opportunity on offer.'



Source: LSEG

Bull points

1. Market leader with strong intellectual property (IP).
2. Substantial new installation and retrofit market.
3. Competitive advantage over rivals.
4. Rapidly growing pipeline of contract opportunities.
5. Highly scalable and operationally geared.
6. High gross margin.
7. Sales growth is accelerating.
8. Strong management team.
9. Fundraising eases working capital constraints.
10. Strong earnings growth forecast .

Bear points

1. Long sales cycle and challenge of ramping up production to meet rising demand.
2. Equity raises relied upon to provide working capital.
3. Potential for US tariffs on EU imports.

Windar Photonics (WPHO)	
Ticker	WPHO
Current mid-price	39.5p
Bid-offer spread	39 - 40p
Target price	80p
52 week high	53p
52 week low	30p
Market cap	£32.1mn
Net cash	€1.1mn (30 June 2024)
Net asset value	€4.9mn (30 June 2024)
2025 Dividend yield	nil
2025 PE ratio	6.3
Shares in issue	81.3mn
Financial year end	31 December
Next event	annual results March 2025
Website	investor.windarphotonics.com

Source: London Stock Exchange and company filings

Windar Photonics (WPHO) is a Danish technology company that develops cost-efficient and innovative Light Detection and Ranging (LiDAR) optimisation systems for use on electricity generating wind turbines. LiDAR wind sensors are designed to remotely measure wind speed and direction, and when fitted to wind turbines, produce improvements in their efficiency and power output.

The technology was originally developed within the Technology University of Denmark and was progressed by a photonic incubator led by the company's chief executive Jørgen Korsgaard Jensen, ultimately leading to the formation of Windar in 2008. The company floated on Aim in 2015 when Windar's offering was seen as a new technology in the market. Although it has been a slow burn for shareholders since then as conservative global service companies and independent power producers (IPP) validated the technology, the company is now gaining real traction.

Having made inroads in China, the world's largest wind power market, a key development in Windar's progression was signing a global distribution agreement in 2018 with Vestas Wind Systems, the largest wind turbine company in the world with an installed base of 55,000 turbines. It proved a gamechanger and led to the first volume order in North America in 2021 after an extensive period of product testing.

Furthermore, the market is now opening for Windar, so much so that in a trading update in mid-November 2024 the directors revealed that they are in advanced discussions with several IPPs in the Americas and Australia. Some of these companies are large multi-national corporations who cumulatively own more than 1,750 Vestas V82 wind turbines and 700 turbines installed by German wind power manufacturer, Senvion.

Financial Summary

Year to December (€m)	2022A	2023A	2024E	2025E
Revenues (€m)	1.9	4.8	6.6	17.2
Adjusted EBITDA (€m)	(0.8)	0.2	0.7	7.0
Adjusted PBT (€m)	(1.1)	(0.3)	0.4	6.7
Adjusted EPS, c	(1.6)	(0.1)	0.4	7.5
DPS, p	0.0	0.0	0.0	0.0
Net cash/(debt)	(0.4)	(1.6)	1.1	4.9
Adjusted EV/EBITDA, x	(48.3)	170.6	55.7	5.4

Source: Windar Photonics, Dowgate Capital estimates

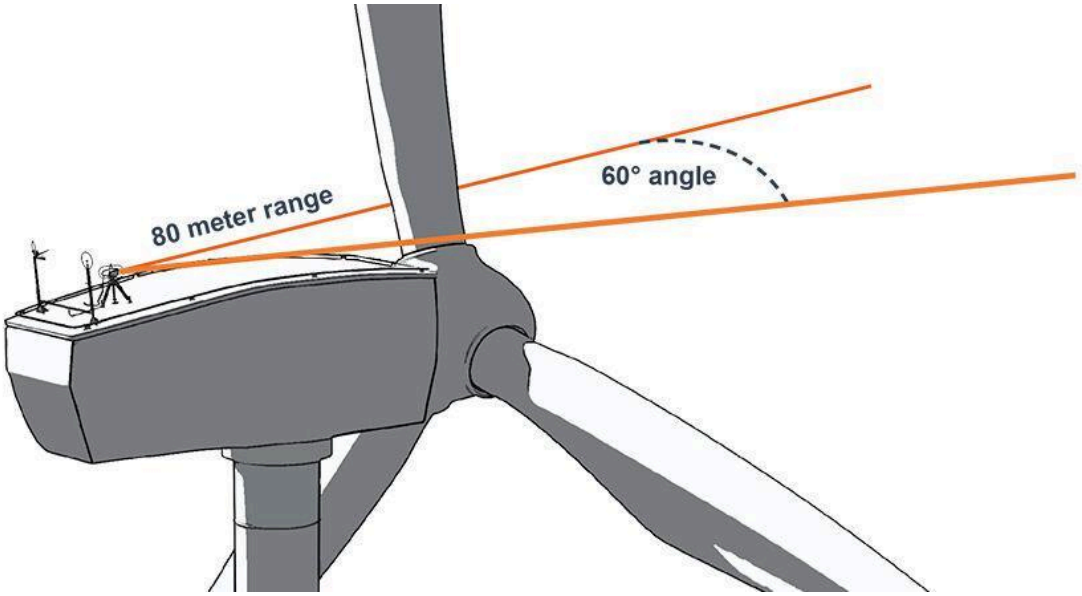
To put the scale of the opportunity into perspective, retrofitting the LiDAR wind measurement technology to each turbine generates around $20,000 of revenue for Windar. So, assuming the company secures the orders, as seems highly likely, the directors believe the contracts support €60mn of revenue for the hardware with recurring software sales on top. In addition, Windar has established preliminary contact with IPPs who control a further 200 Vestas V82 turbines, and is in discussions with IPPs in Japan and China who control several hundred wind turbines of varying types. I understand that product testing has gone well.

There are 4,000 Vestas V82 turbines systems installed, worth around €100mn in revenue to Windar, but the total addressable market (TAM) is much larger as there are 340,000 wind turbines in the world of which 90 per cent are onshore, the market Windar has been focusing on to date. So, as Windar moves beyond the earlier range of Vestas V82 turbine platforms to Senvion and General Electric, the market opportunity is expanding rapidly. Analysts at brokerage firms Zeus Capital and Dowgate Capital both believe that the global onshore TAM for the company's technology is worth more than $6bn (£4.7bn) in revenue for the hardware element.

Strong incentive for IPPs to adopt the technology

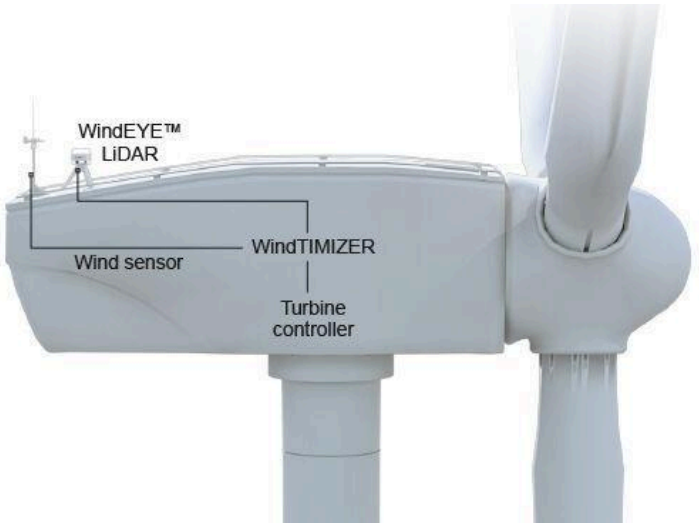
Importantly, there are compelling reasons for turbine operators to adopt Windar's LiDAR-assisted turbine control technology, not least that it increases energy capture by 3-4 per cent, reduces loads on the turbine structure and mitigates extreme weather.

It is achieved by integrating the company's WindEYE LiDAR, a nacelle-mounted LiDAR that measures wind direction and wind speed 80m in front of the turbine, with the wind turbine's control system. This enables the LiDAR to send information to the turbine about the wind, well-before it reaches the turbine. Knowing the correct wind direction allows the turbine to yaw accordingly with the incoming wind, which increases the energy production and reduces loads on vital parts of the turbine.



WindEYE LiDAR measures wind direction and wind speed

Windar's second product, the WindVISION LiDAR, has more advanced detection features to detect and gather additional data including gust detection, wake detection, turbulence detection and rotor effective speed.



WindTIMIZER integrates Windar's hardware with the turbine control system

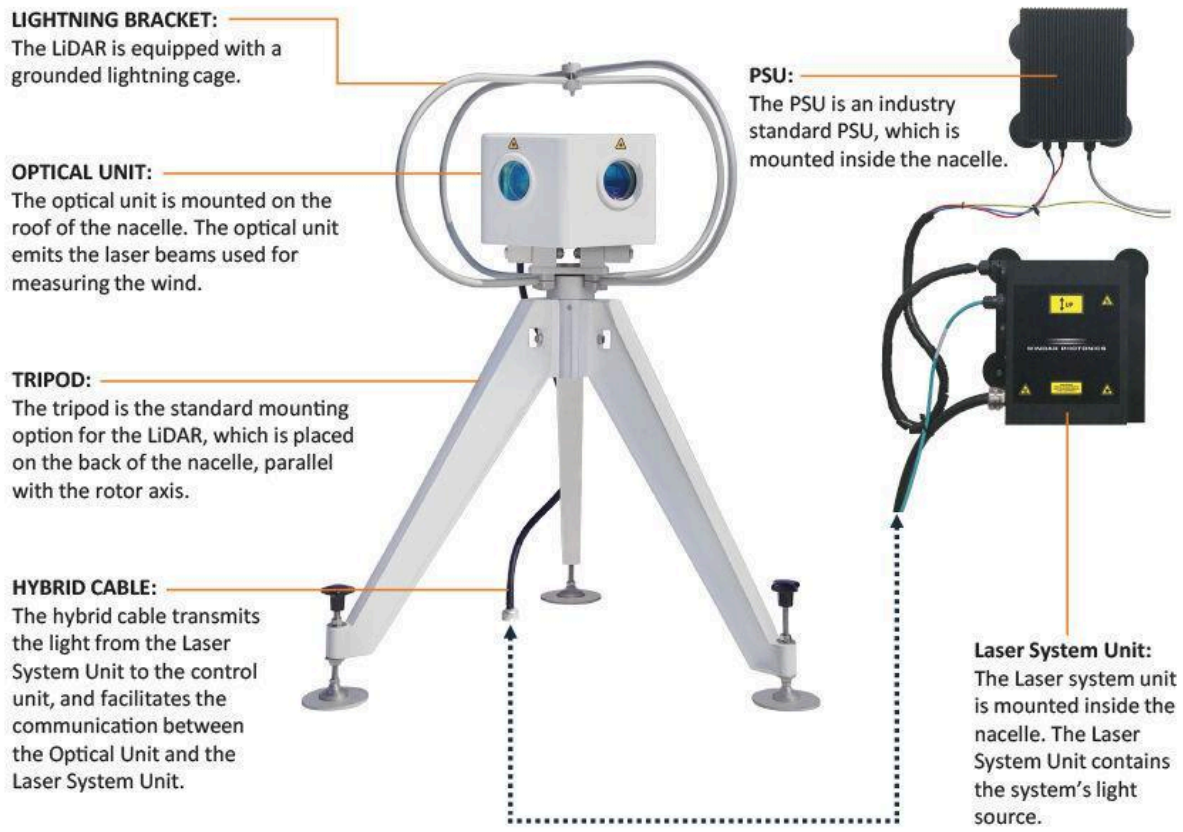
Importantly, both the WindEYE and WindVISION LiDAR's are integrated with the wind turbine's control system without needing to change anything thanks to a mediator software solution, WindTIMIZER. The control-integration is needed to facilitate dynamic yaw correction whereby the turbine will continuously receive data from the WindEYE and WindVISION sensors to ensure that the yawing of the wind turbine is always perfectly optimised.

Both products are relatively easy to install, require no special cranes or hoisting solutions, and the complete installation procedure can be performed in less than a day by a single experienced wind turbine technician. The most rugged components of the systems are installed on the roof of the wind turbine, whereas the more sensitive parts are mounted inside the nacelle.

Windar's technology has a significant cost advantage over rivals. That's because the company uses semiconductor lasers that are significantly cheaper than conventional gas or solid-state lasers used by competitors. They are lightweight, small, have low power consumption, long life span and high reliability. The low-voltage constant current mode reduces the chance of power failure and the hardware has few maintenance requirements. In fact, the LiDAR windows can be cleaned during normal turbine maintenance and replacing the light source every four years is only a 30 minute job for a technician. Data from the LiDAR can also give an advanced warning of undetected maintenance issues.

The cost advantage Windar has over rivals is significant. In fact, its patented protected LiDAR's are offered to customers at 80 per cent lower prices than rival LiDAR manufacturers, and low cost maintenance and extra longevity are major selling points. That's worth noting because even if the incoming Republican Party go ahead and place import tariffs on EU exports to the US, the cost advantage Windar has is such that it is still the lowest cost supplier of the technology by quite

some margin. Furthermore, any import tariffs pale into insignificance relative to the cost benefits Windar's patented technology offers the operators of wind turbines.



LiDAR-assisted turbine control technology significantly improves energy capture

For instance, a 2MW turbine would produce an additional 158 MWh per annum with a 3 per cent improvement in energy capture. The US Energy Information Administration (EIA) estimates an average wholesale electricity price in the US of $50 per MWh in 2024, so installing Windar's LiDAR-assisted turbine control technology could generate upwards of $8,000 per annum of additional revenue per turbine. Based on an installation cost of $20,000, the payback period for the customer is only two and a half years.

Furthermore, analysis by Dowgate Capital highlights that a 4 per cent improvement in energy production would cut the payback period to only 1.9 years at an energy price of $50 per MWh. Turbines have lifespans of decades, so it's easy to see why increasing numbers of IPPs are looking at retrofitting the technology to their existing fleet to enhance profit, boost return on investment, and extend the lifespan of their assets. The $20,000 cost of Windar's LiDAR is less than half the

$40,000 annual maintenance cost of a 2MW turbine and a fraction of the estimated $4mn installation cost.

LiDAR payback calculation

Turbine power rating	2MW
Annual houses (365*24)	8,760 hours
Capacity factor (percentage time generating)	30%
Annual energy production (AEP)	5,256 MWh
3 per cent improvement in AEP	158 MWh
Electricity price	$50
Annual benefit	$7,884
LiDAR estimated cost	$20,000
Payback period	2.5 years

Source: Windar Photonics

Windar's technology is easy to install and has low maintenance costs

Importantly, the technology offers customers access to real-time information on the performance of their turbines through secure remote monitoring to optimise energy capture. The systems are internet connected, but some IPPs and regulators do not allow internet connections for security reasons. So, to remove this potential barrier to sales, Windar launched its Nexus software platform in February 2024. Specifically, it allows local end-user customers to directly monitor the hardware and turbine performance offline using a LAN connection without the need to have an external connection to Windar's servers in Copenhagen. It's already gaining traction.

In April 2024, the company announced a €1.2mn breakthrough order with a major new turbine operator in the North American market. As well as providing the potential for material further

orders in a region that accounted for a fifth of Windar's revenue in 2023, it marked the first revenue from sales of recurring software related services through the Nexus platform.

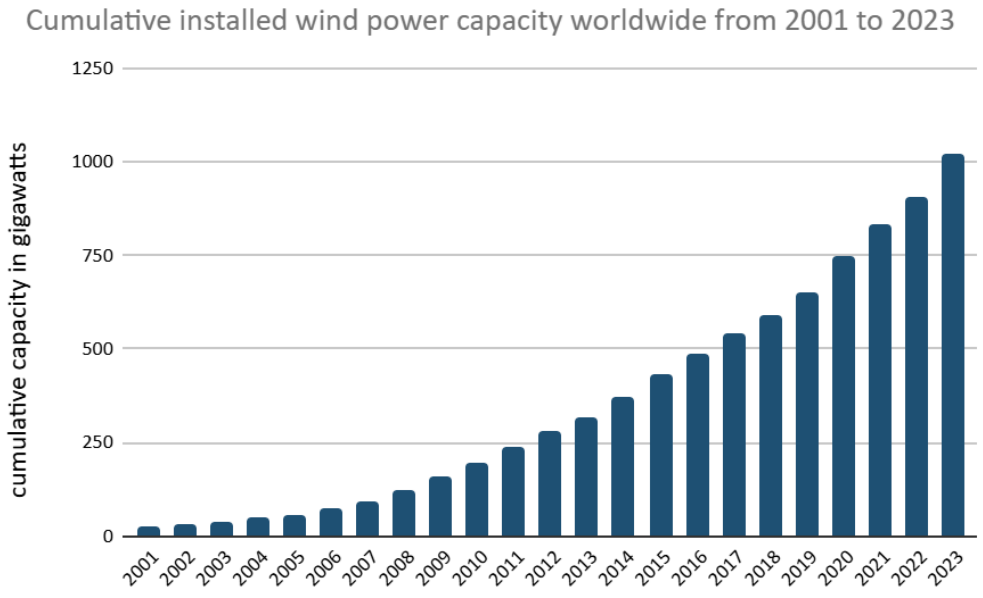
Windar Photonics 2023 revenue by geography

Geographic region	Segmental revenue	Percentage of revenue
Europe	£151,788	3.2%
Americas	£1,008,800	21.2%
Australia	£81,900	1.7%
China	£3,523,996	73.9%
Total revenue	**£4,766,484**	**100.0%**

Source: Windar Photonics 2023 annual report

Market opportunity

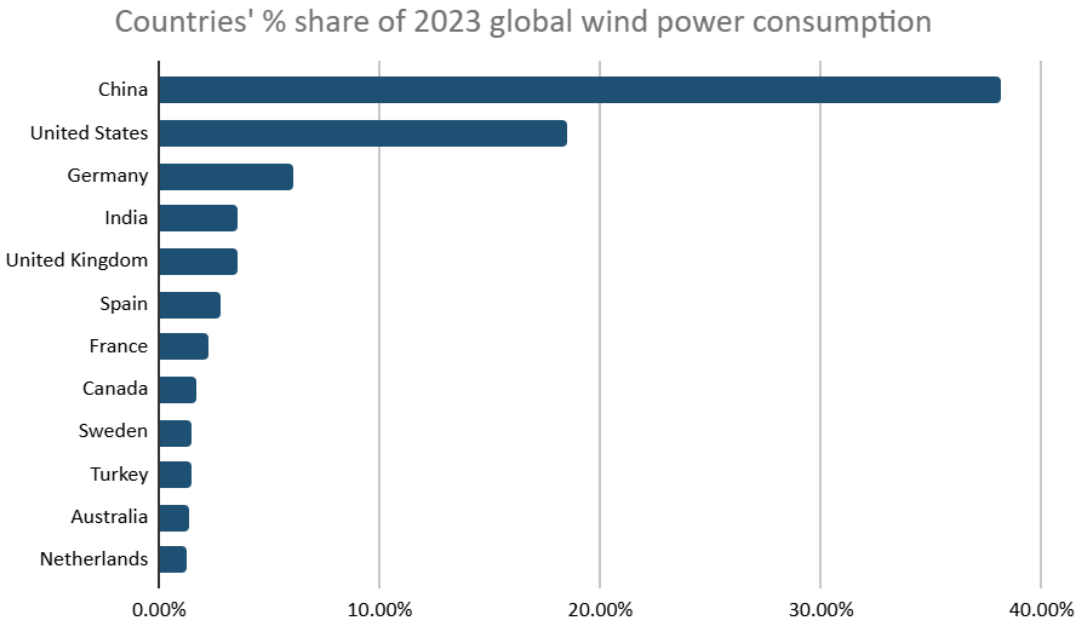
The global wind power market has seen significant growth in the past two decades with global installed capacity rising 98-fold. This has been driven by technology advancement and increasing adoption of renewable energy generation as governments across the world try to reduce carbon emissions. Concerns about climate change have led to tighter regulation, too.



Sources: Statista, GWEC

Last year was a record one for the wind power generation industry. New installed capacity increased 50 per cent year-on-year to 117GW with China setting a record with 75 GW of new

installations, accounting for two-thirds of the global total, according to The Global Wind Energy Council (GWEC). In 2023, cumulative capacity of installed wind power passed 1,000 GW for the first time, rising 13 per cent to 1,021 GW, which prompted analysts at GWEC to upgrade their current year growth forecasts by 10 per cent. They now expect installed wind power capacity to surpass 1,200 GW by the end of 2024.



Sources: Statista, KPMG, Kearney, Energy Institute

China is by far the largest producer of wind power in the world. The country's estimated installed base of 200,000 wind turbines have 474,600 MW of installed capacity, accounting for a global consumption share of 38.1 per cent in 2023. That is more than double the US, which has around 75,000 turbines with installed capacity of 150,465 MW. The US accounted for 18.5 per cent of the world's wind consumption last year, making it the second largest wind power consumer worldwide. Europe has been scaling up its capacity base rapidly, too. Germany, Spain and Denmark are all at the forefront of wind power generation.

Industry experts also highlight that wind turbines are not only becoming larger, but more efficient. To put this into perspective, the average capacity of new wind turbines installed in the US was 3.4 MW in 2023, up from 3.2MW in 2022, and 2.75 MW only four years ago. Larger turbines capture more wind, produce more electricity and are more efficient. As turbines are set higher off the ground and positioned higher on masts, wind speeds increase, too.

Some of the latest turbines have 100 metre blades, so have a span of 200 metres, and hub heights of 160 metres, so they need LiDAR to operate at optimum efficiency given that measurement towers are typically only positioned at 100 metres above the ground. However, Doppler LiDAR are already built into these enormous new wind turbines, hence why Windar focuses on the huge

retrofit market. Specifically, the company is targeting the 340,000 large turbines (1.5 MW or greater) that do not currently use LiDAR technology and the key geographies – China, US, Japan and Australia – where the retrofit opportunity is greatest given the sheer number of installed turbines.

Advances in technology are supportive of the company's growth trajectory. For instance, although the onshore wind power market accounts for more than 90 per cent of global capacity, the development of floating wind turbines is supporting growth of offshore wind farms in deep waters unsuitable for traditional fixed-bottom turbines. At the same time, the explosion in battery storage farms is supporting growth of wind power generation given the intermittency issues faced, so improving consistency of supply. Given newer turbines are more efficient, this is creating an incentive for existing wind farm operators to try to increase the energy capture of their existing installed base. Installing Windar's cost-efficient and innovative LiDAR optimisation systems does exactly that.

In terms of the competitive landscape, the company's two main rivals in the retrofit market are Leosphere, a French subsidiary of Finnish industrial conglomerate Vaisala, and ZX LiDARs, a subsidiary of Fred Olsen, a UK-based group that operates across the renewable energy industry. ZX LiDAR's are exclusively used for performance measurement and testing rather than adjusting and improving turbine performance and efficiency. Although Leosphere's WINDCube nacelle is a similar offering to Windar's WINDEye in the retrofit market and the company also has a data analytics software offering, it appears to be mainly focused on testing and performance measurement rather than improving turbine performance and efficiency.

Moreover, Windar's cost effectiveness, ease of deployment and direct integration of its patented proprietary technology with control systems gives it an edge over its competitors. In any case, the retrofit TAM is huge and all three companies are relatively small, so I don't see either as being threats to Windar.

Production and profits set to ramp up sharply

As with many large projects, the addition of a client and installation of the product for a potential client can entail a long sales cycle, which often involves protracted negotiations and meeting detailed technical specifications and requirements. The length of this process may adversely impact cash flow, increase project costs and ultimately it may not even lead to an order.

Indeed, Windar noted in a recent trading update that such is the demand for the company's technology that its sales resources and capability has been stretched, so it is taking longer to conclude some of the discussions involving substantial orders than previously anticipated. That said, as Windar increases its presence in the market and undertakes an increasing number of projects with IPPs, wind farm operators and original equipment manufacturers (OEMs), the sales cycle risk will be reduced. That's because the non-conversion of any potential client is less of a risk to the business when a company has a much larger client base.

The trading update also revealed that although Windar will report a substantial improvement in revenue, Ebitda and pre-tax profit in 2024, two specific orders with €4mn of revenue are more

likely to slip into the 2025 financial year. One is a follow-on order from an existing US customer and the other relates to a customer related delay in getting the final test results on the client's Senvion turbine platform – the initial results of which are "extremely encouraging."

However, the revenue slippage is expected to be fully booked in 2025. It means that revenue of €6.6mn in 2024 – the mid-point of the €6-7mn range indicated by management in the November trading update – is forecast to more than double to €17.2mn next year after factoring in the growing order book and pipeline of orders that are in the process of being secured. On this basis, analysts at Dowgate Capital expect a step-change in the company's profitability.

Based on a four percentage point improvement in gross margin to 61 per cent, not an unreasonable assumption (given that post pandemic component shortages have eased and the anticipated improvement in pricing as a volume manufacturer selling a high quality product), analysts at Dowgate anticipate gross profit surging 176 per cent from €3.8mn to €10.5mn in 2024. This implies €6.7mn of incremental gross profit from an additional €10.2mn of revenue year-on-year.

Staff costs and expensed research and development costs account for the vast majority of cash overheads. Dowgate's financial models indicate that next year's growth can be achieved with only a modest 13 per cent increase in cash overheads from €3.1mn to €3.5mn. That's because the company already has the facilities in place to deliver annual production of 2,500 units, or more than two and a half times the output needed to support 2025 revenue forecasts.

The plateauing of cash overheads accentuates the drop through of gross profit to Ebitda (earnings before interest, tax, depreciation and amortisation), highlighting the high operational gearing of the business. With the company's annual depreciation and amortisation charge expected to hold steady at €0.2mn, forecast operating profit of €0.5mn in the 2024 financial year could rise 13-fold to €6.8mn in 2025. There is a similar dramatic forecast increase in pre-tax profit from €0.4mn to €6.7mn after factoring in a small finance charge. On this basis, the shares are rated on a forward price/earnings (PE) ratio of 6.3.

Bearing in mind the anticipated step-change in sales, Windar's finances are on a firmer footing after the company raised £4mn at 35p a share in an oversubscribed placing in April 2024. It not only strengthened the company's balance sheet, but is funding the working capital necessary to fulfil contract wins and invest in the sales and marketing capability to deliver the growth opportunity.

Of course, there is execution risk in scaling up production so rapidly. Although the company has the requisite resources and flexibility to produce 2,500 units per annum, there is potential for bottlenecks in testing calibration and there is limited space for inventory. Management has to scale the business in a controlled manner so that costs are kept in check.

Windar Photonics

Profit & Loss

Year to December (€m)	2022A	2023A	2024E	2025E
Revenue	**1.9**	**4.8**	**6.6**	**17.2**
Growth, %	*236*	*157*	*38*	*161*
Organic, %	*236*	*157*	*38*	*161*
Gross profit	0.9	2.4	3.8	10.5
Gross margin, %	*51*	*50*	*57*	*61*
Cash overheads	(1.7)	(2.2)	(3.1)	(3.5)
Adj. EBITDA	**(0.8)**	**0.2**	**0.7**	**7.0**
Adj. EBITDA margin, %	*(42.1)*	*4.6*	*10.3*	*40.9*
D&A	(0.2)	(0.2)	(0.2)	(0.2)
Adj. operating profit	**(1.0)**	**(0.0)**	**0.5**	**6.8**
Adj. operating margin, %	*(51.7)*	*(0.2)*	*7.3*	*39.8*
Finance costs	(0.1)	(0.2)	(0.1)	(0.1)
Adj. PBT	**(1.1)**	**(0.3)**	**0.4**	**6.7**
Adj PBT margin, %	*(60)*	*(5)*	*6*	*39*
Adj PBT growth, %	*(27)*	*(77)*	*(259)*	*1,586*
Normalised tax	0.2	0.2	(0.1)	(0.7)
Normalised tax rate, %	*20*	*67*	*16*	*10*
Adj. PAT	**(0.9)**	**(0.1)**	**0.3**	**6.1**
Exceptional items	(0.2)	(0.1)	(0.0)	0.0
Tax impact	0.0	0.0	0.0	0.0
Reported PAT	(1.1)	(0.2)	0.3	6.1
Wtd avg, shares (m)	56.0	68.4	77.0	81.3
Wtd avg, shares - diluted (m)	56.0	68.4	77.0	81.3
Shares at YE (m)	68.4	68.4	81.3	81.3
Adj. EPS (€ cents)	(1.6)	(0.1)	0.4	7.5
Adj. EPS - diluted (€ cents)	(1.6)	(0.1)	0.4	7.5
Reported EPS (€ cents)	(1.9)	(0.3)	0.4	7.5
Dividends	0.0	0.0	0.0	0.0
Dividend growth, %	n/a	n/a	0.0	0.0

Source: Windar Photonics, Dowgate Capital estimates

That said, if the directors do manage to hit Dowgate's 2025 earnings forecasts, then free cash flow (FCF) generation will strengthen the balance sheet no end. Estimated closing net cash of €1.1mn in 2024 is forecast to increase four-fold to €4.9mn (£4.1mn) by this time next year, buoyed by FCF of €3.9mn (£3.25mn). It implies a bumper FCF yield of 10 per cent on Windar's current market capitalisation of £32.1mn.

Windar Photonics

Cash Flow & Balance Sheet

Year to December (€m)	2022A	2023A	2024E	2025E
Adj. operating profit	(1.0)	(0.0)	0.5	6.8
D&A	0.2	0.2	0.2	0.2
Working capital	0.5	(0.6)	(2.1)	(1.7)
Other (& cash exceptionals)	(0.1)	0.0	0.0	0.0
Cash from operations	**(0.4)**	**(0.4)**	**(1.5)**	**5.3**
Interest - cash	(0.1)	(0.2)	(0.1)	(0.1)
Taxation- cash	0.0	0.0	(0.0)	(0.7)
Other cash	(0.1)	(0.1)	(0.0)	0.0
R&D capitalised	(0.3)	(0.5)	(0.5)	(0.5)
Other capex	(0.1)	(0.3)	(0.1)	(0.2)
Free Cash Flow (Outflow)	**(0.8)**	**(1.2)**	**(2.1)**	**3.9**
Acquisitions / Disposals	0.0	0.0	0.0	0.0
Dividends paid	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0
Cash from (to) equity	2.1	0.0	4.9	0.0
Forex/other	0.0	(0.0)	0.0	0.0
Net cash flow in period	**1.4**	**(1.3)**	**2.3**	**3.3**
Opening net cash (debt)	(1.8)	(0.4)	**(1.6)**	**1.1**
Closing net cash (debt)	**(0.4)**	**(1.6)**	**1.1**	**4.9**
Shareholders funds	0.3	0.3	5.5	11.5

Source: Windar Photonics, Dowgate Capital estimates

If Windar can successfully secure the additional orders to deliver €17.2mn of revenue in 2025 as well as ramping up production to fulfil them, the shares are highly unlikely to be trading on the current implied multiple of 5 times 2025 operating profit to 12-month forward enterprise valuation (EV) by this time next year.

Management team

Non-executive chairman **David George Lis** is an experienced non-executive director within investment and fund management. Lis joined Norwich Union Investment Management in 1997 (later merging to form Aviva Investors), before becoming Head of Equities in 2012 and latterly Chief Investment Officer, Equities and Multi Assets, until his retirement in March 2016.

He is currently chairman of WildLife Group, senior independent director of engineering group Melrose Industries and non-executive director of Dowgate Capital. Lis has previously held the position of senior independent director of Electra Private Equity as well as being a non-executive director of BCA Marketplace and the Multifamily Housing REIT. He was appointed chairman of Windar in October 2023 when the late Johan Black Petersen stepped down from the position he had held for almost six years.

Chief executive officer and founder **Jørgen Korsgaard Jensen** is an expert in optical technology solutions and has been involved in research & development projects in the field of optical technology in collaboration with the Danish Technical University for more than 20 years. Prior to that he held leading positions in international companies with responsibilities for strategy, finance, purchasing and logistics. He is the chief executive and founder of OPDI Technologies A/S, a technology incubator company focused on development of opto/electronic sensors primarily for consumer electronic products. Jensen is also chief executive of optical touch screen technologies group WaveTouch Group.

Non-executive director **Paul Joseph Hodges** had a career in the City of London, spanning 40 years, as an investment analyst, stockbroker and corporate financier. During this period, Hodges held prominent roles at S G Warburg, James Capel, Schroder Securities, Collins Stewart and latterly Cenkos, where he was a founding partner. Holdges now acts as an independent consultant.

Non-executive director **Andrew John Richardson** has a wealth of expertise across a range of organisations including as chairman of Rubicon Partners Industries, chief executive of Arc Specialist Engineering and chief executive of Metalrax Group. He has a strong track record in business transformation and development in quoted, private equity and family office ownership structures.

Non-executive director **Gavin Maxwell Manson** joined the company in February 2024 to take up a position on the board after Johan Black Petersen suddenly passed away. He is an experienced non-executive director and chief financial officer (CFO). Manson is currently CFO of agriculture and engineering group Carr's Group and non-executive director of healthcare group Meallmore.

From 2016 to 2022, he was chief financial and operating officer of Electra Private Equity, having previously held senior finance positions at a number of listed companies including Thomas Cook, Premier Farnell and Merck KGaA.

The directors have significant holdings amounting to 16.5 per cent of the 81.3mn shares in issue and have an average age of 63 years, an indication of the valuable experience they offer. Making capital gains on their holdings far outweighs their remuneration as Petersen doesn't draw a salary and Lis, Hodges and Richardson were paid combined fees of £80,000 in the last financial year. Their financial interests look well aligned with those of outside shareholders.

Major shareholders and directors' holdings

Shareholder	Shares held	Percentage of issued share capital (%)
Jørgen Korsgaard Jensen (chief executive)*	5,649,864	7.0%
Paul Joseph Hodges (non-executive director)	3,545,318	4.4%
Danmarks Tekniske Universitet	2,352,990	2.9%
Milton Holding Horsens A/S	2,119,400	2.6%
Johan Blach Petersen (non-executive and former chairman)	1,882,841	2.3%
David Lis (chairman)	1,826,071	2.2%
Gavin Manson (non-executive director)	428,571	0.5%
Andrew John Richardson (non-executive director)	50,000	0.1%

Source: Windar Photonics 2024 annual report and accounts, London Stock Exchange RNS. *Shares of Jørgen Korsgaard Jensen (chief executive) are held by Pasinika Limited.

The below the radar company lacks an institutional following, so it's reassuring that the insiders backed the oversubscribed placing of 11.3mn shares, at 35p, in April 2024.

In the placing, non-executive chairman David Lis subscribed for 1.43mn shares and non-executive director Gavin Manson subscribed for 0.43mn shares in his maiden purchase. Non-executive director Hodges purchased 295,000 shares at an average price of 42.1p in late Spring 2024 to top up his holding. The company's chief executive Jørgen Korsgaard Jensen holds a 7 per cent stake, so is heavily invested in the company he founded.

The shares currently trade on a relatively tight bid-offer spread of 1p, but even when it widens it's possible to deal well within the official spread in decent volumes. In the past month, bargains as large as 50,000 shares have transacted, although it may pay to deal in smaller lots to build a position.

Target price and valuation

Clearly, there is above average execution risk in scaling up the business next year to the level required to hit analysts' revenue estimates.

However, the near-term pipeline of orders is very encouraging and it's not beyond the realms of possibility that Windar will double annual revenue in 2025 and generate substantial earnings and free cash flow as a result. A 2025 free cash flow yield of 10.1 per cent at the current share price, prospective PE ratio of 6.3 and enterprise valuation to sales multiple of only two times highlight significant potential for a re-rating.

Windar Photonics valuation (at 41p current price)

Year to 31 December	2024E	2025E
Market capitalisation	£32.1mn	£32.1mn
Net cash	€1.1mn (£0.9mn)	€4.9mn (£4.1mn)
Cash per share	1.1p	5.0p
Rolling enterprise valuation	£31.2mn	£28mn
EV/Sales	5.7	2.0
PE ratio	118.5	6.3
Dividend yield	nil	nil
Free cash flow (FCF)	-€2.1mn	€3.9mn
FCF yield	na	10.1%

Source: Dowgate Capital forecasts (12 November 2024)

Even if the share price doubled to 80p the shares would still only be rated on a 2025 PE ratio of 12.8, assuming of course forecasts are met. Although the FCF yield almost halves to 5.3 per cent, it's still attractive for a high growth company as is an enterprise valuation to sales multiple of around 4 times.

Windar Photonics valuation (at 80p price)

Year to 31 December	2024E	2025E
Market capitalisation	£65mn	£65mn
Net cash	€1.1mn (£0.9mn)	€4.9mn (£4.1mn)
Cash per share	1.1p	5.0p
Rolling enterprise valuation	£64.1mn	£60.9mn
EV/Sales	11.7	4.2
PE ratio	240	12.8
Dividend yield	nil	nil
Free cash flow (FCF)	-€2.1mn	€3.9mn
FCF yield	na	5.3%

Source: Dowgate Capital forecasts (12 November 2024)

So, having considered all the risks in the detailed risk assessment below, and taken into account the positive commentary from management in the recent trading update, I initiate coverage with a target price of 80p. Buy.

Risks

Products and services failure. Quality is critical to the company's business solution. While Windar's technology is complete, and extensive security and scalability testing has been carried out, a major system defect due to design mistake or technology failure could impact customer demand. This may lead to adverse press and market commentary damaging the reputation of the company, and require rectification costs and claims against the business. Furthermore, all sales are made with a two-year warranty with the first sale having been made in the fourth quarter of 2013.

So, it's reassuring that no major claims have been made under such warranties, the company has worked with its customers to enhance the installations on site to date, and has not had to initiate a product recall. However, Windar may be exposed to product recalls if its products are faulty although the company has implemented quality control procedures to mitigate this risk.

Reliance on suppliers. Windar develops and assembles its products in its Copenhagen facility, shipping the tested and calibrated units to distributors, IPPs, and OEMs around the world. The manufacture of the high-tech sub-components is outsourced to a range of specialist suppliers (mainly in China) and the in-house assembly process is relatively low skilled with little specialist equipment required. If there was an interruption in the supply, consistency, quality or timely delivery of any of these subcomponents, or an increase in costs above forecast levels, it could adversely affect the company's operating results and harm Windar's reputation.

Other commercial factors. The company is moving from an early business cycle to a higher growth cycle, but it will still be exposed to a concentration of single customers and contracts. In 2023, two customers accounted for 55 per cent of annual revenue. That said, new orders from an enlarged customer base should reduce customer concentration risk, and the company is also focussing on new OEM projects to develop a broader customer base.

Being in an early business cycle the company has been dependent on financing the business through placing of shares in the market to finance annual losses. The board is aware of the risks associated with being dependent on such capital sources and no further issues are anticipated for this purpose following the April 2024 placing that raised £4mn. The focus has always been to arrive at a position where any potential future share placings will be used to fund working capital and not the financing of annual losses. The company's move into profit in 2024 means it has now achieved that inflexion point.

Reliance on key personnel. Windar's future success is substantially dependent on the company's ability to attract, train, motivate and retain key management, commercial and technical personnel

with the necessary skills and experience. The loss of any of these key employees could have an adverse effect on the future of the business.

In mitigation, Windar has a strong board and an impressive senior executive team, led by the original founder for over a decade, that offers a wealth of industry knowledge and connections. The company's team of 27 employees are generally qualified engineers and experienced software developers, committed to its success. However, Windar still needs to expand headcount and infrastructure in both North America and China to support the growing operations in the countries.

Confidentiality. In order to protect its proprietary technology and processes, Windar relies on confidentiality agreements with employees, licensees, independent contractors and other third parties. These agreements may not effectively prevent disclosure of confidential information and may not provide an adequate remedy in the event of disclosure of such information. Costly litigation could be necessary to enforce and determine the scope of the company's proprietary rights, and failure to obtain or maintain trade secret protection could adversely affect the competitive business position.

Small-cap liquidity risk. Windar remains a small company and has relatively low trading volumes, so share price moves can be accentuated. However, the share price has held up well since the company announced a slippage of revenue into 2025, highlighting that shareholders are more focused on the bigger picture and the conversion of a material pipeline of contract opportunities that underpins a step-change in profitability next year.

Foreign currency risk. Windar's exposure to the risk of changes in foreign exchange rates relates primarily to operating activities (when revenue or expense is denominated in a different currency from the company's presentation currency) and its net investments in foreign subsidiaries (translation risk). Management does not consider that at present a hedging programme is required. Raw materials and capital expenditure are primarily in Euros and US dollars whilst the target revenue market is in Asia, Europe and the USA. Windar has significant operations in the following currencies: Euro, Danish Kroner and Chinese Yuan.

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