

HENSOLDT AG

Germany | Industrial Goods & Services | MCap EUR 3,986m

31 July 2024

INITIATION



The brain of the battlefield – Initiated with BUY

What's it all about?

We initiate coverage of HENSOLDT AG with a BUY recommendation and a PT of 44.00 offering an upside potential of 26.9%. Hensoldt, a key player in Europe's defense sector, specializes in defense electronics and sensor solutions. With NATO defense budgets rising amid heightened geopolitical tensions, Hensoldt is poised for substantial growth. European nations like Germany and France are intensifying their defense modernization efforts, presenting robust long-term opportunities. Notably, EU defense expenditures are outpacing those of the US, bolstering Hensoldt's revenue potential.

Upcoming elections across NATO member states could further support defense spending, providing a significant top-line boost. Hensoldt emerges as a compelling investment opportunity among defense stocks, supported by favorable valuations and promising growth prospects compared to the peers.

BUY (na)

Target price	EUR 44.00 (na)
Current price	EUR 34.66
Up/downside	26.9%



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HENSOLDT AG

Germany | Industrial Goods & Services | MCap EUR 3,986m | EV EUR 4,039m

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The brain of the battlefield

Hensoldt: Leading in Defense Sensors. Hensoldt is a prominent producer of radar systems, supplying critical components for the Eurofighter and air shield protection systems in Ukraine. The company boasts a well-diversified product portfolio that includes optics and drone defense systems, which also hold potential for civilian applications.

Diversified Product Portfolio. In addition to radars, Hensoldt is pioneering advancements in digital battlefield solutions, crucial in modern warfare. Its drone defense systems are at the forefront of innovation and are poised for broader market adoption.

Government Support and Market Outlook. With geopolitical tensions escalating, governments worldwide, particularly in Europe – Hensoldt's largest market – are increasing defense spending and GDP ratios. Key EU countries, notably Germany and France, are expected to further bolster defense budgets, benefiting Hensoldt. This contrasts with the US where it's expected that defense spending is growing much slower. The US makes only up to 3% of Hensoldt's regional sales, underlining Hensoldt's good position on the European/German market.

Digital Battlefield Advancements. The evolving digital battlefield necessitates sophisticated sensor integration, a field where Hensoldt is leading. Its leadership in sensor technology positions the company prominently as warfare becomes increasingly digitized and sensors as well as the connection are a deciding factor in current wars.

Valuation and Growth Potential. Hensoldt's valuation is in line with its peers but we expect that they will have higher future growth due to their expertise and increasing relevance of the digitalization of the battlefield where it holds a leading position. We initiate coverage with a BUY rating and a price target of EUR 44.00.

HENSOLDT AG	2021	2022	2023	2024E	2025E	2026E
Sales	1,474	1,707	1,847	2,366	2,785	3,239
Growth yoy	22.1%	15.8%	8.2%	28.1%	17.7%	16.3%
EBITDA	251	267	275	411	478	563
EBIT	125	164	163	246	317	392
Net profit	63	78	54	123	174	223
Net debt (net cash)	420	329	53	585	480	322
Net debt/EBITDA	1.7x	1.2x	0.2x	1.4x	1.0x	0.6x
EPS reported	0.60	0.74	0.51	1.07	1.51	1.94
DPS	0.25	0.30	0.40	0.43	0.56	0.72
Dividend yield	0.7%	0.9%	1.2%	1.2%	1.6%	2.1%
Gross profit margin	22.4%	23.0%	22.5%	25.0%	26.0%	26.0%
EBITDA margin	17.0%	15.6%	14.9%	17.4%	17.2%	17.4%
EBIT margin	8.5%	9.6%	8.8%	10.4%	11.4%	12.1%
ROCE	6.6%	9.1%	7.6%	8.9%	10.9%	13.6%
EV/EBITDA	17.6x	16.2x	14.7x	11.1x	9.3x	7.7x
EV/EBIT	35.2x	26.3x	24.8x	18.6x	14.1x	11.0x
PER	57.8x	46.7x	68.0x	32.4x	23.0x	17.9x
FCF yield	8.2%	6.7%	7.3%	9.8%	7.9%	9.1%

Source: Company data, mwb research



Source: Company data, mwb research

High/low 52 weeks 44.58 / 23.34
Price/Book Ratio 4.5x

Ticker / Symbols

ISIN DE000HAG0005
WKN HAG000
Bloomberg HAG:GR

Changes in estimates

		Sales	EBIT	EPS
2024E	old	2,366	246	1.07
	Δ	0.0%	0.0%	0.0%
2025E	old	2,785	317	1.51
	Δ	0.0%	0.0%	0.0%
2026E	old	3,239	392	1.94
	Δ	0.0%	0.0%	0.0%

Key share data

Number of shares: (in m pcs) 115.00
Book value per share: (in EUR) 7.62
Ø trading vol.: (12 months) 296,646

Major shareholders

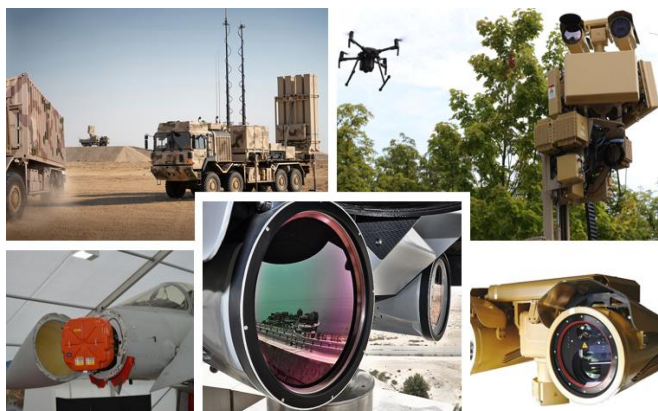
Government of Germany 25.1%
Leonardo SpA 22.8%
Capital Research 5.4%
Free Float 42.2%

Company description

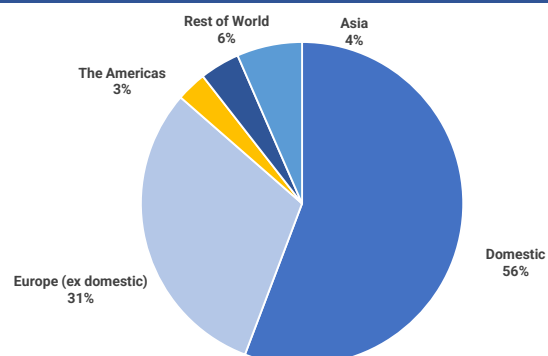
HENSOLDT is a leading German defense company with a strong European market position and global reach. It specializes in sensor solutions for defense and security, and continually expands its cyber portfolio. Key areas include intelligence and reconnaissance sensors, electromagnetic spectrum control, and mission avionics systems. HENSOLDT enhances detection capabilities through sensor and data fusion, aiding in threat mitigation for armed forces and society.

Investment case in six charts

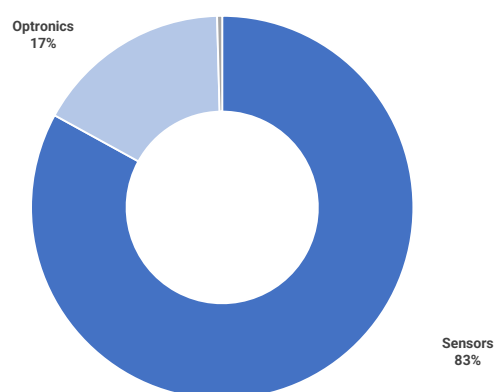
Products & Services



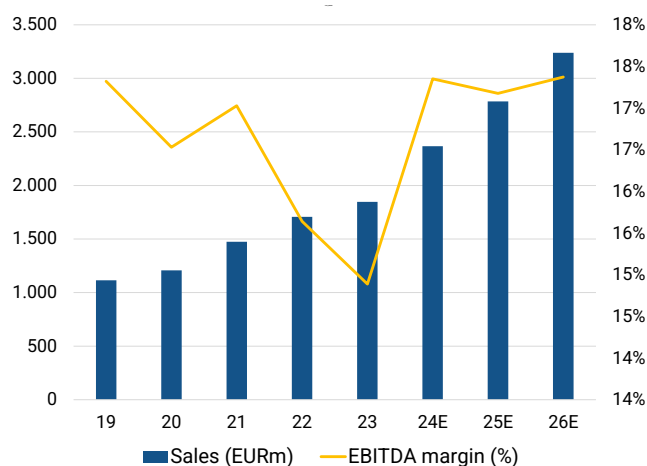
Regional sales split in %



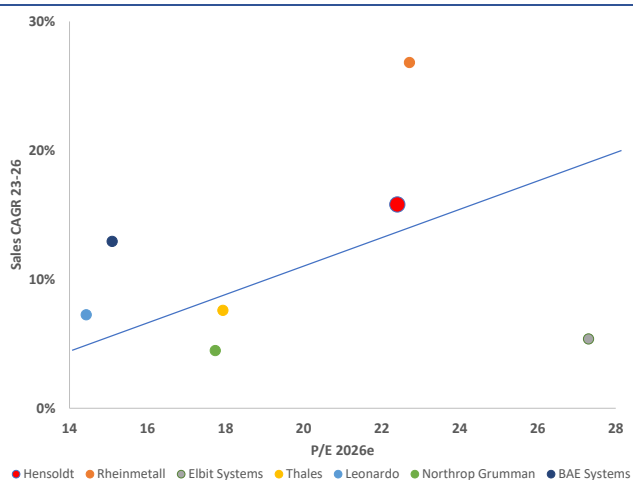
Segmental breakdown in %



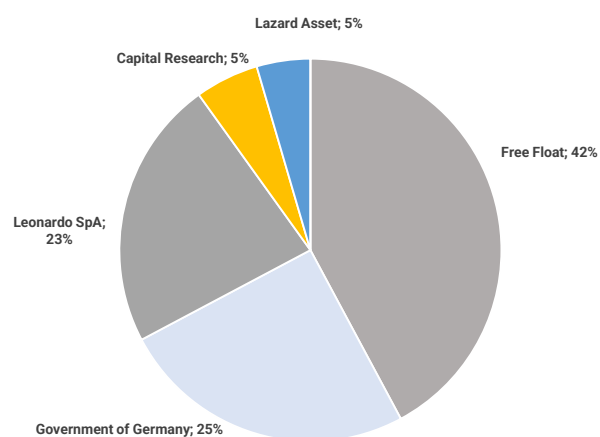
Sales vs. EBITDA margin development



Sales CAGR & P/E



Major Shareholders



Source: Company data; mwb research

Table of content

Investment case in six charts	3
Table of content	4
Company background	5
Quality	11
Competition	12
Growth	17
SWOT analysis	24
Valuation	27
Risk	31
Financials in six charts	32
Financials	33
Conflicts of interest	37
Important disclosures	38
Contacts	39

Company background

Products & services

Hensoldt is a leading German defense and technology company specializing in sensor solutions and mission systems, employing approximately 7,000 people globally. Hensoldt sells its products and solutions to German and international governments, as well as supranational organizations like NATO, and their armed and security forces. These sales occur both directly and indirectly, often through commercial customers or as part of consortiums and joint ventures. Indirect sales typically involve integrating Hensoldt's products into larger systems, such as aircraft, naval vessels (including submarines), and land vehicles (including tanks), for use by government and supranational end-customers.

As a platform-independent provider, Hensoldt supplies products across various platforms, including fighter jets, armored vehicles, and naval vessels, from different manufacturers. Their sensors are used in military systems like the Eurofighter jet (Eurofighter Common Radar System Mk1) and the Leopard 2 main battle tank. They also offer standalone solutions, such as air traffic control (ATC) systems.

Hensoldt operates under two main sector units: *Sensors* and *Optronics*, which will be further explained in the following section.

1) Sensors

The Sensors segment focuses on technical sensor system solutions and is organized into four divisions: Radar & Naval Solutions, Spectrum Dominance & Airborne Solutions, Optronics & Land Solutions, and Services & Aerospace Solutions. These divisions work together to create synergies, particularly in development and production, while Services & Aerospace Solutions primarily operates in aftersales support, and therefore heavily relies on the main business activities of the other divisions.

- **Radar & Naval Solutions (55,1% of new segment orders in 2023):** Develops and manufactures mobile and stationary radar and Identification Friend or Foe (IFF) systems. Applications include surveillance, reconnaissance, civil air traffic control (ATC), and air defense. Systems are deployed on platforms such as the Eurofighter, German Navy frigates (F124 and F126), the US Navy's Littoral Combat Ship, and the IRIS-T SLM air defense system. Additionally, this division provides secure data connection systems for air, sea, and land platforms.
- **Spectrum Dominance & Airborne Solutions (16.9% of new segment orders in 2023):** Includes electronic systems for detecting and analyzing radar and radio signals and jamming systems to protect convoys or vehicles from improvised explosive devices. Expands into defensive cyber solutions and military/civil avionics such as situational awareness systems, mission computers, and flight recorders. Systems are used in Eurofighter and Tornado jets, the Airbus A400M transport aircraft, the airborne signal reconnaissance system PEGASUS, and helicopter models.
- **Optronics & Land Solutions (9.2% of new segment orders in 2023):** Integrates electronic self-protection systems with missile, laser, and radar warning sensors for air, sea, and land platforms. Deployed on various helicopter models and the PUMA infantry fighting vehicle.
- **Services & Aerospace Solutions (18.8% of new segment orders in 2023):** Primarily provides customer support, service, and maintenance throughout the lifecycle of platforms and systems developed by the other divisions. Offers simulation solutions, training, special services, and HENSOLDT Space Solutions, which develops and manufactures components for space-based sensors used in earth observation, weather monitoring, environmental research, and laser communication in space.

Product Examples:

TRML-4D Radars

- **Description:** The TRML-4D is a state-of-the-art radar system designed for air surveillance and target acquisition. It provides 3D tracking of both air and sea targets and can detect and track multiple targets simultaneously.
- **Significance:** This radar system has been particularly crucial in supporting defense operations, such as those for Ukraine. It is a major revenue driver for Hensoldt, reflecting its importance in contemporary military operations.



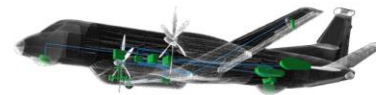
Eurofighter Radars

- **Description:** Hensoldt is involved in the development and upgrading of radar systems for the Eurofighter Typhoon aircraft. These advanced radar systems provide enhanced situational awareness and target tracking capabilities.
- **Significance:** The Eurofighter radar systems are among the key products contributing significantly to Hensoldt's revenue. Their continued development ensures the Eurofighter remains one of the most capable fighter jets in service.



Kalaetron Integral

- **Description:** The Kalaetron Integral is an advanced electronic warfare and signals intelligence system. It integrates electronic support measures (ESM) and electronic attack (EA) capabilities, providing comprehensive situational awareness and self-protection.
- **Significance:** This system is pivotal for modern defense strategies, offering significant advantages in electronic warfare. It has become a crucial component of Hensoldt's product portfolio.



TwlInvis Radar

- **Description:** The TwlInvis radar system is a passive radar technology developed by Hensoldt. Unlike traditional radar systems, TwlInvis does not emit any signals. Instead, it analyzes disturbances in ambient signals to detect and track objects, including stealth aircraft that are designed to be invisible to conventional radar systems. This makes TwlInvis highly effective for air surveillance and target acquisition.
- **Significance:** The TwlInvis system gained significant attention at the ILA 2018 (International Aerospace Exhibition) in Berlin, where it was the only radar system capable of detecting the stealth features of the F-35 aircraft, which remained grounded during the exhibition. This capability underscores Hensoldt's technological leadership and strategic importance in the defense industry. The incident demonstrated TwlInvis's unmatched ability to detect stealth aircraft, leading to increased interest and future contracts for Hensoldt.
- The system's success in detecting the F-35 at ILA 2018, despite significant investments in the aircraft's stealth technology by Lockheed Martin, highlights Hensoldt's innovative approach and why it is expected to secure numerous contracts from 2024 to 2030 and beyond. This technological prowess also justifies the strategic stake held by KfW in Hensoldt.



2) Optronics

The Optronics segment provides system solutions focusing on optronics across three divisions: Optronics & Land Solutions, Radar & Naval Solutions, and Services & Aerospace Solutions. Services & Aerospace Solutions primarily manages the aftersales support.

- **Optronics & Land Solutions (89.9% of new segment orders in 2023):** Offers optronic and optical instruments and precision instruments for military, security, and civil applications across land, sea, and air.
 - Land Applications: Products include telescopic sights, sights, laser rangefinders, night vision devices, and thermal imaging cameras. These products assist snipers and infantry in observation and target acquisition. Includes surveillance and target acquisition devices for armored vehicles.
 - Sea Applications: Products include submarine periscopes, optronic mast systems, and other electro-optical systems.
 - Air Applications: Products include stabilized sensor platforms with image stabilizers for helicopters, airplanes, and drones to support surveillance and target acquisition. Also provides mobile and stationary remote monitoring solutions for security applications and specialized equipment for industrial and aerospace applications.
- **Radar & Naval Solutions (2.6% of new segment orders in 2023):** Provides defense and security solutions and air traffic management systems.
 - Defense and Security Portfolio: Includes Identification Friend or Foe (IFF) systems, cryptographic devices, and tactical point-to-point communication systems.
 - Air Traffic Management Portfolio: Covers the delivery, installation, and maintenance of air traffic control radar, weather radar, navigation, voice communication, and runway lighting systems for military and civil airports.
- **Services & Aerospace Solutions (7.4% of new segment orders in 2023):** Develops, implements, and delivers service solutions for products within the Optronics segment. Ensures the availability and optimal functionality, performance, and operational readiness of products and systems.

Product Examples:

Praetorian Self-Protection System

- **Description:** The Praetorian system is designed to provide advanced defensive capabilities for aircraft. It detects, identifies, and neutralizes incoming threats such as missiles, enhancing the survivability of the aircraft. Hensoldt is one of the key suppliers for the system.
- **Significance:** This system is one of the key revenue drivers for Hensoldt, underscoring its importance in the field of airborne self-protection.
- **Market Impact:** As modern aerial threats become more sophisticated, the demand for effective self-protection systems like Praetorian is expected to rise, bolstering Hensoldt's market position.



ARGOS-II HD

- **Description:** ARGOS-II HD is an airborne observation and targeting system. It provides high-definition imagery for surveillance, reconnaissance, and target acquisition.
- **Significance:** This system enhances situational awareness and operational effectiveness for airborne missions. The increasing need for high-resolution, real-time surveillance in various military and security operations drives the demand for systems like ARGOS-II HD.



HENSOLDT NightOwl

- **Description:** The HENSOLDT NightOwl is a state-of-the-art night vision system designed for a wide range of applications, including surveillance, reconnaissance, and target acquisition in low-light conditions. It provides high-resolution imagery and exceptional performance in total darkness, leveraging advanced image intensification technology.
- **Significance:** NightOwl M enhances situational awareness and operational effectiveness during nighttime operations. By offering clear and detailed imagery in low-light environments, it allows military and security personnel to conduct missions with greater confidence and precision, regardless of lighting conditions.



The recurring revenues, which can be found in both segments benefits from a large installed platform base with long lasting lifecycles, which lead to increasing recurring revenues. In 2019 services accounted for 22% of revenues. Due to the strong increase in sales in the recent years we expect that this number has decreased to 17% as of 2024 but should increase in the years 2027+ again to 24%

With a built-in capacity of more than 70,000 products, these markets offer great potential. Hensoldt has established a network of twelve service stations across five continents to sell spare parts and provide services. Support for the Eurofighter, which has an installed base of more than 650 operational aircraft as of 2024, constituted a significant portion of Hensoldt's Customer Services revenue.

Future Products and Growth Drivers

Spectrum Dominance

- **Description:** Hensoldt is using AI to analyze large datasets for electronic warfare, focusing on identifying potential targets, disrupting enemy communications, and protecting platforms.
- **Significance:** This integration marks a significant advancement in modern warfare capabilities, enhancing operational efficiency and effectiveness, in which the existing capabilities and disciplines of electronic warfare are combined.

Counter Unmanned Aerial Systems (C-UAS)

- **Description** Hensoldt's drone defense and radar systems are designed to counter the growing threat of hostile drones in both military and civilian sectors. These systems provide comprehensive protection for events such as concerts and soccer games, as well as for critical infrastructure and military field camps.
- **Significance:** As drone attacks become more frequent, the need for effective defense systems increases. Hensoldt, a leader in this technology, offers advanced solutions that have been successfully deployed by the German Bundeswehr to safeguard their field operations. The recent acquisition of ESG has expanded Hensoldt's expertise, particularly in providing the Bundeswehr with sophisticated drone protection systems like GUARDION.

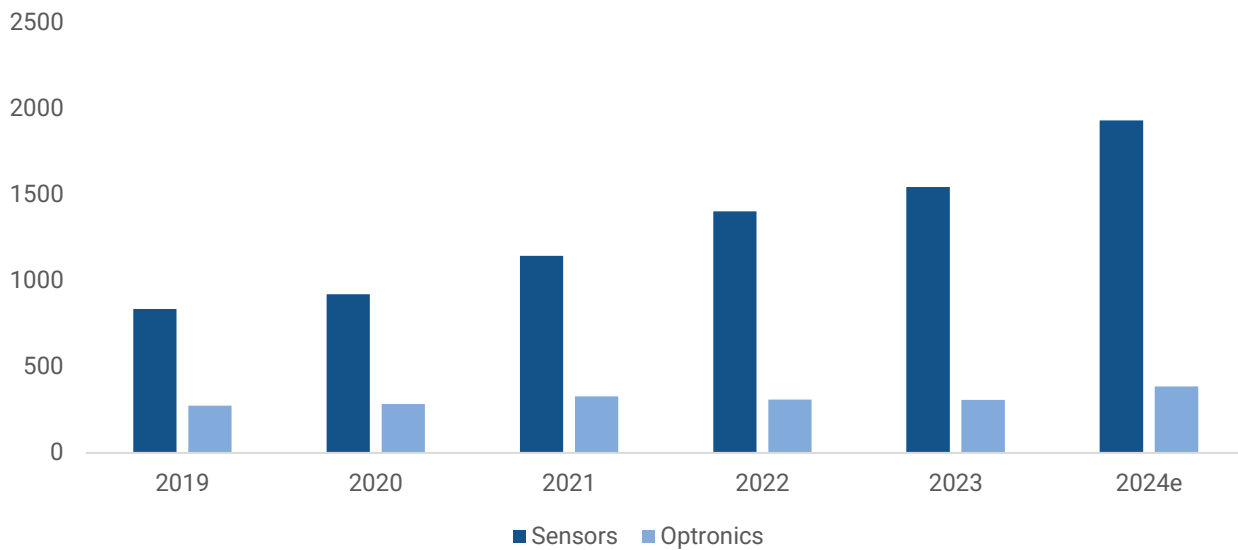


ARGE NNbS (German Short- and Very Short-Range Air Defense System)

- **Description:** In collaboration with Rheinmetall Electronics and Diehl Defence, Hensoldt is developing a new air defense system for Germany, aimed at countering short- and very short-range threats.
- **Significance:** This project is crucial for enhancing Germany's air defense capabilities and reflects Hensoldt's leading role in national defense projects. For Hensoldt, the contract is worth around 284 EUR million.

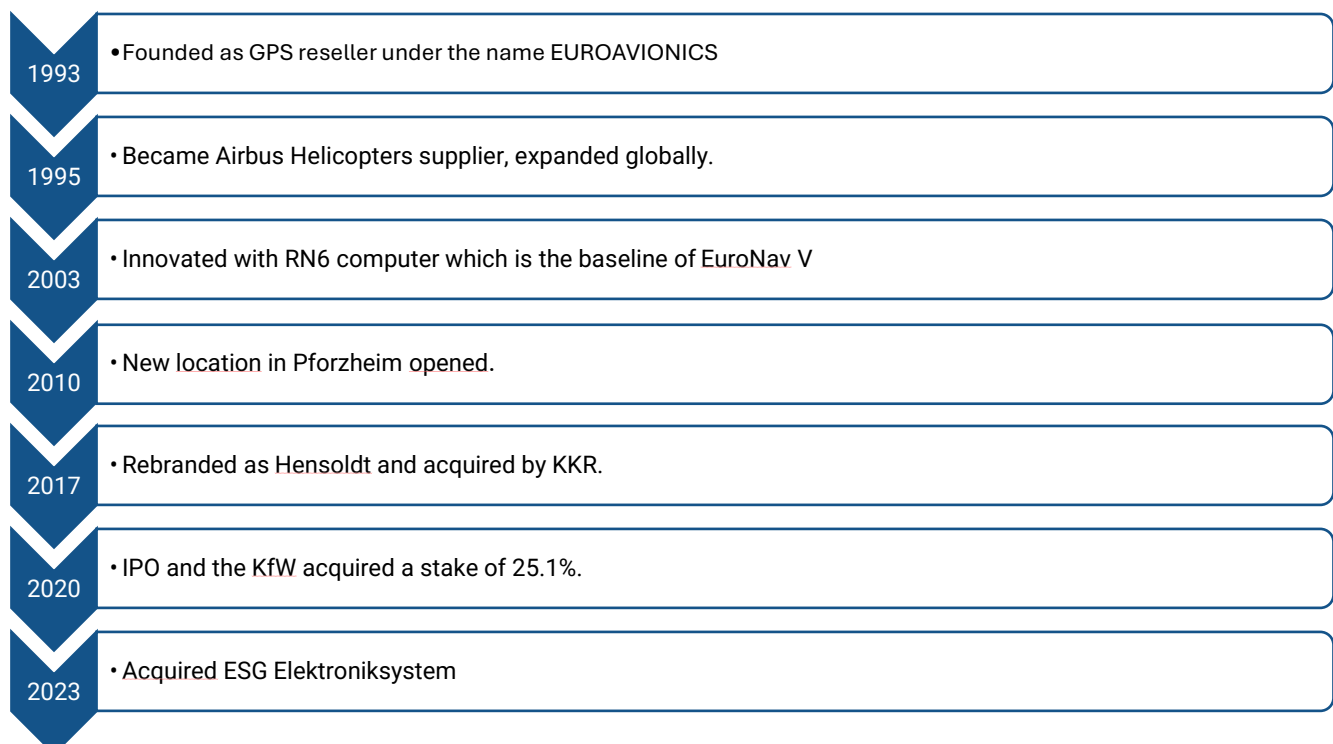


Sector Revenue development in million EUR



Source: Company; mwb Research

History



Management

			
Oliver Dörre Oliver Dörre, CEO and Chairman of Hensoldt since April 2024, previously led Thales Germany and held senior roles in Frequentis AG and the German Air Force.	Christian Ladurner Christian Ladurner, CFO of Hensoldt since July 2022, previously held key financial roles at Hensoldt and Airbus. Ladurner holds an MBA from Henley Business School.	Celia Pelaz Hensoldt COO since Juli 2021, previously Chief Strategy Officer, with extensive leadership roles at Hensoldt and Airbus in defense electronics. She will leave the board with effectiveness of August 2024.	Dr. Lars Immisch Chief HR Officer since October 2022. Previously, he held various leading positions at Airbus and its predecessor companies

Source: Hensoldt; mwb research

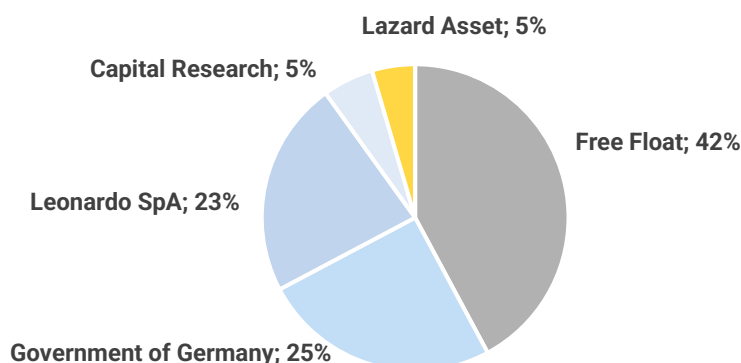
Shareholders

Hensoldt had their IPO in 2020 with KKR holding the majority of shares. KKR has sold all of their shares after the IPO The Federal Republic of Germany increased its strategic holding during this process to 25.1%, which has not changed since then and is executed via the KfW (Kreditanstalt für Wiederaufbau).

Since the IPO, no insider from the management team has sold their stocks; instead, they have purchased additional shares. Since 2021, the (former) management has purchased stocks worth approximately EUR 1.4m. This trend is evident across the German defense industry, including companies like Rheinmetall and Renk, indicating management's belief in the next military cycle.

The majority of the shares are in free float. The largest strategic shareholder is the KfW (Kreditanstalt für Wiederaufbau). In contrast to other European defense companies, Hensoldt is the only one where the government holds a strategic position underlining it's importance. Leonardo, the second largest shareholder, is an Italian defense company, which had decreased their share in the capital increase in 2023 which was due to the ESG acquisition. Capital Research & Management, an American asset manager, is the third largest shareholder with 5%.

Major Shareholders



Source: mwb Research; FactSet

Quality

Customers

In 2019 Hensoldt had three large customers which had a revenue share of 43% but this number decreased to now only two as of 2023 since Hensoldt lost one project where they supplied parts to Airbus. Although the arbitration award was in favor of Hensoldt, this is a sign that there are still other providers and companies like Airbus are not dependent on Hensoldt products.

Due to price control regulations, sales to the German government are limited by the margin they are allowed to include.

Besides German projects, a significant and growing part of the largest current and future defense projects in which Hensoldt participate is undertaken through bi- or multinational cooperation. For example, for the Eurofighter jet they do updates and retrofits to existing aircraft.

Next to direct sales to governments, they also sell to non-government customers, such as prime defense contractors. Typical non-government customers are prime defense contractors, such as Airbus, KMW, Diehl Defence, ThyssenKrupp, Leonardo, and Lockheed Martin. They typically install their products as components into integrated products or onto platforms, such as aircraft, ships, and vehicles, which they then sell on to government end-customers. As an example, the Counter Unmanned Aerial Systems (C-UAS) GUARDION which had been used at the G7 meeting was developed in a consortium of the firms Diehl Defence, ESG (acquired by Hensoldt in 2024) and Rohde & Schwarz.



Strategic Alliances and Partnerships

Hensoldt has been actively forming strategic alliances, underlining its expertise and potential in the defense sector. Notably, Rheinmetall, Diehl, and Hensoldt have signed a collaborative agreement within a working group (ARGE). This partnership is part of a broader trend of increasing joint alliances, which enhances Hensoldt's market position and technological capabilities. Furthermore, it illustrates the need and demand for a closer collaboration between domestic defense companies to get independent of foreign suppliers / customers. Therefore, the former customers are starting to work together, to reveal synergies.

Regional sales split (EURm)	2021	2022	2023	2024E	2025E	2026E
Domestic	861	1,016	1,030	1,319	1,553	1,806
Europe (ex domestic)	330	436	566	725	853	992
The Americas	61	45	56	72	84	98
Asia	58	82	74	95	112	130
Rest of World	165	128	121	155	182	212
Sales	1,474	1,707	1,847	2,366	2,785	3,239

Source: Company data; mwb research

Competition

Hensoldt operates primarily in the defense and security electronics market. They hold significant market shares in Europe, particularly in Germany, and are expanding globally. The increase in market share in other countries is however limited since most of the countries want that these sensible products are produced by domestic firms.

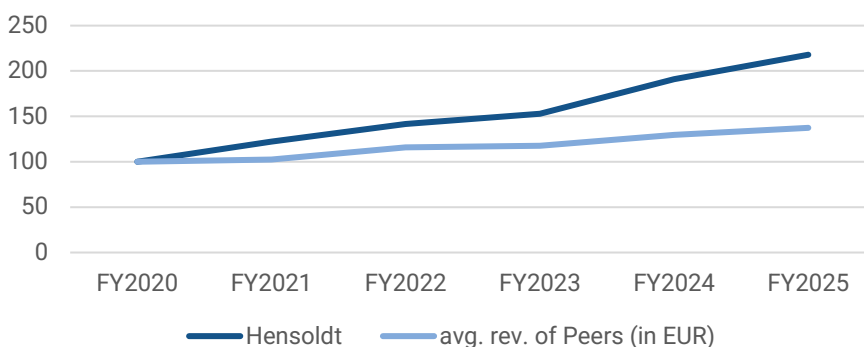
Hensoldt faces several barriers to entry in its market:

- **High Fixed Costs:** Developing and manufacturing advanced defense electronics requires substantial capital investment.
- **Intellectual Property:** Hensoldt holds numerous patents and proprietary technologies, which protect its innovations and provide a competitive edge.
- **Experience:** The company benefits from decades of experience and technical expertise in defense electronics.
- **Access to Supply and Distribution Channels:** Established relationships with suppliers and customers, including government agencies, create barriers for new entrants. Particular the "Bundeswehr" should be mentioned. The acquisition of ESG even increased these relationship and dependencies.
- **Government Restrictions:** Defense markets are heavily regulated, and obtaining the necessary certifications and approvals to operate can be a significant hurdle for new companies.

Market Share Trends

Hensoldt is generally gaining market share, particularly through strategic acquisitions (e.g. ESG) and expanding its product portfolio. The company has been investing in new technologies and entering new markets, which has helped increase its competitive standing, which is one of the reasons why Hensoldt's revenue grows faster than of it's peer group.

Revenue development Hensoldt vs. Peers



Source: mwb Research; FactSet (Peers: RHM; ESLT; LMT; HO; LDO; NOC; RTX)

Copying is difficult due to several reasons:

1. **Technological Complexity:** Hensoldt's products involve highly advanced and specialized technologies that are not easily replicated.
2. **Intellectual Property:** Patents and proprietary technologies protect Hensoldt's innovations.
3. **Experience and Expertise:** Decades of experience and a highly skilled workforce provide a significant competitive advantage.
4. **Regulatory Compliance:** Meeting stringent defense industry regulations and certifications is challenging for new entrants (especially for foreign companies).

Competitors of Hensoldt:

Rheinmetall

- **Products:** Rheinmetall primarily focuses on the defense sectors. In defense, their key products include military vehicles, ammunition, weapons
- **Competition with Hensoldt:** Rheinmetall competes with Hensoldt in electronic solutions and defense systems, though Rheinmetall is more hardware-focused and produces the platform on which the products of Hensoldt are used.
- **Geographical Focus:** Primarily operates in Europe, with significant activities in Germany. They also have a growing presence in international markets, including the US and Asia.



BAE Systems

- **Products:** BAE Systems offers a comprehensive range of defense and aerospace solutions, including advanced electronics, military vehicle systems, naval vessels, munitions, and cybersecurity products. Their portfolio also includes combat aircraft and unmanned systems.
- **Competition with Hensoldt:** BAE Systems competes with Hensoldt in various sectors, particularly in radar systems, electronic warfare, and advanced sensor technologies. They provide critical components for platforms such as the Eurofighter Typhoon and the F-35 Lightning II. BAE's expertise in integrated defense solutions and its strong presence in both air and land domains position it as a formidable competitor. However, Hensoldt's specialization in sensor solutions and its leadership in European defense electronics distinguish it in the market.
- **Geographical Focus:** Headquartered in the UK, BAE Systems has a strong global footprint, with significant operations across Europe, North America, the Middle East, and Asia. This extensive geographical presence enhances its market reach and influence, enabling it to secure diverse and substantial defense contracts worldwide.

The logo for BAE Systems, featuring the words "BAE SYSTEMS" in white, bold, sans-serif capital letters on a red rectangular background.

Elbit Systems

- **Products:** Elbit Systems specializes in defense electronics, including UAVs (unmanned aerial vehicles), communication systems, electronic warfare, and advanced electro-optics.
- **Competition with Hensoldt:** Direct competitor in defense electronics, particularly in electronic warfare and advanced electro-optics. However, Elbit Systems is more dominant in Israel and its financials / value are influenced by the war between Hamas and Israel.
- **Geographical Focus:** Strong presence in Israel and expanding influence in Asia, Europe, and the Americas.



Lockheed Martin

- **Products:** Lockheed Martin offers a wide range of defense and aerospace products, including fighter jets (F-35), missile systems, space systems, and radar technologies.
- **Competition with Hensoldt:** Competes in radar technologies and electronic warfare. However, Lockheed Martin's scale and product diversity are much broader. The F-35 is the Jet from the American Fleet while the Eurofighter is more prominent in the EU. For the F-35 is Northrop Grumman the main supplier of the Radar system. For the Eurofighter Hensoldt. Therefore, Lockheed Martin is more, like Leonardo, a customer
- **Geographical Focus:** Global presence with significant operations in the US and extensive international sales.



Terma

- **Products:** Terma provides aerospace, defense, and security products, focusing on radar systems, electronic warfare, and aircraft self-protection.
- **Competition with Hensoldt:** Competes in niche markets such as radar systems and electronic warfare with Hensoldt. However, Terma is not listed.
- **Geographical Focus:** Based in Denmark, with operations primarily in Europe and North America.

TERMA[®]

Thales

- **Products:** Thales offers a wide range of defense, aerospace, and security products, including communication systems, radar, cybersecurity solutions, and transportation systems. Furthermore, they also provide the Ukraine with a second Air Defense Systems.
- **Competition with Hensoldt:** Competes directly in radar systems, communication systems, and electronic warfare. However, only ~55% of its total sales come from military work and nearly half of the order intake comes from emerging markets (mainly Indonesia/Middle East). The military share is expected to increase based on their current order intake where it has a share of 62%.
- **Geographical Focus:** Strong presence in France and significant operations globally, including Europe, Asia (Indonesia), and the Americas.

THALES

Leonardo

- **Products:** Leonardo produces a broad range of defense and aerospace products, including helicopters, radar systems, and electronic solutions.
- **Competition with Hensoldt:** Direct competitor in radar systems and electronic warfare solutions. However, they focus more on Hardware. Leonardo is a major Shareholder of Hensoldt, holding 23%. Therefore, Leonardo should be seen rather as a strategic Investor and customer than a peer. Furthermore, their revenue from Germany is <25% of total revenue of EUR 10bn. Of that, nearly everything comes from Helicopters (which are equipped with Hensoldt sensors).
- **Geographical Focus:** Headquartered in Italy, with extensive operations in Europe and a strong international presence.

 **LEONARDO**

Northrop Grumman

- **Products:** Northrop Grumman is a leading global aerospace and defense technology company, offering a wide range of products and services, including aircraft, unmanned systems, missile defense, electronic warfare, and radar systems. Notable products that utilize Hensoldt sensors include the E-2 Hawkeye airborne early warning aircraft and the Global Hawk unmanned aerial vehicle.
- **Competition with Hensoldt:** While Northrop Grumman competes with Hensoldt in certain areas such as radar systems and electronic warfare, their focus is more diverse, spanning hardware, software, and integrated systems. Northrop Grumman's extensive product portfolio and capabilities make them a formidable competitor in the defense and aerospace market. They have a US sales share of 88% since they provide for the F-35 the fire control radar and Distributed Aperture System (DAS) & the Communications, Navigation and Identification (CNI) system, which could lead to a possible threat for Hensoldt. Interestingly, the management hadn't bought any stocks since 2014 but sold great amounts. This could, in contrast to Hensoldt's management, be a sign for a greater outlook for Hensoldt, since they benefit from the increasing budgets in the EU.
- **Geographical Focus:** Headquartered in the United States, Northrop Grumman is also present in Europe, with operations and partnerships that extend globally. However, the US make 88% of total sales.

**NORTHROP
GRUMMAN**

RTX (Raytheon Technologies)

- **Products:** RTX provides a wide array of defense and aerospace systems, including missile defense systems, radars, cybersecurity solutions, and precision weapons.
- **Competition with Hensoldt:** Competes in radar systems, missile defense, and electronic warfare. They produce for the F-35 the AN/APG-81 Active Electronically Scanned Array (AESA) radar system, the F-35's DAS, which consists of multiple sensors distributed around the aircraft to provide 360-degree situational awareness, Electronic Warfare (EW) Systems, the CNI System and the Helmet-Mounted Display System (HMDS). This makes them to a serious competitor for Hensoldt. However, Hensoldt is the key supplier for the Eurofighter while RTX is a supplier for the American F-35.
- **Geographical Focus:** Based in the US with a substantial international presence, including Europe, the Middle East, and Asia.



Safran Electronics & Defense

- **Products:** Safran Electronics & Defense provides a comprehensive range of defense and aerospace systems, including avionics, optronics, navigation systems, and drones. Their product portfolio is extensive and serves various applications in both civilian and military sectors.
- **Competition with Hensoldt:** Safran Electronics & Defense competes with Hensoldt primarily in the optronics field, where Safran is a significantly larger player. Although Hensoldt has a smaller market share in optronics, the competition remains relevant. Additionally, Safran is a notable competitor in navigation and avionics systems, further extending their competitive reach.
- **Geographical Focus:** Based in France, Safran Electronics & Defense has a robust international presence, including Europe, North America, Asia, and the Middle East. Their global footprint allows them to serve a diverse range of customers across multiple regions, enhancing their competitive advantage.



Product Overlap:

- **Radar Systems:** Thales, Leonardo, Terma, Northrop Grumman, RTX, BAE
- **Electronic Warfare:** Elbit Systems, Thales, Leonardo, Terma, RTX, BAE
- **Communication Systems:** Thales, Elbit Systems, Leonardo

Main Takeaway:

Due to its expertise in the defense sector, especially in sensors and their increasing importance, we see no real competitors in Europe for Hensoldt. Since military contracts are often awarded domestically, Hensoldt stands out as the only company with this level of expertise in Europe. Furthermore, the ability to connect sensors will give Hensoldt an additional advantage and reinforce its position as a leading tech company in the defense sector. For these reasons, we believe that Hensoldt can trade at higher valuations than its peers, underscored by its strategic relevance as a technology company.

Suppliers

Hensoldt sources a wide range of high-end components and raw materials to meet the technical and performance standards. These components often need to comply with export control regulations, national and international certifications, and special security and confidentiality requirements.

Supplier base for Hensoldt is not heavily concentrated. The company procures relatively low volumes of a diverse array of products, which reduces supplier concentration but also limits procurement strategies due to the small number of qualified suppliers. They aim to maintain competition and have at least two preferred suppliers per component category, but this is not always achievable due to the high specialization. The largest direct supplier accounted for a mid-single-digit percentage share of the total direct purchasing volume, with the remaining direct suppliers in the low single-digit area.

Switching suppliers is challenging for Hensoldt. The process of selecting, approving, and onboarding new suppliers can take up to two years, involving extensive due diligence and quality checks. Furthermore, many of Hensoldt's end-products are customer-certified, requiring additional approvals for any changes in suppliers. This leads to a high dependency for Hensoldt.

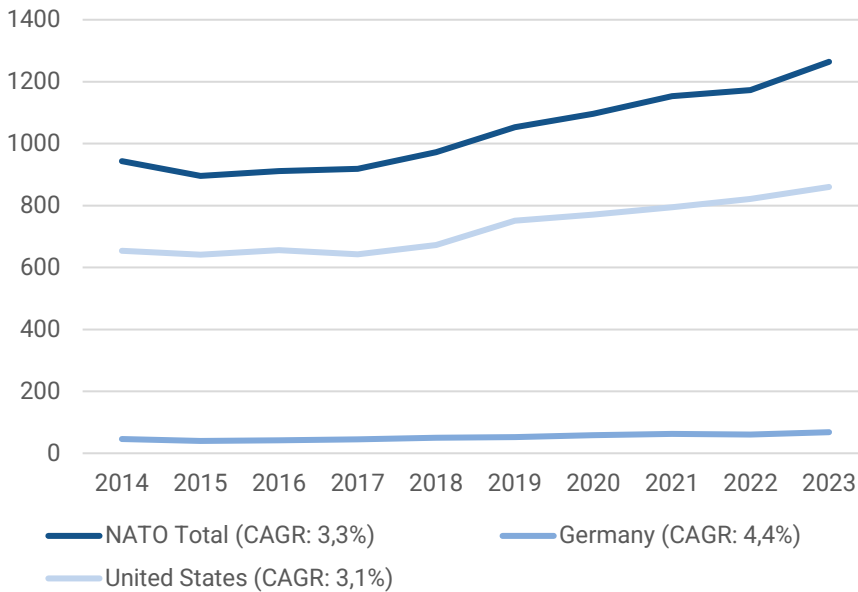
Supplier bargaining power is relatively high. Hensoldt's procurement volumes are small compared to suppliers' total outputs, which weakens Hensoldt's negotiating position on prices and delivery terms. The defense industry's limited number of suppliers for certain critical components exacerbates this issue. Relying on single-source suppliers for some components increases the risk of supply chain disruptions.

Suppliers: Leonardo; Raytheon; Nedinsco; Airbus; ROHDE & SCHWARZ; Glenair; Matrium; Avnet; Bechtle; CHG MERIDIAN; Kappler; Arrow Central Europe; Sofradir; FIMCA

Growth

Regarding NATO's military spending, there has been growth in nearly every member country in 2023. Although the United States had the highest share of NATO's total military expenditure in 2023, its CAGR of 3.1% from 2014 to 2023 is lower than the overall NATO growth rate of 3.3% and Germany's rate of 4.4% during this period.

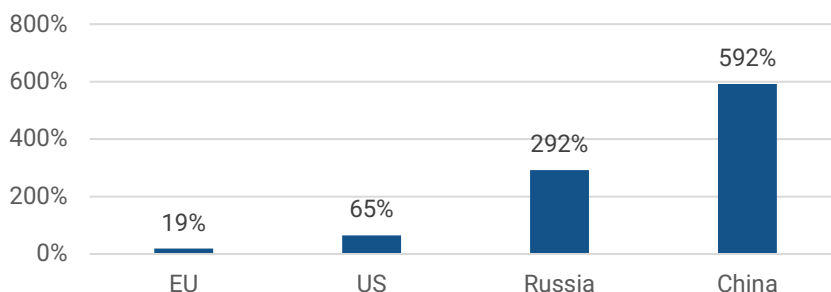
NATO Spending (USD bn)



Source: Nato; mwb Research

Many European countries plan to exceed the 2% GDP defense spending target in response to the Russian threat. For example, Poland already allocates 4% of its GDP to defense. It is expected that European nations will modernize their armed forces across all domains to counter risks in the Baltic and North Seas and to address challenges from ongoing engagements in crisis regions. Furthermore, if Donald Trump wins the next U.S. elections, European countries are likely to further increase their spending, as one of his goals is that all NATO states need to meet the 2% target.

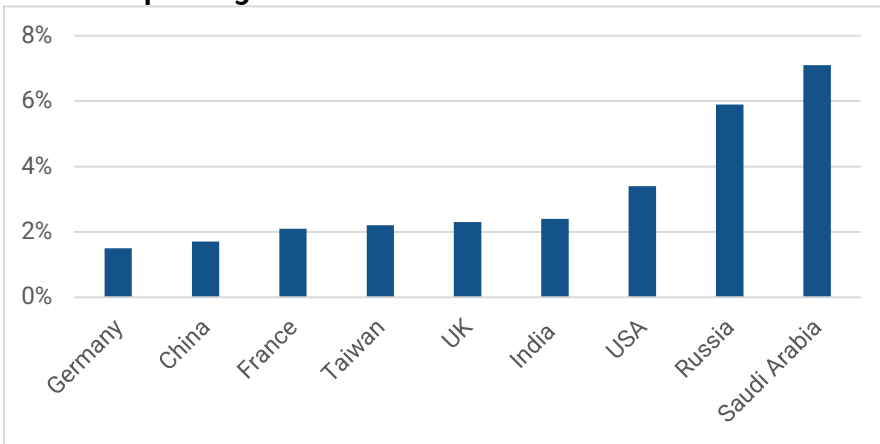
Increase in military spending between 1999-2021



Source: IFO; mwb Research

The graphic above illustrates the underinvestment in the EU's military capabilities. This underinvestment has led to a significant decrease in military equipment. For example, the number of main battle tanks has decreased by 80% between 1992 and 2021, while the number of multiple launch rocket systems fell by 48% (McKinsey). The military assistance provided by the EU to Ukraine has further widened this gap.

Defense spending % of GDP 2023



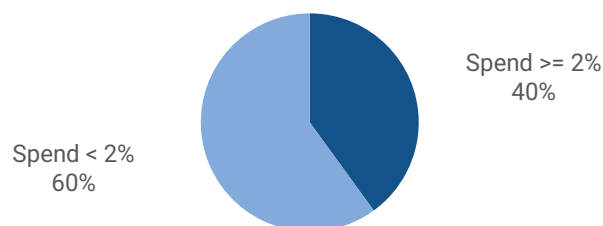
Source: SIPRI; mwb Research

NATO Defense Spending Plans Until 2030

NATO has committed to significant increases in defense spending due to heightened security concerns, particularly following Russia's annexation of Crimea in 2014 and the subsequent invasion of Ukraine in 2022. NATO members have pledged to meet or exceed the 2% GDP spending target on defense. Since the invasion, most NATO members have committed to investing more in defense and reaching the 2% defense-to-GDP target. This target is considered a minimum, with several countries planning substantial increases:

- **Overall Increase:** NATO allies have collectively increased defense budgets by USD 600 bn between 2014 and 2024. Spending is expected to grow further to meet new security challenges (NATO).
- **Long-Term Projections:** By 2028, European NATO members alone could cumulatively spend an additional EUR 700-800 bn on defense. Total European defense spending might reach EUR 500 bn annually by 2028, with the majority of it spent by Germany (McKinsey & Company).

Countries in the EU that reach the 2% NATO target 2023



Source: NATO; mwb Research

The MSC's 2017 European Defense Report revealed that in 2016, European member states used 178 different major weapon systems, compared to only 30 used by the US military. For example, EU member states used 17 different types of main battle tanks (US: 1), 29 types of destroyers/frigates (US: 4), and 20 types of fighter planes (US: 6). This fragmentation has hardly improved and is exacerbated by the proliferation of national requirements and standards. It is expected to decrease in the future.

Given the limited number of military companies in Europe, we anticipate: 1) stronger consolidation in the sector and 2) lower competition. Hensoldt is well-positioned to benefit from this due to its expertise and leading position in its sector, facing only a few competitors.

United States

The United States remains the largest defense spender in NATO, with significant investments planned:

- **Current Spending:** USD 916 bn.
- **Future Investments:** Focus areas include the modernization of nuclear forces, cyber defense, and advanced technologies such as artificial intelligence and hypersonic weapons.
- **Spending Projections:** Although North America remains the world's largest defense spender, contributing roughly 46% of global defense spending from 2018 to 2027, NATO expects the U.S. defense/GDP ratio to decrease from 3.4% to 3.1% by 2028. In contrast, the EU is expected to increase its ratio from 1.6% to 2%, underscoring Hensoldt's strong positioning within the EU.
- **Impact of Political Changes:** If Donald Trump wins the next election, U.S. defense spending is expected to remain flat, but there is a possibility of the U.S. leaving NATO, which would likely increase spending by EU member states. If Joe Biden wins, U.S. defense spending will also remain nearly flat, growing by only about 1% in 2025, much less than the projected growth rates in the EU (Bloomberg) but the US will stay in the NATO.

Germany – the most relevant market

Germany is significantly increasing its defense budget to exceed the 2% GDP target by 2030, leading to substantial increases compared to current levels:

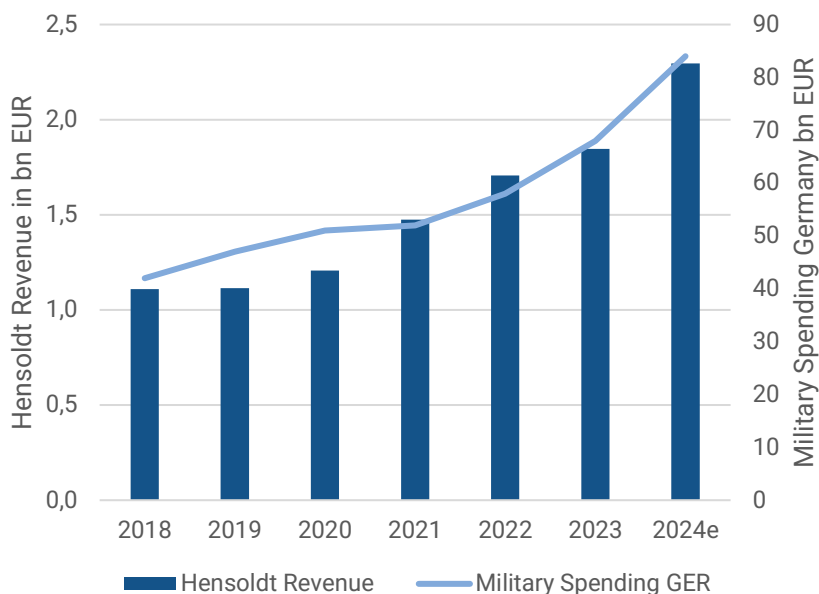
- **Special Fund:** A EUR 100 bn special fund was established for military modernization in 2022, including new aircraft, tanks, and naval vessels. It is expected that this special fund will be exceeded by 2027. Following this period, the Bundeswehr will need new funds. Due to recent increasing tensions, it is expected that this will occur, potentially leading to positive news for Hensoldt and the whole defense industry. Otherwise, there will be a financing gap of ~EUR 56 bn starting in 2028 annually.
- **Annual Spending:** Germany is expected to become one of the top defense spenders in the NATO in the EU, potentially surpassing the UK if current trends continue. In 2023, Germany spend EUR 68 bn.
- **Future Elections:** The next election in Germany will be in 2025. Following current trends, the Christian Democratic Union of Germany (CDU) is expected to be elected and to form the next government. CDU defense politician Roderich Kiesewetter has not ruled out an increase in the special fund to EUR 300 bn, which would mean an increase of more than 400%. Although the probability of reaching EUR 300 bn is low, it shows the ambitions of the next party.
- **Defense Preparedness:** An analysis by the New York Times has shown how unprepared the EU, especially Germany, is in case of a war. Germany would only have munitions for two days, highlighting past underinvestment and the potential for higher future spending. According to Jens Stoltenberg, the waiting time for orders has increased significantly, underpinning the shortage and the intention for new investments in the military.
- **Domestic Military Production:** High dependency on U.S. suppliers is leading to onshoring and an increase in domestic military spending, which is beneficial for Hensoldt.

France

Since the election of President Emmanuel Macron (2017-2024), France's military budget has increased by 46% to EUR 47 bn. This increase supports the priorities set during discussions on the 2024 budget, responding to urgent needs to bolster military capabilities.

- **Military Programming Law (LPM) 2024-2030:** Approved by the French parliament on June 7, 2023, this program aims to modernize the armed forces with a total budget of EUR 414 bn. Annual increments of EUR 3 bn are planned from 2025 to 2027, followed by EUR 4.3bn annually from 2028 onward. These increases could lead to a defense budget of 69 EUR billion by 2030, reflecting a CAGR of ~7%.
- **Future Projections:** Marine Le Pen is expected to win the next election. She advocates withdrawing from NATO and ending defense cooperation with Germany, which could jeopardize key joint projects, including the Future Combat Air System. However, this scenario is unlikely but should be considered. Additionally, Le Pen plans to increase military spending. Her party supports bills that could stabilize predictable revenues, if they don't leave the NATO, which is highly unlikely.
- **Economic Implications:** Widening spreads between German and French 10-year government bonds could lead to downgrades for France by rating agencies, posing financing challenges, followed by less spending for defense investments. Furthermore, current inflation trends may erode approximately 15% of this budget, as it is not indexed for inflation.

Hensoldt Revenue vs. Military Spending Germany in bn EUR



Source: IFO, Hensoldt, mwb Research

Key European Programs

Following decades of underinvestment in defense, catch-up effects are expected to increase over the next decade, particularly in the EU. Europe's annual defense spending is estimated to reach EUR 429 bn by 2027, driven primarily by the Russian invasion of Ukraine. We expect further upside potential due to rising tensions in the Middle East and APAC regions, and upcoming elections that could indicate even higher investments.

Hensoldt is poised to capitalize on several large-scale defense programs in Europe. Notable projects include the Future Combat Air System (FCAS, starting in 2040), the Main Ground Combat System (MGCS), and the Maritime Airborne Warfare System (MAWS, starting in 2030). Hensoldt estimates a potential opportunity worth EUR 14 bn extending beyond 2040 just from these projects. These long-term developments present substantial growth prospects, underlining Hensoldt's strategic importance in the European defense landscape.

APAC

Defense spending in the APAC region remains high and is expected to increase due to tensions between China and Taiwan. China's defense budget has been increasing significantly over the past years, as illustrated above. However, China is not a key customer for Hensoldt since most of Chinese budget is spent domestically in state-owned enterprises. Nevertheless, this impacts neighboring countries like India, Japan, the Republic of Korea (RoK), and Australia, prompting them to modernize their defense capabilities.

China's growing maritime presence challenges U.S. naval dominance, especially in the Western Pacific and South China Sea. With over 340 battle-ready vessels, China's navy surpassed the U.S. in 2020 and plans to expand to 400 ships by 2025 and 440 by 2030 (NATO). China's focus on long-range strike capabilities, like the H-6K bomber with a 3,000 km range, poses a threat to U.S. assets. In response, the U.S. is strengthening regional defenses and alliances, deploying advanced systems in Korea, Japan, and the Philippines. One example here is Taiwan, which have ordered several TRML-4D Radars. According to the management of Hensoldt, Taiwan offers a lot of potential in the future.

Middle East

The Middle East is expected to grow with a CAGR of 3.5% until 2027, reaching a total expenditure of EUR 217 bn (SIPRI). However, the region is increasingly developing its own production capabilities through companies like Elbit Systems, reducing opportunities for Hensoldt. Moreover, strict export controls further constrain business prospects in this area. Nevertheless, they have ordered Eurofighters in 2023 for which Hensoldt produces the radar systems. This is however a very small part of revenue

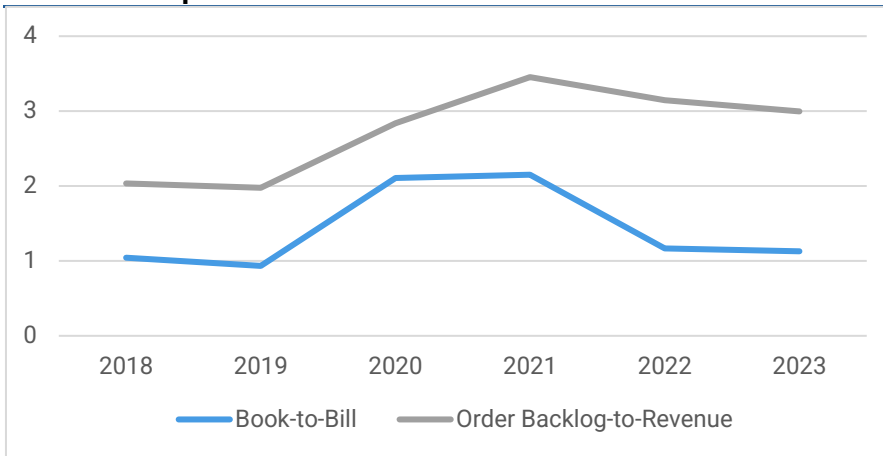
Ukraine

Hensoldt has made a substantial contribution to bolstering Ukraine's air defense capabilities by delivering TRML-4D air defense radars. The agreement entails supplying six radar systems valued at EUR 100-150 m. The announcement was made on May 16, 2023, with deliveries planned for the latter half of 2023 after comprehensive training sessions. This deployment not only enhances Ukraine's air defense capabilities but also demonstrates the effectiveness of Hensoldt's systems, which could open up additional growth opportunities in the future.

Growing Order Backlog

Hensoldt's order backlog has shown impressive growth, increasing from EUR 2.29bn in 2019 to EUR 5.5bn in 2023. This growth reflects the high demand for Hensoldt's products, particularly in the Sensor division, which accounts for approximately 80% of the total backlog. The steady increase in orders underscores the company's strong market position and the robust demand for its advanced sensor technologies. The CAGR is 25% in the order backlog since 2019. For 2024 this number is expected to increase even more, due to high order volume in the Sensor Segment and already high orders in Q1 2024. On a qoq basis, order intake grew by 190% and Order Backlog by 7,5% in Q1 2024.

Order development

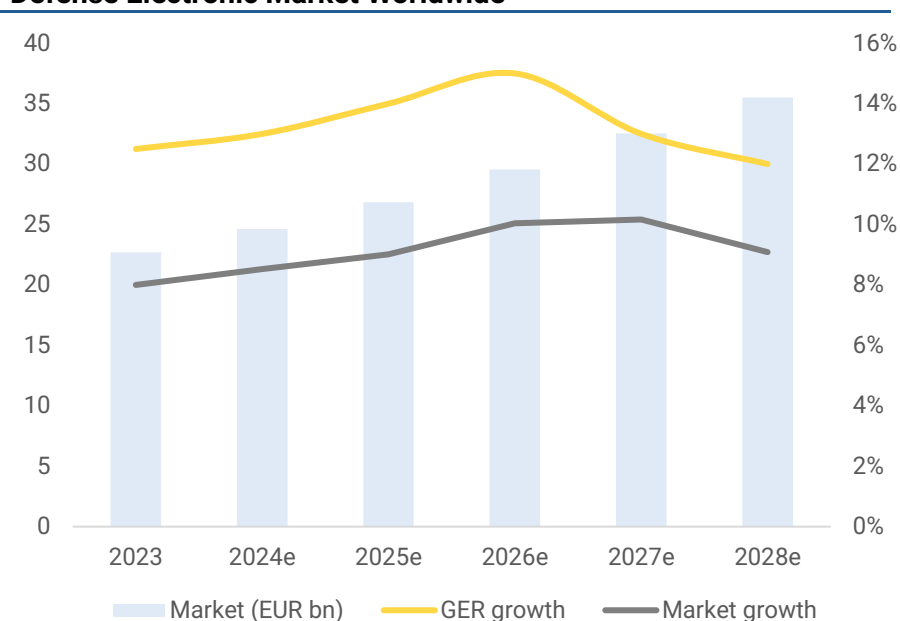


Source: Hensoldt; mwb Research

Market Size

The defense electronics market is one of the fastest-growing sectors in the military industry. Although the international market (excluding the EU) is the largest, the EU market, particularly Germany, is projected to have the highest growth potential, according to Hensoldt and Renaissance Strategic Advisors. The overall market size was approximately EUR 22 bn in 2023 and is expected to grow at a CAGR of about 9% until 2028. However, we anticipate that Germany will experience a significantly faster growth rate, with a CAGR of approximately 14% between 2023 and 2028 due to the factors mentioned in the *Growth* chapter. Given that Hensoldt has increased its market share in Germany through strategic acquisitions and considering the factors mentioned above like onshoring, we are confident that the company will capitalize on this growth and further expand its market share. In 2023, Hensoldt had a market share of ~8%. We expect that the overall market share is expected to grow to 11% until 2028.

Defense Electronic Market Worldwide



Source: mwb Research, Hensoldt

Seasonal Budgetary Impact

A significant portion of budgetary decisions in the defense sector are made in the fourth quarter of the year. As a result, Hensoldt's order intake and backlog, as well as its revenue, are notably impacted during this period. However, the cost base remains relatively stable and less affected by this seasonality. This trend emphasizes the importance of Q4 in Hensoldt's annual financial performance. A study by RSAdvisor indicates that the value of built-in electronic or digital systems as a percentage of total platform value will constantly rise in the future. As a leading provider of sensors and underlying technology, Hensoldt stands to gain significantly from this technological evolution, enhancing its competitive edge in the defense market.

M&A - Acquisition of ESG

Hensoldt's acquisition of ESG (Elektroniksystem- und Logistik-GmbH) is a strategically significant move. The acquisition, approved in March 2024, came at a price of EUR 675m with an earn-out option that could increase the deal's cost by EUR 55m, making the total potential cost EUR 730m. This translates to an EV/EBITA multiple of 10 (incl. cost synergies for 24e). Hensoldt anticipates annual synergy potentials of EUR 20m, which presents substantial opportunities for cross selling and operational integration. Furthermore, we expect Hensoldt's revenue growth rate to increase, as we anticipate that the revenue of ESG will grow more steadily than Hensoldt's revenue. The capital increase to finance the deal was done in December 2023. Previously, ESG was owned by private equity investor Armira, which acquired ESG in 2016. The acquisition is financed by a 450 EURm term loan and a capital increase. This leads to an 2024 net leverage of ~ 2.

ESG brings to Hensoldt a team of 1,380 qualified military software specialists. These are expected to enhance Hensoldt's capabilities, particularly in the areas of digital battlefield solutions and the "battlefield cloud" initiative. ESG has already collaborated with Hensoldt on the Future Combat Air System (FCAS), demonstrating a successful working relationship.

An essential aspect of ESG's current operations is its involvement with the Bundeswehr, specifically through the ZEBEL project. The Koblenz Federal Office for Bundeswehr Equipment, Information Technology and In-Service Support (BAAINBw) recently extended the ZEBEL contract with ESG, ensuring continued support until August 31, 2026. This contract, valued at EUR 51.9m, covers spare parts logistics, transport planning, and execution for Bundeswehr land systems, Air Force equipment, and avionics maintenance facilities. The extension of this contract strengthens Hensoldt's relationship with the Bundeswehr and secures additional recurring revenue streams. Another notable benefit of acquiring ESG is its high cash conversion rate, thanks to its minimal investment requirements.

Name:	Hensoldt	ESG
Employees:	5,500	1,380
Sectors/Products:	Sensor, Radar, Cyber defense	Cyber defense, UAV Systems, IT-Solutions
Customers:	Mainly from GER	Mainly from GER
Revenue EUR m (2023):	1,847	330
EBITDA EUR m (2023):	282	45
EBITDA Margin:	15%	14%

SWOT analysis

Strengths

- **Established Market Presence:** Hensoldt is a well-established player with strong customer connections, underscoring its reliability and expertise.
- **Battlefield Digitization Leader:** As a key player in the digitization of the battlefield, Hensoldt is positioned to benefit significantly from this rapidly growing market over the next decade, as projected by RSAdvisors.
- **Customer Support Solutions:** Hensoldt offers a wide range of customer support solutions, fostering dependency and generating recurring revenues. The share of recurring revenues is rising steadily with a built-in capacity of more than 70,000 devices.
- **Strategic Acquisition:** The acquisition of ESG has strengthened Hensoldt's market position and increased its market share in Germany. Hensoldt is open for further acquisitions
- **R&D Sponsorship:** A substantial part of Hensoldt's R&D efforts is funded by its customers, reducing financial pressure on the company.
- **Exposure to Taiwan:** Hensoldt already secured contracts with Taiwan for their TRML-4D Radar system & submarine periscopes.
- **Secured revenues:** 93% of their programs run until 2029 or even longer

Weaknesses

- **Dividend Policy:** Hensoldt started with a dividend target corridor of 20% of the adjusted net income in 2020, which has risen as planned. However, this could potentially divert funds from R&D investments that could boost future profits, since they currently have a payout corridor of 30%-40%
- **Foreign Investment Restrictions:** The acquisition of substantial interests (>10%) by foreign investors requires government approval, which may limit certain investments and demand for the company's shares.
- **Export Restrictions:** The company faces export limitations to certain countries such as China, Iran, and Russia, which has an impact on revenue and market share.
- **Government Dependency:** Hensoldt's reliance on government budgets for defense spending exposes it to risks like potential debt crises, particularly in France and the U.S., though this risk is lower in Germany, it's domestic market.
- **R&D Growth Concerns:** Although R&D spending has grown with a CAGR of ~6% since 2020, there has been no significant increase in the last two years, possibly indicating a lack of innovation drive. R&D was with 30 EUR million in 2023 (2022) only 1.6% (2.1%) of the revenue. For the time period between 2023-2025 they want to increase it to ~5% of revenue.

Opportunities

- **Non-Defense Markets Expansion:** Hensoldt plans to expand its presence in non-defense markets like aircraft avionics, civil air traffic control systems, border security systems, and counter unmanned aerial vehicle systems, offering potential new revenue streams.
- **Increased NATO Spending:** The company is poised to benefit from increased defense spending by NATO member states. (cf. *Growth*)
- **Domestic Market Growth:** The domestic market for defense is expected to see extraordinary growth, providing further opportunities for Hensoldt compared to the US markets/companies.
- **Drone Prevention Systems:** As a leading supplier of drone prevention systems, Hensoldt is seeing increased demand, particularly for events

like European football matches, concerts and already supplying G7 meetings with drone prevention systems

- **Increases in Defense Budgets:** With the upcoming 2025 German election and potential victory of the Christian Democratic Union of Germany (CDU), defense spending could increase significantly, with discussions about raising the special fund to EUR 300 billion, a potential increase of over 400%, according to the CDU defense commissioner Roderich Kiesewetter. Even though this is a highly unlikely scenario, they also want to excuse defense spending from the debt brake. A potential 2/3 majority is needed for this. Current polls indicate that this will get difficult but illustrates the ambitions and further positive news flow. The next election in France will also be supportive for the defense sector in France since current polls indicate that Le Pen's National Rally (RN) will win which also want to increase military spending.
- Nearly all countries in the EU want to achieve the 2% target for defense spending which will lead to further revenues. Compared to the US which want to decrease spending, Hensoldt is well positioned with only 2% of revenue receiving from the US and the majority from the EU.
- The EU defense sector suffers from past underinvestment. (see *Growth* chapter for more)

Threats

- **Superior Competitor Products:** Competitors like Lockheed Martin's (USA) AN/MPQ-53 radar system (used in Patriot air defense system) could pose a threat due to superior performance in air defense. However, due to onshoring and since EU countries don't want to be dependent on foreign defense equipment we believe the threat is only marginally. Furthermore, it can be expected that the IRIS-System, where Hensoldt radar systems are used, will replace the Patriot-System in the future.
- **No Participation in the Lynx Tank (Rheinmetall):** Hensoldt does not produce parts for the latest Lynx tank by Rheinmetall. This shows strong competition, but it's not critical since Germany, Hensoldt's key market, uses the "Leopard & Puma" tank, where Hensoldt is the main supplier. If Germany orders the Lynx in the future, Hensoldt could potentially become a supplier.
- **Export Control Regulations:** Many of Hensoldt's products are subject to stringent export control regulations, posing compliance challenges and limiting market access.
- **Integrated Product Restrictions:** Products which are incorporated into larger platforms like the Eurofighter jet or Leopard 2 tank face additional restrictions, complicating sales and exports.
- **ITAR Compliance:** Changes in the U.S. International Traffic in Arms Regulations (ITAR) could restrict Hensoldt's market opportunities, requiring approval for certain exports and potentially deterring buyers.
- **U.S. Defense Programs:** U.S.-based defense manufacturers benefit from programs like the Foreign Military Sales (FMS) program, providing them with competitive advantages over foreign suppliers like Hensoldt. Similar programs / incentives can be found in other countries.
- **Technology Transfer Risks:** Initiatives like Saudi Arabia's Vision 2030 aim to develop domestic defense capabilities, posing risks of knowledge loss and requiring Hensoldt to form joint ventures or meet offset obligations.
- **Capital Increase and Shareholding:** Leonardo's decision not to participate in a recent capital increase for the ESG acquisition, despite holding a 25.1% share, reduced its stake to ~23%. This might indicate that Leonardo isn't believing in Hensoldt's products, though the increased free float is a positive outcome.
- **Debt / Household crisis:** Due to the exorbitant and unsustainable high debt levels it can be that countries will try to save money by not increasing their defense spending. This is especially a threat for France with a potential downgrade by S&P and the USA

Growth table (EURm)	2021	2022	2023	2024E	2025E	2026E
Sales	1,474	1,707	1,847	2,366	2,785	3,239
Sales growth	22.1%	15.8%	8.2%	28.1%	17.7%	16.3%
EBITDA	251	267	275	411	478	563
EBITDA margin	17.0%	15.6%	14.9%	17.4%	17.2%	17.4%
EBIT	125	164	163	246	317	392
EBIT margin	8.5%	9.6%	8.8%	10.4%	11.4%	12.1%
Net profit	63	78	54	123	174	223

Source: Company data; mwb research

The following table displays the quarterly performance of **HENSOLDT AG**.

P&L data	Q3 2022	Q4 2022	Q1 2023	Q2 2023	Q3 2023	Q4 2023	Q1 2024	Q2 2024
Sales	418.0	607.0	338.0	388.0	410.0	711.0	329.0	520.0
yoy growth in %	15.0%	-2.8%	18.2%	-2.0%	-1.9%	17.1%	-2.7%	34.0%
Gross profit	90.0	189.0	60.0	64.0	96.0	196.0	59.0	101.0
Gross margin in %	21.5%	31.1%	17.8%	16.5%	23.4%	27.6%	17.9%	19.4%
EBITDA	58.0	150.0	27.0	39.0	61.0	150.0	22.0	57.0
EBITDA margin in %	13.9%	24.7%	8.0%	10.1%	14.9%	21.1%	6.7%	11.0%
EBIT	32.0	125.0	2.0	6.0	33.0	116.0	-7.0	14.0
EBIT margin in %	7.7%	20.6%	0.6%	1.5%	8.0%	16.3%	-2.1%	2.7%
EBT	27.0	116.0	-17.0	4.0	24.0	80.0	-10.0	2.0
taxes paid	12.0	35.0	3.0	0.0	13.0	19.0	6.0	12.0
tax rate in %	44.4%	30.2%	-17.6%	0.0%	54.2%	23.8%	-60.0%	600.0%
net profit	16.0	78.0	-20.0	3.0	13.0	58.0	-15.0	-10.0
yoy growth in %	16.8%	2.5%	25.0%	#DIV/0!	-18.8%	-25.6%	-25.0%	-433.3%
EPS	0.15	0.74	-0.19	0.03	0.12	0.55	-0.13	-0.09

Source: Company data; mwb research

Valuation

DCF Model

The DCF model results in a **fair value of EUR 44.39 per share**:

Top-line growth: We expect HENSOLDT AG to grow revenues at a CAGR of 8.7% between 2024E and 2031E. The long-term growth rate is set at 2.0%.

ROCE. Returns on capital are developing from 8.9% in 2024E to 12.2% in 2031E.

WACC. Starting point is a historical equity beta of 1.20. Unlevering and correcting for mean reversion yields an asset beta of 0.99. Combined with a risk-free rate of 2.0% and an equity risk premium of 6.0% this yields cost of equity of 9.3%. With pre-tax cost of borrowing at 6.5%, a tax rate of 35% and target debt/equity of 0.3 this results in a long-term WACC of 8.0%.

DCF (EURm) (except per share data and beta)	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E	Terminal value
NOPAT	159	208	257	288	287	286	292	304	
Depreciation & amortization	164	161	171	180	188	193	200	201	
Change in working capital	62	31	31	27	10	10	11	11	
Chg. in long-term provisions	90	13	26	35	25	26	27	28	
Capex	-142	-223	-227	-218	-208	-208	-204	-213	
Cash flow	334	190	258	312	302	307	325	331	5,634
Present value	323	171	214	240	215	202	198	187	3,185
WACC	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%

DCF per share derived from		DCF avg. growth and earnings assumptions	
Total present value	4,936	Planning horizon avg. revenue growth (2024E-2031E)	8.7%
Mid-year adj. total present value	5,129	Terminal value growth (2031E - infinity)	2.0%
Net debt / cash at start of year	53	Terminal year ROCE	12.2%
Financial assets	29	Terminal year WACC	8.0%
Provisions and off b/s debt	na		
Equity value	5,105		
No. of shares outstanding	115.0		
Discounted cash flow / share		Terminal WACC derived from	
upside/(downside)	44.39 28.1%	Cost of borrowing (before taxes)	6.5%
		Long-term tax rate	35%
		Equity beta	1.20
		Unlevered beta (industry or company)	0.99
		Target debt / equity	0.3
		Relevered beta	1.22
		Risk-free rate	2.0%
		Equity risk premium	6.0%
		Cost of equity	9.3%
Share price			
	34.66		

Sensitivity analysis DCF								
Change in WACC (%-points)	Long term growth					Share of present value		
		1.0%	1.5%	2.0%	2.5%	3.0%		
	2.0%	31.5	32.5	33.7	35.1	36.7	2024E-2027E	19.2%
	1.0%	35.2	36.6	38.3	40.2	42.4	2028E-2031E	16.3%
	0.0%	40.0	42.0	44.4	47.2	50.5	terminal value	64.5%
	-1.0%	46.5	49.4	52.9	57.2	62.6		
	-2.0%	55.5	60.1	65.8	73.1	82.9		

Source: mwb research

FCF Yield Model

Due to the fact that companies rarely bear sufficient resemblance to peers in terms of geographical exposure, size or competitive strength and in order to adjust for the pitfalls of weak long-term visibility, an Adjusted Free Cash Flow analysis (Adjusted FCF) has been conducted.

The adjusted Free Cash Flow Yield results in a fair value between EUR 31.86 per share based on 2024E and EUR 50.90 per share on 2028E estimates.

The main driver of this model is the level of return available to a controlling investor, influenced by the cost of that investors' capital (opportunity costs) and the purchase price – in this case the enterprise value of the company. Here, the adjusted FCF yield is used as a proxy for the required return and is defined as EBITDA less minority interest, taxes and investments required to maintain existing assets (maintenance capex).

FCF yield in EURm	2024E	2025E	2026E	2027E	2028E
EBITDA	411	478	563	619	626
- Maintenance capex	50	63	84	102	117
- Minorities	1	-2	-2	-2	-2
- tax expenses	67	93	119	129	129
= Adjusted FCF	292	324	362	391	383
Actual Market Cap	4,003	4,003	4,003	4,003	4,003
+ Net debt (cash)	585	480	322	141	-23
+ Pension provisions	0	0	0	0	0
+ Off B/S financing	0	0	0	0	0
- Financial assets	29	29	29	29	29
- Acc. dividend payments	42	92	156	238	328
<i>EV Reconciliations</i>	514	359	137	-126	-381
= Actual EV'	4,517	4,363	4,141	3,877	3,623
Adjusted FCF yield	6.5%	7.4%	8.7%	10.1%	10.6%
base hurdle rate	7.0%	7.0%	7.0%	7.0%	7.0%
ESG adjustment	0.0%	0.0%	0.0%	0.0%	0.0%
adjusted hurdle rate	7.0%	7.0%	7.0%	7.0%	7.0%
Fair EV	4,177	4,633	5,167	5,580	5,472
- <i>EV Reconciliations</i>	514	359	137	-126	-381
Fair Market Cap	3,663	4,274	5,029	5,706	5,853
No. of shares (million)	115	115	115	115	115
Fair value per share in EUR	31.86	37.16	43.73	49.62	50.90
Premium (-) / discount (+)	-8.1%	7.2%	26.2%	43.2%	46.8%

Sensitivity analysis FV						
Adjusted hurdle rate	5.0%	46	53	62	69	70
	6.0%	38	44	51	58	59
	7.0%	32	37	44	50	51
	8.0%	27	32	38	44	45
	9.0%	24	28	34	39	40

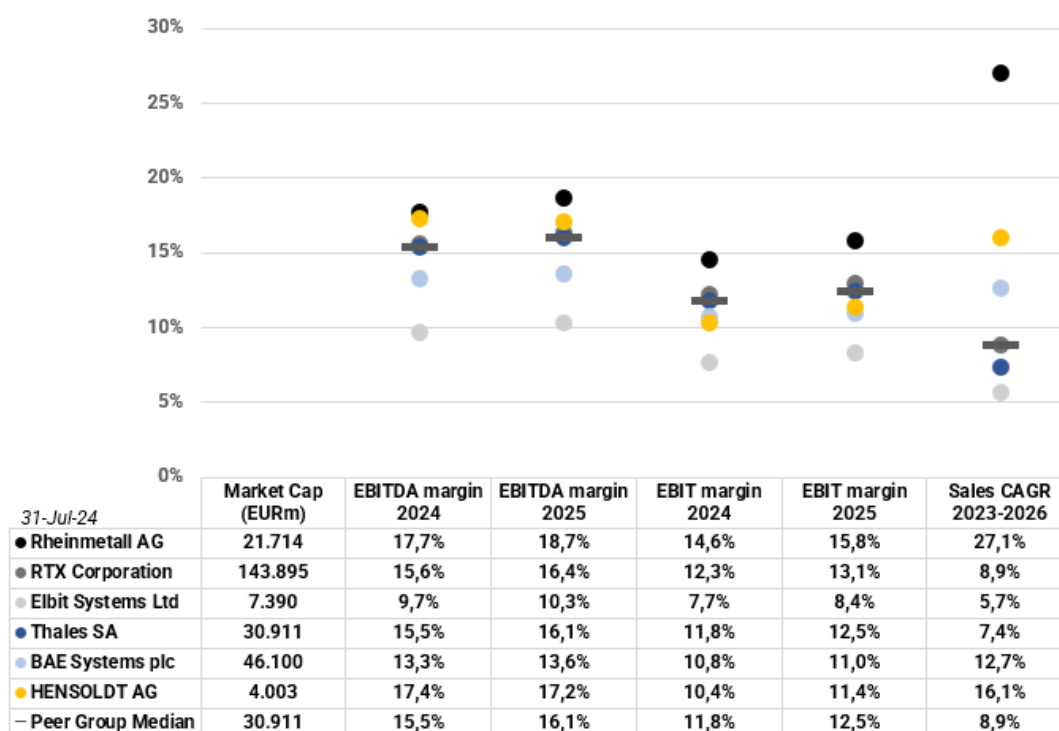
Source: Company data; mwb research

Simply put, the model assumes that investors require companies to generate a minimum return on the investor's purchase price. The required after-tax return equals the model's hurdle rate of 7.0%. Anything less suggests the stock is expensive; anything more suggests the stock is cheap. **ESG adjustments might be applicable. A high score indicates high awareness for environmental, social or governance issues and thus might lower the overall risk an investment in the company might carry. A low score on the contrary might increase the risk of an investment and might therefore trigger a higher required hurdle rate.**

Peer group analysis

A peer group or comparable company (“comps”) analysis is a methodology that calculates a company's relative value – how much it should be worth based on how it compares to other similar companies. Given that **HENSOLDT AG** differs quite significantly in terms of size, focus, financial health and growth trajectory, we regard our peer group analysis merely as a support for other valuation methods. The peer group of HENSOLDT AG consists of the stocks displayed in the below. As of 31 July 2024 the median market cap of the peer group was EUR 30,911m, compared to EUR 3,986m for HENSOLDT AG. In the period under review, the peer group was less profitable than HENSOLDT AG. The expectations for sales growth are lower for the peer group than for HENSOLDT AG.

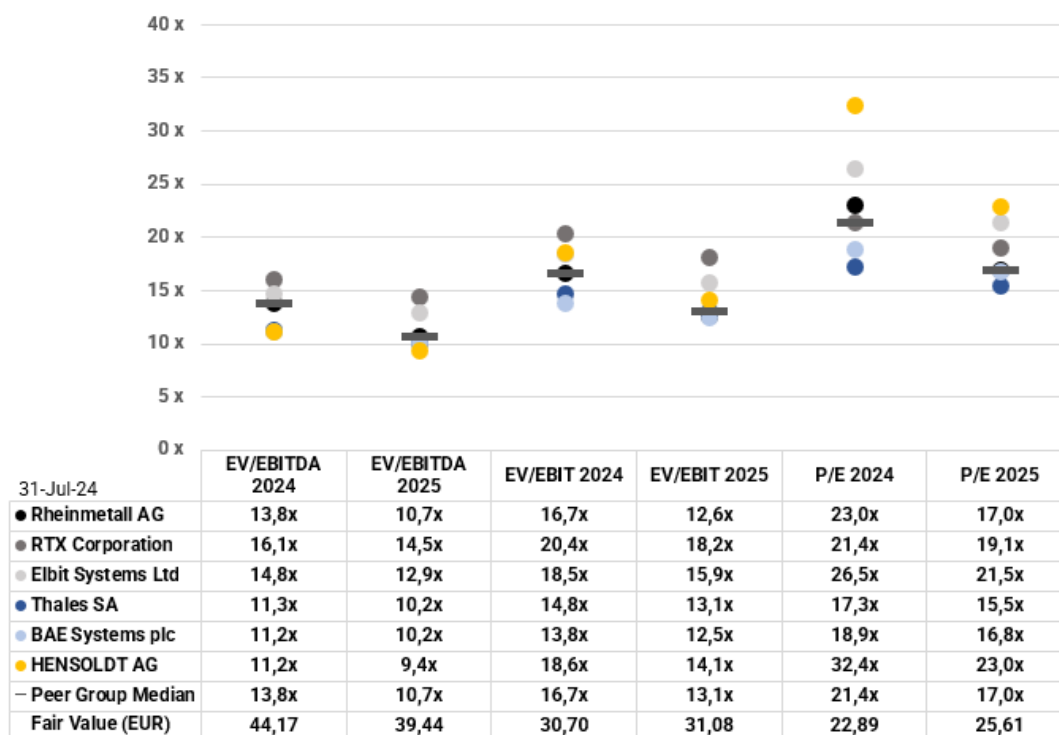
Peer Group – Key data



Source: FactSet, mwb research

Comparable company analysis operates under the assumption that similar companies will have similar valuation multiples. We use the following multiples: EV/EBITDA 2024, EV/EBITDA 2025, EV/EBIT 2024, EV/EBIT 2025, P/E 2024 and P/E 2025. Applying these to HENSOLDT AG results in a range of fair values from EUR 22.89 to EUR 44.17.

Peer Group – Multiples and valuation

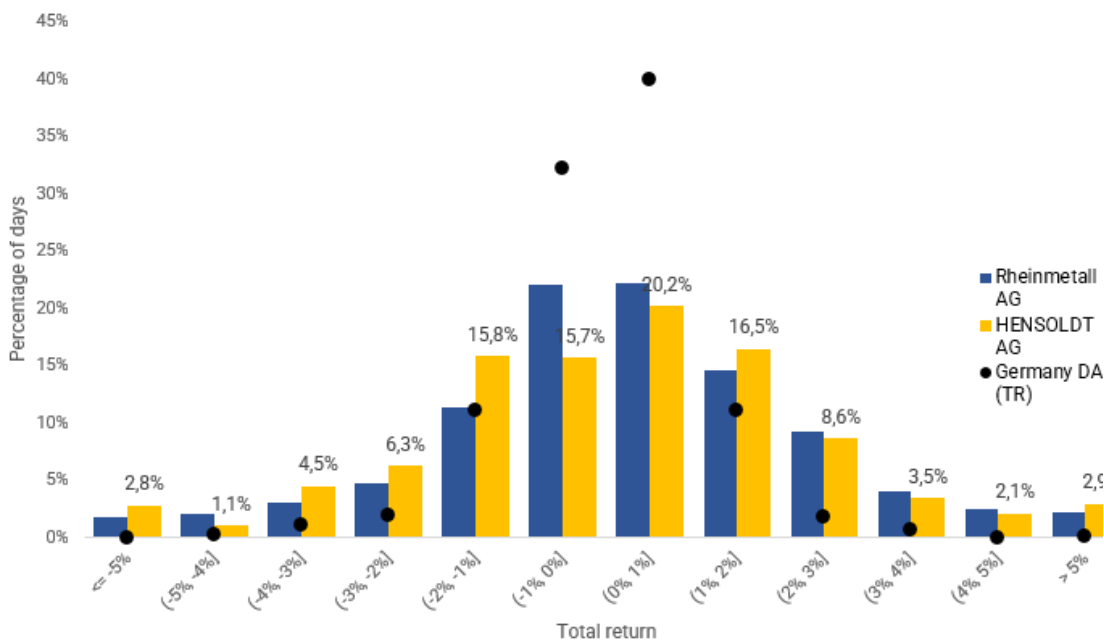


Source: FactSet, mwb research

Risk

The chart displays the distribution of daily returns of HENSOLDT AG over the last 3 years, compared to the same distribution for Rheinmetall AG. We have also included the distribution for the index Germany DAX (TR). The distribution gives a better understanding of risk than measures like volatility, which assume that log returns are normally distributed. In reality, they are skewed (down moves are larger) and have fat tails (large moves occur more often than predicted). Also, volatility treats up and down moves the same, while investors are more worried about down moves. For HENSOLDT AG, the worst day during the past 3 years was 03/03/2022 with a share price decline of -18.5%. The best day was 28/02/2022 when the share price increased by 42.6%.

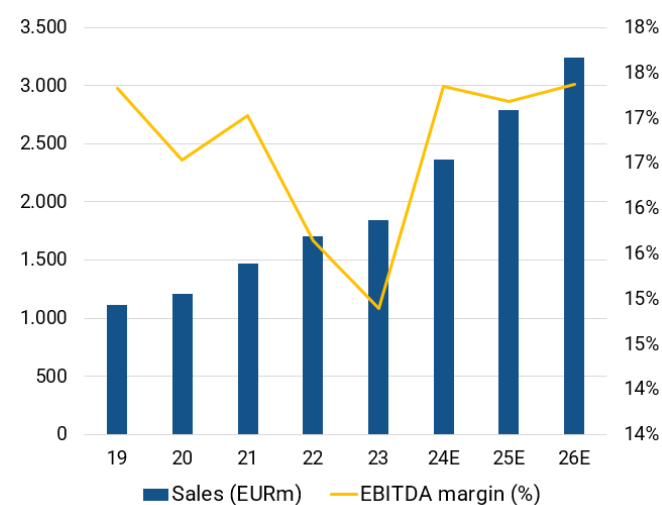
Risk – Daily Returns Distribution (trailing 3 years)



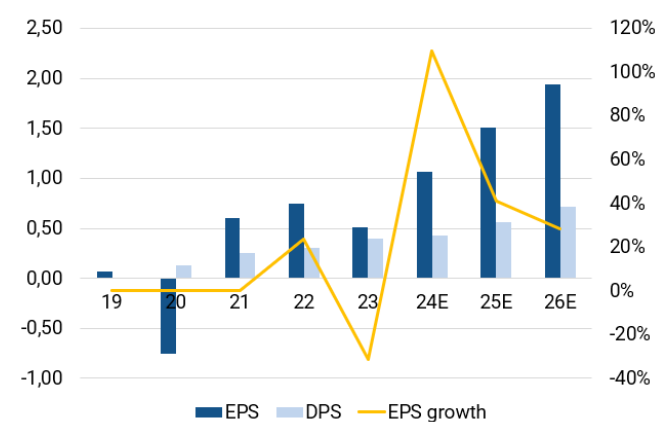
Source: FactSet, mwb research

Financials in six charts

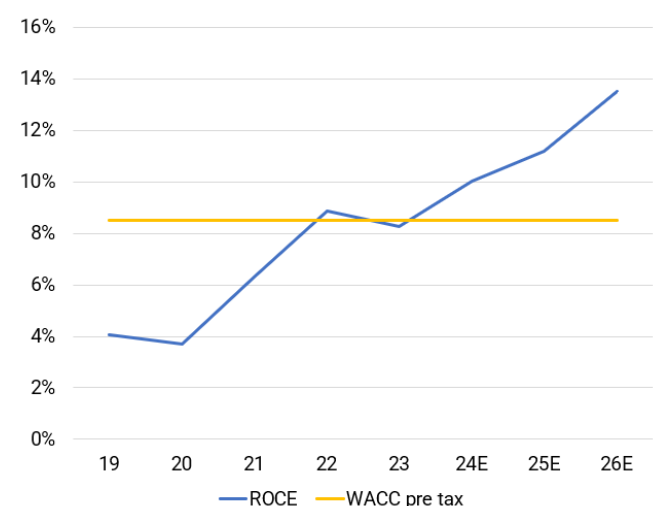
Sales vs. EBITDA margin development



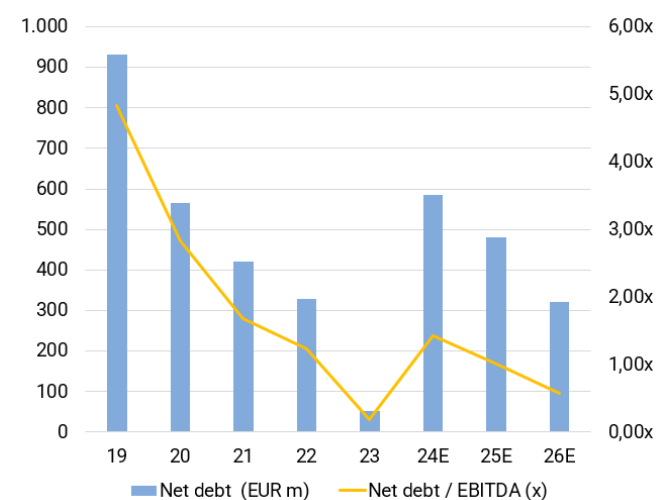
EPS, DPS in EUR & yoy EPS growth



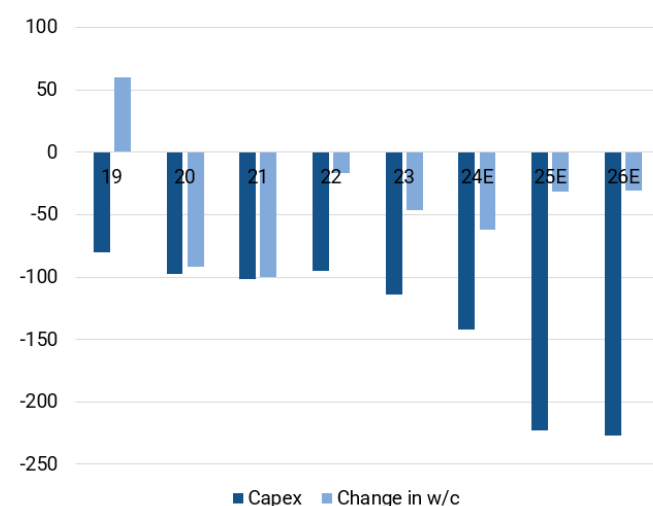
ROCE vs. WACC (pre tax)



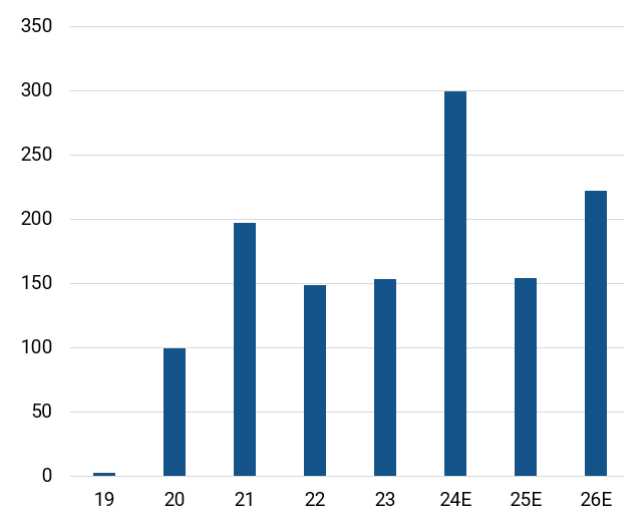
Net debt and net debt/EBITDA



Capex & chgn in w/c requirements in EURm



Free Cash Flow in EURm



Source: Company data; mwb research

Financials

Profit and loss (EURm)	2021	2022	2023	2024E	2025E	2026E
Net sales	1,474	1,707	1,847	2,366	2,785	3,239
Sales growth	22.1%	15.8%	8.2%	28.1%	17.7%	16.3%
Change in finished goods and work-in-process	0	0	0	0	0	0
Total sales	0	0	0	0	0	0
Material expenses	0	0	0	0	0	0
Gross profit	330	393	416	592	724	842
Other operating income	0	0	0	0	0	0
Personnel expenses	0	0	0	0	0	0
Other operating expenses	-8	-6	-6	-2	-3	-3
EBITDA	251	267	275	411	478	563
Depreciation	44	44	48	53	63	84
EBITA	207	223	227	358	415	478
Amortisation of goodwill and intangible assets	82	59	64	112	98	87
EBIT	125	164	163	246	317	392
Financial result	-40	-34	-72	-55	-53	-52
Recurring pretax income from continuing operations	85	130	91	191	264	340
Extraordinary income/loss	0	0	0	0	0	0
Earnings before taxes	85	130	91	191	264	340
Taxes	22	50	35	67	93	119
Net income from continuing operations	63	80	56	124	172	221
Result from discontinued operations (net of tax)	0	0	0	0	0	0
Net income	63	80	56	124	172	221
Minority interest	0	-2	-2	-1	2	2
Net profit (reported)	63	78	54	123	174	223
Average number of shares	105.00	105.00	106.00	115.00	115.00	115.00
EPS reported	0.60	0.74	0.51	1.07	1.51	1.94

Profit and loss (common size)	2021	2022	2023	2024E	2025E	2026E
Net sales	100%	100%	100%	100%	100%	100%
Change in finished goods and work-in-process	0%	0%	0%	0%	0%	0%
Total sales	0%	0%	0%	0%	0%	0%
Material expenses	0%	0%	0%	0%	0%	0%
Gross profit	22%	23%	23%	25%	26%	26%
Other operating income	0%	0%	0%	0%	0%	0%
Personnel expenses	0%	0%	0%	0%	0%	0%
Other operating expenses	-1%	-0%	-0%	-0%	-0%	-0%
EBITDA	17%	16%	15%	17%	17%	17%
Depreciation	3%	3%	3%	2%	2%	3%
EBITA	14%	13%	12%	15%	15%	15%
Amortisation of goodwill and intangible assets	6%	3%	3%	5%	4%	3%
EBIT	8%	10%	9%	10%	11%	12%
Financial result	-3%	-2%	-4%	-2%	-2%	-2%
Recurring pretax income from continuing operations	6%	8%	5%	8%	9%	10%
Extraordinary income/loss	0%	0%	0%	0%	0%	0%
Earnings before taxes	6%	8%	5%	8%	9%	10%
Taxes	1%	3%	2%	3%	3%	4%
Net income from continuing operations	4%	5%	3%	5%	6%	7%
Result from discontinued operations (net of tax)	0%	0%	0%	0%	0%	0%
Net income	4%	5%	3%	5%	6%	7%
Minority interest	0%	-0%	-0%	-0%	0%	0%
Net profit (reported)	4%	5%	3%	5%	6%	7%

Source: Company data; mwb research

Balance sheet (EURm)	2021	2022	2023	2024E	2025E	2026E
Intangible assets (excl. Goodwill)	385	384	380	611	541	487
Goodwill	658	658	658	1,128	1,128	1,128
Property, plant and equipment	249	261	329	395	526	637
Financial assets	24	26	29	29	29	29
FIXED ASSETS	1,316	1,329	1,396	2,162	2,224	2,280
Inventories	444	516	625	690	802	932
Accounts receivable	479	505	578	713	839	976
Other current assets	30	54	62	62	62	62
Liquid assets	529	460	802	735	840	798
Deferred taxes	11	6	9	9	9	9
Deferred charges and prepaid expenses	147	109	88	118	139	162
CURRENT ASSETS	1,640	1,650	2,164	2,328	2,691	2,939
TOTAL ASSETS	2,956	2,979	3,560	4,490	4,915	5,219
SHAREHOLDERS EQUITY	406	604	808	890	1,013	1,169
MINORITY INTEREST	11	13	16	16	16	16
Long-term debt	761	759	812	1,300	1,300	420
Provisions for pensions and similar obligations	0	0	0	0	0	0
Other provisions	523	400	454	544	557	583
Non-current liabilities	1,284	1,159	1,266	1,844	1,857	1,003
short-term liabilities to banks	188	30	43	20	20	700
Accounts payable	269	379	457	486	565	657
Advance payments received on orders	0	0	0	0	0	0
Other liabilities (incl. from lease and rental contracts)	787	775	931	1,183	1,392	1,619
Deferred taxes	11	19	39	39	39	39
Deferred income	0	0	0	12	14	16
Current liabilities	1,255	1,203	1,470	1,740	2,030	3,031
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	2,956	2,979	3,560	4,490	4,915	5,219

Balance sheet (common size)	2021	2022	2023	2024E	2025E	2026E
Intangible assets (excl. Goodwill)	13%	13%	11%	14%	11%	9%
Goodwill	22%	22%	18%	25%	23%	22%
Property, plant and equipment	8%	9%	9%	9%	11%	12%
Financial assets	1%	1%	1%	1%	1%	1%
FIXED ASSETS	45%	45%	39%	48%	45%	44%
Inventories	15%	17%	18%	15%	16%	18%
Accounts receivable	16%	17%	16%	16%	17%	19%
Other current assets	1%	2%	2%	1%	1%	1%
Liquid assets	18%	15%	23%	16%	17%	15%
Deferred taxes	0%	0%	0%	0%	0%	0%
Deferred charges and prepaid expenses	5%	4%	2%	3%	3%	3%
CURRENT ASSETS	55%	55%	61%	52%	55%	56%
TOTAL ASSETS	100%	100%	100%	100%	100%	100%
SHAREHOLDERS EQUITY	14%	20%	23%	20%	21%	22%
MINORITY INTEREST	0%	0%	0%	0%	0%	0%
Long-term debt	26%	25%	23%	29%	26%	8%
Provisions for pensions and similar obligations	0%	0%	0%	0%	0%	0%
Other provisions	18%	13%	13%	12%	11%	11%
Non-current liabilities	43%	39%	36%	41%	38%	19%
short-term liabilities to banks	6%	1%	1%	0%	0%	13%
Accounts payable	9%	13%	13%	11%	11%	13%
Advance payments received on orders	0%	0%	0%	0%	0%	0%
Other liabilities (incl. from lease and rental contracts)	27%	26%	26%	26%	28%	31%
Deferred taxes	0%	1%	1%	1%	1%	1%
Deferred income	0%	0%	0%	0%	0%	0%
Current liabilities	42%	40%	41%	39%	41%	58%
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	100%	100%	100%	100%	100%	100%

Source: Company data; mwb research

Cash flow statement (EURm)	2021	2022	2023	2024E	2025E	2026E
Net profit/loss	63	80	56	124	172	221
Depreciation of fixed assets (incl. leases)	44	44	48	53	63	84
Amortisation of goodwill	0	0	0	0	0	0
Amortisation of intangible assets	82	59	64	112	98	87
Others	10	44	53	90	13	26
Cash flow from operations before changes in w/c	199	227	221	379	346	418
Increase/decrease in inventory	-44	-75	-128	-65	-111	-131
Increase/decrease in accounts receivable	89	-38	-1	-135	-126	-137
Increase/decrease in accounts payable	107	110	78	29	78	92
Increase/decrease in other w/c positions	-52	20	97	234	191	207
Increase/decrease in working capital	100	17	46	62	31	31
Cash flow from operating activities	299	244	267	441	377	449
CAPEX	-102	-95	-114	-142	-223	-227
Payments for acquisitions	-12	-1	-1	-789	0	0
Financial investments	-6	-5	-8	0	0	0
Income from asset disposals	3	0	1	0	0	0
Cash flow from investing activities	-117	-101	-122	-931	-223	-227
Cash flow before financing	182	143	145	-490	154	222
Increase/decrease in debt position	-180	-150	0	465	0	-200
Purchase of own shares	0	0	0	0	0	0
Capital measures	-3	0	238	0	0	0
Dividends paid	-14	-26	-32	-42	-49	-64
Others	-100	-38	-9	0	0	0
Effects of exchange rate changes on cash	-1	2	0	0	0	0
Cash flow from financing activities	-298	-212	197	423	-49	-264
Increase/decrease in liquid assets	-116	-69	342	-67	105	-42
Liquid assets at end of period	529	460	802	735	840	798

Source: Company data; mwb research

Regional sales split (EURm)	2021	2022	2023	2024E	2025E	2026E
Domestic	861	1,016	1,030	1,319	1,553	1,806
Europe (ex domestic)	330	436	566	725	853	992
The Americas	61	45	56	72	84	98
Asia	58	82	74	95	112	130
Rest of World	165	128	121	155	182	212
Total sales	1,474	1,707	1,847	2,366	2,785	3,239

Regional sales split (common size)	2021	2022	2023	2024E	2025E	2026E
Domestic	58.4%	59.5%	55.8%	55.8%	55.8%	55.8%
Europe (ex domestic)	22.4%	25.5%	30.6%	30.6%	30.6%	30.6%
The Americas	4.1%	2.6%	3.0%	3.0%	3.0%	3.0%
Asia	3.9%	4.8%	4.0%	4.0%	4.0%	4.0%
Rest of World	11.2%	7.5%	6.6%	6.6%	6.6%	6.6%
Total sales	100%	100%	100%	100%	100%	100%

Source: Company data; mwb research

Ratios	2021	2022	2023	2024E	2025E	2026E
Per share data						
Earnings per share reported	0.60	0.74	0.51	1.07	1.51	1.94
Cash flow per share	2.85	2.32	2.52	3.40	2.73	3.17
Book value per share	3.87	5.75	7.62	7.74	8.80	10.17
Dividend per share	0.25	0.30	0.40	0.43	0.56	0.72
Valuation						
P/E	57.8x	46.7x	68.0x	32.4x	23.0x	17.9x
P/CF	12.2x	14.9x	13.8x	10.2x	12.7x	10.9x
P/BV	9.0x	6.0x	4.5x	4.5x	3.9x	3.4x
Dividend yield (%)	0.7%	0.9%	1.2%	1.2%	1.6%	2.1%
FCF yield (%)	8.2%	6.7%	7.3%	9.8%	7.9%	9.1%
EV/Sales	3.0x	2.5x	2.2x	1.9x	1.6x	1.3x
EV/EBITDA	17.6x	16.2x	14.7x	11.1x	9.3x	7.7x
EV/EBIT	35.2x	26.3x	24.8x	18.6x	14.1x	11.0x
Income statement (EURm)						
Sales	1,474	1,707	1,847	2,366	2,785	3,239
yoy chg in %	22.1%	15.8%	8.2%	28.1%	17.7%	16.3%
Gross profit	330	393	416	592	724	842
Gross margin in %	22.4%	23.0%	22.5%	25.0%	26.0%	26.0%
EBITDA	251	267	275	411	478	563
EBITDA margin in %	17.0%	15.6%	14.9%	17.4%	17.2%	17.4%
EBIT	125	164	163	246	317	392
EBIT margin in %	8.5%	9.6%	8.8%	10.4%	11.4%	12.1%
Net profit	63	78	54	123	174	223
Cash flow statement (EURm)						
CF from operations	299	244	267	441	377	449
Capex	-102	-95	-114	-142	-223	-227
Maintenance Capex	0	0	0	50	63	84
Free cash flow	197	149	153	299	154	222
Balance sheet (EURm)						
Intangible assets	1,043	1,042	1,038	1,739	1,669	1,615
Tangible assets	249	261	329	395	526	637
Shareholders' equity	406	604	808	890	1,013	1,169
Pension provisions	0	0	0	0	0	0
Liabilities and provisions	1,472	1,189	1,309	1,864	1,877	1,703
Net financial debt	420	329	53	585	480	322
w/c requirements	654	642	746	917	1,076	1,252
Ratios						
ROE	15.5%	13.2%	6.9%	14.0%	17.0%	18.9%
ROCE	6.6%	9.1%	7.6%	8.9%	10.9%	13.6%
Net gearing	103.4%	54.5%	6.6%	65.8%	47.4%	27.6%
Net debt / EBITDA	1.7x	1.2x	0.2x	1.4x	1.0x	0.6x

Source: Company data; mwb research

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