REDEYE

Update

Equity Research

2 November 2021

Artificial Solutions

Sector: Software/ Artificial Intelligence

Funding Secured, Strengthened Team, and Improved Offering

Redeye raises its fair value range. Above all, we find the recent financing agreement positive, essentially derisking the case.

Back to Growth

Adjusted net sales increased 4% y-o-y, and 11% q-o-q, owing to, among other things, a steady uptick in usage. Additionally, the company improved its EBITDA materially, beating expectations. This reflects, in our opinion, solid cost-control execution on behalf of management – the annualized OpEx run rate decreased 24% y-o-y.

SEK 250m Financing Agreement

Artificial Solutions agreed to a long-term financing agreement with Capital Four, a leading credit asset management firm in the Nordics. Essentially, the company will not need to make cash interest payments during the five-year tenure, in addition to interest expenses decreasing by 7ppts. Near- and mid-term financing issues are out of the picture, providing management ample room to execute on its SaaS model and sales ramp-up.

Anticipating an Eventful 2022

Three important customers agreed to renew and expand commitments with the company. Management commentary anticipates most existing customers transitioning to the SaaS model in 2022, representing a SEK 78m ARR opportunity. Additionally, the company has strengthened its go-to-market capabilities with some senior staff recruitments.

Valuation: Raised Fair Value Range, 40%+ Upside Potential

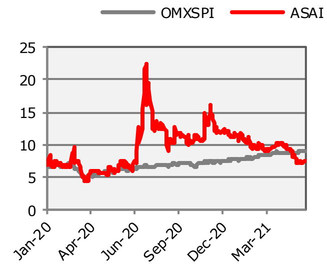
In this research update, we revise our fair value range to SEK 2-36 (2-30) with Base Case at 11 (9). Essentially, the recent financing agreement derisks the case, in our opinion, and we lower our WACC to 11% (12). In combination with catalysts such as increased usage revenues and customer wins, the strengthened financial situation should, in our opinion, result in positive market sentiment.

Key Financials (SEKm)	2019	2020	2021E	2022E	2023E	2024E
Sales	49	54	40	57	80	110
Sales growth	9%	10%	-25%	41%	40%	37%
EBITDA	-135	-86	-61	-53	-39	-19
EBIT	-146	-98	-73	-65	-53	-35
EBIT Margin (%)	-298%	-182%	-181%	-114%	-66%	-32%
Net Income	-182	-154	-76	-89	-79	-64
EV/S	6.9	12.4	15.4	12.4	9.8	7.7
EV/EBITDA	neg	neg	neg	neg	neg	neg
EV/EBIT	neg	neg	neg	neg	neg	neg

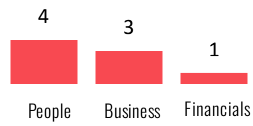
FAIR VALUE RANGE

BEAR	BASE	BULL
2.0	11.0	36.0

ASAI VERSUS OMXSPI



REDEYE RATING



KEY STATS

Ticker	ASAI
Market	First North
Share Price (SEK)	7.56
Market Cap (SEKm)	497
Net Debt 2021E (SEKm)	126
Free Float (%)	71

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Artificial Solutions Q3 2021: Near Forecast Beat Across the Board

Essentially, most key metrics developed positively during Q3. Adjusted net sales increased 4% y-o-y and 11% q-o-q, owing to, among other things, a positive development in adjusted usage. Additionally, adjusted recurring revenues, i.e., combined license & support and adjusted usage, amounted to SEK 9.5m (9.0m), increasing 6% y-o-y and 8% q-o-q. Usage on Teneo – Artificial Solutions' Conversational AI platform – represents the true scalability in the current business model. Thus, we regard the recent progress in a positive light.

Artificial Solutions communicated in Q4 2020, it had begun to transition to a SaaS business and delivery model. For this reason, usage revenues are recognized as consumed rather than invoiced, typically resulting in decreased reported revenues. In the previous model, an up-front usage payment in a multi-year deal was recognized to 100% in a single quarter. Instead, in the current model, it is evenly spread out throughout its lifetime. Against this backdrop, management has prepared adjusted usage revenues – helping investors better understand the business's underlying performance amid the transition.

Actual and forecast Artificial Solutions Q3 2021

SEKm	Q3 20	Actual Q3 21	Estimated Q3 21	Diff (%)	Diff (abs)
License & Support	*6.5*	*5.3*	*6.2*		
Usage	*4.4*	*3.2*	*1.8*		
Other	*2.4*	*2.4*	*2.4*		
Reported Net Sales	13.3	11.0	10.3	*6%*	*0.6*
Adjusted Usage	*2.5*	*4.2*	*3.8*		
Adjusted Net Sales	11.4	11.9	12.3	*-3%*	*-0.4*
Gross Profit	9.4	7.6	7.2	*4%*	*0.3*
margin	*71%*	*69%*	*70%*		
EBITDA	-17.9	-12.6	-15.8	*-20%*	*3.2*
margin	*-135%*	*-115%*	*-153%*		

Source: Redeye Research & company data

The gross profit margin amounted to 69% and developed more or less flat – in line with forecast. Looking ahead, we expect this metric to increase materially and to eventually compare to other SaaS companies, typically reporting well above 90%. Management commentary attributes the modest gross profit margin to professional services revenues. In combination with the transition to SaaS, Artificial Solutions no longer expects to support a professional services capability in-house – this has been outsourced to its partners and systems integrators. To comply with commitments in the previous model, the company is buying some professional services externally, weighing on the gross profit margin. However, once Artificial Solutions begins to 1) scale its SaaS offering; and 2) transition existing customers to the new model, we should expect, over time, a gross profit margin >90%. Incremental usage revenues require close-to-zero incremental costs.

On a final note, we recognize Artificial Solutions improved its EBITDA y-o-y and exceeded expectations, reflecting, in our opinion, management's solid cost-control execution. Annualized operating expenses (excl. D&A) amounted to SEK -106m (-139m), decreasing 24% y-o-y. While Artificial Solutions remains unprofitable, the updated cost-suit reflects much better the company's revenue profile.

Secures Additional Executing Power – SEK 250m Financing Agreement

On October 5, Artificial Solutions agreed to a long-term financing agreement with Capital Four, a leading credit asset management firm in the Nordics (€15 billion AUM). Essentially, Artificial Solutions raises SEK 250m gross through a five-year credit facility carrying a 9.5% interest rate and payment-in-kind (PIK) interest. The interest expenses will be capitalized and added to the underlying loan and will, therefore, have a non-cash impact on Artificial Solutions' financial statements.

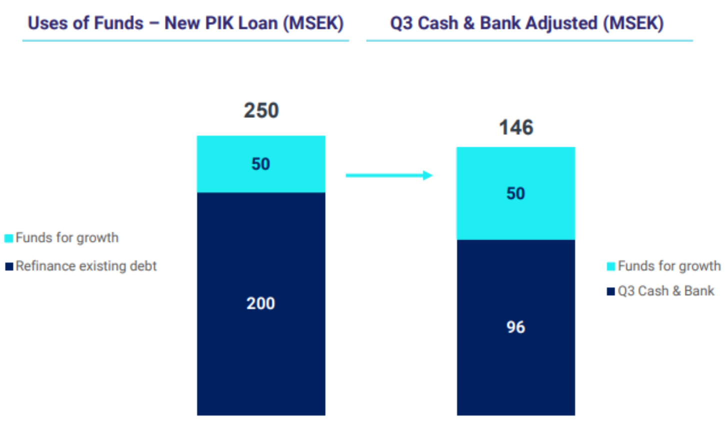
After repayment and refinancing of existing debt (about SEK 200m), Artificial Solutions will attain proceeds of SEK 50m (before transaction costs). Thus, its SEK 96m reported cash position on September 30 actually amounts to SEK 146m.

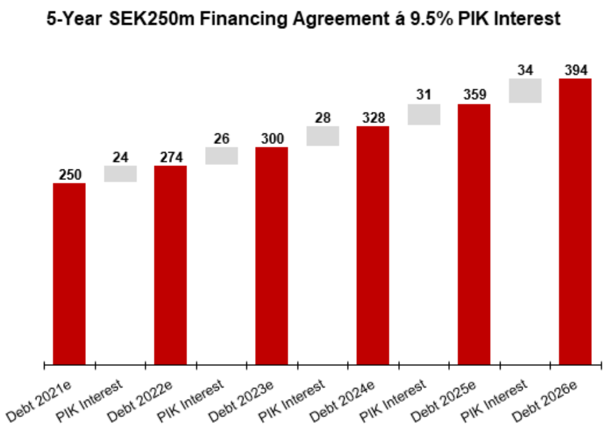
Fundamentally, we find the financing agreement positive:

- Artificial Solutions will not need to make cash interest payments during the tenure – crucial with respect to the company's negative cash flow profile
- Interest expenses are reduced by ~7ppts compared to the previous debt financing agreements, according to management commentary
- The interest rate is lower than the cost of equity financing – we apply an 11% WACC

In our latest update, we pointed to Artificial Solutions' uncertain financial situation and its possible impact on the negative share price sentiment. This should no longer be the case – which we find very encouraging. Essentially, the five-year agreement provides management ample room to execute on its SaaS model and sales ramp-up. Additionally, near- and mid-term financing issues are out of the picture. Artificial Solutions won't need to raise additional capital within the coming ~18 months, according to our modeling assumptions.

At the same time, it is worth mentioning a counterpoint. We expect interest expenses to increase each year, as these are capitalized and added to the underlying loan. By the end of the agreement in 2026, we believe the debt value will have grown to almost SEK 400m, assuming no further financing, as set out in the diagram. At the end of the tenure, we believe the most likely scenario is that the debt is refinanced – at improved terms – and continues to run. However, it should be said, in our opinion, that the benefits clearly outweigh the risks. Previous management at Artificial Solutions has struggled historically to secure a long-term sustainable financing plan. In contrast, current management has shown excellent executing capabilities in dealing with this matter.





Source: Redeye Research & company data

Anticipating an Eventful Year – SaaS Transition in Focus

Based on current usage volumes, transitioning Artificial Solutions' installed base to the SaaS model renders a SEK 78m opportunity in recurring usage revenues. This is more than 2x Artificial Solutions' current recurring revenues, which amount to SEK 35m (last-twelve-months). Management expects to transition most of its customers to SaaS in 2022, which we regard as a significant catalyst for the share price, as it could result in a hockey-stick-like effect on the company's revenue profile. Additionally, the company has recruited key personnel to support the expansion of the sales organization and the Microsoft partnership.

Strengthened Partnership with Microsoft

On September 6, Artificial Solutions announced it would join an IP Co-Sell Incentivized Partnership with Microsoft. Essentially, it means that Microsoft's sales team is incentivized (through, e.g., commissions) to promote Teneo – Artificial Solutions' Conversational AI platform – to enterprise clients on Microsoft Azure.

The partnership with Microsoft dates back to Q1 2021 when Artificial Solutions announced 1) the availability of Teneo in the Microsoft Azure Marketplace; and 2) LUIS^Teneo, a SaaS-based development suite and bot engine using Microsoft LUIS. The incentivized partnership strengthens, in our opinion, the company's relationship with Microsoft and supports its updated go-to-market strategy.

The agreement marks a vote of confidence in Teneo – we assume demanding requirements and significant testing before gaining such a partnership with Microsoft. Second, Artificial runs and develops solutions on Microsoft's cloud technology, validating the stack and making it more competitive. Last, it could enable significant lead-generation among the 1,700+ organizations using Microsoft Azure and LUIS.

While the agreement does not guarantee sales/ volumes, it positions Artificial Solutions well, in our opinion, to pursue Microsoft Azure enterprise clients. Overall, we believe partnerships of this kind are vital to achieving the ~40% top-line growth we forecast in 2022E and 2023E.

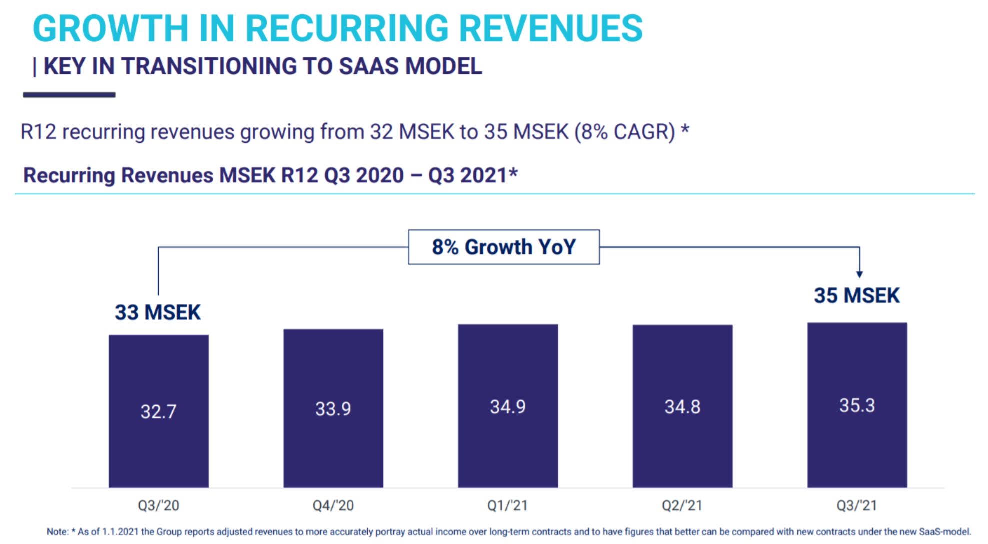
Several Renewed Commitments in Q3...

Three important customers – Scania, Circle K, and a US government agency – committed to renewing and expanding their agreements with Artificial Solutions in Q3. The agreement with Scania is of particular interest, in our opinion, as it shows just how multifaceted the Teneo platform is. While most use-cases concern customer-facing services, Scania largely applies the solution for internal uses.

...Reveal the Significant Potential Among Existing Customers...

Customers in the SaaS model accounted for 14% of total adjusted recurring revenues in the quarter. Thus, the vast majority of customers remain in the legacy business model. Transitioning these to the SaaS model will, over time, have a significant impact on Artificial Solutions' revenue profile.

Our Q2 research update pointed to the SEK 78m ARR opportunity within the installed base. Essentially, Teneo manages about 10 million 'sessions' on its platform each month – corresponding to about 80 million API Calls. Artificial Solutions expects to charge 0.08 SEK per API Call, generating SEK 6.5m each month, or 78m pa. Migrating all customers to the SaaS model would more than double Artificial Solutions' recurring revenues. In Q3, the company reported last-twelve-months recurring revenues of SEK 35m, growing at an 8% CAGR. A swift transition to SaaS should, in our opinion, have a hockey-stick-like effect on its revenue profile.



Source: company data

...Best Reflected in the Swisscom Account

Swisscom is the largest telecom provider in Switzerland and a long-term customer of Artificial Solutions. The customer journey began with Swisscom seeking to replace its tone-controlled IVR (e.g., press one for billings, two for repairs, and so on) with a conversational IVR (e.g., describe in one sentence what you need help with). Our understanding is that Swisscom manages millions of calls each year with its Teneo-developed solution and has, since then, increased its transaction NPS by 18ppts.

Management commentary indicates that Swisscom is one of its 'largest' large customers. At this point, it generates about 10m API calls each month, accounting for >10% of Artificial Solutions' usage volumes. Once it migrates to the SaaS model, the Swisscom account should generate SEK 0.8m in MRR and almost 10m in ARR.

Management Expects Most Customers to Transition to SaaS in 2022

Q3 management commentary indicates a clear intent to transition all existing customers to the SaaS model in 2022. This is indeed exciting as it could, in a short time period, bolster Artificial Solutions' revenue profile. At the same time, management points to some data legislation that could potentially postpone matters in the US and Switzerland. Essentially, it affects customers transitioning from legacy to SaaS in those countries, but not the prospect of making direct SaaS customer acquisitions. Management expects to launch a security framework in the near-term to work around this matter.

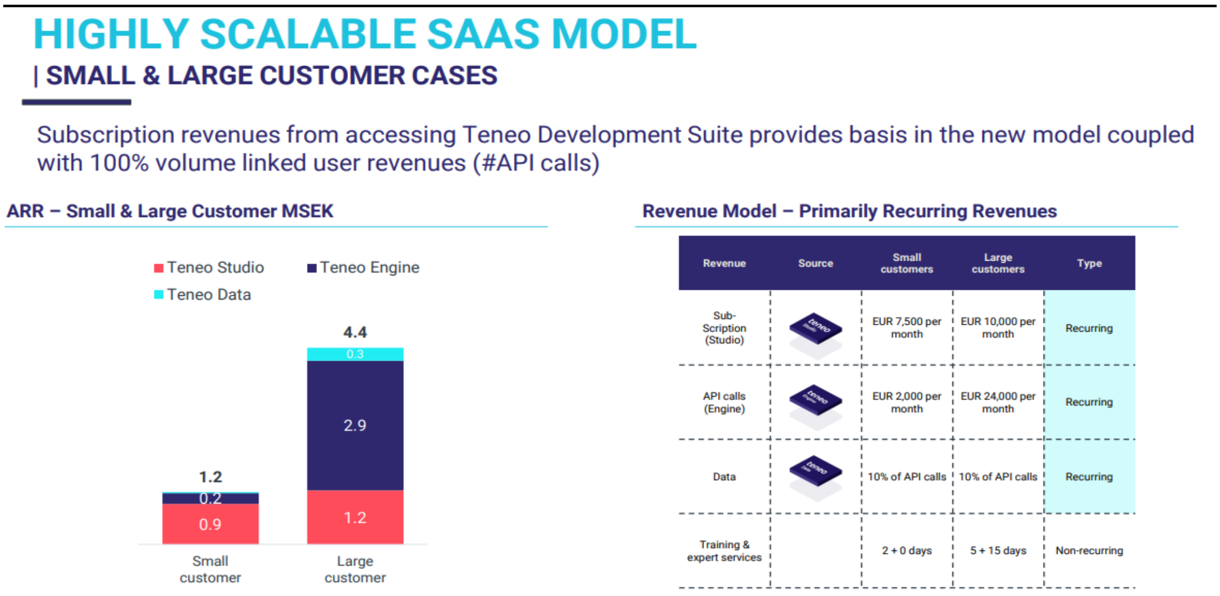
We regard 'transitioning customers to the SaaS model' as a key catalyst. Essentially, it validates the model's scalability and functionality, in addition to greatly impacting revenue recognition.

Key Recruitments to Support the Go-To-Market

Artificial Solutions has recruited several key personnel to support its go-to-market initiatives. In particular, it has appointed Nicolas Köllerstedt as Chief Revenue Officer. Prior to joining Artificial Solutions, Köllerstedt headed the Nordic and Baltic operations at Snowflake – a $100B market cap cloud-computing SaaS company. Additionally, the company has appointed Gavriella Schuster as Chair of the Advisory Board. Schuster has previously served as Corporate Vice President at Microsoft – essentially managing its partner network. Both appointees bring, in our opinion, excellent experience with respect to expanding the sales organization and growing in the Microsoft ecosystem. Together with Artificial Solutions' highly capable team, we set high expectations on its go-to-market capabilities.

Financial Forecast

Artificial Solutions has provided some guidance with respect to the recurring revenues it anticipates generating through its SaaS model. Essentially, the scalability is reflected in the usage-component, fundamentally setting apart 'small' and 'large' customers. The updated business model is depicted in the illustration below.



Revenue	Source	Small customers	Large customers	Type
Sub-Scription (Studio)		EUR 7,500 per month	EUR 10,000 per month	Recurring
API calls (Engine)		EUR 2,000 per month	EUR 24,000 per month	Recurring
Data		10% of API calls	10% of API calls	Recurring
Training & expert services		2 + 0 days	5 + 15 days	Non-recurring

Source: company data

Six Large Customer Wins in the SaaS Model YTD – SEK 26m ARR Potential

So far, Artificial Solutions has announced six large customer wins in the SaaS model year-to-date, although none since the Q2 report. These customers include SelectQuote, HelloFresh, a global American tech firm, Telefónica Deutschland/ O2, A1 Bulgaria, and Circle K.

Management commentary indicates a 12-month ramp-up period before starting to generate meaningful API Call/ usage revenues. Thus, our understanding is that management expects large accounts to generate, on average, a first-year ARR of around SEK 1.2m and thereafter 4.4m. Therefore, the six customer wins year-to-date could, over time, yield an ARR of SEK >26m.

Streamlining the Process to Attracting Smaller Accounts

Artificial Solutions has a clear intent to attract smaller accounts too. As the potential scalability is far less significant, the aim is to attract small customers en masse at a limited customer acquisition cost. Artificial Solutions expects to attract SMEs and developers to its development environment – Teneo.ai – by offering to start developing for free, i.e., product-led growth. It will, among other things, ramp-up marketing, webinars and hire a developers' advocate to promote usage and interact with users.

Essentially, the go-to-market differs materially from traditional large account routes. Artificial Solutions has largely focused on 1) direct enterprise sales; and 2) channel sales, where a partner on its side executes the transaction. Looking ahead, management expects to build out its channel network further, e.g., finding the right partners in the Microsoft ecosystem becomes increasingly important from a strategical point of view.

Illustrating the SaaS Model Scalability

Applying some of the assumptions mentioned above, we illustrate the SaaS model's potential scalability in the table beneath. To some extent, our churn rate assumptions could appear conservative – 8% and 15% for large and small customers, respectively. Artificial Solutions claims to have a >95% renewal rate in the last two years. However, this rate applies to the legacy model, while that of the SaaS model will remain unknown for some time. Also, we assume that small accounts are more prone to halt their commitments.

SEKm	2021e	2022e	2023e	2024e
Large customers				
# of wins	6	9	12	15
First-year sales per customer	1.2	1.2	1.2	1.2
Sales	7.2	10.8	14.6	18.2
# of remaining customers, beginning of period, 8% churn		6		
Sales per customer		4.4		
Sales		24.3		
# of remaining customers, beginning of period, 8% churn			13	
Sales per customer			4.4	
Sales			58.8	
# of remaining customers, beginning of period, 8% churn				23
Sales per customer				4.4
Sales				103.3
Large customer sales	7.2	35.1	73.4	121.5
Small customers				
# of wins		8	20	36
First-year sales per customer		0.9	0.9	0.9
Sales		7.2	18.0	32.4
# of remaining customers, beginning of period, 15% churn			7	
Sales per customer			1.2	
Sales			8.2	
# of remaining customers, beginning of period, 15% churn				25
Sales per customer				1.2
Sales				29.6
Small customer sales		7.2	26.2	62.0
Total sales	**7.2**	**42.3**	**99.5**	**183.5**
y-o-y growth		*487%*	*135%*	*84%*

Source: Redeye Research & company data

Essentially, the sales forecast in the illustration is considerably more bullish from 2023e and beyond, in contrast to our current estimates in Base Case. The reasoning for maintaining our estimates is based on 1) the SaaS model being launched less than a year ago and remaining therefore somewhat unproven; 2) wanting to see initial signs of customers scaling in the model and generating a material increase in usage revenues; and 3) current sales being fairly close to our estimates, absolutely speaking – the sales deviation in Q3 was ~500,000 SEK.

Instead, our take is that the illustration above represents a highly successful launch and rollout of the SaaS offering. To some extent, such a scenario is reflected in our Bull Case. Essentially, if sales and usage were to increase at a much faster rate than forecast, we expect to significantly revise our fair value range with an upward bias.

Forecast Adjustments

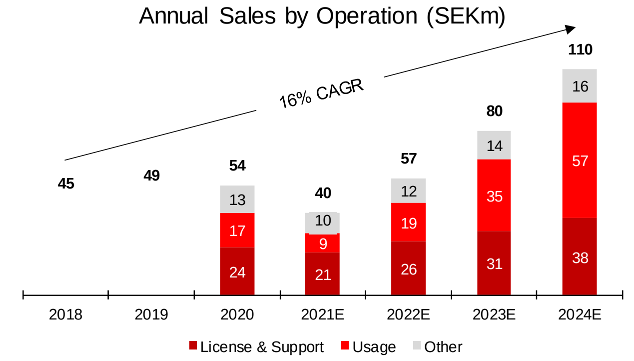
The Q3 top-line came in slightly better than forecast. However, the absolute deviation amounted to about SEK 500,000 – relatively close in other words. As the fundamentals remain more or less the same, we only revise our sales forecast with a slight upward bias. Increased sales in combination with somewhat lower cost assumptions result in an improved operating loss. The net income remains more or less the same, owing to higher interest expenses. However, as previously mentioned, these are non-cash and are instead due for repayment at the end of the tenure in 2026 – significantly improving Artificial Solutions' financial situation.

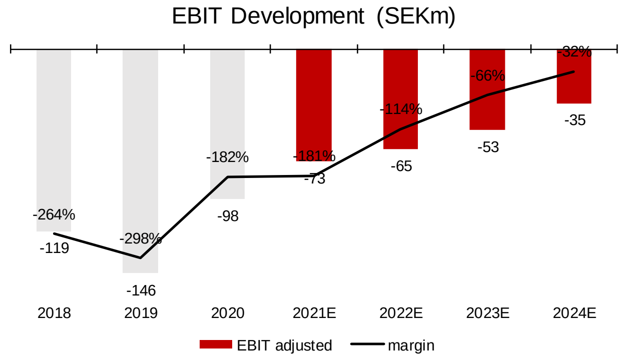
Forecast adjustments

SEKm		2021E	2022E	2023E	2024E
Net Sales	Old	40	56	78	107
	New	40	57	80	110
change (%)		*1%*	*2%*	*3%*	*3%*
EBIT	Old	-75	-67	-56	-40
	New	-73	-65	-53	-35
change (%)		*-2%*	*-4%*	*-7%*	*-13%*
Net Income	Old	-73	-88	-77	-64
	New	-76	-89	-79	-64
change (%)		*4%*	*1%*	*2%*	*-1%*

Source: Redeye Research, company data

The case relies, to a great extent, on Artificial Solutions' scalable business model. Over time, we expect the company to render highly profitable revenues from usage, potentially bolstering its gross profit margin to >90%, in line with SaaS peers. Incremental usage from existing accounts comes at close-to-zero incremental costs. Meanwhile, we expect costs to increase ~10% pa, resulting in an improved operating loss, before eventually becoming profitable around 2025E.





Source: company data

Income Statement	2020	Q1	Q2	Q3	Q4E	2021E	2022E	2023E	2024E
Net sales	**53.7**	**9.8**	**8.2**	**11.0**	**11.5**	**40.5**	**57.1**	**80.2**	**110.2**
Y/Y Growth	10%	-36%	-47%	-18%	19%	-25%	41%	40%	37%
Cost of sales	-18.3	-2.7	-2.7	-3.4	-3.5	-12.3	-14.9	-16.0	-16.5
Gross Profit	**35.4**	**7.1**	**5.5**	**7.6**	**8.1**	**28.2**	**42.3**	**64.2**	**93.7**
Gross Profit Margin	66%	72%	67%	69%	70%	70%	74%	80%	85%
Other operating income	20.1	2.2	2.8	3.0	3.0	11.0	16.0	17.6	19.4
Personnel expenses	-116.1	-17.6	-18.6	-16.7	-18.5	-71.4	-79.4	-86.6	-94.4
External expenses	-25.1	-6.0	-7.9	-6.4	-8.0	-28.3	-31.4	-34.3	-37.3
Other operating expenses	-	-	-	-	-	-	-	-	-
EBITDA adjusted	**-85.7**	**-14.3**	**-18.2**	**-12.6**	**-15.5**	**-60.5**	**-52.6**	**-39.0**	**-18.6**
EBITDA adj. Margin	-160%	-146%	-222%	-115%	-134%	-150%	-92%	-49%	-17%
Depreciation & amortization	-12.0	-3.2	-3.2	-3.1	-3.1	-12.6	-12.6	-13.6	-16.5
EBIT adjusted	**-97.7**	**-17.5**	**-21.4**	**-15.7**	**-18.6**	**-73.1**	**-65.1**	**-52.7**	**-35.2**
EBIT adj. Margin	-182%	-179%	-261%	-143%	-161%	-181%	-114%	-66%	-32%
Interest income	-	11.4	12.8	-	-	24.2	-	-	-
Interest expenses	-56.5	-5.8	-6.3	-8.7	-6.0	-26.8	-23.8	-26.0	-28.5
EBT	**-154.2**	**-11.9**	**-14.9**	**-24.4**	**-24.6**	**-75.7**	**-88.9**	**-78.7**	**-63.6**
Income tax expenses	-0.2	-	-	-	-	-	-	-	-
Effective Tax Rate	0%	0%	0%	0%	0%	0%	0%	0%	0%
Translation differences	-	-	-	-	-	-	-	-	-
Net Income	**-154.4**	**-11.9**	**-14.9**	**-24.4**	**-24.6**	**-75.7**	**-88.9**	**-78.7**	**-63.6**
Net Income Margin	-288%	-121%	-182%	-222%	-214%	-187%	-156%	-98%	-58%

Valuation

We derive our fair value range from a fundamental DCF framework for three scenarios, base case (most likely), bear case (pessimistic), and bull case (optimistic), using a WACC of 11% across all scenarios – previously 12%. Essentially, we believe the SEK 250m financing agreement with Capital Four derisks the case. In brief, Artificial Solutions will not need to make cash interest payments during the tenure, and interest expenses are reduced by ~7p pts. We have pointed to the company's uncertain financial situation in previous reports and its impact on the negative share price sentiment. This should no longer be the case. The five-year agreement provides management ample room to execute on its SaaS model and sales ramp-up.

Consequently, we raise our fair value range to SEK 2-36 (2-30) with Base Case at 11 (9). The fair value range continues to be very wide, owing to the unpredictable nature of Artificial Solutions' long-term growth and profitability. In this update, we provided an illustration of a 'highly successful SaaS rollout' and its effect on sales. The estimates from 2023E and beyond are considerably more bullish compared to what we outline in Base Case. To some extent, such a scenario is reflected in our Bull Case. Essentially, if sales and usage were to increase at a much faster rate than forecast, we expect to significantly revise our fair value range with an upward bias.

Bear Case 2 (2) SEK

Sales CAGR 2021E-2025E: 25%
Sales CAGR 2025E-2030E: 15%
Avg. EBIT-m 2021E-2025E: -31%
Avg. EBIT-m 2025E-2030E: 15%
Terminal growth: 2%
Terminal EBIT-m: 15%
WACC: 11%

Base Case 11 (9) SEK

Sales CAGR 2021E-2025E: 39%
Sales CAGR 2025E-2030E: 28%
Avg. EBIT-m 2021E-2025E: -81%
Avg. EBIT-m 2025E-2030E: 22%
Terminal growth: 2%
Terminal EBIT-m: 34%
WACC: 11%

Bull Case 36 (30) SEK

Sales CAGR 2021E-2025E: 44%
Sales CAGR 2025E-2030E: 32%
Avg. EBIT-m 2021E-2025E: -30%
Avg. EBIT-m 2025E-2030E: 36%
Terminal growth: 2%
Terminal EBIT-m: 38%
WACC: 11%

Investment Case

Scalable SaaS Business Model

Artificial Solutions announced its transition to a SaaS business and delivery model in Q1 2021. In contrast to its previous model, the SaaS model is inherently scalable, owing to its usage-based revenues. Additionally, the company expects to transition most of its installed base from the legacy to the SaaS model in 2022, representing a SEK >75m ARR opportunity.

Major Partners to Drive Growth

Since Q3 2021, Artificial Solutions has an IP Co-Sell Incentivized Partnership with Microsoft. Essentially, it means that Microsoft's sales team is incentivized through commissions to promote Teneo to enterprise clients on Microsoft Azure. The agreement marks a vote of confidence in Teneo and could enable significant lead-generation among the 1,700+ organizations using Microsoft Azure and LUIS.

Artificial Solutions relies on systems integrators and channel partners such as Tech Mahindra, CGI, and Deloitte to drive sales and usage. These partners have a global profile and could reach many potential customers at a limited customer acquisition cost.

Attractive Exposure to the Conversational AI Market

The Conversational AI Market is a $50B industry, while its software segment represents a $14B opportunity growing at a 22% CAGR. As one of the leading companies in this space, and one of the only publicly listed peers, Artificial Solutions provides attractive exposure to this sought-after market.

Solid Financial Position

In Q3 2021, Artificial Solutions agreed to a long-term SEK 250m financing agreement with Capital Four, a leading credit asset management firm in the Nordics (€15 billion AUM). Essentially, the company will not need to make cash interest payments during the five-year tenure, in addition to interest expenses decreasing by 7ppts. Near- and mid-term financing issues are out of the picture, providing management ample room to execute on its SaaS model and sales ramp-up.

Counter-thesis

Increased Competition

It would weigh heavily on the conversational AI industry if the tech giants flex their muscles and exploit their dominant market positions in the cloud, data, and AI. Even if they do not, this area's significant potential makes it likely that competition will increase further in the future.

Failing to Commercialize the SaaS Model

Artificial Solutions failing to acquire new customers to its SaaS offering and/ or not transitioning its installed base to the SaaS model would jeopardize the growth story.

Catalysts

Lighthouse Customer Agreements

We see great potential in large corporations choosing to implement Teneo and Conversational AI for an increasing number of use-cases. Apart from yielding a significant ARR at high margins, it could indicate that its industry is truly ready to adopt the technology on a larger scale.

Early Signs of Significant Usage Revenue Potential

The SaaS model launched in 2021 could turn out to be highly scalable. However, it is still early days, and the model remains unproven. Early signs of scalability, such as steady sequential usage growth, should inspire confidence in its long-term potential.

Significant ARR and Top-Line Growth

Solid quarterly reports demonstrating significant top-line growth, and thus a path to profitability should positively impact the share price.

Summary Redeye Rating

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

Rating changes in the report: none

People: 4

Artificial Solutions appointed Per Ottosson as CEO in November 2020. Ottosson brings extensive C-suite experience from highly successful companies within software and AI – most recently as CRO at IPSoft. Additionally, Ottosson has attracted many high-profile senior recruitments to Artificial Solutions. So far, management has delivered on its goals, i.e., transition to a SaaS model, expand partnerships, and decrease the cost base. Also, we value the ownership and long-term commitment of Scope (>20% of the capital/ votes), in addition to some founders having ownership stakes. Greater consistency in the capital allocation and increased management ownership could help improve the rating.

Business: 3

Since transitioning to a SaaS business model in 2021, the company has operated an asset-light (Kubernetes cloud infrastructure) and highly scalable venture, owing to its usage-based revenues – creating product stickiness. Additionally, it relies on global partners such as Microsoft, Deloitte, and CGI to drive sales – which on the flip side, makes some dependencies. The Software Conversational AI market is a $14B industry, growing at a 22% CAGR – the prospect of achieving long-term organic growth is highly feasible. However, Artificial Solutions is not immune to competition and innovations in the space and has, to some degree, high customer concentration, although this is steadily decreasing.

Financials: 1

Artificial Solutions has a negative cash flow track record and will likely remain unprofitable for some years to come – investing significant resources in sales growth. The rating's retrospective nature limits the company from achieving a higher score. However, we positively regard the increasing gross profit margin and expect it to, over time, compare to other SaaS companies (>90%). Also, we are encouraged by the SEK 250m financing agreement with Capital Four in Q3 2021, essentially derisking the case.

	2020	2021E	2022E	2023E
INCOME STATEMENT				
Sales	54	40	57	80
Cost of Sales	18	12	15	16
Gross Profit	35	28	42	64
Operating Expenses	141	100	111	121
EBITDA	-86	-61	-53	-39
Depreciation & Amortization	12	13	13	14
EBIT	-98	-73	-65	-53
Net Financial Items	-57	-3	-24	-26
EBT	-154	-76	-89	-79
Income Tax Expenses	0	0	0	0
Non-Controlling Interest	0	0	0	0
Net Income	-154	-76	-89	-79
BALANCE SHEET				
Assets				
Current assets				
Cash & Equivalents	20	124	60	10
Inventories	0	0	0	0
Accounts Receivable	8	4	9	12
Other Current Assets	15	8	11	14
Total Current Assets	43	136	80	36
Non-current assets				
Property, Plant & Equipment, Net	1	1	1	1
Goodwill	0	0	0	0
Intangible Assets	30	30	30	30
Right-of-Use Assets	0	0	0	0
Shares in Associates	0	0	0	0
Other Long-Term Assets	3	3	3	3
Total Non-Current Assets	34	35	34	34
Total Assets	77	171	114	70
Liabilities				
Current liabilities				
Short-Term Debt	70	0	0	0
Short-Term Lease Liabilities	0	0	0	0
Accounts Payable	7	12	15	18
Other Current Liabilities	5	0	0	0
Total Current Liabilities	134	42	50	59
Non-current liabilities				
Long-Term Debt	116	250	274	300
Long-Term Lease Liabilities	0	0	0	0
Other Long-Term Liabilities	0	0	0	0
Total Non-current Liabilities	116	250	274	300
Non-Controlling Interest	0	0	0	0
Shareholder's Equity	-173	-121	-210	-289
Total Liabilities & Equity	77	171	114	70
CASH FLOW				
NOPAT	-98	-73	-65	-53
Change in Working Capital	30	-11	0	3
Operating Cash Flow	-76	-47	-52	-36
Capital Expenditures	-1	-1	-1	-1
Investment in Intangible Assets	-10	-12	-11	-13
Investing Cash Flow	-11	-13	-12	-14
Financing Cash Flow	102	164	0	0
Free Cash Flow	-87	-60	-64	-49

DCF Valuation Metrics	**Sum FCF (SEKm)**
2021-25	-136
2026-34	471
2034-	515
Firm Value	851
Net Debt	126
Equity Value	725
Fair Value per Share	11

	2020	2021E	2022E	2023E
CAPITAL STRUCTURE				
Equity Ratio	-2.2	-0.7	-1.8	-4.1
Debt to equity	-1.1	-2.1	-1.3	-1.0
Net Debt	166	126	214	289
Capital Employed	-57	129	64	11
Working Capital Turnover	-1.3	-1.4	-1.9	-2.4
GROWTH				
Sales Growth	10%	-25%	41%	40%
Basic EPS Growth	-61%	-68%	17%	-11%
Adjusted Basic EPS Growth	-61%	-68%	17%	-11%
PROFITABILITY				
ROE	85%	52%	54%	32%
ROCE	172%	-57%	-102%	-474%
ROIC	-1568%	1783%	-5267%	5661%
EBITDA Margin (%)	-160%	-150%	-92%	-49%
EBIT Margin (%)	-182%	-181%	-114%	-66%
Net Income Margin (%)	0%	0%	0%	0%
VALUATION				
Basic EPS	-3.6	-1.2	-1.4	-1.2
Adjusted Basic EPS	-3.6	-1.2	-1.4	-1.2
P/E	neg	neg	neg	neg
EV/S	12.4	15.4	12.4	9.8
EV/EBITDA	neg	neg	neg	neg
EV/EBIT	neg	neg	neg	neg
P/B	neg	neg	neg	neg

SHAREHOLDER STRUCTURE	**CAPITAL %**	**VOTES %**
Scope	25.6%	25.6%
Nice & Green	5.6%	5.6%
AFA Försäkring	5.0%	5.0%
SEB-Stiftelsen	4.4%	4.4%
C WorldWide Asset Management	2.6%	2.6%

SHARE INFORMATION	
Reuters code	ASAI.ST
List	First North
Share price	7.56
Total shares, million	65.7

MANAGEMENT & BOARD	
CEO	Per Ottosson
CFO	Fredrik Törgren
Chairman	Åsa Hedin

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Redeye Rating and Background Definitions

Company Quality

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

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

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

People

At the end of the day, people drive profits. Not numbers. Understanding the motivations of people behind a business is a significant part of understanding the long-term drive of the company. It all comes down to doing business with people you trust, or at least avoiding dealing with people of questionable character.
The People rating is based on quantitative scores in seven categories:

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

Business

If you don't understand the competitive environment and don't have a clear sense of how the business will engage customers, create value and consistently deliver that value at a profit, you won't succeed as an investor. Knowing the business model inside out will provide you some level of certainty and reduce the risk when you buy a stock.
The Business rating is based on quantitative scores grouped into five sub-categories:

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

Financials

Investing is part art, part science. Financial ratios make up most of the science. Ratios are used to evaluate the financial soundness of a business. Also, these ratios are key factors that will impact a company's financial performance and valuation. However, you only need a few to determine whether a company is financially strong or weak.
The Financial rating is based on quantitative scores that are grouped into five separate categories:

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

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Disclaimer

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Redeye Rating (2021-11-02)

Rating	People	Business	Financials
5p	33	15	4
3p - 4p	136	122	43
0p - 2p	5	37	127
Company N	174	174	174

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