Gauzy Ltd.

2Q earnings review - Soft 2Q EBITDA/ FCF, but appealing narrative intact w/revenue growth ahead

CORE

Key takes: 1. 2Q revenue inline with pre-release, EBITDA modestly below ingoing estimates; 2. FCF use sharper than we'd hope to see, but path to improvement in 2H; 3. Revenue and margins guided to improve h/h in 2H, reinforces positive momentum; 4. Stock may take time to be understood, but we remain bullish. Reit. OW, $24

GAUZ's 2Q print was its first as a public company and while soft EBITDA and FCF were soft vs. consensus, we overall viewed the quarter as net positive given commentary of sequential growth in revenue and margin ahead...much needed given ingoing weak sentiment embedded in the stock. More importantly, the core tenets of the GAUZ growth narrative remain intact and we believe that improving profitability and moderating cash burn should leave a path for GAUZ to realize this opportunity, rewarding patient investors.

As we've noted in our initiation report on GAUZ, a volatile stock price is to be expected given its limited trading liquidity and nascent status as a public company. Moreover, we believe investors are still working to figure out what exactly to make of GAUZ. 2Q gave some indication, but we expect a stronger 2H24 earnings profile and reduced cash burn to offer a better opportunity for GAUZ to prove itself. Indeed, with near-term liquidity needs covered we believe that GAUZ is now more of an execution story, with ongoing revenue growth + improved EBITDA, as well as potential new customer win announcements serving as catalysts for the narrative.

We continue to see the post-IPO sell-off of GAUZ as an attractive entry point, with the stock trading at a meager 2.0x/1.5x '24/'25E EV/Sales despite a robust growth opportunity ahead. Accordingly, we reiterate our OW rating and $24 PT.

2Q miss, FCF burn sharper than we hoped but this includes non-repeats

GAUZ's -$3.9mn EBITDA loss was a miss vs. our est. of -$2.2mn and Bloomberg consensus, albeit this is comprised of a limited set of estimates. Revenue of $24.4mn was towards the higher end of the range GAUZ pre-announced in mid-July and reflected an encouraging +22% y/y growth rate led by Safety-Tech and Aeronautics. Further, solid Aero and Safety-Tech results drove GAUZ gross margins to 27%, +680bps y/y.

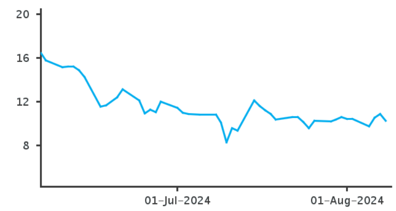
FCF burn was sharper than we'd hope to see at -$11.6mn (Barc. -$3.3mn). This made 1H24 FCF a ~$20mn use and rightfully puts a focus on the trajectory of GAUZ cash burn given that a key

GAUZ	OVERWEIGHT Unchanged	
U.S. Autos & Mobility	NEUTRAL Unchanged	
Price Target	USD 24.00 Unchanged	
Price (08-Aug-24)	USD 10.27	
Potential Upside/Downside	+133.7%	

Market Cap (USD mn)	195
Shares Outstanding (mn)	19.05
Free Float (%)	23.15
52 Wk Avg Daily Volume (mn)	N/A
Dividend Yield (%)	N/A
Return on Equity TTM (%)	N/A
Current BVPS (USD)	N/A

Source: Bloomberg

Price Performance	Exchange-Nasdaq
52 Week range	USD 17.10-8.17



Source: IDC
Link to Barclays Live for interactive charting

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point in the GAUZ narrative relates to its ability reach FCF breakeven without the need for additional dilutive raises. Some of the elevated FCF drag related to working capital and capex. Additionally, mgmt called out $4-5mn of one-time expenses in 1H that won't repeat in 2H, but the timing of how this will flow into FCF is mixed. And while 3Q should see some continued working capital drag, 4Q should be improved. Overall, we believe improved 2H24 profitability will soften FCF burn and we see an ~$6mn h/h improvement, with an encouraging exit rate for a moderated outflow in 2025.

Understanding the GAUZ backlog – indication of near-term revenue predictability, but long-term growth will come from incremental program wins which are not yet included

Given that backlog is not a GAAP figure it has no standard measure and this makes GAUZ's backlog worth further explanation. Within our auto supplier coverage the definition often includes the value of expected lifetime revenues from booked programs. Conversely, mgmt explained that GAUZ's backlog reflects its booked orders (based on purchase orders or hard commitments) that have not yet been recognized in revenue, but are very close to being recognized, often in the next 1-2 quarters. Accordingly, GAUZ's backlog will remain inherently smaller than many auto investors may be accustomed given this stricter definition.

GAUZ's $36.2mn 2Q24 backlog figure was up ~35% y/y driven in large part by its Automotive segment, albeit Auto remains quite small at 12% of the total. At 55% of the total Aeronautics still dominates the backlog, with Safety-Tech making up another 23%. Architecture (10%) has some projects included, but additional near-term sales not yet included in the backlog could materialize given the less predictable nature of its business model.

Looking ahead we believe it's important to consider that under GAUZ's definition its backlog won't necessarily reflect the robustness of its long-term growth opportunity until the associated revenues are imminent. Rather, we believe that following incremental program wins will be the more important indicator of forthcoming growth, especially series production agreements in Auto and Safety-Tech.

2Q serves as reminder that GAUZ Auto biz is very nascent, opportunity very long-dated

In 2Q GAUZ saw just ~$900k of Automotive revenue, up 80% y/y but still under 4% of total GAUZ revenue. While we have known that Auto is currently very small, its break-out as a separately reported segment makes this all the more visible. On one hand this makes the path for accelerating Auto growth very obvious and feasible with even modest commercial success. Yet on the other it reminds us that GAUZ's opportunity in Auto is extremely nascent and that even with significant growth ahead the segment will remain relatively small for some time.

The other new segment break-out, Architecture, posted greater revenue than Auto, but is also still minimal compared to Aeronautics and Safety-Tech. Moreover, 2Q Architecture revenue being down y/y reflect the lumpy nature of orders in the segment that are based upon specific projects vs. ongoing production programs.

More broadly, it's important to remember that Auto and Architecture are the only two GAUZ segments based purely on smart glass products. At this time Auto end market uptake of smart glass is still in the very early stages, largely reserved for very premium, low-volume vehicle programs. It makes sense that the market will start at the high end and we appreciate that these early programs lay the groundwork for an eventual expansion to the mass market, but we would note that the move into more mainstream vehicles will take time to inflect.

Looking ahead, 2H should see improved earnings on stronger sales, EBITDA breakeven the next major milestone, awaiting further program wins

GAUZ did not provide an explicit guide on 2H financials, but mgmt talked to directionally stronger h/h sales amid seasonality and solid demand, and improving margins as fixed costs are further spread; specifically, mgmt noted that it expects 3Q revenue modestly higher q/q, with 4Q up more significantly q/q. We were somewhat disappointed not to see EBITDA by segment reported, as this makes the ramp towards profitability a bit more difficult to pin down, but GAUZ gross margin by segment can still help give a sense as to where the improvement is coming from.

Considering the 2Q EBITDA miss vs. our estimate, we now assume EBITDA breakeven in 4Q vs. our prior expectation of 3Q, but we still find the trajectory of earnings improvement to be encouraging. Indeed, with Aeronautics providing a steady base, we expect the growth of Safety-Tech to drive most of the near-term trajectory. And more importantly, for GAUZ stock to work it will need to post EBITDA beats and drive flow-through of these incremental profits to soften near-term FCF burn, and ultimately reach breakeven and beyond.

Lastly, alongside crafting a path to breakeven and eventually positive EBITDA, GAUZ will need to provide further announcements/program wins demonstrating uptake of their technology.

ICYMI – a summary of our GAUZ thesis

We believe GAUZ is a high-risk / high-reward narrative, with upside especially compelling after a soft start to trading post IPO.

- **Unique asset:** Israel-based light and vision control company with vertically integrated capabilities, and a range of products including in smart glass and commercial vehicle active safety. GAUZ has a number of “shots on goal” with a range of growth verticals, but at the same time benefits from a well-established core business that has the company nearing EBITDA profitability and limiting cash burn. While finding an appropriate comp set isn't easy, we believe there’s an appeal in the unique blend of GAUZ's tech, products, and end market exposures.

- **Aligned to megatrends:** GAUZ’s leading-edge growth products in smart glass and active safety are both well-aligned with key megatrends, and in our view support 30%+ revenue CAGR over the coming years. Timeline for end market inflections will likely vary, but a number of drivers for growth exist, including regulatory factors – third-party forecasts suggest notably large TAMs for smart glass in automotive and architecture end markets.

- **Balanced growth story:** After a very challenging stretch for auto-tech new entrants and profitless growth companies post the 2020/’21 SPAC era, we appreciate the skepticism around the GAUZ narrative. That said, GAUZ benefits from a solid existing business within its Aero and Safety Tech segments that should support patience around awaiting the inflection of longer-dated growth verticals / end markets.

- **We see EBITDA breakeven in 2H24E, FCF breakeven in 2027E:** Despite a runway for significant growth, GAUZ is nearing profitability today, and we expect it to post positive EBITDA in 2H24E. Moreover, management expects the cash received in the IPO to be sufficient to fund the company through FCF breakeven, with any incremental raises only required for M&A opportunities and large-scale program wins that require additional investments.

- **Understanding the story demands some work:** Beyond concerns associated with GAUZ’s small capitalization and trading liquidity, GAUZ also faces the challenge of disassociating from 2020/’21 growth narratives, including bankrupt architectural smart glass player VIEW.

Additionally, the opacity of GAUZ's end markets and still emerging competition make it difficult to validate where GAUZ stands today.

See our full GAUZ initiation here: A compelling growth story with multiple ways to win; initiate at OW, $24 PT

GAUZ: Quarterly and Annual EPS (USD)

	2023	2024			2025			Change y/y	
FY Dec	Actual	Old	New	Cons	Old	New	Cons	2024	2025
Q1	N/A	-0.67A	-2.51A	N/A	N/A	N/A	0.04E	N/A	N/A
Q2	N/A	-0.34E	-2.60A	-0.22E	N/A	N/A	0.10E	N/A	N/A
Q3	N/A	-0.22E	-0.41E	-0.13E	N/A	N/A	0.11E	N/A	N/A
Q4	N/A	-0.11E	-0.26E	0.02E	N/A	N/A	0.18E	N/A	N/A
Year	-19.72A	-1.33E	-3.77E	-0.98E	-0.17E	-0.20E	0.14E	81%	95%
P/E	N/A		N/A			N/A			

Consensus numbers are from Bloomberg received on 08-Aug-2024; 12:53 GMT
Source: Barclays Research

U.S. Autos & Mobility — NEUTRAL

Gauzy Ltd. (GAUZ) — OVERWEIGHT

Income statement	2023A	2024E	2025E	2026E	CAGR
Revenue ($mn)	78	106	143	198	36.5%
EBITDA (adj) ($mn)	-21	-10	14	30	N/A
EBIT (adj)	N/A	N/A	N/A	N/A	N/A
Pre-tax income (adj)	N/A	N/A	N/A	N/A	N/A
Net income (adj)	N/A	N/A	N/A	N/A	N/A
EPS (adj) ($)	-19.72	-3.77	-0.20	0.52	N/A
Diluted shares (mn)	4	13	21	21	74.0%
DPS ($)	N/A	0.00	0.00	0.00	N/A

Margin and return data	2023A	2024E	2025E	2026E	Average
EBITDA (adj) margin (%)	-26.5	-9.7	9.7	15.1	-2.9
EBIT (adj) margin (%)	N/A	N/A	N/A	N/A	N/A
Pre-tax (adj) margin (%)	N/A	N/A	N/A	N/A	N/A
Net (adj) margin (%)	N/A	N/A	N/A	N/A	N/A
ROA (%)	N/A	N/A	N/A	N/A	N/A
ROE (%)	N/A	N/A	N/A	N/A	N/A

Balance sheet and cash flow ($mn)	2023A	2024E	2025E	2026E	CAGR
Tangible fixed assets	21	23	26	35	19.3%
Intangible fixed assets	45	40	36	31	-11.9%
Cash and equivalents	5	35	29	29	83.3%
Total assets	128	168	176	202	16.5%
Short and long-term debt	67	61	61	61	-3.3%
Pension liabilities	N/A	N/A	N/A	N/A	N/A
Other long-term liabilities	13	12	12	12	-4.1%
Total liabilities	194	118	126	137	-10.9%
Net debt/(funds)	62	26	32	32	-20.3%
Shareholders' equity	35	274	274	274	97.7%
Change in working capital	-7	-3	-7	-11	N/A
Cash flow from operations	-31	-27	1	13	N/A
Capital expenditure	-6	-7	-8	-13	N/A
Free cash flow	-37	-34	-6	0	N/A

Valuation and leverage metrics	2023A	2024E	2025E	2026E	Average
P/E (adj) (x)	N/A	N/A	N/A	19.7	19.7
EV/sales (x)	1.5	0.8	0.6	0.4	0.8
EV/EBITDA (adj) (x)	-5.6	-7.8	6.2	2.9	-1.1
EV/EBIT (adj) (x)	N/A	N/A	N/A	N/A	N/A
Equity FCF yield (%)	N/A	N/A	N/A	N/A	N/A
P/BV (x)	N/A	0.5	0.8	0.8	0.7
Dividend yield (%)	N/A	0.0	0.0	0.0	0.0
Total debt/capital (%)	N/A	N/A	N/A	N/A	N/A
Net debt/EBITDA (adj) (x)	-3.0	-2.5	2.3	1.1	-0.5

Selected operating metrics	2023A	2024E	2025E	2026E	Average
FCF/NI (x)	0.5	0.7	1.5	0.0	0.7
R&D/sales (%)	20.6	12.7	7.5	5.8	11.6
Capex/sales (%)	7.6	6.3	5.5	6.6	6.5
D&A/sales (%)	7.3	7.0	6.2	4.7	6.3

Note: FY End Dec

Source: Company data, Bloomberg, Barclays Research

Price (08-Aug-2024)	**USD 10.27**
Price Target	**USD 24.00**

Why OVERWEIGHT?

GAUZ represents a unique asset with exposure to a variety of end markets, offering a number of "shots on goal" for an appealing growth trajectory associated with the adoption of smart glass and commercial vehicle ADAS. Patience around growth is enabled as it's nearing profitability and cash burn is mitigated by a relatively established base business.

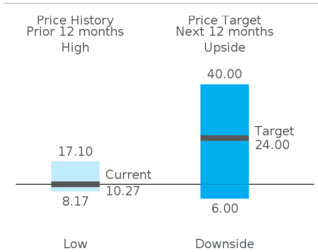
Upside case — USD 40.00

Our upside case assumes a stronger near-term uptake of GAUZ products that translates into higher revenues as well as a more robust multiple from the market that is toward the upper end of the peer group range.

Downside case — USD 6.00

Our downside case assumes a sluggish growth trajectory for GAUZ product uptake driving lower revenues, a trading multiple at the low end of the GAUZ peer group range, and a higher level of net debt.

Upside/Downside scenarios



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Primary Stocks (Ticker, Date, Price)
Gauzy Ltd. (GAUZ, 08-Aug-2024, USD 10.27), Overweight/Neutral, A/CE/D/E/J/L

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Ford Motor (F)	Gauzy Ltd. (GAUZ)	General Motors (GM)
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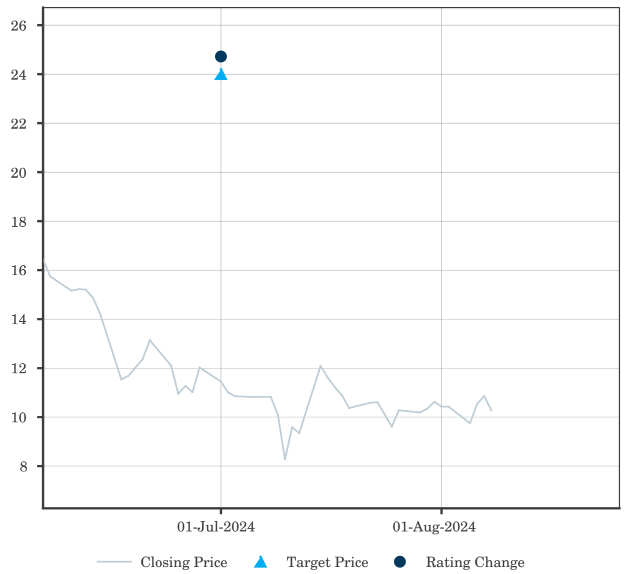
Stock Rating: **OVERWEIGHT**

Industry View: **NEUTRAL**

Closing Price: **USD 10.27** (08-Aug-2024)

Rating and Price Target Chart - USD (as of 08-Aug-2024)

Currency=USD



Source: IDC, Barclays Research

Link to Barclays Live for interactive charting

Publication Date	Closing Price*	Rating	Adjusted Price Target
01-Jul-2024	12.02	Overweight	24.00

Source: Bloomberg, Barclays Research

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Valuation Methodology: Our $24 price target is based on a 3.7x 2025 EV/Sales multiple applied to our model, toward the middle-to-lower part of the multiple range for the GAUZ peer group. We find 2025 EV/Sales to be the most appropriate metric on which to value GAUZ as it reflects a period of revenue with reasonable visibility and GAUZ earnings are not yet reflective of GAUZ's forthcoming scale.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: 1. GAUZ is a complex business covering a range of emerging and opaque end markets. This makes validation of where GAUZ stands competitively and gaining confidence on the timeline for inflection difficult. 2. End market inflection (especially Auto and Architecture) could prove slow, a point which we suspect would draw investor scrutiny. 3. The GAUZ comp set is generally unclear and this may require time for the market to get comfortable with the GAUZ narrative. 4. Investors are largely skeptical of newly public auto-tech / mobility growth after the disappointments of 2020-2021 stories; the recent bankruptcy of architectural smart glass player VIEW (the only publicly traded smart glass company) compounds this and may be a source of investor concern. 5. Some investors may be limited from considering a position amid potentially low trading liquidity. Similarly, limited volumes could lead to considerable volatility in the stock on a day-to-day basis. 6. If GAUZ sees sharper-than-expected FCF burn, liquidity may be (or become) a concern.

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