

# German industrials spotlight

## Industrial machinery

- Industrial machinery stocks are attracting EPS upgrades.
- Export growth and falling metal prices are positive for earnings.
- We highlight three companies that may interest investors.

### Grinding on

We find it interesting that several industrial machinery stocks appear at the top of our rising revisions screen this month. Earnings in this sector are sensitive to the economic cycle, which appears at odds with weak macroeconomic data released in recent weeks. In particular, German GDP fell by -0.6% in Q412 and the Ifo business expectations survey fell to 101.6 in April (vs 103.6 in March). In addition, GDP growth in China slowed to +7.7% year-on-year in Q1 vs market expectations of +8%. We believe there are other, more specific, factors at play including the continued success of German global exports and the potential for gross margins across the sector to expand as metal prices decline. On a wider scale, central banks continue to provide ongoing liquidity and maintain interest rates at low levels; this encourages capital flow into cheaper, riskier assets such as industrial machinery stocks. We identify three companies in this sector that screen well and should attract investors; Koenig & Bauer, KSB and Schaltbau. Koenig & Bauer is a company we have previously highlighted and is one of only three stocks to make the top 20 in both our value and momentum screens.

### Koenig & Bauer: Value rank four; momentum rank 11

Koenig & Bauer's core business is printing presses. This stock, highlighted as a value opportunity in our March edition, is even more interesting now it is attracting 2013 EPS upgrades. Since we [last commented](#) on the company, on 6 March, the stock has risen by 10% despite management postponing its official 2013 guidance. This is a deep value stock (P/BV=0.6x), which may have already factored in a lot of negative newsflow.

### KSB: Net gearing -15%; value rank 10

KSB produces pumps and valves, mainly for the energy and shipbuilding industries. KSB has a decent operating track record with a five-year average ROE of 15.2%. The stock looks good value on various multiples including a free cash flow yield of 6.3% (using a five-year average FCF) and a 2013 P/E and dividend yield of 9.2x and 3.2% respectively (using Bloomberg consensus forecasts).

### Schaltbau: 2013 consensus EPS +10% over one month

Schaltbau produces electromechanical components principally for railways and rolling stock. At the Q1 stage management cited strong organic growth in Asia and the Americas and raised guidance for 2013 sales and EBIT to €390m and €35.9m respectively. On these numbers, 2013 EV/Sales = 0.75x and 2013 EV/EBIT = 8.1x, which look fair. Further upgrades are required to drive the shares higher.

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#### MDAX Industrials Index



#### Ifo Business Expectations



#### CRB Metals Index (3 years)



Source: Deutsche Bundesbank

**Exhibit 1: Overlooked and undervalued**

Stock name	Sub-sector	Market cap (€m)	Quality		Value		Rank
			Net gearing %	EBIT margin* %	P/BV	EV/EBITDA	
<b>KOENIG &amp; BAUER</b>	<b>Industrial machinery</b>	<b>296</b>	<b>(27)</b>	<b>1.3</b>	<b>0.6</b>	<b>2.0</b>	<b>1</b>
STEICO SE	Building products	54	(4)	5.1	0.7	3.0	2
SALZGITTER AG	Steel	1,801	(7)	0.0	0.4	4.1	3
NORDWEST HANDEL	Trading companies & distributors	43	(51)	0.6	0.9	1.9	4
EUROKAI KGAA	Marine ports & services	290	28	10.5	0.8	4.0	5
JOYOU AG	Building products	261	(6)	16.8	0.8	4.2	6
NORDDEUTSCHE STE	Building products	23	68	4.4	0.7	4.6	7
YOUBISHENG GREEN	Paper packaging	50	(51)	23.4	1.1	1.1	8
BREMER LAGERHAUS	Marine ports & services	222	120	5.8	0.6	5.1	9
<b>KSB AG</b>	<b>Industrial machinery</b>	<b>796</b>	<b>(15)</b>	<b>7.0</b>	<b>1.0</b>	<b>3.7</b>	<b>10</b>
AURUBIS AG	Diversified metals & mining	2,177	3	4.2	1.0	4.0	11
RHEINMETALL AG	Industrial conglomerates	1,445	7	6.9	1.0	3.5	12
GREIFFENBERGER	Industrial machinery	27	131	2.1	0.8	4.2	13
DEUTZ AG	Industrial machinery	505	10	4.5	1.1	4.0	14
WACKER CHEMIE AG	Specialty chemicals	2,811	29	12.3	1.0	4.1	15
SIXT AG	Trucking	797	144	10.9	1.3	3.6	16
HOMAG GROUP AG	Industrial machinery	221	(24)	2.9	1.4	3.2	17
TELEGATE AG	Diversified support services	154	(93)	20.7	1.5	1.0	18
NABALTEC	Specialty chemicals	52	105	3.8	1.0	5.5	19
BAUER AG	Construction & engineering	364	119	5.3	0.8	6.4	20

Source: Bloomberg. Note: \*Three-year historical average. Data as at 30 April 2013.

**Exhibit 2: Rising revisions**

Stock name	Sub-sector	Market cap (€m)	Performance* %			EPS revisions %			Rank
			1m	3m	12m	1m	3m	12m	
SFC ENERGY AG-BR	Electrical components & equipment	38	(3.0)	(16.7)	3.6	28.6	400.0	175.0	1
BAYWA AG-VINK.	Trading companies & distributors	1,305	2.4	2.5	37.6	2.9	9.1	42.2	2
MBB INDUSTRIES	Industrial conglomerates	125	4.2	(4.3)	163.3	1.0	9.5	80.0	3
HOMAG GROUP AG	Industrial machinery	221	(2.1)	20.7	37.6	1.6	19.3	3.6	4
KUKA AG	Industrial machinery	1,151	(0.2)	21.2	90.7	1.4	5.9	40.8	5
R STAHL AG	Industrial machinery	226	17.4	20.9	33.5	1.3	8.3	11.4	6
DUERR AG	Industrial machinery	1,493	3.9	19.5	83.6	0.8	10.2	39.7	7
<b>SCHALTBAU HOLD</b>	<b>Industrial machinery</b>	<b>230</b>	<b>17.8</b>	<b>7.1</b>	<b>42.0</b>	<b>9.9</b>	<b>6.1</b>	<b>2.1</b>	<b>8</b>
KRONES AG	Industrial machinery	1,674	(3.5)	13.8	26.9	1.5	4.8	(0.1)	9
OHB AG	Aerospace & defence	282	(3.8)	6.0	28.4	1.0	1.1	10.6	10
<b>KOENIG &amp; BAUER</b>	<b>Industrial machinery</b>	<b>296</b>	<b>(1.2)</b>	<b>26.0</b>	<b>44.2</b>	<b>12.2</b>	<b>33.4</b>	<b>(12.6)</b>	<b>11</b>
BILFINGER SE	Diversified support services	3,581	(0.2)	8.1	21.4	1.1	3.8	(0.4)	12
JOYOU AG	Building products	261	(8.6)	13.2	25.3	0.9	0.9	0.3	13
CENTROTEC SUSTAI	Building products	271	6.5	(1.0)	28.3	0.0	3.1	3.2	14
BERTRANDT AG	Research & consulting services	880	(5.0)	8.9	60.5	0.0	0.8	5.1	15
HERMLE BERTH-PFD	Industrial machinery	674	1.3	27.8	59.1	0.0	0.0	16.1	15
EHLEBRACHT AG	Building products	37	(1.0)	5.5	24.4	4.8	4.8	(12.0)	17
WASHTEC AG	Industrial machinery	149	0.9	18.2	16.3	0.0	11.1	(7.9)	18
NORMA GROUP	Industrial machinery	869	10.7	28.0	40.0	0.6	3.6	(4.2)	19
BRENNTAG AG	Trading companies & distributors	6,601	4.9	20.9	39.7	0.1	2.5	(1.9)	20

Source: Bloomberg. Note: \*Total return. Data as at 30 April 2013.

## Appendix 1: Screening methodology

### Universe

We include all non-DAX30 stocks classified under GICS Level 1 Industrials or GICS Level 1 Materials, subject to a minimum market cap of €10m. This provides a universe of 140 stocks, some of which are excluded from the analysis due to lack of data.

### Exhibit 1: Overlooked and undervalued

Our first screen looks for financially sound companies trading on low multiple of assets (P/BV) and low multiple of core profits (EV/EBITDA). The universe of stocks is ranked first by P/BV and secondly by EV/EBITDA. An equal weighted composite rank is then computed.

This screen provides us with a list of top 20 'value' stocks which may have been neglected by investors.

This may be due to structural reasons such as low free float or poor liquidity. It may also indicate a business that is in serious operational or financial difficulty. Alternatively, a low rating may simply be a result of cyclical pressures. Empirical evidence suggests that stock-markets de-rate industrial stocks too aggressively when earnings are at or are close to cyclical troughs.

### Exhibit 2: Rising revisions

Generally speaking, stock-markets struggle to value companies with cyclical earnings streams.

Analysts struggle to model operating leverage, particularly in asset intensive companies such as those found in the Industrials sector. As a result, consensus earnings may be upgraded continually as business conditions improve. Empirical evidence suggests this alone can drive positive share price performance.

Our second screen looks for companies with positive earnings revisions. The stock universe is ranked by percentage change to 2013 consensus earnings over one-month, three-months, and 12-months respectively. An equal weighted composite rank is then computed.

This screen provides us with a list of top 20 'momentum' stocks which have the potential to both produce positive earnings surprises and attract a higher stock-market rating, particularly if valuation is supportive.

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