

# Deutsche Beteiligungs

Steady progress in the first quarter of FY18

Deutsche Beteiligungs (DBAG) reported a 2.7% NAV return for the three months ended 31 December 2017, with the period characterised by a high level of transaction activity at existing portfolio companies. Two new management buyout investments alongside the DBAG ECF fund were completed after the quarter end, with DBAG investing a total of up to €9.1m in specialist aluminium and steel component manufacturer, Sjølund, and fibre optic network services provider, netzkontor nord. Management guidance for FY18 is unchanged, with net income expected to be above the five-year average and NAV return below the five-year average.

12 months ending	Share price (%)	NAV (%)	LPX Europe (%)	LPX Europe NAV (%)	SDAX (%)	FTSE All-Share (%)
31/01/14	14.8	12.4	23.8	13.5	21.9	14.9
31/01/15	33.3	15.6	20.3	15.4	8.8	17.0
31/12/15*	14.6	15.1	14.0	7.5	18.9	0.3
31/12/16	4.8	8.7	10.3	7.5	4.6	0.8
31/12/17	60.7	24.6	18.9	13.2	24.9	8.8

Source: Thomson Datastream, Bloomberg. Note: \*11-month period due to change in financial year end. Discrete total return performance in euros.

## Gains driven by improving underlying earnings

DBAG reported €11.4m net income, with a 2.7% NAV return for the first quarter of FY18. Valuation gains were driven by improved earnings expectations for portfolio companies, partly offset by a decline in the market valuation multiples applied to portfolio holdings. Private equity investments accounted for the bulk of earnings, with fund investment services also making a positive contribution. There was a high level of transaction activity involving DBAG's existing portfolio companies, including Cleanpart selling one of its business lines, the partial disposal of Silbitz to a strategic investor, a number of strategic acquisitions by Pfaudler and vitronet, and Polytech pursuing a merger accompanied by a capital increase.

## Outlook: Robust medium-term perspective

DBAG management has confirmed its outlook for FY18 and the following two financial years, given on publication of FY17 results in November 2017. Guidance is for FY18 net income to be more than 20% higher than the €43m average of the last five financial years, followed by a moderate 10-20% rise in FY19 and FY20. DBAG's dividend-adjusted NAV return in FY18 is anticipated to be more than one-fifth lower than the 15.7% five-year average, then rising by more than 20% in FY19 and FY20. Cash drag on performance is expected to decline over these three financial years, as the current high level of financial resources is invested and the pace of realisations moderates after the exceptional level of divestments in FY17.

## Valuation: Premium reflects continuing robust growth

In our view, the primary contributor to DBAG's shares trading at a premium to NAV is the value attributed by the market to its fund services business. We see the current headline 52.8% premium to NAV implying that a c 18% premium is also being applied to the private equity investment business, arguably reflecting an expectation of robust growth continuing over the next 12 to 24 months.

## Investment companies

13 February 2018

**Price** €46.35  
**Market cap** €697m  
**NAV\*** €456m

NAV\* €30.34  
 Premium to NAV 52.8%

\*As at 31 December 2017.

Yield 3.0%  
 Ordinary shares in issue 15.0m  
 Code DBAN  
 Primary exchange Frankfurt  
 Sector Private equity  
 Benchmark N/A

## Share price/premium performance



## Three-year performance vs index



52-week high/low €52.20 €31.21  
 NAV\*\* high/low €30.34 €26.26

\*\*Including income.

## Gearing

Gross\* 0.0%  
 Net cash\* 34.0%

\*As at 31 December 2017.

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### Exhibit 1: Company at a glance

#### Investment objective and fund background

DBAG is a Germany-based and listed private equity investment and fund management company that invests in mid-sized companies in Germany and neighbouring German-speaking countries via MBO transactions and growth capital financings. There is a focus on growth-driven profitable businesses valued at between €50m and €250m. DBAG's core objective is to sustainably increase net asset value.

#### Recent developments

- 8 February 2018: Q118 results – NAV TR +2.6% vs LPX Europe NAV TR +5.3%.
- 15 January 2018: Announcement of MBO investment in netzkontor nord, a fibre optic network construction and network management services provider.
- 9 January 2018: Announcement of MBO investment in Sjølund, a Denmark-based manufacturer of aluminium and steel components, focused on the wind power and rail industries.
- 23 November 2017: FY17 final results – NAV TR +25.8% vs LPX Europe NAV TR +14.6%; €1.40 per share FY17 dividend proposed.

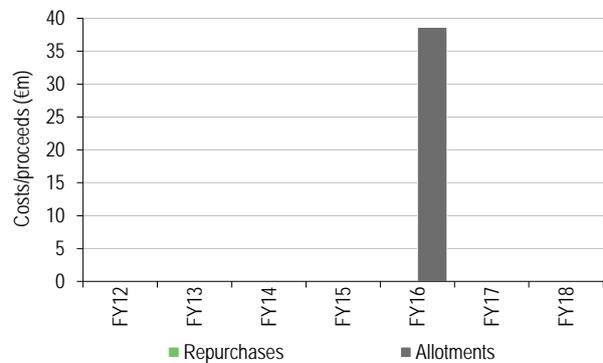
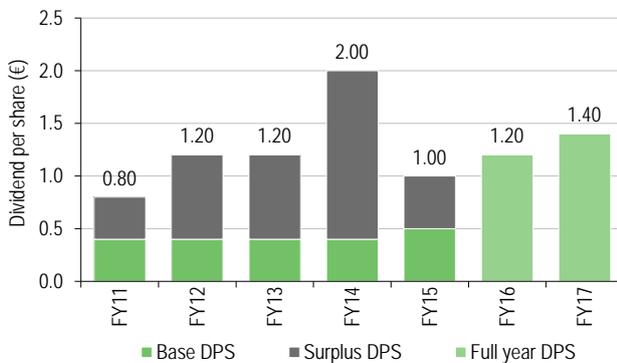
Forthcoming		Capital structure		Fund details	
AGM	21 February 2018	FY17 net expense ratio*	0.4% (0.8% unadjusted)	Group	Deutsche Beteiligungs
Quarterly results	8 May 2018	Net cash	34.0%**	Manager	Team managed
Year end	30 September	Annual mgmt fee	N/A (self-managed)	Address	Boersenstrasse 1
Dividend paid	26 February 2018	Performance fee	N/A (self-managed)		60313 Frankfurt am Main, Germany
Launch date	December 1985	Company life	Unlimited	Phone	+49 69 95787-01
Continuation vote	N/A	Loan facilities	€50m	Website	<a href="http://www.dbag.de">www.dbag.de</a>

#### Dividend policy and history (financial years)

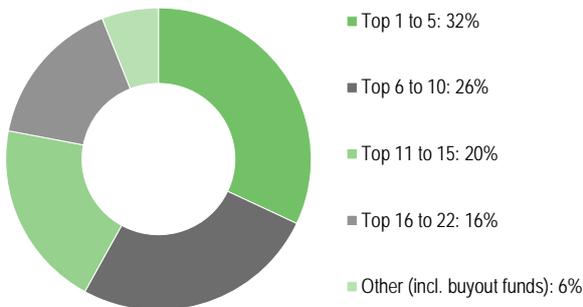
DBAG's policy is to pay a stable or rising annual dividend. Prior to FY16, a base dividend was paid, supplemented by a surplus dividend based on realised gains.

#### Share buyback policy and history (financial years)

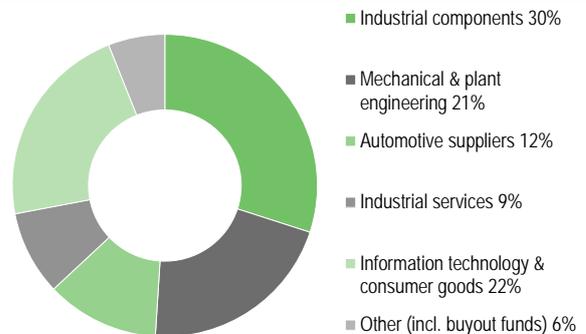
Share buybacks and capital increases are used to manage longer-term capital requirements. In FY16, a 10% capital increase raised €38.6m.



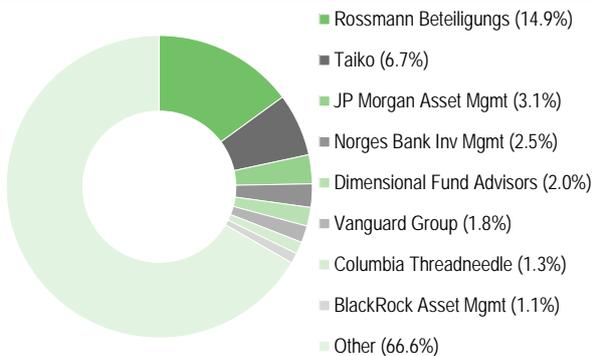
#### Concentration of portfolio value by size (as at 31 December 2017)\*\*\*



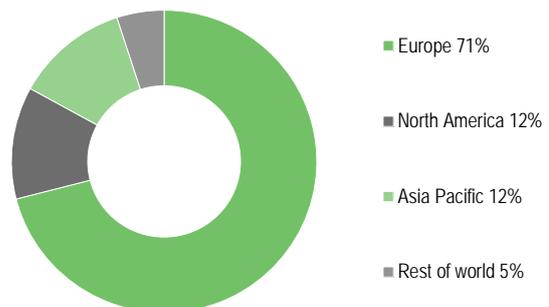
#### Portfolio exposure by sector (as at 31 December 2017)\*\*\*



#### Shareholder base (latest available data as at 12 February 2018)



#### Portfolio companies' revenues by region (latest available data)\*\*\*



Source: DBAG, Edison Investment Research, Bloomberg, Thomson Reuters. Note: \*Based on expenses net of fee income; adjusted for non-recurring items. \*\*Including €33.5m of securities classified as long-term assets. \*\*\*Does not include co-investment funds.

## Highlights of the first quarter of FY18

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DBAG reported net income of €11.4m and a NAV return of 2.7% for the first quarter of FY18, with valuation gains mainly driven by an improvement in earnings expectations for the portfolio companies in 2018 versus 2017. A decline in the market earnings multiples used to value portfolio companies (largely a result of moving from 2017 EV/EBITDA multiples to 2018 EV/EBITDA multiples) held back valuation gains during the quarter. Both business lines reported positive pre-tax income; private equity investments contributed €10.8m and fund investment services €0.7m. NAV per share increased from €29.57 at end-September 2017 to €30.34 at end-December 2017.

The first three months of the financial year were characterised by a high level of transaction activity involving DBAG's existing portfolio companies, including Cleanpart selling one of its business lines, the partial disposal of Silbitz to a strategic investor, a number of strategic acquisitions by Pfaudler and vitronet, and Polytech pursuing a merger accompanied by a capital increase.

### New investments

DBAG agreed two new investments alongside DBAG ECF during the quarter, representing the fund's first transactions since the start of its new investment period in June 2017. The management buyouts of Sjølund and netzkontor nord were completed after the quarter-end and, following these investments, more than a quarter of the capital committed to this investment period (referred to as DBAG ECF I) has been called.

#### Sjølund

In January 2018, the DBAG ECF fund acquired a c 51% stake in specialist aluminium and steel component manufacturer, Sjølund, from its founder and CEO Søren Ravn Jensen, with DBAG investing up to €4.5m for a c 21% stake. Søren Ravn Jensen has retained a c 49% stake in Sjølund and continues to serve as CEO alongside the other members of the management team. This is the first acquisition within the DBAG ECF I investment period, and the second buyout transaction for the DBAG ECF fund, which broadened its investment criteria in 2016 to include MBO transactions as well as expansion capital investments.

Since 1994, Sjølund has grown to become a leading manufacturer of complex bent aluminium and steel components, generating around half of its c €31m revenues in the year to 30 September 2017 in the wind power industry, mainly from wind turbine components. Headquartered in Denmark, with a production site in China and around 110 employees, Sjølund generates c 35% of its revenues from German customers but has established a global presence.

Sjølund's end-markets are expected to grow significantly over the next few years, driven by the increasing use of renewable energy, global population growth and increasing urbanisation. DBAG's investment will support the company's plans to expand its business with existing customers in high-growth markets such as China and the US, as well as increasing its focus on the highly profitable mechanical engineering sector, one of DBAG's core areas of expertise.

#### netzkontor nord

Also in January 2018, DBAG ECF invested in the management buyout of netzkontor nord, with DBAG contributing up to €4.6m for a c 34% stake. The company's founders, Dirk Müller and Peter Schmidt, have retained an equity stake and continue to serve as managing partners. Established in 2008 and headquartered in Flensburg, Germany, netzkontor offers planning and supervision services for fibre optic network construction, while its subsidiary OpenXS provides fibre optic network management services. Currently focused on the region of Schleswig-Holstein, netzkontor has c 100 employees and generated sales of c €8m in 2017.

Broadband coverage has expanded at a sluggish pace in Germany, with over 40 million households not yet connected to a fibre optic network, and the government is subsidising network development. Its reputation as a reliable, high-quality provider and its project management expertise provide a strong foundation for netzkontor's plans to pursue regional expansion and diversify its customer base. DBAG will support this development with the investment and expertise gained from its three current investments in the sector (inexio, DNS:NET, vitronet).

## Commitments and financial resources

At 31 December 2017, DBAG had €256.4m in undrawn capital commitments to the DBAG ECF and DBAG Fund VII funds. Based on the expected investment programmes for these two funds over the current and two following financial years, DBAG management anticipates an average annual investment run rate of c €70m.

During the first quarter of FY18, DBAG's financial resources declined modestly from €161.6m to €155.3m (including €33.5m of securities classified as long-term assets), with no major new investments or divestments completed during the period. At end-December 2017, a further €25.9m in cash and securities was held in unconsolidated investment entities, which included proceeds received following the sale of a business line by portfolio company Cleanpart and its subsequent refinancing. DBAG's share of the new investments in Sjølund and netzkontor nord, which were completed after the quarter-end, totalled €9.1m, leaving DBAG with sufficient funds to meet its expected financial commitments over at least the next 12 months. In addition to its current funds, realisations from the existing portfolio would add to DBAG's financial resources and it also has a €50m credit facility, which it can draw on to manage short-term cash flow timing differences.

## Valuation: Near-term robust growth being discounted

As illustrated in Exhibit 2, DBAG's shares have traded at a premium to NAV for most of the period since end-January 2015, shortly after it started reporting separately on its private equity investment and fund services businesses. While its investment portfolio is reported at fair value, DBAG's published NAV does not reflect the market value of its fund services business, which has c €1.7bn of third-party assets under management and generates a substantial fee income stream. DBAG's share price reflects the value of both businesses, and we see the value attributed by the market to the fund services business as the principal reason for DBAG's shares trading at a premium to NAV.

**Exhibit 2: Share price premium/discount to NAV over three years (%)**



Source: Thomson Datastream, Edison Investment Research

In our view, the expected strong valuation gains from several successful realisations accounted for the premium reaching 62.4% in May 2017 (an all-time high at that point), while the current c €240m or 52.8% premium to NAV appears to reflect a premium being applied to the private equity investment business, in addition to the value attributed to the fund services business.

Our earlier analysis (included in our [August 2017 note](#)) suggested that the market was attributing a valuation of up to c €160m to DBAG's fund services business, giving a market-implied valuation multiple of between 23x and 40x earnings. We do not consider that the earnings outlook for the fund services business has altered materially since the launch of DBAG Fund VII at the end of 2016, which leads us to infer that the market is applying a c €80m premium to DBAG's private equity investments business, which equates to a c 18% premium to NAV. The implication of this premium is that the market has increased conviction that DBAG's robust NAV growth will continue over the next 12 to 24 months. This expectation is arguably driven by DBAG's exceptionally strong performance in FY17, as well as the broader development of the business, giving an expanded universe of investment opportunities.

## Peer group comparison

Exhibit 3 shows a comparison of DBAG with a selected peer group of Europe-focused, listed private equity investment companies. As well as its particular focus on German Mittelstand companies, DBAG is differentiated from its listed private equity peers by managing third-party funds, with the exception of 3i in the UK. As noted in the Valuation section above, DBAG's shares are trading at a substantial premium to its reported NAV. This contrasts with the majority of the peer group that do not manage third-party funds, some of which are trading at a significant discount to NAV. DBAG's 3.0% yield, based on its proposed €1.40 dividend for FY17, is higher than the peer group average.

**Exhibit 3: Listed private equity investment companies peer group as at 12 February 2018\***

% unless stated	Country	Mkt cap €m	NAV TR 1 year	NAV TR 3 years	NAV TR 5 years	NAV TR 10 years	Price TR 1 year	Price TR 3 years	Price TR 5 years	Price TR 10 years	Premium/ (discount)	Dividend yield (%)
Deutsche Beteiligungs	Europe	619.2	29.0	85.9	127.2	173.0	66.3	141.0	230.5	408.4	52.6	3.0
3i	Global	8,660.5	31.2	117.5	214.4	33.9	33.7	126.8	409.9	52.9	27.9	3.0
Electra Private Equity	UK	337.3	7.3	86.4	140.6	199.3	17.0	98.0	212.7	284.5	(20.9)	0.0
HgCapital Trust	UK	640.1	17.2	59.1	75.5	153.1	19.3	85.4	106.3	204.8	(5.2)	2.7
ICG Enterprise Trust	UK	556.9	16.3	46.4	73.0	109.4	21.2	54.4	103.9	102.7	(12.8)	2.5
Oakley Capital Investments	Europe	336.9	1.0	18.5	31.6	140.5	1.5	10.6	25.2	68.3	(28.8)	2.7
Princess Private Equity	Global	590.2	15.7	68.9	87.9	106.9	34.8	109.9	139.6	171.4	(10.0)	5.7
Standard Life Private Equity	Europe	513.5	10.8	55.4	88.4	75.4	21.2	75.1	137.5	90.2	(14.1)	3.7
<b>Average</b>		<b>1,531.8</b>	<b>16.1</b>	<b>67.3</b>	<b>104.8</b>	<b>123.9</b>	<b>26.9</b>	<b>87.7</b>	<b>170.7</b>	<b>172.9</b>	<b>(1.4)</b>	<b>2.9</b>
<b>Rank in peer group</b>		<b>3</b>	<b>2</b>	<b>3</b>	<b>3</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>3</b>

Source: Morningstar, Edison Investment Research. Note: \*Performance data to end-December 2017. TR = total return. All returns expressed in sterling terms.

DBAG's NAV total return in sterling terms to 31 December 2017 is appreciably ahead of the peer group average over one, three, five and 10 years, ranking second or third out of eight over each time period. DBAG's share price total return has outperformed its NAV total return over all time periods shown to end-December 2017. This reflects the shares moving to trade at a significant premium to NAV over the last two years, while the shares traded at a discount as wide as 57.8% during the 2008 global financial crisis.

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