EDISON

Scale research report - Update

Delignit

Materials

12 September 2017

Investment paying off

Strong H1 results (EBITDA +42%) and recent major orders in the LCV and rail transport segments reinforce confidence in confirmed positive profit guidance for 2017. Moreover, it is particularly encouraging that well-defined strategic development looks increasingly to be paying off, with the current 2016/17 €6m bumper capex affording capacity expansion, efficiency gains and a more diversified revenue base. Finances remain secure (net debt/EBITDA of 1.3x for the last 12 months), allowing ample room for further investment.

Pleasing H1

The half to June combined continued buoyancy (revenue +11%) with a significant improvement in profitability (EBITDA margin 9% against 7% y-o-y). While Automotive, Delignit's principal sector, was to the fore (+12%) thanks, as in 2016, to strong OEM business and new orders from carmakers, Technological Applications managed to improve on a demanding comparative. Again, as previously, exports were the driver, justifying the company's strategic broadening. The step-change in trading profit (+65%) reflected investment-led economies of scale, with material costs and depreciation respectively up just 4% and 7%.

More growth to come – 2017 forecasts maintained

Management expects more of the same in the second half. Positive conditions apart, Automotive should benefit materially from follow-up work from 2016 as well as new orders, while Technological Applications has newly won contracts for floor solutions for trains from the European subsidiary of an Asian group. Confirmed full-year guidance is for 10-15% higher sales and EBITDA margin of 7.5-8.3% against 7.5% in 2016. Clear EBITDA margin outperformance (9%) in H1 on such volume enhancement suggests that this full-year forecast may well prove cautious.

Valuation: Not cheap

Recent share price consolidation (flat over the past two months) after sharp c 30% appreciation in June suggests that the market is awaiting further evidence of Delignit's strong growth prospects. The stock is now trading at an FY16 P/E ratio of c 33x – a premium to both its wood processing and automotive supplier peer group. Management guidance (no consensus data available) for FY17 suggests an EV/EBITDA multiple of 12.2-14.2x, which, even if cautious, is well ahead of the 5.9x peer average.

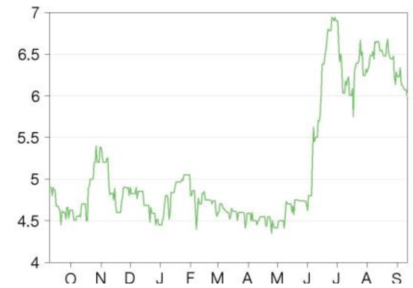
Historical financials

Year end	Revenue (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/13	35.3	2.2	0.21	0.00	28.5	N/A
12/14	42.7	1.7	0.13	0.03	46.1	0.5
12/15	44.4	1.7	0.14	0.03	42.8	0.5
12/16	48.6	2.1	0.18	0.03	33.3	0.5

Source: Delignit accounts, Edison Investment Research

Price	**€5.99**
Market cap	**€49m**

Share price graph



Share details

Code	DLX
Listing	Deutsche Börse Scale
Shares in issue	8.2m
Last reported net debt at June 2017	€5.8m

Business description

Delignit is a German manufacturer of ecological products and system solutions based on hardwood for the automotive, rail and safety equipment industries. It was acquired by Germany-based industrial holding company MBB (Messerschmitt-Bölkow-Blohm) in 2003 and was listed in 2007. Two-thirds of group sales are derived domestically.

Bull

- Solid order intake in the LCV and rail transport segments.
- Increased and enhanced applications for existing products.
- Rapid take-up of the products in global markets.

Bear

- High dependence on large OEM contracts.
- An increase in oil prices could reduce the company's profitability.
- Valuations already factor in growth prospects, creating downside risk.

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Review of H117 results

Exhibit 1: Analysis of half-yearly revenue and profit

Year end December (€m)	H116	H216	FY16	H117	FY17 F/C
REVENUE	**24.4**	**24.2**	**48.6**	**27.1**	**53.5 – 55.9**
Change (%)	**+6%**	**+13%**	**+9%**	**+11%**	**+10-15%**
Automotive			35.2		
Change	+1%		+8%	+12%	
Technological applications			13.3		
Change	+22%		+12%	+8%	
Germany	17.4	16.6	34.0	16.6	
Change	+1%	+2%	+1%	-5%	
Exports	7.0	7.6	14.6	10.5	
Change	+23%	+46%	+34%	+50%	
Other income	0.5	0.4	0.9	0.3	
Total income	**24.9**	**24.6**	**49.5**	**27.4**	
Material costs	(14.9)	(14.0)	(28.9)	(15.5)	
Labour costs	(6.6)	(6.9)	(13.5)	(7.6)	
Other operating costs	(1.7)	(1.7)	(3.4)	(1.8)	
EBITDA	**1.7**	**2.0**	**3.7**	**2.5**	**4.0 – 4.6**
Margin	**7.0%**	**8.1%**	**7.5%**	**9.0%**	**+7.5 – 8.3%**
Depreciation	(0.7)	(0.7)	(1.4)	(0.7)	
EBIT	**1.1**	**1.3**	**2.4**	**1.7**	
Net interest	(0.1)	(0.1)	(0.2)	(0.1)	
Pre-Tax Profit	**1.0**	**1.1**	**2.1**	**1.6**	
Taxation	(0.3)	(0.4)	(0.7)	(0.5)	
Net income	**0.7**	**0.7**	**1.4**	**1.1**	

Source: Delignit accounts

While Delignit's H1 performance was much as expected, it was no less impressive. Strong top-line growth across the board at much higher margin was accompanied by a further surge in export business (c 40% of group sales against c 30% y-o-y) and consequent successful diversification. The main activity, Automotive, saw double-digit growth thanks to continued OEM demand and additional orders from car makers. Notwithstanding positive macro conditions, such buoyancy is justifiably attributed by management to early signs that its record investment (€6m) last year and this is paying off in terms of both customised system solutions and expanded product applications.

Good control of costs (see Exhibit 1) elicited material margin gain, notably an EBITDA margin of 9% against 7% in H116. With depreciation and finance costs broadly unchanged, the revenue boost was yet more evident further down the line (pre-tax profit up 70%).

H2 confidence

Maintained trading momentum and H1 EBITDA margin (9%) well ahead of full-year guidance give confidence that management expectations should be met, if not exceeded. As shown above, even management's worst-case EBITDA outturn in H2 (€1.5m) would imply c 6% margin, which the company has comfortably achieved throughout the last five years. Even their best-case EBITDA outturn (€2.1m) may prove cautious as the assumed margin would only be on a par with that of H216. This would seem to contradict management's conviction that economies of scale from the ongoing investment programme should only boost margins.

Balance sheet and cash flow

Cash flow was slightly negative in H117 as a result of continued historically high capex and increased stocks. Nevertheless period end net debt of €5.8m ensures that Delignit remains lowly borrowed with minimal interest cover.

Valuation

As there are no companies that match closely Delignit's profile, we have identified for peer comparison four wood processing companies, even if with lower exposure to the automotive sector (Westag & Getalit, Pfleiderer, Surteco and Ober) as well as four automotive suppliers (Grammer, Progress Werk, SHW and Delfingen) offering products such as seat covers, insulation, components and systems for car interiors.

As consensus forecasts for Delignit are not available, we have conducted a comparative analysis based on the last two reported years, as well as management's EBITDA margin guidance for 2017. After the Q2 share price rally Delignit trades at a marked premium to the blended peer group on trailing P/E (84%) and trailing EV/EBITDA (127%). This suggests that the company's robust growth outlook is priced in. Management's newly confirmed guidance for the full-year implies EV/EBITDA of 12.2-14.2x, well ahead of the 5.9x peer average.

Exhibit 2: Peer group comparison

	Market cap	P/E (x)		EV/EBITDA (x)	
	(€m)	2016	2017e	2016	2017e
Wood processing companies					
Westag & Getalit	137	18.3	17.3	5.7	N/A
Pfleiderer	661	44.4	19.7	8.2	5.9
Surteco	385	16.5	14.6	7.0	6.8
Ober	18	14.1	N/A	7.6	N/A
Automotive suppliers					
Grammer	568	11.3	10.7	5.9	5.8
Progress Werk	136	14.3	11.4	5.8	5.5
SHW	228	17.9	N/A	5.2	N/A
Delfingen	96	13.3	N/A	7.5	5.6
Peer group average		18.8	14.7	6.6	5.9
Delignit	51	34.6	N/A	15.0	12.2-14.2
Premium (discount) to peer group		84%	N/A	127%	124%

Source: Company accounts, Bloomberg, company guidance. Note: Prices as of 4 September 2017.

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