EDISON Scale research report - Update

Delignit

Materials

1 September 2020

Gradual recovery ahead

Delignit's H120 results were clearly affected by the COVID-19 pandemic, with revenues down 20.6% and EBITDA decreasing by 35%. Cost-cutting measures, such as using so-called Kurzarbeit (short-time working arrangements) and reducing temporary work, have somewhat limited the decline in profitability. Delignit's FY20 guidance assumes a 5–21% y-o-y fall in revenues in H220, which implies at least flat revenue in H2 vs H1. Longer term, Delignit will benefit from expected growth in commercial vehicles, further geographical expansion and broadening its product offering.

H120 results clearly hit by COVID-19

After a good start to 2020, Delignit's performance was hit by the impact of COVID-19 as many customers temporarily closed their plants. This resulted in a decline in H120 revenues of 20.6% to €25.6m. The company reacted to the changed market environment by adjusting its own capacity, using short-time working arrangements and reducing the number of temporary staff. These factors have somewhat limited the decline in EBITDA, which fell 35% to €1.6m. This implies a margin decline of 70bp to 6.2%.

FY20 guidance assumes 13–21% revenue decline

Delignit updated its guidance for FY20 and now expects revenues in the range of €51–56m, which reflects a decline of 5–21% y-o-y in H220. This implies at least flat revenue in H2 vs H1. If the current economic recovery continues in the second half, Delignit could therefore end up at the higher end of the guidance range. In its automotive activities, the company is experiencing a stabilisation in orders for the remainder of the year. Industry data also show strong growth in the motor caravan market in Germany, a relatively new market segment for Delignit. While its long-term ambition of generating revenues in excess of €100m and an EBITDA margin of at least 10% remain intact, COVID-19 could result in a delay in achieving these targets to beyond 2023.

Valuation: Assuming strong recovery

Consensus expects a decline in EBITDA to €3.7m in FY20, which assumes a better result in H220 compared to the first half. Based on consensus figures for EV/EBITDA in FY21e, Delignit is valued at a premium to its peers of 97%. This suggests that investors are confident in management's ability to deliver growth over the next few years on the back of the post COVID-19 economic recovery.

Consensus estimates

Year end	Revenue (€m)	EBITDA (€m)	EPS (€)	DPS (€)	P/E (x)	EV/EBITDA (x)
12/18	60.3	5.6	0.31	0.05	14.3	7.0
12/19	64.4	4.8	0.17	0.00	26.0	8.1
12/20e	54.5	3.7	0.05	0.01	88.4	13.0
12/21e	60.7	5.1	0.17	0.05	26.0	9.4

Source: Delignit, Refinitiv as at 27 August 2020

Price	€4.42
Market cap	€36m

Share price graph

Share details

Code	DLX
Listing	Deutsche Börse Scale
Shares in issue	8.2m
Net debt at 30 June 2020	€12m

Business description

Delignit manufactures ecological products and system solutions based on sustainable raw materials for technology sectors such as the automotive and rail transport industry. Delignit's material is predominantly based on European hardwood and is CO_2 neutral in its lifecycle. Exports account for >50% of sales. MBB is the majority shareholder with 76%.

Bull

- New serial supply contracts LCV segment.
- Increased and enhanced applications for existing products.
- Expanding in adjacent markets.

Bear

- High dependence on large OEM contracts.
- An increase in oil prices could reduce the company's profitability.
- Valuation already factors in growth prospects.

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Edison profile page

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H120 results negatively affected by COVID-19

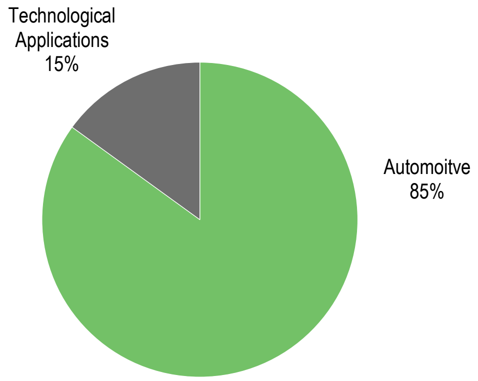
At the beginning of 2020, management was very positive about the company's outlook for FY20, which was supported by revenue growth in the first two months of the year. Due to the impact of COVID-19, Delignit's performance in H1 was negatively affected by the temporarily closure of plants by its customers. In H120, revenues declined 20.6% to €25.6m. Most market segments in the automotive and engineered wood industries were severely affected as described below.

According to the European Automobile Manufacturers' Association (ACEA), the number of new registrations of light commercial vehicles (LCVs) in Europe in H120 fell by 32%, with the decline in Delignit's home market, Germany, better than the average at 25%. New registrations of passenger cars in Europe declined by 38% in H120, while the decline in Germany was also better than the European average at 35%.

The market for motor caravans in Germany showed good growth of 12% in H120, with strong numbers in June after the negative impact of COVID-19 in April and May (according to the Caravaning Industry Association, CIVD). Delignit showed higher revenues in this segment, although the number of call-offs under the serial supply contract were lower than expected at the beginning of the year, which seemed to be caused mainly by over-planning on the part of the customer. In this multiple-year contract, Delignit is delivering its proposition for a completely new model for this customer.

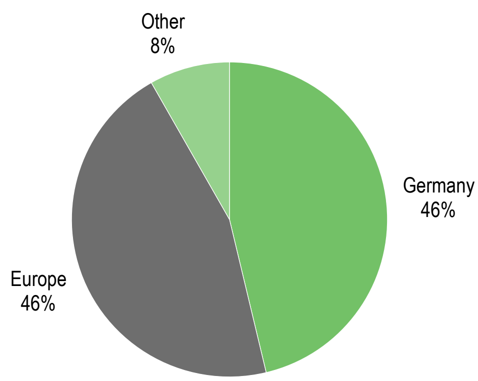
According to the German Federal Statistical Office, the engineered wood industry started the year on a strong note, with 3.4% growth in the first quarter, but due to the impact of COVID-19 the first five months of the year ended with a decline of 6%.

Exhibit 1: Revenue by segment FY19



Source: Delignit, Edison Investment Research

Exhibit 2: Revenue by geography FY19



Source: Delignit, Edison Investment Research

In Delignit's Automotive segment, comprising the product groups LCVs, motor caravans and passenger cars, revenues declined by 19.6% in H120 after good growth over the past two years. This decline is less severe compared to figures for the respective broader market segments in Europe (LCV -32% and passenger cars -38%). The company seems to have gained market share in its respective markets. Another reason for the relative outperformance is the build-up of volumes under the serial supply contract in the motor caravan market, where revenues increased by €1.2m to €3.1m in H120. On the other hand, the new order for transport fastening, which was announced at the beginning of the year, was amended by the customer and is now much smaller than previously anticipated.

In Technological Applications, revenues declined 25.8% in H120, thereby continuing the trend demonstrated over the past two years. This segment has also seen a negative impact from the COVID-19 pandemic. The positive development in building equipment was offset by declines in compressed wood, railfloor and special applications.

In response to the shutdown of plants by its customers, Delignit has adapted its own capacity to the changing market conditions. It also made use of the government arrangement, Kurzarbeit, in Germany (short-time working) and cut back on temporary work. In the motor caravan segment, Delignit improved its cost structure with the optimisation measures taken in mid-2019, which reduced the negative effect of this activity on earnings in H120. These factors somewhat limited the decline in EBITDA, which ended up 35% lower at €1.6m.

Exhibit 3: H120 results

€m	H118	H119	H120
Automotive, change y-o-y	15%	20%	-20%
Technological Applications, change y-o-y	-10%	-21%	-26%
Total revenues	29.4	32.3	25.6
Change y-o-y	8%	10%	-21%
Gross margin	47.3%	42.3%	44.7%
Staff costs	-8.6	-8.4	-7.8
Other operating expenses	-2.4	-2.8	-2.1
EBITDA	2.9	2.4	1.6
Change y-o-y	16%	-16%	-35%
EBITDA margin	9.9%	6.9%	6.2%
Depreciation	-0.8	-1.1	-1.3
EBIT	2.1	1.3	0.3
Net interest	-0.1	-0.1	-0.1
Pre-tax profit	2.0	1.2	0.1
Taxation	-0.6	-0.4	-0.1
Net income	1.4	0.8	0.0
Number of shares (m)	8.2	8.2	8.2
EPS (€)	0.17	0.10	0.01

Source: Delignit

Outlook

Delignit had to revise its positive outlook for 2020 due to the impact of the COVID-19 pandemic. On 24 February 2020, management provided guidance for revenues to exceed €70m with an EBITDA margin of >8%. In March, management stated that the previous guidance could not be upheld. After the decline in revenues of 20.6% in the first half of 2020, the company now expects full-year revenues in the range of €51–56m, assuming the economic recovery that started in June continues in the second half of 2020. The updated guidance reflects revenue of €25.4–30.4m in the second half, or a decline of 5–21% y-o-y. The eventual outcome obviously depends on the development of the COVID-19 pandemic and the pace of economic recovery. In the automotive market, the company is seeing orders stabilising for the remainder of the year. Looking at the data provided by ACEA, June showed a decline of 10% y-o-y in the LCV segment, which is significantly better than the reported decline of 41% in May. Management confirmed the same trend at Delignit. The motor caravan market is holding its momentum, with almost double the number of new registrations in July in Germany, resulting in growth of 23% in the first seven months of 2020.

Due to the uncertainty about economic development, management is not providing guidance at profit level.

Delignit continues to expand in the automotive segment. Last November, the company announced a new order for a system floor solution for a new eLCV, which has sales potential of more than €15m over the term of the contract (2022–32). According to IDTechEx, the eLCV segment represents 3% of the total LCV segment and is expected to increase to 23% in 2030.

The company's long-term ambition remains for revenue of at least €100m and an EBITDA margin of at least 10%. These targets were previously set for 2022, but at the beginning of 2020 were 'postponed' to the end of 2023. Due to the COVID-19 pandemic it is currently uncertain whether these ambitions will be further delayed. Despite the short-term uncertainty, in the longer term the company will benefit from expected growth in commercial vehicle usage, further geographical expansion and broadening its product offering.

Financial position

Despite the lower results, the level of Delignit's equity ratio is still strong at 48%. H120 net debt increased by €1.4m to €12.0m vs H119. There are no bank covenants. Management expects the company to be able to meet its financial obligations at all times and sees no risks in the short term that interest costs might increase.

The company does not have a specific dividend policy but has paid a dividend over the past few years. However, due to the impact of the COVID-19 pandemic, management decided not to pay any dividends for 2019.

Valuation

There are no companies that closely match Delignit's business profile. We have selected two wood processing companies, namely Surteco and Ober, although these companies have lower exposure to the automotive sector compared to Delignit. We also compare Delignit with automotive suppliers Grammer, Progress Werk, SHW and Delfingen, which offer a range of products such as seat covers, insulation, components and systems for car interiors.

As shown in Exhibit 4, Delignit trades at a large premium to the peer group on EV/EBITDA. This might suggest that investors are confident in management's ability to deliver growth over the next few years on the back of the post COVID-19 economic recovery. Also, Delignit could be less affected by current market conditions than its pure automotive peers, thanks to its more diversified business model.

Exhibit 4: Peer group comparison

	Market cap	EV/EBITDA (x)			P/E (x)		
	(€m)	FY19	FY20e	FY21e	FY19	FY20e	FY21e
Wood processing companies							
Surteco	342.7	7.7	7.5	6.7	36.2	22.0	14.9
Ober	11.4	N/A	N/A	N/A	9.5	785.0	12.1
Automotive suppliers							
Grammer	174.3	3.0	8.0	3.5	4.0	N/A	6.3
Progress Werk	59.1	4.2	8.3	4.7	N/A	N/A	8.0
SHW	96.5	3.6	8.4	4.9	9.7	N/A	N/A
Delfingen	33.1	3.6	7.0	4.1	3.9	16.5	4.0
Peer group average		**4.4**	**7.8**	**4.8**	**12.7**	**274.5**	**9.1**
Delignit	36.0	8.1	13.0	9.4	31.4	88.4	26.0
Premium/(discount) to peer group		**83%**	**66%**	**97%**	**148%**	**(68%)**	**187%**

Source: Refinitiv. Note: Prices at 27 August 2020.

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