

## DVS TECHNOLOGY

**Industrials**
**14 July 2020**

### Machine tools market under pressure

Significantly weaker markets and increased costs ahead of a ramp up in production, drove DVS TECHNOLOGY's 2019 revenue and reported EBIT down 1% and 49%, respectively. A comprehensive cost and efficiency plan was initiated after the H119 results and should bring savings in 2020. The coronavirus crisis has materially worsened the economic outlook and management now expects 2020 revenues and EBIT to be significantly lower compared to last year. The market contraction is also affecting the company's financial position, but management has stated that its financial resources should be sufficient to meet its existing payment obligations.

### FY19 results affected by weak markets

Weaker market conditions in machine tools in 2019 resulted in a decline in group revenues of 1% to €261.6m. Operating costs were up 8% in anticipation at that time of an upcoming ramp up in production. EBIT reported declined 49% to €8.8m, reflecting a margin decline of 310bps to 3.4%. The weaker markets resulted in losses at three of the 13 subsidiaries. Net profit was around zero compared to a profit of €8.6m in FY18. We expect no dividend payment from the 2019 results.

### Outlook worsened by the coronavirus crisis

With its order intake down 18% at end 2019 compared with end 2018, management started 2020 with a cautious yearly budget. At that point, it had expected 7% lower revenues and an improvement in adjusted EBIT margin of 160bps to 4.4%, driven by cost savings. Deteriorating market conditions and then the coronavirus led to a 22% drop in Q120 in the company's order intake. This is a better performance than the decline of 30% in the machining tools market segment relevant for DVS. Management now anticipates significantly lower revenues and EBIT in 2020. In light of the deteriorating results, the company is in talks with its banks, seeking some debt condition flexibility if necessary. Management stated that it fulfilled all bank covenants in 2019 and that it can meet its existing financial obligations.

### Long recovery ahead

It is likely that the automotive sector, a key market for DVS, may be slow to recover. Industry body LMC Automotive predicts that it may take until 2025 to return to 2018 levels. Meanwhile, this period of weakness may mask the full benefits of DVS's cost control programme. The free float is only 2% and there are currently no consensus estimates available for DVS TECHNOLOGY. Recovery in demand is needed before the market can assess prospects.

#### Historical financials

Year end	Revenues (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/16	218.4	8.4	0.52	0.20	28.7	1.3
12/17	246.9	13.6	0.75	0.25	19.9	1.7
12/18	264.0	14.6	0.89	0.25	16.7	1.7
12/19	261.6	5.3	0.00	0.00	N/A	0.0

Source: DVS TECHNOLOGY

**Price** €14.90  
**Market cap** €143m

#### Share price graph



#### Share details

Code	DIS
Listing	Deutsche Börse Scale
Shares in issue	9.7m
Net debt at year-end FY19	€67m

#### Business description

Besides engineering and manufacturing machine tools as well as grinding and honing tools, DVS TECHNOLOGY operates two production sites where automotive parts are machined in series production exclusively on DVS machines. The company is organised around three business units: Machine Tools & Automation, Tools & Components and Production.

#### Bull

- Strong market position.
- Few strategic threats.
- Growth in contract manufacturing and tooling business.

#### Bear

- Very low free float.
- Several loss-making subsidiaries.
- Development of the automotive industry.

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## Review of 2019 results

In 2019, DVS TECHNOLOGY reported a decline in revenues of 1% to €261.6m, mainly driven by weaker market conditions across its businesses. According to the German Machine Tool Builders' Association (VDW), global production of machine tools in 2019 was down 4.5% from the record year 2018.

Results were under pressure from losses at three of the 13 subsidiaries (Buderus Grinding Technology, DVS Production South and DVS Production). EBIT dropped 49% to €8.8m reflecting a reported EBIT margin decline of 310bps to 3.4% (adjusted EBIT margin was 2.8%). Average staff numbers were 80 higher at 1,434, due to the start-up and ramp-up of new orders at DVS Production. Pre-tax profit came in at €5.3m, which is, as to be expected, below the guidance of €10m provided at the time of the H119 results.

After the lower than expected H119 results, DVS TECHNOLOGY took several measures to support its profitability, including a sales offensive, a halt to investment, a hiring freeze and further cost reductions in materials purchasing and personnel. Some of the benefits of these programmes were realised in 2019 but the full effect will be felt in 2020.

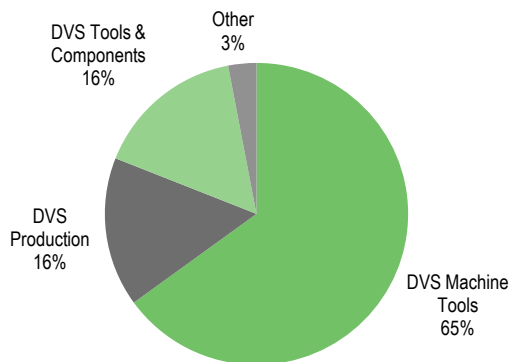
Net interest paid in 2019 was higher, including losses at associates. As a result, net profit came in at almost zero compared to a net profit of €8.6m in 2018. DVS TECHNOLOGY paid a dividend per share of €0.25 for 2018 but we do not expect any dividend payments for 2019. The company's AGM will be held on 19 August 2020.

<b>Exhibit 1: 2019 results DVS TECHNOLOGY</b>			
<b>Year-end December (€m), HGB</b>	<b>FY18</b>	<b>FY19</b>	<b>% change</b>
Revenue	264.0	261.6	-1%
Change in inventory	5.4	(2.5)	
Other operating income	1.8	3.7	
Total operating income	271.2	262.8	-3%
Other income	4.5	3.7	
Total income	275.7	266.5	-3%
Cost of materials	(126.1)	(113.8)	-10%
Personnel costs	(80.3)	(85.9)	7%
Other operating costs	(42.3)	(46.3)	9%
EBITDA	27.0	20.4	-24%
EBITDA margin	10.2%	7.8%	
Depreciation	(9.8)	(11.6)	18%
EBIT reported	17.2	8.8	-49%
EBIT adjusted	17.2	7.4	-57%
EBIT margin adjusted	6.5%	2.8%	
Net interest	(2.7)	(3.5)	33%
Pre-tax profit	14.6	5.3	-63%
PBT margin	5.5%	2.0%	
Tax	(6.0)	(5.3)	-11%
Net profit	8.6	0.0	

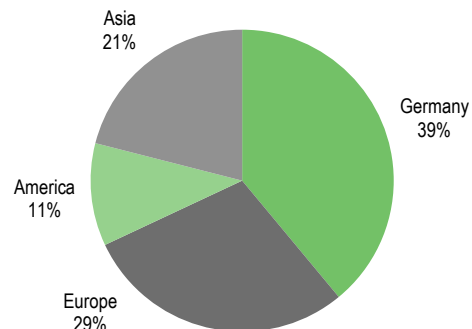
Source: DVS TECHNOLOGY, Edison Investment Research

DVS TECHNOLOGY has 13 subsidiaries, which are grouped in three divisions: Machine Tools (65% of total revenues), Production (16%) and Tools & Components (16%). Several smaller units are grouped in 'Other', which represented 3% of total revenues in 2019.

The largest geography remains homeland Germany, which represented 39% of total revenues in 2019 (see Exhibit 3 below). Growth in the different regions showed large differences in 2019 with Germany reporting a decline of 6% in revenues but the rest of Europe and America realising large increases of 19% and 58%, respectively. Revenues in Asia declined by 25% and the share in total revenues of this region declined to 21%.

**Exhibit 2: Revenues split by segment, FY19**


Source: DVS TECHNOLOGY

**Exhibit 3: Revenues split by geography, FY19**


Source: DVS TECHNOLOGY

## Outlook

Due to the weakened market conditions during H219, order intake at year-end 2019 was 18% lower at €225.7m, compared to end 2018. Almost all subsidiaries felt the impact of the market weakness and reduced customer demand. The order backlog at year-end 2019 stood at €101.0m, down 27% from end 2018. At the beginning of 2020, management had expected revenues in 2020 to be 7% lower at €245m and the EBIT margin, driven by cost savings, had been expected to rise to 4.4% up from 2.8% in 2019.

Since then, markets have contracted sharply, amplified by the effect of the coronavirus. This has seriously affected the performance of DVS TECHNOLOGY, in particular in the automotive segment. According to the German Machine Tool Builders' Association (VDW), the overall order intake in the machining segment relevant for DVS TECHNOLOGY was 30% lower in Q120 while production was down 23%. In Q120, order intake at DVS TECHNOLOGY declined 22%, thereby outperforming the market. Management refrains from any specific guidance for 2020 due to the highly uncertain market environment but does expect a significant decline in both revenues and EBIT.

Giving an oversight of the automotive industry, industry body LMC Automotive is projecting a fall of more than 20% in global light vehicle production to c 71m units in 2020 as a result of the COVID-19 pandemic. According to the European Automobile Manufacturers Association (ACEA), car sales volumes were down 42% in Q120 in China, 27% in Europe and 12% in the US. LMC does not anticipate a quick recovery in automotive and estimates that it could take five years until the levels of 2018 will be reached again.

## Financials

The lower than expected results in 2019 also had an effect on the company's financial position. Although solvency remained at a sound level of 51%, net debt/EBITDA increased from 2.4x to 3.3x. Net debt year-on-year was up 5% to €67.4m. Operating cash flow amounted to €13.1m and capex was €9.8m in 2019 while management expects a significantly lower capex of below €5m for 2020, mainly forced by the worsened market conditions.

In response to the worsening market conditions due to the coronavirus crisis, DVS TECHNOLOGY is in talks with its banks, for instance about the possibility of a covenant holiday. The company also agreed to suspend repayment of its real estate loans by up to six months and it is making use of Kurzarbeit (a short-term work allowance programme). In its press release of 29 May 2020, management stated that it assumes that its current financial resources will be sufficient to meet its existing payment obligations.

**Exhibit 4: Balance sheet DVS TECHNOLOGY**

Year-end December (€m)	FY18	FY19
Fixed assets	94	93
Current assets	151	155
Cash	10	9
Balance sheet total	259	253
Equity	132	129
Interest bearing debt	74	77
Other liabilities	53	47
Solvency	50.7%	51.1%
Net debt	64.4	67.4
Net debt / EBITDA	2.4	3.3

Source: DVS TECHNOLOGY, Edison Investment Research

The shareholder base of DVS TECHNOLOGY has not changed much in recent years with 98% currently in the hands of shareholders holding a stake of more than 5%. The shareholder base is dominated by the Rothenberger family, which remains on board as a long-term investor.

**Exhibit 5: Shareholders DVS TECHNOLOGY**

Shareholder	Stake
Rothenberger 4xS Vermögensverwaltung GmbH	65.8%
Günther Rothenberger Beteiligungen GmbH	17.6%
FWI Fritz Werner International GmbH	7.9%
Maschinenfabrik Heid AG	6.8%
Total of >5% stakes	98.1%
Free float	1.9%

Source: DVS TECHNOLOGY

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