

Blue Cap

Industrials

2 September 2019

Growing organically and through M&A

Blue Cap's (B7E) first-half revenues grew strongly, driven by Knauer (acquired in June 2018). Organic sales growth was c 4% and adjusted EBITDA was up 8% to €6.5m. Management retained its FY19 guidance for a slight y-o-y increase in EBIT. End-June NAV increased by €1.6m to €119.8m, with the bulk of the uplift from coatings and plastics. Importantly, the dispute with Blue Cap's major shareholder (46%), PartnerFonds (PF), seems to be resolved following the recent changes to the latter's management and supervisory board. At the same time, Blue Cap's supervisory board was extended to four members and the executive board is planned to be broadened (supported by CEO Dr Hannspeter Schubert). The company seems well positioned to take advantage of M&A opportunities arising amid the broader economic slowdown.

H119 results assisted by Knauer consolidation

We calculate Blue Cap's H119 EPS at €1.02 after a twofold y-o-y increase (H118: €0.35) from a low base. Group revenues grew 25% y-o-y to €102m, driven by the consolidation of Knauer in late June 2018. Investment costs and initial depreciation at Knauer are still weighing on profitability. Nonetheless, Blue Cap's adjusted EBITDA for its whole portfolio was up by 8% y-o-y to €6.5m. Net debt increased, translating into a net debt to equity ratio of 60% vs 47% at end-FY18. However, leverage remains at reasonable levels, in our view.

FY19 guidance reiterated

Management reiterated its earlier guidance of clear growth in revenue and a slight increase in EBIT in FY19. This is underpinned by favourable trading conditions for portfolio companies in H119, which management expects to continue into H219, and planned progress in restructuring measures at Gämmerler and Knauer. Blue Cap also continues to explore M&A opportunities, especially in the context of improving deal flow and less demanding valuations reported by German private equity companies.

Valuation: Trading at a wide discount to NAV

Current Refinitiv consensus expects gradual EBITDA growth, which implies an undemanding FY20e EV/EBITDA multiple of 6.7x. Blue Cap estimates the NAV of its portfolio at €119.8m at end-June 2019 (or €30.10 per share), which implies a c 43% share price discount to NAV. Blue Cap's last dividend payment offers a dividend yield of 3.8%.

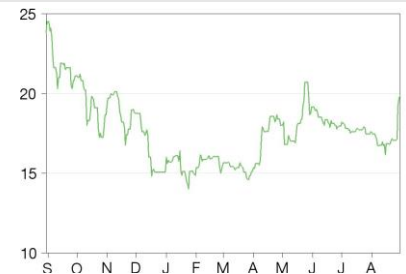
Consensus estimates

Year end	Revenue (€m)	Adj EBITDA (€m)	Net profit (€m)	EPS (€)	DPS (€)	EV/EBITDA (x)
12/17	141.8	11.2	39.9	10.0	1.00	10.2
12/18	176.1	11.5	4.6	1.1	0.75	9.9
12/19e	206.5	14.7	5.4	1.4	0.80	7.7
12/20e	210.5	17.0	6.6	1.7	1.00	6.7

Source: Blue Cap, Refinitiv consensus based on estimates of one analyst (Warburg)

Price €19.85
Market cap €79m

Share price graph



Share details

Code B7E
Listing Deutsche Börse Scale
Shares in issue 4.0m
Net debt at 30 June 2019 €35.3m

Business description

Blue Cap is a Munich-based industrial holding company, investing in medium-sized manufacturing companies with a turnover range of €20–100m.

Bull

- Proven business model and management.
- Strong finances set for boost from transformative transactions.
- Economic downturn enhances buying opportunities.

Bear

- Execution risk in restructuring processes.
- Valuation risk in identifying acquisitions.
- Dependence on economic conditions, mitigated by diverse business and geographical mix.

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Financials: H119 broadly in line with budget

Blue Cap reported a significant increase in revenues in H119 to €101.8m (+25% y-o-y) and only slightly below budget. This was driven by the first-time consolidation of Knauer (plastics technology) from June 2018, which was only partially offset by sales 'lost' with the disposal of WISAP in September 2018. Excluding consolidation effects, we calculate underlying revenue growth at 4% year-on-year, led mainly by the coating technology and precious metals recycling businesses (see below for a detailed discussion of segment performance). With Knauer still weighing on profitability, the group adjusted EBITDA margin declined to 6.1% in H119 (1.2pp lower y-o-y), although overall adjusted EBITDA improved by 8% y-o-y to €6.5m (slightly ahead of budget). Reported EBITDA improved 44% y-o-y due to €1.1m in net one-off/irregular items (H118: -€0.8m), including in particular a €1.2m gain on a terminated rental contract as well as the release of difference from capital consolidation of €1.4m (vs €0.7m in H118). Adjusted EBIT of €3.6m was ahead of budget, but below last year (€4.5m) due to increased D&A associated with a higher capitalisation ratio and higher depreciation at Knauer.

Net debt at end June 2019 amounted to €35.3m, up 28% from end December 2018. This translated into higher leverage ratios, with 2.9x of trailing 12-months adjusted EBITDA (FY18: 2.3x) and 60% equity (FY18: 47%). With debt broadly flat y-o-y, Blue Cap reduced its cash position by €7.8m (to €21.1m), which was mostly consumed by €4.5m in capital expenditure and €3.0m dividend from FY18 profits (DPS of €0.75 per share). Nevertheless, we believe leverage could be reduced following potential successful restructuring at Knauer, which still weighs on the ratios. We note that, on acquisition (H118), Blue Cap's net debt increased by €16.3m.

Exhibit 1: Analysis of revenue and profit

€m	H119	H118	y-o-y	FY18	Guidance: FY19 vs FY18	H119 as % of FY18	H119 as % of FY19 consensus	FY19 consensus
Revenues:								
Coating technology (Neschen)	32.4	30.6	6%	61.1	Higher	53%		
Plastics technology (Knauer)	28.4	9.6	N/M	37.7	Higher	N/M		
Adhesive technology (Planatol)	17.8	18.7	-5%	36.2	Higher	49%		
Precious metals recycling (Carl Schaefer)	9.5	6.3	50%	12.5	Higher	76%		
Production technology	8.7	10.6	-19%	17.8	Higher	49%		
Medical technology	5.0	5.5	-10%	10.6	Lower	47%		
em-tec	5.0	4.2*	18%	N/D				
WISAP	-	1.3*	N/M	N/D				
Sales	101.8	81.4	25%	176.1	Clearly higher	58%	49%	206.5
EBITDA	7.7	5.4	44%	10.6				
<i>Margin</i>	<i>7.1%</i>	<i>6.4%</i>	<i>63bp</i>	<i>5.7%</i>				
Adj EBITDA	6.5	6.0	8%	11.5		57%	44%	14.7
<i>Margin</i>	<i>6.1%</i>	<i>7.3%</i>	<i>-115bp</i>	<i>6.3%</i>				<i>7.1%</i>
EBIT	4.8	3.7	27%	5.6				
Adj EBIT	3.6	4.5	-20%	6.7	Slightly higher	54%	40%	9.0
Net profit	4.1	1.4	195%	4.6		89%	75%	5.4

Source: Blue Cap accounts, Refinitiv consensus estimates, Edison Investment Research. Note: *Edison calculations.

Blue Cap's management confirmed its earlier guidance and still expects revenues clearly ahead of last year (current Refinitiv consensus for FY19e is €206.5m vs €176.1m reported in FY18), largely driven by the Knauer consolidation, as well as favourable conditions in the precious metals recycling business (Carl Schaefer) and the production technology segment (nokra and SMB-David in particular). Moreover, management continues to expect a slight y-o-y increase in adjusted EBIT (Refinitiv consensus for FY19e at €9.0m vs €6.7m reported in FY18). Earnings growth should be supported by positive restructuring effects at Gämmerler and Knauer on top of overall strong business development. Having said that, results may be affected by expenses and one-off charges associated with the restructuring and integration of Blue Cap's holdings (an inherent part of the company's business model).

Apart from organic growth, Blue Cap continues to explore new investment opportunities and expects positive trends in deal flow and M&A activity. We believe this could be assisted by the improved pricing environment and overall availability of acquisition targets. This seems to be confirmed by the results of the Q119 edition of the survey conducted by the German development bank, KfW, which indicates an improved level of comfort in the private equity industry with respect to entry prices and deal flow.

Segment performance

Blue Cap focuses on industrial companies in the DACH region (in particular, chemical companies active in the coating, adhesives and plastics sectors), with 57% of revenues coming from Germany (H118: 50%). The company's current portfolio includes eight businesses, with the newest investment (June 2018) being the plastic packaging producer Knauer-Uniplast.

Exhibit 2: H119 segmental split

€m	NAV	Change ytd	Revenues	Change y-o-y
Coating technology (Neschen)	61.7	1.0%	32.4	6%
Adhesives (Planatol)	15.6	-0.6%	17.8	-5%
Plastics (Knauer)	11.1	3.7%	28.4	196%
Production	16.2	1.9%	8.7	-19%
Medical	11.8	1.7%	5.0	-10%
Precious metals (Carl Schaefer)	3.4	6.3%	9.5	50%
Other	-	-	0.1	122%
Total	119.8	1.4%	101.8	25%

Source: Blue Cap accounts, Edison Investment Research

The **coating technology** business, carried out by Neschen, remains the largest contributor to Blue Cap's revenues and portfolio value. In H119, it delivered a decent increase in revenues by 6% y-o-y to €32.4m (32% of group revenue), on the back of stronger order intake from the industrial coating business. Neschen is proceeding with the capacity increase and is convinced there is further room for productivity improvement. Furthermore, after implementing a new group-level customer relationship management (CRM) system, it is currently preparing the launch of a unified website as a platform for new e-commerce functionalities. Neschen acquired Netra (renamed Filmolux Swiss) in H119, which had been a business partner for 30 years. As this was consolidated for only one month in H119, its impact on revenues was limited. Blue Cap confirmed its 2019 guidance for the segment, with a sales increase on the back of favourable market conditions in industrial coatings. However, EBIT is expected to decline slightly, reflecting expansion costs at the main site and digitalisation-related costs.

Production technology segment revenues declined 19% y-o-y to €8.7m in H119 (9% of Blue Cap revenue). The decline was from a high base, as a large contract realised by Gämmerler in 2017 was recognized in revenues in early 2018. Meanwhile, both SMB-David and nokra were able to increase sales versus last year and the segment overall is expected to deliver higher turnover and earnings in FY19 compared to last year.

The **adhesives** segment (Planatol System) delivered €17.8m in revenues in H119. This represents a 5% y-o-y sales decrease caused by timing the order intake. An improvement programme was introduced to realise cost savings and enhance efficiency in adhesive application systems, with the first positive effects expected in H219. Following changes made to the ERP software and the introduction of a new head of sales, the focus here is on further expansion. Blue Cap reiterated its expectations of a slight y-o-y EBIT decline in FY19.

Organic sales in the **medical technology** segment grew by a healthy 18% y-o-y to €5.0m, while overall revenues declined 10% due to the disposal of WISAP in September 2018. Em-tec (now the only company in the segment) has benefited from favourable progress in its sensor business and positive customer response to the newly introduced multichannel platform. The company started to

expand capacity (including a new R&D centre) last year and expects to complete the investment in 2020.

The **plastics technology** segment comprises Knauer-Uniplast, first consolidated in June 2018. The company delivered €28.4m in revenue in H119, but still reports an EBIT loss (which management also expects for FY19). Knauer provides plastic packaging for the fast-moving consumer goods (FMCG) industry, with around 25% market share in the DACH region. The restructuring measures incorporated by Blue Cap include capacity concentration at the main production site (closing the site in Bad Laasphe), as well as realignment of the technology, R&D and production areas. Blue Cap plans to tighten its cost structure through, eg better materials sourcing. After the balance sheet date, Blue Cap announced the takeover of friedola TECH, a global manufacturer of plastic products mainly for the packaging and automotive sectors with €55m of revenue in 2018. The transaction price was in the low double-digit million euros. Blue Cap expects synergy effects with Knauer in the areas of material procurement, development and recycling.

Carl Schaefer (**precious metals recycling**) delivered a strong 50% y-o-y sales increase in H119 to €9.5m, supported by both the higher gold price and rising purchase volumes. Blue Cap expanded the company's distribution activities and will focus on the intensification of precious metals purchase, which should deliver healthy earnings growth in FY19. Despite the steady growth in NAV (+6.3% ytd to €3.4m), the segment still makes up only 3% of the whole portfolio.

Shareholder dispute coming to an end

After a rather bumpy start to the co-operation with new major shareholder (45.6% stake) PartnerFonds (described in our [previous note](#)), the situation seems to have improved recently. This is the result of a complete reconstruction of PartnerFonds' supervisory board to include Evoco and Dr Hannspeter Schubert's (Blue Cap's CEO via Southern Blue Beteiligungsgesellschaft) representatives, as well as the departure of its CEO Oliver Kolbe (who was the sole management board member).

The expansion of Blue Cap's supervisory board to four members was agreed at the last AGM in June 2019, supported by Blue Cap's CEO, Dr Hannspeter Schubert. Two board members remain unchanged, one of Evoco's founding partners (Michel Galeazzi), as well as an independent corporate governance expert (Professor Dr Grenz) will join Blue Cap's supervisory board. Moreover Blue Cap's supervisory board plans to extend the executive board to three members (currently one) to align the company's structure to the next development stage.

Valuation

Blue Cap's NAV at end-June 2019 reached €119.8m, c €30.10 on a per-share basis, marginally ahead (by €1.6m) of €118.2m at end 2018. Of the €1.6m increase, the two largest contributors were coating technology (+€0.6m) and acquisition-derived plastics (+€0.4m). The current share price trades at a c 35% discount to the end-June NAV per share. The company values its portfolio based on in-house discounted cash flow models and excludes any value associated with non-operating assets and liabilities at holding level and those in its real estate business. Including these assets, the NAV valuation would be higher. Based on current Refinitiv consensus, Blue Cap's shares trade at a relatively undemanding FY20e EV/EBITDA ratio of 6.7x. The company has a short history of dividend payments, introducing a dividend policy after the successful disposal of Biolink in 2017. It recently paid a dividend from FY18 profits of €0.75 per share (vs €1.00 from FY17 profits). This offers a 3.8% yield on current share price.

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