Research Report (Update)

Fall in turnover in 1st half year 2013 due to a weaker Q1 2013 – forecasts for 2013 slightly reduced – shares clearly undervalued

Price target: €9.30

Rating: BUY

IMPORTANT NOTE:
Please take note of the disclaimer/risk warning, as well as the disclosure of potential conflicts of interest as required by section 34b of the Securities Trading Act (WpHG) on page 11 and ff.

Completion: 26/8/2013 **First publication: 27/8/2013**

Greiffenberger AG *5,7

Rating: Buy

Price target: € 9.30

current price: € 5.70
26/8/2013 / ETR

currency: EUR

Key date:

ISIN: DE0005897300

WKN: 589730

Ticker symbol: GRF

Number of shares³: 4.839

Marketcap³: 27.58
Enterprise Value³: 88.18
³ in m / in EUR m

Freefloat: 38.0 %

Transparency Level:
General Standard

Market Segment:
Regulated Market

Accounting Standard:
IFRS

Financial year-end: 12/31

Designated Sponsor:
Donner & Reuschel AG

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* catalogue of potential conflicts of interests on page 13

Company profile

Sector: Industry

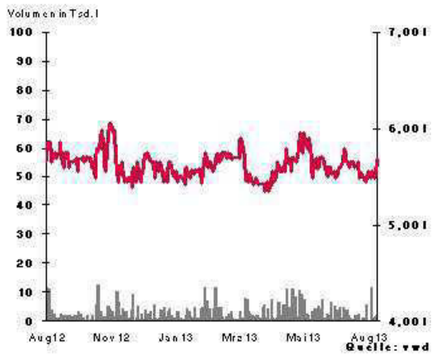
Speciality: Drive technology, Metal Band Saw Blades & Precision Strip Steel, Sewer renovation

Employees: 979 (30/6/2013)

Founded: 1986

Registered office: Marktredwitz

Executive Board: Stefan Greiffenberger



Greiffenberger AG, with its registered office in Marktredwitz and its management in Augsburg, is a family-run holding company with shareholdings in various industries divided into three business areas. The Drive Technology business area is represented by the largest subsidiary ABM Greiffenberger Antriebstechnik GmbH, based in Marktredwitz. In addition, ABM has foreign subsidiaries in China, France, Austria, Poland, Turkey and the USA. The Metal Band Saw Blades & Precision Strip Steel business unit comprises J. N. Eberle & Cie. GmbH, based in Augsburg. Eberle also has subsidiaries in France, Italy and the USA. BKP Berolina Polyester GmbH & Co. KG, based in Velten, operates in the fields of sewer renovation technology and pipe lagging. Greiffenberger AG has been listed since 1986.

Data & forecasts

P&L in EURm / Due date	31/12/2011	31/12/2012	31/12/2013e	31/12/2014e
Sales	156.61	157.96	159.00	169.00
EBITDA	14.78	15.39	13.76	16.84
EBIT	8.32	8.80	6.96	9.94
Net profit	2.52	2.55	2.32	4.36
Figures in EUR				
Net Profit per share	0.52	0.53	0.48	0.90
Dividend per share	0.00	0.00	0.00	0.00
Ratios				
EV/Sales	0.56	0.56	0.55	0.52
EV/EBITDA	5.97	5.73	6.41	5.24
EV/EBIT	10.60	10.02	12.67	8.87
P/E	10.96	10.75	11.88	6.33
P/B		0.85		

Financial Dates:

Date: Event

07/11/2013: Report Q3

**** last research published by GBC:**

Date: publication/price target in €/Rating

19/7/2013: RG / 9.30 / BUY
29/4/2013: RS / 9.30 / BUY
12/2/2013: RG / 11.00 / BUY
5/11/2012: RG / 11.00 / BUY
24/8/2012: RS / 11.00 / BUY

RS = Research Studie; RG = Research Guide;
RS = Research Report; RG = Research Guide;
** the research reports can be found on our webside www.gbc-ag.de or can be requested at GBC AG, Halderstr. 27, D-86150 Augsburg

Company

Profile

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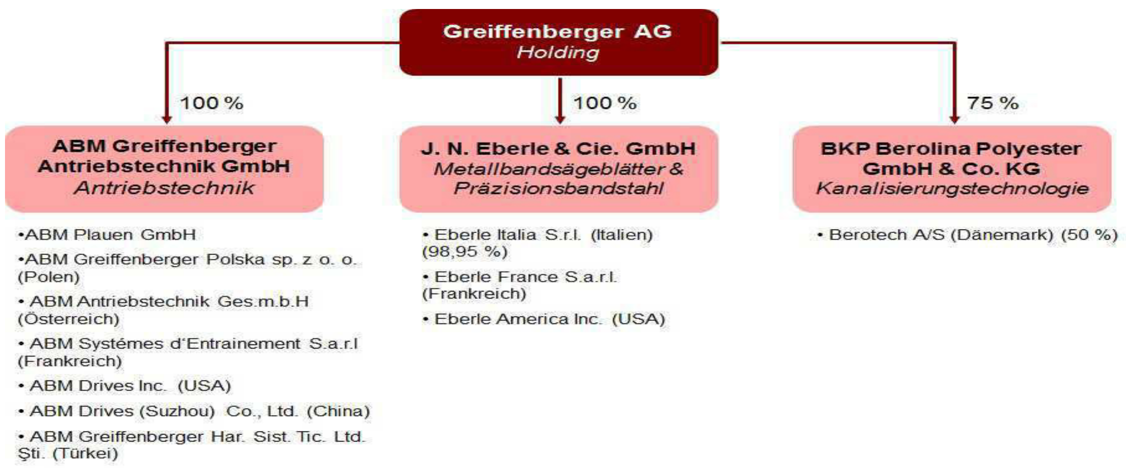
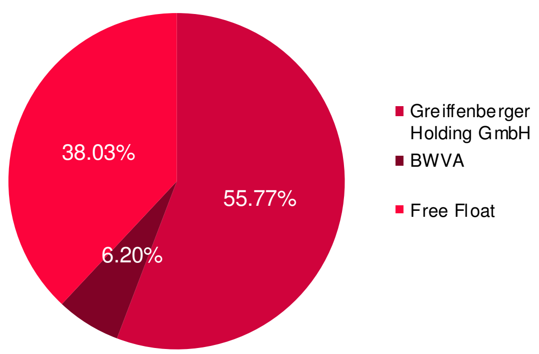
The following diagram shows Greiffenberger AG's organisational chart:



Source: Greiffenberger, GBC

Shareholder structure

Shareholder	30/06/2013
Greiffenberger Holding GmbH	55.77 %
Baden-Württembergische Versorgungsanstalt (BWVA)	6.20 %
Free Float	38.03 %
Total	100.0 %



Source: Greiffenberger, GBC

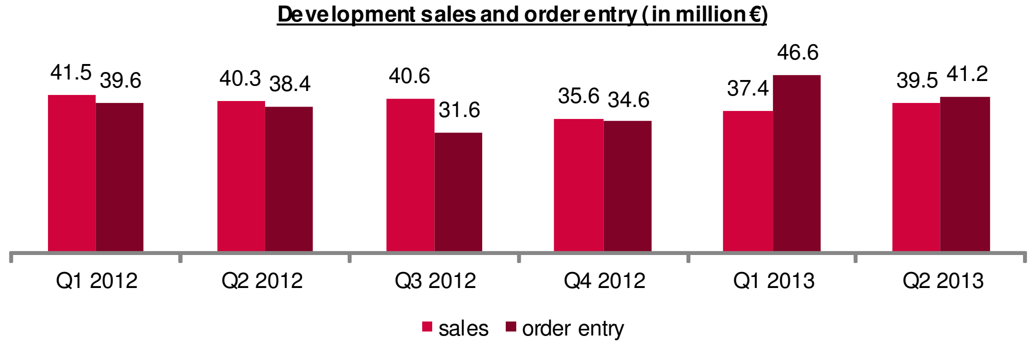
Business development in the first six months of the year 2013

in m €	First six months of the year 2012	Δ 2012/2013	First six months of the year 2013
Sales	81.81	-6.0 %	76.90
EBITDA	8.18	-16.2 %	6.85
EBITDA-Margin	10.0 %	-1.1 Pp.	8.9 %
EBIT	4.95	-29.3 %	3.50
EBIT-Margin	6.1 %	-1.5 Pp.	4.6 %
Net Profit	1.07	+18.6 %	1.27
EPS in €	0.22	+18.6 %	0.26

Source: Greiffenberger, GBC

Turnover trends - Pronounced revival following weaker Q1 2013

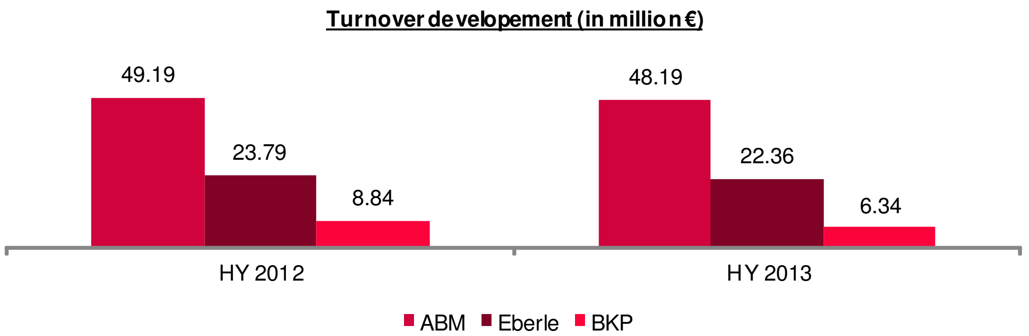
After a weaker 4th quarter 2012 and a more or less stable beginning in 2013 Greiffenberger AG was able to gain momentum again thanks to a good second quarter 2013. That trend was accompanied by strongly increasing incoming orders since the beginning of the year 2013. Especially the first quarter was characterized by a very strong development regarding the incoming orders.



Source: Greiffenberger, GBC

In the first half year of 2013 Greiffenberger AG reported sales revenues of €76.90 million (PY: €81.81 million). Compared with the previous year this represents a reduction in turnover of 6.0%. After the first quarter of 2013 the business still showed a 10.0% fall in turnover. An upward trend in quarterly turnover development is thus clearly visible since Q4 2012.

Incoming orders are showing an even more encouraging development. At the end of the first six months of the current business year 2013 these were at €87.8 million and thus significantly above the previous year's level of €78.0 million. At the same time the book-to-bill ratio was 1.14 and thus provides a solid starting basis for the coming quarters.



Source: Greiffenberger, GBC

In the largest subsidiary ABM, customer demand revived significantly following a faltering start to the year. Thus proceeds from turnover in the second quarter of 2013 are already at €25.4 million compared to just €22.8 million in the first quarter of 2013. Due to the weaker business development at the start of the year the turnover in the first half year of 2013 was also, at €48.19 million, lower than the previous year's figure (PY: €49.19 million). According to company data, the renewable energies, textile machinery and medical technology sectors should all be flagged up as particularly positive.

The subsidiary firm Eberle achieved a turnover in the first six months of the current business year 2013 of €22.36 million compared with €23.79 million in the previous year. The reduction in turnover can be explained above all by a lower demand in the metal band saw blades sector. Eberle realises more than 60% of its turnover here. Compared with the weaker second half of 2012 (2nd half year 2012: €21.64 million) it was nevertheless already possible to record an increase in turnover again. The export ratio in the first half of 2013 was, at more than 90%, unaltered and at a very high level, and is an expression of Eberle's international client base.

BKP's turnover in the first half of 2013 was €6.34 million and thus lower than the previous year's level (PY: €8.84 million). In the previous year, BKP received, however, an unexpectedly large contract in the gas pipe lagging sector. The size of the contract came, according to our estimates, to around €2 million. The drop in turnover in the first half year of 2013 can above all be explained by the long winter, which also explains a more limited number of public tenders for sewer renovation.

Earnings development - ABM's EBIT margin at 6%; BKP falls short of expectations

The company achieved a marked improvement in terms of its cost of materials ratio. The purchased materials ratio fell significantly in the first half of 2013 to 48.97% (PY: 49.86%). The subsidiary companies profited here from lower prices of important raw materials as well as progressive improvements in purchasing activities.

The outlay on staff rose in the first half of 2013 to €25.80 million compared to €24.86 million in the previous year. This was caused on the one hand by a rise in headcount (30.6.2013: 979 vs. 30.6.2012: 944) and on the other hand high wage settlements in autumn, which led to an increase in wages.

The reduction in gross yield which resulted from the drop in turnover, along with increased staff costs, meant that the operating profit did not reach the level of the previous year. Thus earnings before interest, taxes, depreciation and amortisation (EBITDA) were €6.85 million (PY: €8.18 million). Furthermore it is important to note that expenses for the new plant in Lublin are accounted for in the first half of 2013. The greater part of the anticipated €1.7 million one-off expenditure involved in starting up the new plant should fall, according to our projections, in the second half of the year.

Depreciation in the first half of 2013 came to €3.35 million and thus show an increase due to an increased investment volume compared to the previous year (PY: €3.23 million). Thus earnings before interest, taxes, depreciation and amortisation (EBITDA) were €3.5 million (PY: €4.95 million) which corresponds to an EBIT margin of 4.6% (PY: 6.1%). The most important contribution to earnings by far was delivered by the subsidiary ABM with an EBIT of €2.89 million (PY: €1.96 million). Thus the positive trend towards improvements in its operating margin has continued. We are firmly convinced that ABM's EBIT margin will increase further in the coming years. On the other hand the segment earnings of Eberle and BKP came to €0.93 million (PY: €1.72 million) and €0.01m (PY: €1.57 million) respectively, thus falling short of our expectations.

Greiffenberger AG was able to make significant progress with regards to financial results. Financial results improved significantly in the first half of the current business year 2013 to €-1.65 million (PY: €-3.28 million). This welcome development is, alongside the absence of one-off expenditures incurred in the course of re-ordering company financing in March 2012, also the result of the much more favourable refinancing conditions as well as a somewhat positive result from the market valuation of interest hedges. In the previous year the market valuation of interest hedges led to a loss of around €0.6 million. Furthermore, minority interests turned out smaller, due to the subsidiary BKP's balanced earnings.

The significant improvement in financial results in combination with a reduced group corporate tax ratio ultimately meant that the annual net profit rose compared to the previous year. The annual net profit after the first six months of 2013 came to €1.27 million (PY: €1.07 million). Thus a profit per share of €0.26 was achieved, compared to €0.22 in the previous year.

Assets, liabilities and financial situation - Ratios slightly improved in the first six months of 2013

in m €	FY 2009	FY 2010	FY 2011	FY 2012	HY 2013
Equity	23.44	28.22	30.65	31.25	32.56
Equity-Ratio	*20.6 %*	*22.9 %*	*25.1 %*	*25.3 %*	*25.7 %*
Net debt	37.43	34.79	40.43	41.66	40.47
Operating fixed Assets	52.32	56.94	56.99	58.10	58.84
Net Working Capital	23.33	23.55	33.30	36.29	34.99

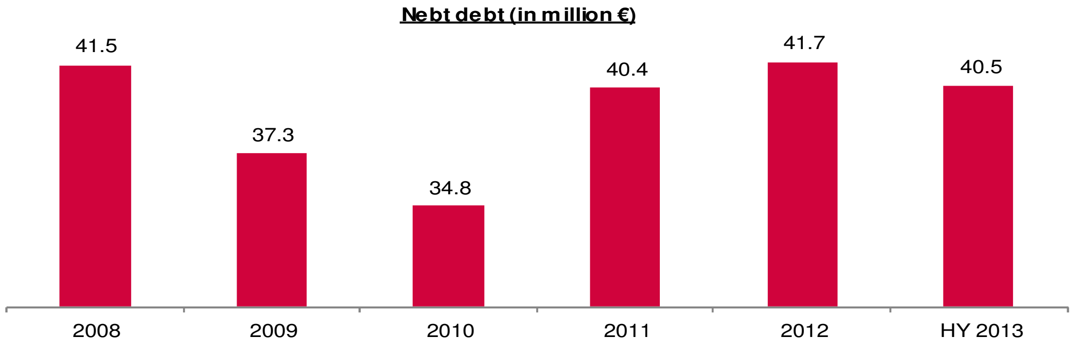
Source: Greiffenberger, GBC

Greiffenberger AG was able to further improve financial ratios moderately in the first half of 2013. Thanks to the positive annual net profit, equity has increased to €32.56 million. This corresponds to a book value per share of around €6.7, which is close to 20% more than the current market capitalisation. At the same time the equity ratio could be slightly increased to 25.7% by the end of June 2013. We regard this value as solid.

It is the continued aim of management to raise the equity ratio to 33%, which should, according to our assessments, be achieved in the coming business year 2014. We regard dividend disbursements to be realistic given an equity ratio of 30%.

The net debt could be reduced further in the first half of 2013, back down to €40.47 million (31.12.2012: €41.66 million). The reduction in debt is thanks to the positive development of the operating cash flow in the first half of the year. The operating cash flow reached €7.77 million in the reported period (PY: €3.20 million) which is clearly positive.

The following diagram shows the trend in net debt since 2008.



Source: Greiffenberger, GBC

The level of investment in the first half of 2013 came to around €4.1 million compared to €2.6 million in the previous year. It was possible to finance all investments entirely from the operating cash flow. A majority of the investments went to the subsidiaries ABM and Eberle. While ABM invested in motor and engine production at its headquarters in Marktredwitz and made down-payments on its investments in its new plant in Lublin, Eberle invested in expanding its product portfolio as well as in modernising its IT landscape. BKP's investments were moderate at barely €0.1 million.

Forecast and model assumptions

in m €	FY 2012	FY 2013e (new)	FY 2013e (old)	FY 2014e (new)	FY 2014e (old)
Sales	157.96	159.00	162.00	169.00	169.00
EBITDA (*margin*)	15.39 *(9.8 %)*	13.76 *(8.7 %)*	14.33 *(8.9 %)*	16.84 *(10.0 %)*	16.84 *(10.0 %)*
EBIT (*margin*)	8.80 *(5.6 %)*	6.96 *(4.4 %)*	7.53 *(4.7 %)*	9.94 *(5.9 %)*	9.94 *(5.9 %)*
Net profit	2.55	2.32	2.51	4.36	4.36
EPS in €	0.53	0.48	0.52	0.90	0.90

Source: GBC

Sales and Earnings forecast – Start up costs for new plant in Lublin cause strain

With the publication of the half year report we have corrected our projections for the present business year 2013 downward slightly. We have, however, not altered our forecast for the coming business year 2014.

Henceforth, we expect sales revenues of around €159.00 million (previously: €162.00 million) in 2013. The weaker first quarter is responsible for this, with a reduction in turnover of around 10%. Despite expectations of a good turnover development in the second half of the year, from today´s perspective the previously-projected turnover of €162.00 million seems too ambitious.

Reasons to be confident about the course of the rest of the year are also provided by the encouraging development of incoming orders in the first half of 2013 with a book-to-bill ratio of more than 1.14 as well as a comfortable volume of orders on hand. Furthermore, we are optimistic regarding the direction of other economic trends. The German Chamber of Commerce and Industry (DIHK) also has a positive outlook on future economic development. According to a recent survey, German exports in 2013 and 2014 are expected at a 2% to 4% rate of increase. Due to its high export ratio, Greiffenberger AG should profit accordingly.

We expect the EBITDA to come to €13.76 million for the present business year 2013. Thus we have revised our estimates slightly downwards (previously: €14.33 million). For ABM we assume that a majority of the one-off costs of around €1.7 million for the new plant in Lublin will be incurred in the second half of the year. Thus it seems unlikely to us that ABM will be able to repeat its good EBIT margin of 6.0% in the second half of the year. On the other hand we expect the other two subsidiaries to see improved earnings compared with the first half of 2013. In particular we expect BKP to experience a marked increase in demand after the first half of 2013, which was below our expectations. So BKP should achieve a clearly positive result for the year overall.

Depreciations for 2013 should come to €6.80 million. Financial results should turn out much better than we previously expected. Our new assessment of financial results now assumes €-3.70 million (previously: €-4.00 million). The effects of the lowered interest rates realized thanks to the revised company financing the previous year are unfolding their full impact in the business year 2013.

Furthermore we expect a very positive operating cash flow in 2013. It already reached just under €8 million in the first half of 2013. This should then also lead to a further increase in the equity ratio. We have not assumed a dividend disbursement for 2013 in our calculations so far.

A glance at the valuation figures indicates a significant undervaluation of Greiffenberger shares. So the 2013 price to earnings ratio is below 12. Another substantial consideration is that the shares with a price-to-book ratio of around 0.8 are valued favourably. The undervaluation becomes even more apparent when one turns one’s attention to the coming 2014 business year. Here the price-to-earnings-ratio is less than 7, which we consider to be especially attractive. The disappearance of the start-up costs associated with the new plant in Poland as well as an overall increase in business volumes should produce a sizeable leap in earnings.

Valuation

DCF valuation

Model assumptions

We valued Greiffenberger AG using a three-phase DCF model. Starting from the real-life estimates for the years 2013 to 2014 in phase 1, the second phase from 2015 to 2020 forecasts the effect of value drivers. For this we are using a conservative approach, assuming average annual increases in sales of 3.0%. We took as our target an EBITDA margin of 10.5%.

We applied a tax ratio of 29.0%. For the third phase beyond the forecast horizon, a residual value was calculated using a perpetual annuity formula. For the final value we assume a growth rate of 2.0%. To date we have not included dividend payments in our DCF model.

Calculation of the cost of capital

The weighted average cost of capital (WACC) for Greiffenberger AG is calculated on the basis of internal capital costs and external capital costs. In order to determine the internal cost of capital, the fair market premium, the company beta and the risk-free interest rate need to be established.

The interest rate for 10-year German federal bonds is taken as the risk-free interest rate. This is currently 2.00%.

We used the historic market premium of 5.50 % as being a suitable expectation of market premium. This is supported by historical analyses of stock market yields. The market premium reflects the percentage of the expected excess return of the stock market over the low-risk government bonds.

Using the GBC estimation method there is currently a beta of 1.47.

Applying these assumptions we can calculate an internal cost of capital of 10.1% (beta multiplied by the risk premium, plus 10-year interest rate). As we assume a long-term weighting of internal capital costs of 80%, the weighted average cost of capital (WACC) is 9.2%.

Valuation result

Discounting future cash flows was done using the entity approach. We calculated the relevant capital cost (WACC) at 9.2%. The resulting fair value per share at the end of financial year 2014 corresponds to a target price of €9.30.

This means that we have not changed our target price.

Greiffenberger AG - Discounted Cashflow (DCF) Valuation

Value driver of the DCF model after the estimate phase:

consistency - Phase	
Sales growth	3.0%
EBITDA-Margin	10.5%
Depreciation to fixed assets	11.9%
Working Capital to sales	21.9%

final - Phase	
Eternal growth rate	2.0%
Eternal EBITA - Margin	7.1%
Effective tax rate in final phase	29.0%

Three phases DCF-Model:

Phase	estimate		consistency						final
in Mio.	FY 2013e	FY 2014e	FY 2015e	FY 2016e	FY 2017e	FY 2018e	FY 2019e	FY 2020e	Terminal
Sales	159.00	169.00	174.07	179.29	184.67	190.21	195.92	201.79	
Sales change	0.7%	6.3%	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%	2.0%
Sales to fixed assets	2.73	2.91	3.00	3.09	3.18	3.28	3.38	3.47	
EBITDA	13.76	16.84	18.28	18.83	19.39	19.97	20.57	21.19	
EBITDA-Margin	8.7%	10.0%	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%	
EBITA	6.96	9.93	11.38	11.92	12.49	13.07	13.67	14.29	
EBITA-Margin	4.4%	5.9%	6.5%	6.7%	6.8%	6.9%	7.0%	7.1%	7.1%
Taxes on EBITA	-2.02	-2.88	-3.30	-3.46	-3.62	-3.79	-3.96	-4.14	
Taxes to EBITA	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%
EBI (NOPLAT)	4.94	7.05	8.08	8.47	8.87	9.28	9.71	10.14	
Return on capital	5.2%	7.5%	8.5%	8.8%	9.1%	9.4%	9.7%	10.1%	10.1%
Working Capital (WC)	36.00	37.00	38.10	39.25	40.42	41.64	42.89	44.17	
WC to sales	22.6%	21.9%	21.9%	21.9%	21.9%	21.9%	21.9%	21.9%	
Investment in WC	0.29	-1.00	-1.10	-1.14	-1.18	-1.21	-1.25	-1.29	
Operating fixed assets (OAV)	58.30	58.00	58.00	58.00	58.00	58.00	58.00	58.12	
Depreciation on OAV	-6.80	-6.90	-6.90	-6.90	-6.90	-6.90	-6.90	-6.90	
Depreciation to OAV	11.7%	11.9%	11.9%	11.9%	11.9%	11.9%	11.9%	11.9%	
Investment in OAV	-7.00	-6.60	-6.90	-6.90	-6.90	-6.90	-6.90	-7.02	
Capital employed	94.30	95.00	96.10	97.25	98.42	99.64	100.89	102.29	
EBITDA	13.76	16.84	18.28	18.83	19.39	19.97	20.57	21.19	
Taxes on EBITA	-2.02	-2.88	-3.30	-3.46	-3.62	-3.79	-3.96	-4.14	
Total invesment	-6.71	-7.60	-8.01	-8.05	-8.08	-8.11	-8.15	-8.30	
Invesmtent in OAV	-7.00	-6.60	-6.90	-6.90	-6.90	-6.90	-6.90	-7.02	
Investment in WC	0.29	-1.00	-1.10	-1.14	-1.18	-1.21	-1.25	-1.29	
Investment in Goodwill	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	
Free Cashflows	5.03	6.35	6.97	7.32	7.69	8.07	8.46	8.74	113.97

Value operating business (due date)	98.92	101.71
Net present value explicit free Cashflows	37.54	34.66
Net present value of terminal value	61.38	67.05
Net debt	59.25	56.70
Net present value of options	0.00	0.00
Value of equity	39.66	45.01
Minority interests	0.00	0.00
Value of share capital	39.67	45.01
Outstanding shares in m	4.839	4.839
Fair value per share in €	8.20	9,30

Cost of capital calculation:

Risk free rate	2.0%
Market risk premium	5.5%
Beta	1.47
Cost of equity	10.1%
Target weight	80.0%
Cost of debt	7.5%
Target weight	20.0%
Taxshield	22.5%
WACC	**9.2%**

Sensitivity analysis - fair value per share in EUR

	WACC				
Return on capital	8.2%	8.7%	9.2%	9.7%	10.2%
6.7%	4.01	3.16	2.44	1.81	1.26
8.7%	8.22	6.95	5.87	4.93	4.12
10.7%	12.43	10.74	9.30	8.06	6.97
12.7%	16.64	14.53	12.73	11.18	9.83
14.7%	20.85	18.32	16.17	14.30	12.68

Conclusion

Greiffenberger AG had to record a reduction in turnover in the first half of 2013. Although the group was able to grow considerably following a weaker first quarter 2013, it was not yet able to fully compensate the fall in turnover. While the largest subsidiary ABM can look back on an encouraging operating development, turnover at Eberle and BKP fell markedly. For BKP, the long winter and a smaller number of public tenders had their impact on turnover figures.

Greiffenberger AG's financial ratios have further improved in the first half of 2013. Due to a positive annual net profit, equity increased to €32.56 million, which corresponds to an equity ratio of 25.7% by the end of June 2013. At the same time, thanks to a positive cash flow it was possible to reduce the net debt by more than €1 million to €40.5 million.

The half year figures for 2013 were, due to a weaker first quarter, slightly below our expectations. We have thus adjusted our forecasts for the business year 2013 slightly downward. Our prediction for 2013 is now sales revenues of €159.00 million (previously: €162.00 million) and an EBIT of €13.76 million (previously: €14.33 million). Our forecast takes into account an exceptional burden due to the new plant in Lublin, of around €1.7 million. Thanks to the disappearance of these start-up costs for the new plant in Poland as well as an overall increase in business volume, a marked increase in earnings can be assumed for the coming business year 2014.

On the basis of the current share price, our valuation figures indicate a significant undervaluation of Greiffenberger shares. In particular when one's attention is drawn to the year 2014, the price-to-earnings-ratio of around 7 appears especially attractive and is, according to our assessment, unduly low. The share price is currently noted at just under 20% below the shares' book value.

Our target for Greiffenberger AG share prices is still €9.30. We are therefore reiterating our recommendation to buy shares. Taking the current share price as a starting point, a significant share price potential of more than 60% is obtained.

Annex

Section 1 Disclaimer and exclusion of liability

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