EDISON

Deutsche Beteiligungs

New €1bn buyout fund launched

Investment companies

26 August 2016

Deutsche Beteiligungs (DBAG) reported a 9.1% dividend-adjusted NAV return for the first nine months of FY16, despite the sharp market drop following the Brexit vote, which reduced the valuation multiples applied to portfolio investments at the end of the third quarter. In July 2016, DBAG closed the fundraising for DBAG Fund VII with €1bn in commitments, which will significantly increase DBAG's fee income from FY17. DBAG's €200m commitment to this new fund provides scope for its investment portfolio to grow significantly over the medium term. These factors support the change in DBAG's dividend policy to the payment of a stable or rising single annual dividend from FY16.

12 months ending	Total share price return (%)	Total NAV return (%)	LPX Europe (%)	LPX Europe NAV (%)	DAX 30 (%)
31/07/12	(6.4)	5.7	(7.0)	(0.3)	(5.4)
31/07/13	15.8	7.4	32.6	5.4	22.2
31/07/14	28.2	17.6	12.0	16.3	13.7
31/07/15	40.6	10.0	32.5	15.6	20.2
30/06/16*	(6.5)	8.5	(8.3)	(4.6)	(14.4)

Source: Thomson Datastream, Morningstar, Bloomberg. Note: *11-month period due to change in financial year end. Discrete total return performance in euros.

Results for nine months to 30 June 2016

DBAG reported €26.3m group net income for the first nine months of FY16, slightly below the €28.3m recorded for the comparative period in FY15. After a strong first half, Q316 saw a net loss of €5.7m, mainly due to a drop in market valuations of the listed peers of DBAG's portfolio companies following the Brexit vote. The majority of portfolio companies have performed well year to date, with earnings for the year expected to increase significantly in some cases. While there was a modest €3.5m decline in DBAG's overall portfolio valuation in Q316, over nine months the portfolio saw a healthy €35.5m valuation gain. Adjusted for the FY15 dividend payment, DBAG's NAV per share increased by 9.1% to €23.09 in the nine months.

DBAG Fund VII launched

In July 2016, DBAG closed the fundraising for DBAG Fund VII with €1bn in capital commitments, including a €200m co-investment commitment from DBAG. This new buyout fund is significantly larger than its predecessor fund, DBAG Fund VI, which closed in 2012 with commitments of €700m. The new fund will significantly increase DBAG's fee income from FY17, and its launch signifies a strategic advancement as it will be able to invest up to €200m in a single larger buyout. DBAG has expanded the remit of its other co-investment fund, DBAG Expansion Capital Fund (ECF) to include smaller buyouts in addition to growth financings.

Valuation: Premium to NAV; greater dividend visibility

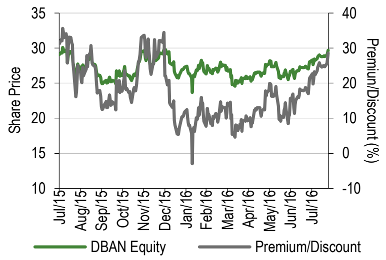
DBAG shares are trading at a 28.6% premium to NAV compared with an average 17.5% premium over the past 12 months. In our view, this reflects a greater value being ascribed to DBAG's fund services business. DBAG has revised its dividend policy to provide greater visibility over future dividend payments, intending that the current year dividend will be at least in line with the total €1.00 dividend for FY15.

Price	**€29.70**
Market cap	**€406m**
NAV*	**€316m**
NAV per share*	€23.09
Premium to NAV	28.6%

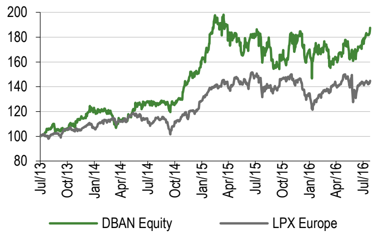
* As at 30 June 2016.

FY15 total dividend yield	3.4%
Ordinary shares in issue	13.7m
Code	DBAN
Primary exchange	Frankfurt
Sector	Private equity

Share price/premium performance



Three-year cumulative perf. graph



52-week high/low	€29.80	€23.68
NAV** high/low	€24.41	€22.16

**Including income.

Gearing

Gross*	0.0%
Net cash*	18.7%

*As at 30 June 2016.

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Edison profile page

Exhibit 1: Company at a glance

Investment objective and fund background

DBAG acquires subsidiaries of corporate groups and mid-sized enterprises in Germany and neighbouring German-speaking countries. It focuses on growth-driven profitable businesses valued at between €50m and €250m.

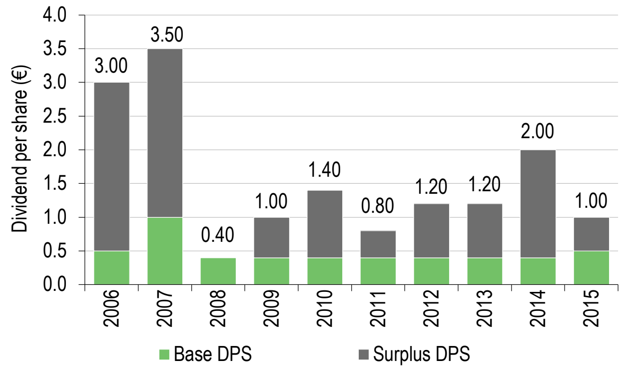
Recent developments

- 26 August 2016: DBAG invests up to €7m expansion capital in R&M international, a provider of interior fittings for ships and marine installations.
- 15 August 2016: Divestment of 15% stake in Broetje-Automation to Shanghai Electric Group for c €25m, representing an exit multiple of over 4.0x.
- 9 August 2016: DBAG invests up to €15m in management buyout of Frimo, a technology leader in tooling and plants for the automotive industry.
- 27 July 2016: Launch of DBAG Fund VII with €1bn capital commitments.

Forthcoming		Capital structure		Fund details	
AGM	22 February 2017	FY15 net expense ratio*	0.6% (0.8% unadjusted)	Group	Deutsche Beteiligungs
Final results	14 December 2016	Net cash	18.7%**	Managers	Team managed
Year end	30 September	Annual mgmt fee	N/A (self-managed)	Address	Boersenstrasse 1
Dividend payment	February 2017	Performance fee	N/A (self-managed)		60313 Frankfurt am Main, Germany
Launch date	December 1985	Trust life	Unlimited	Phone	+49 69 95787-01
Continuation vote	N/A	Loan facilities	€50m	Website	www.dbag.de

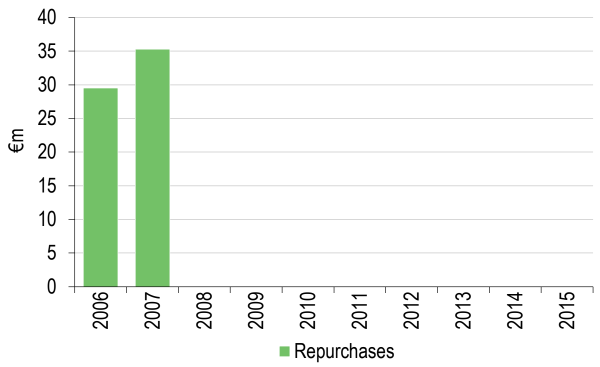
Dividend policy and history

From FY16, DBAG's policy is to pay a stable or rising annual dividend, compared with the previous policy to pay a base annual dividend from retained profits supplemented by a surplus dividend based on realised gains.

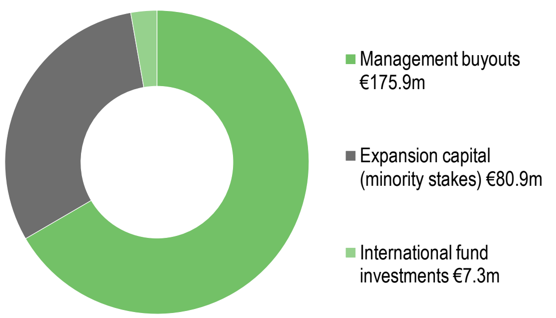


Share buyback policy and history

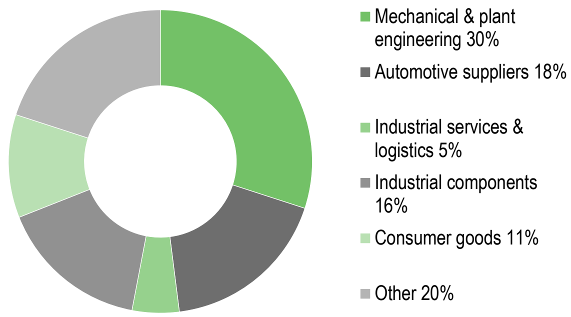
DBAG uses share repurchases and capital increases to manage longer-term capital requirements.



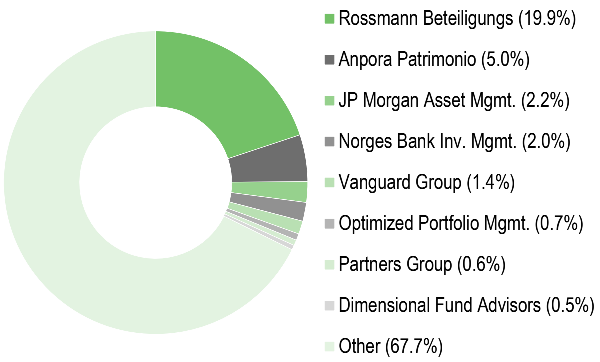
Portfolio split by investment type (as at 30 June 2016)***



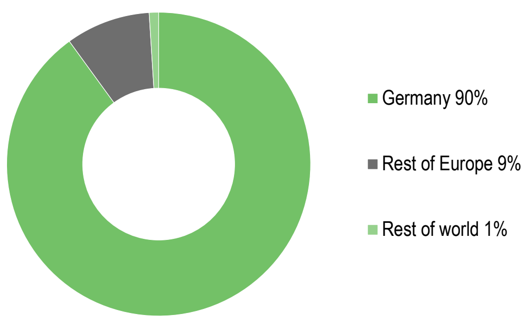
Portfolio exposure by sector (as at 30 June 2016)***



Shareholder base (as at 22 August 2016)



Portfolio exposure by geography (as at 30 June 2016)***

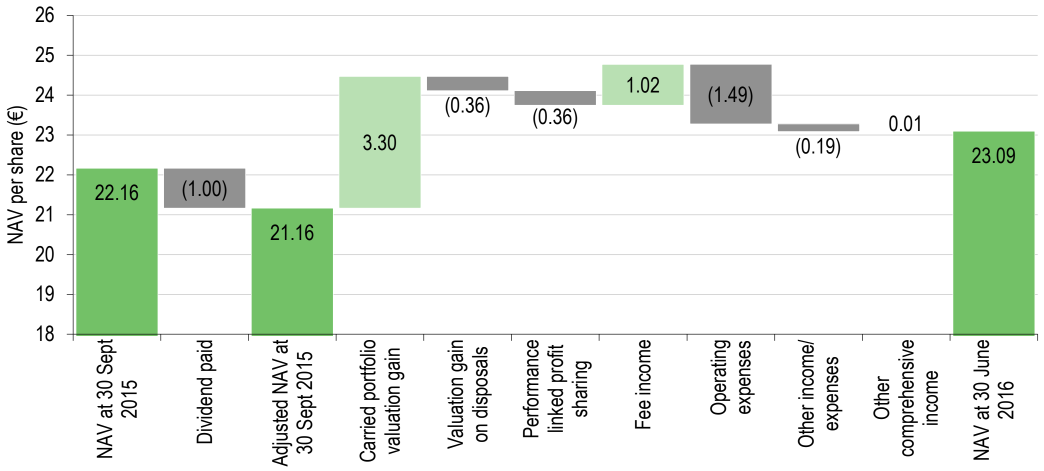


Source: DBAG, Edison Investment Research, Dealogic, IPREO, Thomson. Note: *Based on expenses net of fee income; adjusted for performance-related remuneration. **Including €21.3m of securities classified as long-term assets. ***Does not include parallel funds.

Results for the nine months to 30 June 2016

DBAG reported €26.3m group net income for the nine months to 30 June 2016, slightly below the €28.3m recorded for the comparative period in FY15. After a strong first half (primarily Q1), the third quarter of FY16 saw a net loss of €5.7m, principally due to a sharp drop in stock market prices immediately after the Brexit vote. At end-June 2016, market multiples of the peer companies used by DBAG to evaluate its portfolio were significantly lower than three months earlier, which translated into a negative effect on the portfolio valuation of €11.7m. While this was largely offset by an €11.0m valuation gain resulting from an increase in overall portfolio company earnings, changes in debt, forex rates and other factors had a €2.8m negative effect.

Exhibit 2: DBAG's NAV per share progression in 9M16



Source: DBAG, Edison Investment Research

The majority of portfolio companies have achieved a strong performance so far in 2016, with revenues and earnings for the year expected by management to increase significantly in some cases. Valuation gains were seen across the portfolio in the third quarter, although there was a €10.0m negative valuation contribution from two portfolio companies primarily as a result of lower than budgeted earnings due to project deferrals. While there was a modest €3.5m decline in DBAG's overall portfolio valuation in the third quarter, over nine months the portfolio saw a healthy €35.5m valuation gain. As illustrated in Exhibit 2, after adjusting for the €1.00 FY15 total dividend, DBAG's NAV per share increased by 9.1% to €23.09 in the nine months to end-June 2016.

Performance by business segment

Exhibit 3: DBAG segmental analysis

€m unless stated	Investments				Fund Services				Group			
	Q116	Q216	Q316	9M16	Q116	Q216	Q316	9M16	Q116	Q216	Q316	9M16
Segment income*	32.5	3.7	(3.2)	33.0	5.1	5.0	4.7	14.8	37.3	8.3	1.3	46.9
Segment expenses*	(1.5)	(2.4)	(1.5)	(5.4)	(5.3)	(5.2)	(5.7)	(16.2)	(6.5)	(7.2)	(7.0)	(20.7)
Segment net income before taxes	31.0	1.3	(4.7)	27.6	(0.2)	(0.2)	(1.0)	(1.4)	30.8	1.1	(5.7)	26.2
Pre-tax margin	95%	35%	N/A	84%	-4%	-4%	-21%	-9%	83%	13%	N/A	56%
Taxes & minority interests	-	-	-	-	-	-	-	-	-	0.1	(0.0)	0.1
Consolidated net income	-	-	-	-	-	-	-	-	30.8	1.2	(5.7)	26.3
Proportion of group net income	101%	118%	82%	105%	-1%	-18%	18%	-5%	-	-	-	-
Financial assets, loans & receivables	290.1	291.5	262.9	262.9	-	-	-	-	-	-	-	-
Investment portfolio	278.7	257.6	264.1	264.1	-	-	-	-	-	-	-	-
Financial resources**	61.7	37.0	59.0	59.0	-	-	-	-	-	-	-	-
Assets/managed assets***	333.8	321.6	315.8	315.8	1,018.0	946.8	998.3	998.3	-	-	-	-

Source: DBAG, Edison Investment Research. Note: *Synthetic internal transfers (€0.3m, €0.4m, €0.2m, €0.9m) between divisions to reflect management fees on DBAG's share of fund assets have been eliminated in group figures. **Financial resources exclude cash held in investment vehicles. ***Managed assets recognised at cost.

While market volatility negatively affected DBAG's investment business in the third quarter, this was significantly outweighed by the strong valuation gains and profitable realisations that were recorded in the first quarter, and the €27.6m net income for this business segment over the nine months was ahead of the €25.8m reported for the comparable period in the prior year. Higher costs for the investment business in the current financial year compared with the prior year included €1.6m of non-recurring expenses relating to the development of DBAG's operational structure and the arrangement of the new five-year €50m credit facility.

The decline in the value of managed assets as investments are realised translates into a reducing fee income for DBAG's fund services business, which saw fee income reduce to €14.8m for the first nine months of FY16 compared with €17.0m in the prior year period. Expenses for the fund services business were higher in the current financial year due to the €1.4m additional costs incurred relating to the initiation of DBAG Fund VII, while no additional fee income will be generated by the new fund until its investment period commences (expected during 2017). Adjusting for non-recurring expenses, the fund services business would have reported positive net income for 9M16.

Recent portfolio activity

Having agreed new investments in Telio Group and mageba and the divestments of Spheros and Clyde Bergemann Power Group in H116, DBAG has announced further portfolio activity in the second half of FY16. In August 2016, DBAG announced new investments in Frimo, a technology leader in tooling and plants for the automotive industry, and R&M International, a provider of interior fittings for ships and marine installations; and the divestment of Broetje-Automation, a global leader in the design and manufacture of automated aircraft production lines, to Shanghai Electric Group.

New investment in Frimo Group

Frimo Group develops and manufactures tooling, machinery and automated production lines for the production of high-performance plastic components, with its clients largely comprising automotive suppliers and automobile manufacturers. Headquartered in Lotte (North Rhine-Westphalia) with operations in Germany, Hungary, the US and China, Frimo has a global footprint with a strong market position in Europe and North America. It employs around 1,400 people and generated revenues of €207m in 2015. Frimo's business comprises two of DBAG's core sectors: mechanical and plant engineering and automotive suppliers, and the company expects to benefit from DBAG's experience and network. Key elements for Frimo's development following DBAG's investment include geographical expansion, particularly in China, the US and Mexico, the enlargement of the services and spare-parts business as well as potential add-on acquisitions of supplementary technologies and applications.

DBAG and DBAG Fund VI will acquire a majority interest in the management buyout of Frimo Group, with DBAG investing up to €15m for a c 15% stake. The purchase agreement is subject to regulatory approval, with the transaction expected to be completed by late September 2016.

New investment in R&M International

R&M International's product portfolio encompasses the interior fittings for new ship builds and refits, and ship maintenance. R&M distinguishes itself from its competitors in operating manufacturing facilities in addition to designing and installing complete fit outs for cabins and fittings for passenger and crew areas. R&M's focus is on interior outfitting for cruise ships and ferries (over two thirds of revenues), special vessels and freighters as well as the offshore market. Headquartered in Hamburg, R&M has manufacturing sites in Germany and China and 13 project offices and service centres worldwide. It employs around 550 people and generated revenues of €122m in 2015. R&M's industrial services business represents one of the core sectors in which DBAG has extensive investment experience. In a fragmented market for marine interior outfitting, R&M is one of the larger players that are in a position to drive consolidation in that market. R&M has a strong market position in the structurally growing cruise ship market and has growth opportunities through geographical expansion, a broader product range and extension of its service business.

DBAG and DBAG ECF will acquire a 33% interest in R&M International, with DBAG investing up to €7m for a c 16% stake. The purchase agreement is subject to regulatory approval, with the transaction expected to be completed by late September 2016.

Divestment of Broetje-Automation

DBAG's investment in Broetje-Automation, including the exit via sale to a strategic buyer reflects the typical transaction that DBAG management seeks to achieve. Following DBAG's investment in March 2012 alongside DBAG Fund V, Broetje-Automation more than doubled annual revenues from €83m, reporting revenues of €87m for the six months to end-March 2016. DBAG's expertise supported the quadrupling in size of Broetje-Automation's services business to generate over 20% of total revenues, alongside broadening its product and services range and international expansion, which included establishment of a sales office in Shanghai. Growth was achieved both organically and through the acquisition of Dürr Group's aircraft assembly technology business in 2014.

DBAG held a 15% stake in Broetje-Automation and its c €25m share of the agreed sale proceeds represents an exit multiple of more than 4x its investment cost of €5.6m. The sale valuation is higher than DBAG's most recent investment valuation for Broetje-Automation, with the uplift, which will be reflected in DBAG's Q416 results, already incorporated into management's FY16 guidance.

Financial resources and commitments

DBAG's financial resources (comprising cash and long-term securities) increased marginally from €58.3m at 30 September 2015 to €59.0m at 30 June 2016, with the major cash flows being €24.0m of new investments, the €13.7m FY15 dividend payment and €41.2m of inflows, primarily from realisations. Investments included €12.8m in Telio Group and €6.6m in mageba. The largest inflows were €22.6m from the sale of Spheros and €8.8m from the recapitalisation of Schülerhilfe. Sale proceeds from the divestment of Clyde Bergemann Power Group will be received over a three-year period with no cash receipts scheduled for the current financial year.

At 30 June 2016, DBAG had total undrawn capital commitments of €98m relating to the DBAG ECF and DBAG Fund VI parallel funds, with a further €5m outstanding commitment to older funds. Added to this will be DBAG's €200m commitment to DBAG Fund VII, with draw-downs spread over an investment period of up to six years once the new buyout fund commences investing in 2017. Given DBAG's current c €50m pa target investment run rate and fee income covering the majority of ongoing operating expenses, financial resources of €59m appear sufficient to cover DBAG's funding requirements for the next 12 months, with c €25m proceeds from the divestment of Broetje-Automation adding more to financial resources than the c €22m committed to the new investments in Frimo and R&M International. Realisations from the maturing of DBAG's current investment portfolio are expected to fund its commitment to DBAG Fund VII, while its €50m credit facility provides additional flexibility to manage short-term timing differences in cash inflows and outflows.

Launch of DBAG Fund VII

In July 2016, DBAG announced the closing of DBAG Fund VII with €1bn in capital commitments, including a €200m co-investment commitment from DBAG. The fundraising took less than three months, with around 80% of commitments coming from investors in preceding DBAG funds. This new buyout fund is significantly larger than DBAG Fund VI, which closed in 2012 with commitments of €700m, and its launch signifies a strategic advancement for DBAG. DBAG Fund VII will be able to invest up to €200m in a single larger buyout, while the existing DBAG Expansion Capital Fund (ECF) will start to invest in smaller buyouts in addition to growth financings.

DBAG Fund VII consists of an €800m principal fund and a supplementary €200m top-up fund, which will be used for larger investments, providing scope for the fund to invest up to €200m in a single transaction (representing a €40m investment for DBAG). The increase in scale provides scope for DBAG to engage with larger mid-market companies as well as improving its operational leeway in transaction processes. While DBAG Fund VII has scope to invest in larger companies, investments will continue to be made in companies with enterprise values between €75m and €250m, typically generating €50m to €500m in annual revenues.

DBAG ECF primarily addresses owner-managed German mid-market companies. To date, the fund has invested exclusively in minority stakes in family-run businesses. In future, it will have scope to take a majority interest in companies as well as structuring smaller buyouts, with investments ranging from €10m to €30m. DBAG has frequently identified attractive smaller buyouts, which it did not pursue due to the size of DBAG Fund VI. The extension of DBAG ECF to include the acquisition of majority stakes in growth businesses is seen by DBAG management as a logical progression.

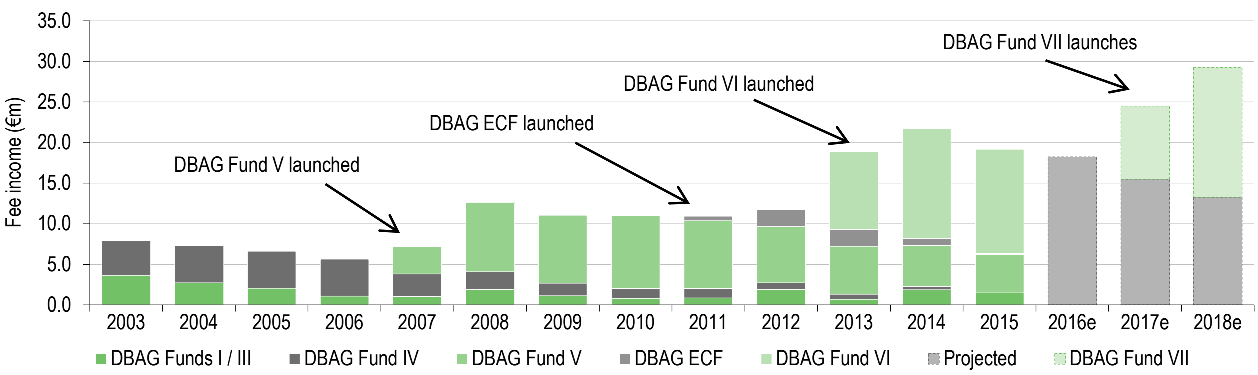
Improved longer-term outlook

The quality and profitability of its portfolio companies supports DBAG management's confidence in the earnings outlook for the remainder of the financial year, and their expectation is maintained for FY16 net income to exceed the €27.0m reported for FY15 by at least 20%. However, management highlights greater market uncertainty and potential near-term volatility of valuation multiples, which increases the risk of FY16 net income not reaching the €40m which was anticipated following the first quarter's €10m contribution from the sale of Spheros and a realisation by the DBG Eastern Europe II buyout fund, which had not been included in the original guidance.

As in 2012, 2013 and 2014, a further allocation to pension provisions is expected in FY16 due to the declining interest rate trend. The expected charge to other comprehensive income for FY16 of up to €8m will reduce year-end NAV by c 2.5% and lower the NAV total return reported for the year.

DBAG Fund VII's investment period will commence as DBAG Fund VI reaches capacity. Following the investment in Frimo, DBAG Fund VI will be over 70% invested, suggesting that DBAG Fund VII is likely to start investing in 2017. The launch of DBAG Fund VII will enlarge DBAG's assets under management or advice to c €1.8bn and lead to a significant increase in DBAG's fee income from the €18.6m projected for FY16 to c €25m in FY17 and c €29m in FY18, as illustrated in Exhibit 4.

Exhibit 4: Fee income analysis



Source: DBAG, Edison Investment Research

Change in dividend policy

An increased level of recurring fee income, together with the expectation that a larger portfolio will generate more stable inflows from divestments, has provided scope for DBAG to revise its dividend policy in order to provide greater consistency in dividend payments.

DBAG is changing its dividend policy effective from the current financial year, with the intention of paying a stable or rising annual dividend. The policy of paying a sustainable annual base dividend of €0.50 from retained profits supplemented by a surplus dividend dependent on the gains realised in each financial year will be discontinued and the board will recommend payment of a single dividend. Although a surplus dividend has been paid in nine of the last 10 years (see Exhibit 1), the total dividend has varied significantly, notably declining by 50% in 2015, creating uncertainty for shareholders over the dividend income they will receive each year. Under the new policy, shareholders should expect a smoother progression of the dividend payment each year. For the current financial year, DBAG has stated that the dividend recommendation is to be at least in line with the total €1.00 dividend paid for FY15.

Valuation

The value of the recurring fee income stream from DBAG's fund services business is not reflected in its reported NAV and we see the value of this business as the explanation for DBAG's shares trading at a premium to NAV in contrast with its listed private equity peers. However, assessing the value of DBAG's fund services business is highly subjective, requiring judgement over both the normalised level of earnings, which is complicated by the fee income profile (see Exhibit 4), and an appropriate peer group. DBAG shares currently stand at a 28.6% premium compared with a 12.3% discount for the LPX Europe Index (and 10.7% peer-group average discount – see Exhibit 6), with DBAG's premium having expanded by 12.5 percentage points over the last 12 months, compared with the 2.6 percentage point narrowing of the LPX Europe Index discount.

Exhibit 5: DBAG's share price premium/discount to NAV over three years (%)

Source: Thomson Datastream, Edison Investment Research. Note: Negative values indicate a discount, positive values a premium.

As illustrated in Exhibit 5, DBAG shares have traded almost continuously at a premium to NAV since October 2014, when DBAG started providing separate disclosure on the performance of its investment and fund services business segments. Having peaked at 47% in March 2015, DBAG's share price premium to NAV steadily declined over the following 12 months, briefly moving to a discount in February 2016, before moving higher again. The recent widening of the premium reflects the share price recovering along with the wider market, while reported NAV has remained relatively stable. The current 28.6% share price premium to NAV compares with a one-year average premium of 17.5%.

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Peer group comparison

Exhibit 6 shows a comparison of DBAG with a selected peer group of listed private equity investment companies. With the exception of 3i in the UK, which also manages third-party funds, DBAG is differentiated from peers by the recurring fee income stream generated by its fund services business as well as its regional and sector focus.

Exhibit 6: Selected peer group as at 24 August 2016

% unless stated	Country	Mkt cap £m	NAV TR 1 year	NAV TR 3 years	NAV TR 5 years	NAV TR 10 years	Price TR 1 year	Price TR 3 years	Price TR 5 years	Price TR 10 years	Discount (ex par)	Dividend yield (%)
Deutsche Beteiligungs	Europe	345.7	29.3	36.8	41.8	256.0	13.7	61.1	61.5	305.5	29.0	3.4
3i	Global	6,030.1	42.2	91.7	86.4	30.6	10.7	85.7	139.8	2.2	18.0	3.6
Altamir	Europe	326.1	25.0	41.5	50.5	119.2	13.0	22.9	39.2	51.2	(43.4)	0.0
GIMV	Global	986.5	21.1	16.9	7.9	69.3	39.3	44.2	28.8	113.3	5.6	0.0
Electra Private Equity	UK	1,526.3	32.3	75.1	112.0	243.7	18.9	72.5	120.5	208.3	(11.3)	0.0
HgCapital Trust	UK	479.1	11.5	31.4	40.3	155.3	12.4	18.0	20.7	146.7	(9.2)	3.1
ICG Enterprise Trust	UK	417.5	12.0	28.5	48.8	107.7	(2.9)	23.4	54.6	77.7	(24.0)	1.7
Oakley Capital Investments	Europe	261.0	16.8	9.0	18.1		(21.7)	(17.0)	(16.0)		(35.3)	0.0
Standard Life Euro Private Eq	Europe	379.6	22.5	42.7	45.0	107.7	7.3	34.3	54.4	59.7	(25.3)	2.1
Average		**1,194.7**	**23.6**	**41.5**	**50.1**	**136.2**	**10.1**	**38.3**	**55.9**	**120.6**	**(10.7)**	**1.5**

Source: Morningstar, Edison Investment Research. Note: Performance data to end-June 2016. TR=total return. All returns expressed in sterling terms.

DBAG's NAV total return in sterling terms to 30 June 2016 is ahead of the peer group average over one year and substantially ahead over 10 years, although below the average over three and five years. When comparing DBAG with UK and global peers, consideration should be given to sterling weakness against the euro helping performance over one and 10 years, while euro weakness against sterling has weighed on DBAG's performance over three and five years (the euro strengthened by 16.9% and 19.7% over one and 10 years and weakened by 3.4% and 8.3% over three and five years, respectively to end-June 2016). As noted in the Valuation section above, DBAG's shares are trading at a premium to NAV in contrast to the majority of its peers, which do not manage third-party funds, many of which are trading at a substantial discount to NAV. DBAG's above-average 3.4% yield is based on its €1.00 total dividend for FY15, which represents at least the expected level for the FY16 dividend payment under the new dividend policy.

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