August 9th, 2023
Research update

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STS Group AG

Strong EBITDA increase leads to positive EBIT

Rating: Buy (unchanged) | **Price:** 5.15 € | **Price target:** 19.50 € (prev.: 16.00 €)

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Current development

Basic data

Based in:	Hagen
Sector:	Automotive supplier
Headcount:	>1,400
Accounting:	IFRS
Ticker:	SF3:GR
ISIN:	DE000A1TNU68
Price:	5.15 Euro
Market segment:	General Standard
Number of shares:	6.5 m
Market Cap:	33.5 m Euro
Enterprise Value:	38.5 m Euro
Free Float:	22.4 %
Price high/low (12 M):	6.30 / 3.52 Euro
Øturnover (12 M Xetra):	10,100 Euro

Tailwind from the market

The Chinese market for heavy commercial vehicles had slumped by 51 percent to only about 670,000 units last year due to the restrictive COVID-19 policy and the end of a special boom, which had previously been triggered by a tightening of regulatory provisions. In the first half of 2023, it recovered by 25 percent to 470,000 vehicles, thanks to the relaxation of COVID-19 requirements and the economic recovery (source: steelorbis/cvworld/STS). In Europe, too, the development was positive, spurred by lesser problems with material shortages. In the EU, truck sales increased by 20 percent to just under 180,000 thousand, with double-digit growth in Germany (+24.8 percent) and France (+12.3 percent), markets of particular importance to STS (source: ACEA).

Strong sales growth

STS was able to translate the positive market development into a significant increase in revenue. In China, sales increased by 54.3 percent to EUR 23.8 m. Thus, it paid off that the capacities had not been fully adjusted to the low market level from 2022 despite a restructuring. But also in the largest segment, Plastics,

FY ends: 31.12.	2020	2021	2022	2023e	2024e	2025e
Sales (m Euro)	235.0	242.0	235.1	280.4	294.9	319.0
EBITDA (m Euro)	14.7	19.2	9.6	17.3	21.3	26.2
Net profit	-15.9	1.8	-9.9	-0.8	2.3	6.8
EpS	-2.60	0.28	-1.53	-0.13	0.35	1.04
Dividend per share	0.00	0.04	0.00	0.00	0.00	0.00
Sales growth	-35.2%	3.0%	-2.9%	19.3%	5.2%	8.2%
Profit growth	-	-	-	-	-	201.0%
PSR	0.14	0.14	0.14	0.12	0.11	0.10
PER	-	18.6	-	-	14.9	4.9
PCR	-	0.9	5.2	1.8	4.1	1.8
EV / EBITDA	2.6	2.0	4.0	2.2	1.8	1.5
Dividend yield	0.0%	0.8%	0.0%	0.0%	0.0%	0.0%

which reflects revenue in Europe and Mexico, there was a strong growth in sales of 19.4 percent to EUR 107.0 m. The smallest division, Materials, also recorded double-digit growth of 12.2 percent to EUR 20.6 m. After consolidation, group revenue increased by a total of 22.3 percent to EUR 143.5 m. Of this, EUR 74 m was generated in the first three months and EUR 69.5 m in the period from April to June, which is due to a somewhat weaker development in France and lower revenue from the sale of tools.

Business figures	6M 22	6M 23	*Change*
Sales	117.4	143.5	*+22.3%*
- Plastics	89.6	107.0	*+19.4%*
- China	*15.4*	*23.8*	*+54.3%*
- Materials	*18.4*	*20.6*	*+12.2%*
- consolidation	*-6.0*	*-7.9*	-
EBITDA	2.9	8.4	*+189.7%*
- Plastics	3.5	5.9	*+68.6%*
- China	*-0.2*	*2.9*	-
- Materials	*0.3*	*1.1*	*+266.7%*
- consolidation	*-0.7*	*-1.5*	-
EBITDA margin	*2.5%*	*5.8%*	*+3.3Pp.*
EBIT	-4.9	2.1	-
EBIT margin	*-4.2%*	*1.5%*	*+5.7Pp.*
Period result	-6.3	-0.8	-

In m Euro and percent; source: Company

Increase in material costs compensated

Due to significantly higher input prices, the cost of materials increased more than sales (and also than total output), by 26.6 percent to EUR 100.9 m. This means that the cost of materials ratio rose from 63.6 to 67.1 percent within a year. This was offset by a 2.6 percent reduction in personnel costs to EUR 30.1 m (ratio 20.0 percent, previous year: 24.7 percent) – a remarkable achievement in view of the high sales growth. The increase in other operating expenses was also only disproportionately low (+12.6 percent to EUR 15.2 m), while other operating income was significantly higher year-on-year (EUR 4.2 m, previous year: EUR 1.7 m), partly due to a positive one-off effect from energy cost reimbursements. In total, this enabled an improvement of the half-year EBITDA by 190 percent to EUR 8.4 m. The EBITDA margin increased thus from 2.4 to 5.8 percent. While profit before tax, interest and depreciation in the first three months had been EUR 3 m (margin: 4.1 percent), in the period from April to June it was EUR 5.4 m (margin: 7.8 percent) – despite lower sales in the period. The delayed but ultimately largely successful passing on of higher input prices, further increasing revenue in China and the adjustment of structures had a positive impact here.

EBIT positive

Decreasing depreciation and amortisation (-18 percent to EUR 6.3 m) in combination with the EBITDA growth resulted in EBIT turning positive from EUR -4.9 m in the previous year to EUR +2.1 m, equivalent to a margin improvement of 5.7 percentage points to 1.5 percent. After deducting the financial result (EUR -2.1 m, previous year: EUR -1.4 m), this led to a balanced pre-tax result, only the net result was still slightly negative at EUR -0.8 m (previous year: EUR -6.3 m) due to the tax expense of EUR 0.7 m.

High free cash flow

The improvement in earnings was an important driver of operating cash flow, which more than doubled from EUR 7.4 m to EUR 16.7 m in the first half of the year. Other positive factors were advance payments for tool production and an increase in trade payables. As the cash outflow from investment activities decreased from EUR -8.2 to -3.4 m at the same time, the free cash flow shot up from EUR -0.8 m to EUR +13.3 m. This was partly used for a net repayment of liabilities (financing CF: EUR -8.1 m), but liquidity has nevertheless increased from EUR 25.6 m to EUR 31.2 m in the year to date.

Net financial debt greatly reduced

Net financial debt was thus greatly reduced, from EUR 15.0 m at the end of 2022 to only EUR 4.0 m at the end of June. Due to growth, the balance sheet total expanded significantly during this period, from EUR 211.6 m to EUR 231.1 m. On the assets side, in addition to the expansion of liquidity, this was mainly due to increases in inventories (from EUR 49.2 m to EUR 56.3 m) and in trade receivables (from EUR 41.9 m to EUR 49.9 m). On the liabilities side, this was offset in particular by a sharp increase in short-term contract liabilities (from EUR 3.4 m to EUR 15.7 m, mainly from advance payments for the production of tools) and trade payables (from EUR 50.9 m to EUR 64.5 m). Equity, on the other hand, fell from EUR 49.5 m to EUR 46.3 m due to the loss for the period and currency translation losses, reducing the equity ratio from 23.4 percent to 20.1 percent. At the Annual General Meeting, the company renewed the expiring authorised capital of EUR 3.5 m as a precautionary measure, but no plans for possible measures are currently known.

Forecast confirmed

The figures for the first half of the year were as planned, and on this basis the management has also confirmed the forecast for the entire year. Accordingly, a slight growth in revenue is still targeted, which is to be accompanied by a significant increase in EBITDA. As no special effects are expected, the adjusted EBITDA will be the same as that reported. At the same time, the prerequisites for further growth are already being created, and here the main focus is currently on the USA. The company had won a major contract for the market in 2019 to supply a complete truck roof system made of fibre-reinforced plastic (SMC), with series production set to start next year. For this purpose, a new plant has been built in an existing hall since November 2022. There was an update on this at the Annual General Meeting (see illustration). Accordingly, the first part was already pressed in May after the assembly of the press and by the end of June, 90 percent of the conversion work had been completed. The company is thus fully on track.

Decreasing market drivers

The unchanged forecast of slight revenue growth seems very cautious after the strong growth in the first six months, especially since the reference value from the second half of 2022 (due to weak business in China) was also low at EUR 117.7 m. However, the growth drivers on the market are currently weakening noticeably. In China, the peak of the recovery movement so far was already reached in March with 115,000 units, since then sales have been declining from month to month, to only 65,000 in July. However, this is still an increase of 44 percent compared to the previous year. In addition, STS has won new orders in China, which should mitigate possible slowing effects from the market. In Europe, the figures for the

Progress at the new US plant; source: Company second quarter were also below those of the first three months (but significantly above the previous year). In the second half of the year, some downward pressure is to be expected from the difficult economic situation, although the market is currently relatively stable, according to the company. As a precaution, we assume that STS sales in the period from July to December will be below the level of the first six months (one-off revenue from the sale of tools is not yet included) and now expect annual revenue of EUR 280.4 m, which is, however, significantly higher than our previous expressly conservative calculation (EUR 256.1 m). We see EBITDA in the second half of the year above the level of the period January to June due to the major progress in profitability in the second quarter (which is, however, somewhat overstated by one-off effects in other operating income), so that we now estimate the annual figure at EUR 17.3 m (previously: EUR 16.0 m). This means that we expect a revenue growth of 19 percent and an 80 percent improvement in EBITDA in 2023 compared to 2022.

2024: Growth impulses from the USA

For the coming year, we have already anticipated stagnating business in the Plastics and Materials segments (assumed revenue growth: 0.8 percent), and we are maintaining this. For China, we have so far assumed a further recovery to a revenue of EUR 52 m, which might be too high given the current trend in the country. Therefore, we reduce our estimate to EUR 49 m. However, there will be still growth impulses from the start of series production in the USA, so that we expect an overall increase in group revenue of 5 percent to EUR 294.9 m (previously: 8.8 percent to EUR 278.6 m). Despite possible moderate start-up losses of the new plant, we see EBITDA at EUR 21.3 m above the level estimated for 2023, which is due to further growth in high-margin revenue in China and the full-year effects of cost increases passed on this year.

Good basis for expansion

Due to the development of the US market and the strong position in China, the medium-term growth prospects are very promising. For the period 2024 to 2030, we expect an average sales growth rate of 4.5 percent (previously 4.6 percent), which, together with the higher baseline from 2024, will lead to a target sales volume of EUR 383 m in 2030 (previously: EUR 366 m). Thanks to economies of scale, we then trust the company to achieve an EBITDA margin of 8.7 percent (unchanged). The table on this page shows the revenue development we have assumed for the individual divisions and the table on the next page contains the key cash flow figures up to 2030; further details of the estimates are provided in the Annex.

Frame parameters unchanged

Subsequently, we continue to calculate the terminal value with a 25-percent discount to the target margin of 2030 and a "perpetual" cash flow growth of 1 percent p.a. The discount rate (WACC) also remains unchanged at 6.7 percent. For this, we have assumed a cost of equity according to CAPM of 11.2 percent (with: safe interest rate of 2.5 percent, market risk premium of 5.8 percent and beta factor of 1.5), as well as a target capital structure of 65 percent debt, an interest rate on borrowed capital of 6 percent and a tax rate for the tax shield of 29 percent.

New price target: EUR 19.50

With the model adjustments, the fair value we have determined is now EUR 126.6 m or EUR 19.48 per share, from which we derive EUR 19.50 as the new

Revenue model (m Euro)	2023	2024	2025	2026	2027	2028	2029	2030
Plastics	210.4	212.1	214.0	217.4	224.2	230.9	236.7	242.6
China	46.0	49.0	55.4	58.7	62.2	65.9	69.2	72.7
Materials	40.0	40.3	40.6	41.2	42.4	43.7	44.8	45.9
USA	0.0	10.0	26.0	31.2	36.0	37.8	39.7	41.7
consolidation	-16.0	-16.5	-17.0	-17.5	-18.0	-18.5	-19.1	-19.7
Total sales	**280.4**	**294.9**	**319.0**	**331.0**	**346.8**	**359.8**	**371.3**	**383.2**

Estimates SMC-Research

m Euro	12 2023	12 2024	12 2025	12 2026	12 2027	12 2028	12 2029	12 2030
Sales	280.4	294.9	319.0	331.0	346.8	359.8	371.3	383.2
Sales growth		5.2%	8.2%	3.8%	4.8%	3.7%	3.2%	3.2%
EBITDA	**17.3**	**21.3**	**26.2**	**28.1**	**29.8**	**31.3**	**32.3**	**33.3**
EBIT	4.1	7.3	12.7	15.1	17.2	19.0	20.0	21.1
Tax rate	35.0%	30.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%
Adjusted tax payments	1.4	2.2	3.7	4.4	5.0	5.5	5.8	6.1
NOPAT	**2.7**	**5.1**	**9.0**	**10.7**	**12.2**	**13.5**	**14.2**	**15.0**
+ Depreciation & Amortisation	13.2	14.0	13.4	13.0	12.6	12.3	12.3	12.3
+ Increase long-term accruals	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
+ Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating cash flows	16.2	19.4	22.8	24.1	25.1	26.1	26.8	27.5
- Increase Net Working Capital	1.4	-11.8	-5.7	-4.6	-4.2	-3.6	-3.7	-3.8
- Investments in fixed assets	-7.9	-9.7	-11.9	-11.6	-12.0	-12.4	-12.7	-13.0
Free cash flow	**9.7**	**-2.1**	**5.1**	**7.8**	**9.0**	**10.1**	**10.4**	**10.7**

SMC estimation model

price target (a sensitivity analysis for the price target determination can be found in the Annex). The increase compared to our last estimate (EUR 16.00) is due to the higher revenue and earnings projections as a result of the strong development in 2023. We continue to rate the forecast risk of our estimates as slightly above average at four points on a scale of 1 (low) to 6 (high).

Conclusion

In the first half of 2023 STS grew dynamically by 22 percent and used this to achieve a strong 190 percent improvement in EBITDA to EUR 8.4 m. As a result, EBIT also turned positive from EUR -4.9 m to EUR 2.1 m. Also noteworthy is the high free cash flow of EUR 13.3 m, which has enabled a reduction in net financial liabilities from EUR 15.0 m to EUR 4.0 m. The cash balance is comfortable at EUR 31.2 m.

For the full year, management continues to target slight revenue growth and a significant increase in adjusted EBITDA.

According to our current assessment, the growth drivers from the market are likely to weaken somewhat in the second half of the year. Nevertheless, we consider the growth assessment as very cautious; we now expect a revenue increase of 19 percent to EUR 280.4 m and EBITDA of EUR 17.3 m (+80 percent). For 2024, however, we have slightly reduced our estimate for China revenue, taking into account the current somewhat weaker market development there.

Nevertheless, we see STS on a growth course overall, which is also supported by the new plant in the USA scheduled to start series production next year. The extension of the factory building is already 90 percent complete.

Overall, our new estimates are higher than the previous figures and our price target has thus increased from EUR 16.00 to EUR 19.50. Given positive growth and earnings prospects and a now almost balanced net financial position, we thus consider the STS share massively undervalued and reiterate our “Buy” rating.

Annex I: SWOT analysis

Strengths

- STS has established itself as a global tier-one truck supplier for plastic parts.
- The company has expertise and flexibility in the application of a wide range of manufacturing techniques (SMC, thermocompression and injection moulding), materials and batch sizes, and is increasingly becoming a system supplier.
- Successful international expansion with strong growth in China and the acquisition of a major order from the USA.
- Proved competence in acquisition and integration of companies as well as in the implementation of efficiency enhancement measures.
- With Adler Pelzer, the company has a strong parent company.

Weaknesses

- The EBITDA margin has recently improved but was still quite low at 5.8 percent in the first half of 2023.
- The operating surpluses are not yet sufficient for a positive net result.
- Due to the long lead time from order placement to revenue generation, sales initiatives only show up in group revenue with a significant delay.
- Structural growth dynamics in the still important European commercial vehicle market are low.
- In the wake of the takeover by Adler Pelzer, the liquidity of the share has decreased.

Opportunities

- With the new major shareholder at its side, STS's chances for further market share gains in China and a successful market entry in the USA have increased significantly.
- The construction of new plants in the USA and possibly also in China creates high growth potential in the medium term.
- Electromobility and new emission regulations (Europe, China) act as growth drivers.
- Adler Pelzer could transfer its hard-trim activities to STS; further acquisitions to strengthen its market position are conceivable.
- If STS establishes a growth path with rising margins, the share could be revalued.

Threats

- STS benefited significantly from a market recovery in the first half of 2023. However, the positive momentum in the European and Chinese markets for heavy commercial vehicles is currently declining again.
- In a recessionary environment, the pressure on margins could increase again.
- The start-up of the new plant in the USA could incur higher costs than expected.
- International conflicts (especially with China) could make business development more difficult.
- Adler Pelzer could decide to delist the share.

Annex II: Balance sheet and P&L estimation

Balance sheet estimation

m Euro	2022 act.	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e
ASSETS									
I. Total non-current	83.2	77.9	73.6	72.0	70.6	70.0	70.0	70.5	71.2
1. Intangible assets	18.7	18.0	17.4	16.9	16.5	16.2	15.9	15.7	15.4
2. Tangible assets	60.2	55.6	51.8	50.8	49.7	49.5	49.8	50.5	51.5
II. Total current assets	128.4	151.9	162.5	171.2	180.4	189.9	199.8	212.6	227.4
LIABILITIES									
I. Equity	49.5	48.4	50.7	57.4	66.1	76.4	88.1	100.8	114.6
II. Accruals	11.2	11.5	11.8	12.1	12.4	12.7	13.0	13.3	13.6
III. Liabilities									
1. Long-term liabilities	46.9	59.6	60.1	58.4	55.9	53.2	50.2	48.3	47.0
2. Short-term liabilities	104.0	110.2	113.6	115.3	116.5	117.6	118.5	120.7	123.4
TOTAL	**211.6**	**229.8**	**236.1**	**243.2**	**251.0**	**259.8**	**269.8**	**283.1**	**298.6**

P&L estimation

m Euro	2022 act.	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e
Sales	235.1	280.4	294.9	319.0	331.0	346.8	359.8	371.3	383.2
Total operating revenue	242.3	292.4	297.9	319.0	331.0	346.8	359.8	371.3	383.2
Gross profit	91.6	101.7	107.7	117.1	121.8	128.0	133.1	137.4	141.8
EBITDA	9.6	17.3	21.3	26.2	28.1	29.8	31.3	32.3	33.3
EBIT	-6.6	4.1	7.3	12.7	15.1	17.2	19.0	20.0	21.1
EBT	-9.1	0.2	4.1	9.5	12.2	14.4	16.5	18.0	19.3
EAT (before minorities)	-9.9	-0.8	2.3	6.8	8.7	10.2	11.7	12.8	13.7
EAT	-9.9	-0.8	2.3	6.8	8.7	10.2	11.7	12.8	13.7
EPS	-1.53	-0.13	0.35	1.04	1.33	1.58	1.80	1.96	2.11

Annex III: Cash flows estimation and key figures

Cash flows estimation

m Euro	2022 act.	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e
CF operating	6.5	18.1	8.1	18.2	20.6	22.2	23.7	24.2	24.9
CF from investments	-8.7	-7.9	-9.7	-11.9	-11.6	-12.0	-12.4	-12.7	-13.0
CF financing	-0.2	-9.1	-2.6	-6.6	-7.8	-8.4	-8.6	-6.1	-4.8
Liquidity beginning of year	28.3	25.6	26.7	22.6	22.3	23.5	25.4	28.1	33.5
Liquidity end of year	25.6	26.7	22.6	22.3	23.5	25.4	28.1	33.5	40.6

Key figures

percent	2022 act.	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e
Sales growth	-2.9%	19.3%	5.2%	8.2%	3.8%	4.8%	3.7%	3.2%	3.2%
Gross margin	39.0%	36.3%	36.5%	36.7%	36.8%	36.9%	37.0%	37.0%	37.0%
EBITDA margin	4.1%	6.2%	7.2%	8.2%	8.5%	8.6%	8.7%	8.7%	8.7%
EBIT margin	-2.8%	1.5%	2.5%	4.0%	4.6%	5.0%	5.3%	5.4%	5.5%
EBT margin	-3.9%	0.1%	1.4%	3.0%	3.7%	4.2%	4.6%	4.8%	5.0%
Net margin (after minorities)	-4.2%	-0.3%	0.8%	2.1%	2.6%	3.0%	3.3%	3.4%	3.6%

Annex IV: Sensitivity analysis

	Perpetual cash flow growth				
WACC	**2.0%**	**1.5%**	**1.0%**	**0.5%**	**0.0%**
5.7%	32.05	28.34	25.43	23.07	21.13
6.2%	27.26	24.44	22.16	20.29	18.72
6.7%	23.49	21.29	**19.48**	17.96	16.67
7.2%	20.45	18.70	17.24	15.99	14.92
7.7%	17.95	16.54	15.33	14.30	13.40

Disclaimer

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Charts
The charts were made with Tai-Pan (www.lp-software.de).

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II) Preparation and updating

The present financial analysis was prepared by: Dipl.-Kfm. Holger Steffen

Participants in the preparation of the present financial analysis: -

The present analysis was finished on 09.08.2023 at 7:15 and published on 09.08.2023 at 8:15.

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Buy	We expect an increase in price for the analysed financial instrument by at least 10 percent. We assess the estimation risk as average (3 to 4 points).
Speculative Buy	We expect an increase in price for the analysed financial instrument by at least 10 percent. We assess the estimation risk as above average (5 to 6 points).
Hold	We expect that the price of the analysed financial instrument will remain stable (between -10 and +10 percent). The forecast risk (1 to 6 points) has no further impact on the rating. The rating "hold" is also used in cases where we perceive a price potential of more

	than 10 percent, but explicitly mentioned temporary factors prevent a short-term realisation of the price potential.
Sell	We expect that the price of the analysed financial instrument will drop by at least 10 percent. The forecast risk (1 to 6 points) has no further impact on the rating.

The expected change in price refers to the current share price of the analysed company. This price and any other share prices used in this analysis are XETRA closing prices as of the last trading day before publication. If the share is not traded on XETRA, the closing price of another public stock exchange is used with a separate note to that effect.

The price targets published within the assessment are calculated with common methods of financial mathematics, especially with the DCF (discounted cash flow) method, the sum of the parts valuation and a peer group analysis. The valuation methods are affected by economic framework conditions, especially by the development of the interest rates.

The rating resulting from these methods reflects current expectations and can change anytime subject to company-specific or economic changes.

More detailed explanations of the models used by SMC Research can be found at:
http://www.smc-research.com/impressum/modellerlaeuterungen

An overview of the recommendations prepared and distributed by SMC Research in the last 12 months can be found at: http://www.smc-research.com/publikationsuebersicht

In the past 24 months, sc-consult GmbH has published the following financial analyses for the company:

Date	Investment recomm.	Target price	Conflict of interests
30.05.2023	Buy	16.00 Euro	1), 3), 10)
26.04.2023	Buy	16.00 Euro	1), 3), 10)
07.12.2022	Buy	12.60 Euro	1), 3), 4), 10)
17.08.2022	Hold	11.80 Euro	1), 3), 10)
02.06.2022	Speculative Buy	12.90 Euro	1), 3), 10)
19.04.2022	Speculative Buy	10.90 Euro	1), 3), 10)

In the course of the next twelve months, sc-consult GmbH will presumably prepare the following financial analyses for the company: one report, one update and two comments.

The publishing dates for the financial analyses are not yet fixed at the present moment.

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