November 23rd, 2020
Research update

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STS Group

Positive outlook for the end of the year

Rating: Speculative Buy (unchanged) | **Price:** 4.29 € | **Price target:** 7.20 € (prev.: 5.70 €)

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Recent business development

Basic data

Based in:	Hallbergmoos
Sector:	Automotive technology
Headcount:	approx. 1,600
Accounting:	IFRS
Bloomberg:	SF3:GR
ISIN:	DE000A1TNU68
Price:	4.29 Euro
Market segment:	General Standard
Number of shares:	6.5 m
Market Cap:	27.9 m Euro
Enterprise Value:	97.3 m Euro
Free Float:	approx. 27 %
Price high/low (12 M):	6.95 / 1.73 Euro
Øturnover (12 M Xetra):	33,000 Euro

As in the second quarter, the impact of the Covid-19 pandemic and the implementation of the agreed change in Group strategy were the main factors influencing the course of the third quarter for the STS Group. A capital increase of 500,000 shares provided short-term relief for the liquidity situation and improved the equity situation on the part of STS AG. At the beginning of November, the change in strategy towards a focus on the Plastics segment took effect with the completion of the sale of the Acoustics business.

The Group has thus divested the largest loss-maker of the first nine months of 2020, providing significant relief. The figures for the third quarter, announced at the beginning of November as well, also show an improvement of the operating situation in existing business. Thanks to a significant recovery in Europe compared to the second quarter and strong growth in China, total sales and adjusted EBITDA were at last year's level. At the same time, the liquidity situation at Group level was again significantly improved. The recently published specification of the annual outlook now also points to a strong fourth quarter 2020.

FY ends: 31.12.	2017	2018	2019	2020e*	2021e	2022e
Sales (m Euro)	310.0	401.2	362.8	308.2	245.9	270.7
EBIT (m Euro)	46.9	-1.3	-6.5	-23.3	4.9	10.2
Net profit	47.0	-4.8	-12.1	-29.1	-1.4	4.1
EpS	9.39	-0.74	-1.86	-4.47	-0.21	0.64
Dividend per share	0.00	0.00	0.00	0.00	0.00	0.00
Sales growth	127.7%	29.4%	-9.6%	-15.0%	-20.2%	10.1%
Profit growth	525.9%	-	-	-	-	-
PSR	0.09	0.07	0.08	0.09	0.11	0.10
PER	0.6	-	-	-	-	6.7
PCR	-	3.9	0.8	7.2	1.8	1.8
EV / EBIT	2.1	-	-	-	20.1	9.5
Dividend yield	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

**including one-off effects, in 2020 from November without Acoustics*

Crisis and capital increase

The beginning of the third quarter of 2020 was marked by the crisis for the STS Group. After the company had to report weak half-year figures on 10 August 2020, it became necessary to convene an extraordinary general meeting in accordance with section 92 of the German Stock Corporation Act (AktG). Due to the value adjustments resulting from the sale of the Acoustics division, the equity of the parent company STS AG had fallen to less than EUR 3 m, corresponding to less than 50 percent of the share capital. In response to this, one month later, the Management Board announced the issue of 500,000 new shares under exclusion of subscription rights at a nominal value of EUR 1 and a price of EUR 3 per share, all of which were subscribed by the major shareholder Mutares SE & Co. KGaA. This capital increase resulted in a gross cash injection of EUR 1.5 m and thus helped solving the equity problem. The necessary extraordinary general meeting was held on 25 September, thus fulfilling the legal requirements.

Sale of Acoustics division completed

The sale of the Acoustics Division to the Adler Pelzer Group, announced on 7 August, was finalised on 1 November. Prior to the sale, the relevant competition authorities in the countries concerned (Italy, Poland, Brazil) had given their approval. Management sees the sale as an opportunity to focus even more strongly on composite and injection moulding technologies in the future. The company believes that the growth opportunities in China and the USA – important for the future of the STS Group – will remain intact, as STS only markets plastic products in both regions.

The economy recovers

In accordance with the expectation that the worst of the Covid-19 crisis would be over in the second quarter, numerous research institutes have now slightly increased their economic growth figures for 2020. In line with this, the business performance of the STS Group also recovered somewhat in the third quarter. While the decline in sales for the first half of the year was 29.8 percent, sales for the first nine months of 2020 fell by "only" 20.9 percent compared to the previous year. As in previous quarters, the Plastics segment was particularly weak with a 37.8 percent year-on-year decline in sales, while the sales explosion in China continued impressively with a 79.9 percent increase over the same period last year. There were no more plant closures in the third quarter of 2020.

Revenues	9M 2019	9M 2020	*Change*
Acoustics	87.5	62.6	-28.5%
Plastics	131.6	81.9	-37.8%
China	33.3	59.9	79.9%
Materials	30.8	18.7	-39.3%
Consolidated	-6.9	-4.6	N.A.
Total	***276.3***	***218.5***	***-20.9%***

In m Euro and percent; source: Company

Quarterly sales at previous year's level

In the publication of the quarterly results for the third quarter, management speaks of a recovery in customer call-off rates to the level of the previous year. And indeed, consolidated sales in the third quarter of 2020 are exactly the same as in the previous year at EUR 82.5 m. This reflects strong growth in China (+128 percent) and a significant decline in sales in the Plastics segment.

Revenues	Q2 2020	Q3 2020	*Change*
Acoustics	15.0	25.0	66.7%
Plastics	20.3	28.5	40.4%
China	24.8	23.5	-5.2%
Materials	2.7	7.2	166.7%
Consolidated	-1.2	-1.7	N.A.
Total	***61.7***	***82.5***	***33.7%***

In m Euro and percent; source: Company

Recovery compared to previous quarter

Compared to the immediate previous period, segment revenues in the third quarter developed positively across all divisions. In total, sales increased by 33.7

percent. In China, revenues were down slightly quarter-on-quarter at -5.2 percent, but this has to be seen in the context of the sharp rise in revenues following the complete reopening of the Chinese plants at the beginning of the second quarter.

Adj. EBITDA slightly positive again ...

The operating result for the first nine months of 2020 (adjusted EBITDA) of EUR 1.9 m is significantly below the previous year's figure of EUR 14.1 m. As was the case with sales, there had been an opposite development between China and the other segments. The China division improved its earnings from EUR 4.6 m to EUR 12,5 m and achieved an adjusted EBITDA margin of 20.9 percent. In contrast, all other divisions turned into the red, with Acoustics being the main loss-maker with EUR -5.3 m.

Adjusted EBITDA	9M 2019	9M 2020	*Change*
Acoustics	0.9	-5.3	N.A.
Plastics	9.9	-3.1	N.A.
China	4.6	12.5	171.7%
Materials	1.5	-0.6	N.A.
Consolidated	-2.8	-2.9	N.A.
Total	***14.1***	***1.9***	***-86.5***

In m Euro and percent; source: Company

... through loss limitation in Europe

On a positive note, however, adjusted EBITDA at Group level improved significantly from Q2 to Q3. In the Acoustics, Plastics and Materials segments, mainly active in Europe, the respective segment losses were contained and, thanks to a surplus in the Materials segment, the company even managed to return to the profit zone with an adjusted EBITDA of EUR 0.4 m. The lion's share of the operating profit, however, is still attributable to business in China that generated, as in the previous quarter, an adjusted EBITDA of around EUR 5 m.

Adjusted EBITDA	Q2 2020	Q3 2020	*Change*
Acoustics	-2.6	-0.2	N.A.
Plastics	-2.4	-0.1	N.A.
China	5.2	4.9	-5.8%
Materials	-0.6	0.7	N.A.
Consolidated	-0.7	-1.2	N.A.
Total	***-1.0***	***4.1***	***N.A.***

In m Euro and percent; source: Company

Personnel costs reduced

The recovery in group sales in the third quarter of 2020 was also reflected in a stabilisation of the expense ratios.

Expense ratios	9M 2019	9M 2020	*Change*
Sales	**276.3**	**218.5**	**-20.9%**
Material costs	161.6	127.3	-21.2%
Ratio	*58.5%*	*58.3%*	*-0.2 pp.*
Personnel costs	77.0	66.4	-13.8%
Ratio	*27.9%*	*30.4%*	*+2.5 pp.*
Other operating expenses	35.1	34.5	-1.7%
Ratio	*12.7%*	*15.8%*	*2.9 pp.*

In m Euro and percent; source: Company

Expense ratios	H1 2019	H1 2020	*Change*
Sales	**193.8**	**136.0**	**-29.8%**
Material costs	113.9	79.1	-30.6%
Ratio	*58.8%*	*58.2%*	*-0.6 pp.*
Personnel costs	54.0	44.7	-17.2%
Ratio	*27.9%*	*32.9%*	*+5.0 pp.*
Other operating expenses	24.9	19.9	-20.1%
Ratio	*12.9%*	*14.6%*	*1.8 pp.*

In m Euro and percent; source: Company

The cost of materials ratio in the first three quarters was kept at 58.3 percent, while the personnel cost ratio in the first three quarters of 2020 improved from 32.9 percent in the first half of 2020 to 30.4 percent. For the third quarter, the personnel costs ratio was 26.3 percent, which represents an improvement of 1.6 percentage points compared with the same quarter a year ago and indicates that it was possible to successfully counteract the negative economies of scale resulting from the year-on-year drop in sales. By contrast, there was a significant increase in other operating expenses both compared with the first half of 2020 and the same quarter of the previous year. This is due to the extraordinary expenses related to the restructuring of the corporate headquarters and the sale of the Acoustics segment totalling EUR 6.0 m during the reporting period. Of this total amount, EUR 1.7 m was incurred in the first half of 2020 in connection with the closure of the company's headquarters, while EUR 4.3 m originated in the third quarter of 2020 due to the negative purchase price of the sale of Acoustics and an earn-out clause with Autoneum.

Net loss for the period remains high

The extraordinary expenses associated with the sale of the division are largely responsible for the fact that a high net loss of EUR 7.6 m had to be reported in the third quarter as well. The cumulative net loss for the current financial year thus rose from EUR 27.7 m for the first half of the year to EUR 35.3 m for the first nine months of 2020.

New forecast for 2020 ...

Following the closing of the sale of the Acoustics division at the beginning of November and the publication of the results for the third quarter, management specified its forecast for the 2020 fiscal year on 17 November. For the entire company, including Acoustics, sales of between EUR 305 and 312 m and an EBITDA margin (adjusted for special effects) of 4.0 to 4.8 percent are expected. Compared to the previous year, this represents a decline in sales of 14 to 16 percent and a margin that is slightly below the previous year's level of 4.9 percent.

... implies a strong fourth quarter

The company's full-year forecast implies a strong operating improvement in the fourth quarter. While sales for the remaining segments were EUR 57.5 m in the third quarter, the Management Board's forecast for the last three months of 2020 expects Group sales (with Acoustics revenues of only one month) between EUR 72 and 82 m. At the same time, the target margin for the year means that the EBITDA margin adjusted for one-off effects is expected to reach double figures in the fourth quarter of 2020. This strong improvement is explained with a significant recovery in call-off rates in Europe, the deconsolidation of the Acoustics business, the conclusion of high-margin tooling orders in Europe and the growth of the high-margin business in China.

Adjustment of our 2020 estimate

Based on the management's forecast, we are increasing our estimate for annual sales for the entire company (including Acoustics) from EUR 288.4 m to EUR 308.2 m. At the same time, we are raising our estimate for adjusted EBITDA from EUR 6.1 m to EUR 13.3 m, corresponding to a margin of 4.3 percent. This reflects the expectation of a fourth quarter with strong sales and margins in both the Plastics and China segments. For the fourth quarter, we do not expect any further extraordinary expenses and thus arrive at a new estimate of the net loss for the year amounting to EUR 29.1 m (previously EUR 36.7 m).

Adjustment of our long-term estimates

The strong performance expected by management and by us for the fourth quarter has no direct impact on our long-term estimates, as we were already assuming a strong margin improvement in 2021. We therefore largely maintain our estimate, but now expect segment sales to recover to the 2019 level as early as 2021. With regard to the development of the North American business, we are a little more cautious than we were in the summer and are adjusting our expectations insofar as we are not expecting significant sales until 2023/2024.

m Euro	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
Sales	**308.2**	**245.9**	**270.7**	**289.0**	**318.1**	**338.9**	**359.7**	**382.4**
Sales growth	-15.0%	-20.2%	10.1%	6.8%	10.0%	6.5%	6.1%	6.3%
EBIT margin	-7.6%	1.2%	3.8%	4.1%	4.5%	4.8%	5.0%	5.2%
EBIT	**-23.3**	**4.9**	**10.2**	**11.8**	**14.3**	**16.1**	**17.9**	**19.9**
Tax rate	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%
Adjusted tax payments	1.5	1.5	3.0	3.4	4.2	4.7	5.2	5.8
NOPAT	**-24.8**	**3.4**	**7.2**	**8.4**	**10.2**	**11.4**	**12.7**	**14.1**
+ Depreciation & Amortisation	30.6	13.3	13.3	13.3	13.3	13.3	13.3	13.3
+ Increase long-term accruals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross operating cash flows	**5.8**	**16.6**	**20.5**	**21.7**	**23.4**	**24.7**	**26.0**	**27.4**
- Increase Net Working Capital	2.3	4.0	-1.6	-1.2	-1.9	-1.3	-1.3	-1.5
- Investments in fixed assets	-11.5	-13.0	-10.9	-11.4	-12.2	-12.8	-13.4	-14.1
Free cash flow	**-3.4**	**7.6**	**8.1**	**9.1**	**9.3**	**10.6**	**11.2**	**11.8**

SMC estimation model

Liquidity and solvency

As of 31 September 2020, cash and cash equivalents amounted to EUR 31.8 m. It was thus significantly higher than the corresponding figure as of 30 June 2020 of EUR 22.8 m. Since additional borrowings were taken out at the same time, net financial debt nevertheless rose over the quarter from EUR 43.0 m to EUR 48.9 m. In the meantime, the shortfall in the equity of the AG has been remedied by the aforementioned capital increase and a revaluation of segment assets in the Plastics segment, which will be reflected in future balance sheets. Management is currently not planning any further capital increase. In our view, this has significantly improved the company's short-term liquidity outlook. However, a detailed assessment will only be possible with the publication of the balance sheet adjusted for the deconsolidated Acoustics division.

Framework data adjusted

We have adjusted the model's framework data in response to recent developments. The gradual improvement of the operating and liquidity situation has prompted us to reduce the imputed borrowing costs from 11 percent to 9 percent. We have left the remaining basic data of the model unchanged. Thus, we now discount the cash flows resulting from our estimates at a WACC rate of 7.9 percent (previously 8.8 percent), based on a cost of equity of 10.75 percent (consisting of: beta factor: 1.5, risk-free interest rate: 1.0 percent, risk premium 6.5 percent), borrowing costs of now 9 percent and a target debt ratio of 65 percent. The assumptions used to determine the terminal value have remained unchanged. Therefore, we continue to work with a 25 percent safety discount on the target margin of the detailed forecast period and a "perpetual" cash flows growth of 1.0 percent.

Target price: EUR 7.20 per share

The model results in a market value of equity of EUR 47,0 m or around EUR 7.20 per share, which we set as a new price target. The increase in the price target is mainly due to the positive outlook for the end-of-year business and the improved liquidity situation. We reduce the forecast risk of our estimates from the maximum value to five points (on a scale of 1 to 6), which means that it is still high.

Sensitivity analysis

When the input parameters are varied for our sensitivity analysis (WACC between 6.9 and 8.9 percent and perpetual cash flows growth between 0 and 2 percent), the fair value of the share lies between EUR 3.50 and EUR 13.80.

Sensitivity analysis	Perpetual cash flows growth				
WACC	**2.0%**	**1.5%**	**1.0%**	**0.5%**	**0.0%**
6.9%	13.80	12.20	10.90	9.80	8.80
7.4%	11.20	10.00	8.90	8.00	7.20
7.9%	9.10	8.10	7.20	6.50	5.80
8.4%	7.30	6.50	5.80	5.20	4.60
8.9%	5.80	5.10	4.50	4.00	3.50

Conclusion

As a company in the automotive supply industry, STS Group was severely affected by the outbreak of the Covid-19 pandemic in the first half of the year, which led to a rethink of its corporate strategy. The prospect of restructuring the Acoustics division and putting it on a sound economic footing was abandoned and it was decided instead to focus even more strongly on the Plastics division and in particular on the booming business in China.

With the completion of the sale of the Acoustics division and the recovery of the European business in the third quarter, the new management team has now achieved its first successes. Business in China continues very good but is also being boosted by a special economic situation in the current year due to new regulations. Another positive aspect is that the company was able to significantly improve its liquidity situation.

The annual outlook points to a further recovery of the operating business in the fourth quarter, with the renewed worsening of the pandemic situation in Europe representing an uncertainty factor. But the next year will be decisive. STS must then show that it can return to the growth path and achieve a sustainable improvement in profitability.

The company is currently very favourably valued. A further deterioration of the situation is still possible, but we consider the risk to be largely reflected in the share price. The upside potential provided by good business in China and the potential for recovery in Europe leads us to continue to rate the share as a "speculative buy" with a price target of EUR 7.20.

Annex I: Balance sheet and P&L estimation

Balance sheet estimation

m Euro	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
ASSETS									
I. Total non-current	136.4	97.4	97.1	94.7	92.8	91.7	91.3	91.4	92.2
1. Intangible assets	23.8	11.0	11.0	11.0	11.0	11.0	11.0	11.0	11.0
2. Tangible assets	102.9	76.7	76.4	73.9	72.1	71.0	70.5	70.7	71.5
II. Total current assets	120.0	121.3	114.8	123.5	132.7	143.9	155.1	167.2	180.3
LIABILITIES									
I. Equity	68.6	41.0	39.7	43.8	49.4	57.1	66.1	76.5	88.4
II. Accruals	21.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8	11.8
III. Liabilities									
1. Long-term liabilities	33.3	33.7	33.7	33.7	33.7	33.7	33.7	33.7	33.7
2. Short-term liabilities	132.8	132.2	126.8	128.9	130.5	133.1	134.9	136.7	138.7
TOTAL	256.5	218.7	211.9	218.2	225.4	235.6	246.4	258.6	272.5

P&L estimation

m Euro	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
Sales	362.8	308.2	245.9	270.7	289.0	318.1	338.9	359.7	382.4
Total operating revenues	369.6	308.2	245.9	270.7	289.0	318.1	338.9	359.7	382.4
Gross profit	160.3	135.9	108.2	119.1	127.2	139.9	149.1	158.3	168.2
EBITDA	17.6	13.3	20.1	23.5	25.1	27.6	29.4	31.2	33.2
EBIT	-6.5	-23.3	4.9	10.2	11.8	14.3	16.1	17.9	19.9
EBT	-9.9	-27.1	0.6	6.1	7.9	10.7	12.7	14.6	16.8
EAT (before minorities)	-12.1	-29.1	-1.4	4.1	5.6	7.6	9.0	10.4	11.9
EAT	-12.1	-29.1	-1.4	4.1	5.6	7.6	9.0	10.4	11.9
EPS	-1.86	-4.47	-0.21	0.64	0.87	1.17	1.38	1.60	1.83

Annex II: Cash flows estimation and key figures

Cash flows estimation

m Euro	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
CF operating	36.6	3.9	15.9	15.8	17.7	19.0	20.9	22.3	23.7
CF from investments	-15.0	-11.5	-13.0	-10.9	-11.4	-12.2	-12.8	-13.4	-14.1
CF financing	-35.6	14.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liquidity beginning of year	33.2	17.2	24.1	27.0	32.0	38.3	45.1	53.2	62.2
Liquidity end of year	17.2	24.1	27.0	32.0	38.3	45.1	53.2	62.2	71.8

Key figures

percent	12 2019	12 2020	12 2021	12 2022	12 2023	12 2024	12 2025	12 2026	12 2027
Sales growth	-9.6%	-15.0%	-20.2%	10.1%	6.8%	10.0%	6.5%	6.1%	6.3%
Adj. EBITDA margin	4.9%	4.3%	8.2%	8.7%	8.7%	8.7%	8.7%	8.7%	8.7%
EBIT margin	-1.8%	-7.6%	2.0%	3.8%	4.1%	4.5%	4.8%	5.0%	5.2%
EBT margin	-2.7%	-8.8%	0.3%	2.3%	2.7%	3.4%	3.7%	4.1%	4.4%
Net margin (after minorities)	-3.3%	-9.4%	-0.6%	1.5%	1.9%	2.4%	2.7%	2.9%	3.1%

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: Dr. Bastian Brand

Participants in the preparation of the present financial analysis: Dipl.-Kfm. Holger Steffen

The present analysis was finished on 23.11.2020 at 7:20 and published on 23.11.2020 at 7:30.

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Strong Buy	We expect an increase in price for the analysed financial instrument by at least 10 percent. We assess the estimation risk as below average (1 to 2 points).
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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 realization 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	Rating	Target price	Conflict of interests
10.11.2020	Speculative Buy	5.70 Euro	1), 3), 4)
14.08.2020	Hold	4.30 Euro	1), 3), 4)
14.05.2020	Speculative Buy	7.00 Euro	1), 3), 4)
04.05.2020	Speculative Buy	7.00 Euro	1), 3), 4)
12.03.2020	Speculative Buy	7.50 Euro	1), 3), 4)
13.01.2020	Speculative Buy	10.00 Euro	1), 3), 4)
19.11.2019	Speculative Buy	10.00 Euro	1), 3), 4)
10.10.2019	Speculative Buy	10.00 Euro	1), 3), 4)
14.08.2019	Speculative Buy	10.00 Euro	1), 3), 4)
21.05.2019	Speculative Buy	14.10 Euro	1), 3)
15.04.2019	Speculative Buy	15.10 Euro	1), 3), 4)

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, two comments

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

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