

INTERVIEW

Mr Grede, what sets DBAG apart from other private equity companies?

How does DBAG manage to write success stories in eventful times? What does software have to do with the Old Economy? What does DBAG need the funds for? And most importantly of all: what does this mean for the shareholders? Spokesman of the Board of Management Torsten Grede answers these and other questions on the strategy pursued by Deutsche Beteiligungs AG.

A real estate agent, software for route optimisation and the construction of fibre-optic networks – has DBAG recently entered completely different sectors than before?

That's true – we have broadened the range of industries in our portfolio. The focus, however, is still on investments in companies that are particularly characteristic of the German economy in what we describe as our core sectors: automotive suppliers, mechanical and plant engineering, companies that produce industrial components – from engine blocks to high-tech films and electronic controls for trains – and industrial service providers. But we no longer want to focus exclusively on these sectors.

Why is that?

Our success over the past fifteen years has significantly increased the size of the funds we advise. The size of the market for equity investments, on the other hand, is finite. That's why we are now also taking a targeted look at business models outside the industrial sector. We make plans for the long term: before exploring new avenues, we perform a very careful assessment and establish a network of professionals with experience in the sector concerned.

So this isn't a new development?

No, not at all. The eleven investments made by DBAG Fund V all came from our traditional core sectors. In DBAG Fund VI, this now only applies to seven out of eleven investments. One of the "new business models" was Schülerhilfe, a company that we acquired in 2013: after a holding period of just under four years, we sold the tuition company, in an exceptionally successful transaction. And DBAG ECF has invested outside of our core sectors in five out of the six most recent transactions.



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THE DBAG BUSINESS MODEL



And now you're adding digital business models to the portfolio?

Recently, we have been witnessing an increasing number of companies with digital business models on our market, operating in areas such as software, IT services and also e-commerce. These companies have often been sold at high prices. They also, however, offer considerable growth opportunities, for example due to the digitalisation of traditional business models or the trend towards companies shifting their own server and data centre capacities to the cloud. These companies can no longer be classed as start-ups. We have identified IT services and software as particularly attractive sub-segments.

duagon is a good example of how traditional business models are being digitalised: the company intends to use a major corporate acquisition to create a leading provider of solutions for data processing and communication in railway vehicles – digital solutions for products of the Old Economy.

DBAG has also had a stake in the fibre-optic sector for a number of years now. What sort of prospects do you expect to see in this sector?

In order to achieve digitalisation across the board, the right infrastructure is an absolute must. We first invested in high-speed Internet infrastructure providers more than five years

ago. With the help of additional equity provided by us as real growth capital, these companies can make rapid investments in expansion so as to establish themselves on key markets. We have expanded our network in this sector, giving us access to further investment opportunities and resulting in us structuring three further MBOs since 2017.

What about investments in non-German-speaking countries?

While we are also open to attractive investment opportunities outside of the German-speaking world, this only applies to companies in our core sectors. This gives us an opportunity to make even broader use of the excellent understanding that our investment team has of the business models in our core sectors.

Much more return-seeking capital has been flowing into the private equity sector lately. Are there any transactions available at attractive prices at all these days?

It all depends on how you define “attractive”. There is no doubt that prices have risen in recent years – as have share prices. Our market has also matured.

We therefore concentrate on understanding as early as possible where a company’s development potential lies, and what can be done to tap into it. That’s what “attractive” means for us.



»The achievements of entrepreneurs and employees in mid-market companies are something that really inspires us.«

The same answer that any of your competitors would give ...

We have organised our team and our business processes to reflect this. This is why Deutsche Beteiligungs AG has been the most active private equity company in the German mid-market sector over the last ten years. We structured an impressive seven buyouts in 2017/2018. In five of these transactions, our partners were the company founders. DBAG obviously has something that other private equity companies don't.

What do you mean by that?

The achievements of entrepreneurs and employees in mid-market companies are something that really inspires us. In the past financial year, much of our business has involved interacting with company founders. Each one of them has a different personality. But they all have one objective in common: they want the new shareholder to develop "their" company in the best way possible and at the same time at least preserve what the founder has achieved to date. I think that we can often score points with our understanding of the business model concerned, since we get competent experts who are either working in the relevant sector themselves, or have gained management experience there, on board early on. This helps us to quickly get to grips with complex matters and to come across as a competent partner.

How do you then go about tapping into a company's development potential?

We can look back on numerous examples of healthy and successful development within our portfolio companies. These success stories are visible to the market thanks to the transparency that we offer ourselves as a listed company, which creates trust. Entrepreneurs can see how we define partnership and put it into practice.

What does that mean specifically?

As soon as we are even in the process of analysing a new investment opportunity, we start preparing for the establishment of our corporate governance system at the potential portfolio company. We seek out experienced entrepreneurial personalities to help us achieve this. They then support the management team of the portfolio companies, who have full responsibility for the operating business, on advisory councils/supervisory boards and act as their strategic sparring partners.

Private equity on the stock market is rather unusual – DBAG invests using funds from its balance sheet; the greater part of the funds comes from closed-end private equity funds. Why does DBAG need the funds?

They increase our capital base. Without the funds, we would not be able to achieve such a broadly diversified portfolio with what are now 27 investments. None of these investments account for more than six percent of our equity. This ensures broad risk diversification for our company and its shareholders.

We use DBAG ECF to invest in smaller companies, often companies that are experiencing strong growth. DBAG Fund VII is a private equity fund in the conventional sense, with a fund volume of one billion euros – the largest ever initiated by a German private equity company. The investors in our funds, who are predominantly international investors, come to us because we give them better access to the German mid-market segment that they would get by buying shares on the stock market.

And the investors clearly seem to keep coming back ...

Around 90 percent of the funds for DBAG ECF II come from existing investors. The proportion of funds supplied by investors who are, or have been, invested in two or more DBAG funds is almost just as high. Success is a good argument. On average, we have generated more than 2.5 times the original capital invested. This lays the foundation for growth: we currently have assets under management and advisement totalling around 1.8 billion euros; ten years ago, this figure was half the size.

What is more, the funds pay us to find investment opportunities that will support companies in their development, and then to organise the disposal later down the line. This creates a steady stream of income that is easy to plan. This income covers DBAG's costs and also ensures a regular surplus – this increases the appeal of our shares.

When is the next fund coming?

That depends on a number of factors. The degree of investment is, of course, a key aspect. When a fund is more than 50 per cent invested, that's normally when you start thinking about a successor fund.

The closed-end funds have a term of ten years, meaning that your investments are made for a limited period of time. Doesn't that work to your disadvantage when negotiating with entrepreneurs?

It's true that situations sometimes arise in which someone who is currently the owner of a company is seeking a long-term partner. We can offer DBAG ECF, which embarks on a new ten-year term every two years, in situations like these. This allows us to offer an investment term of eight years or more.

Our balance sheet isn't aware of any such limits. Equity investments made exclusively from DBAG's balance sheet would be one way of broadening the scope of our investments. But co-investing alongside a closed-end private equity fund is and remains the core element of our offering.

In 2016, you raised additional equity from your shareholders. How has DBAG developed since then?

At the time, DBAG had a net asset value of just under 390 million euros. Although we have since distributed almost 40 million euros to our shareholders, the net asset value has risen to more than 475 million euros, an increase of one third in two years all in all. We set the course for growth back in 2016 and went on to structure twelve MBOs in 2017 and 2018. Since the capital increase, the investment team has made investments accounting for a volume of more than 650 million euros. The DBAG balance sheet accounts for 150 million euros of this amount – significantly more than in the past.

Our current portfolio is young: more than half of our acquisition costs relate to investments made over the last two years. This is another high value in a historical comparison. These investments will form the basis for a further increase in DBAG's portfolio value and, as a result, in the value of the Company itself.

What are the next steps?

First of all, these figures clearly show that we have delivered on our growth promise. We have also benefited from favourable overall conditions in the process. In addition, our Company has undergone extensive internal development. Our processes are even more efficient and our decision-making processes are even quicker. We have worked hard on our market presence.

So, all in all, this creates a positive environment for ongoing investment and, as a result, for increases in value and further growth. The overall conditions, however, have deteriorated in general lately. This could hinder both our investment progress and the financial performance of our portfolio companies.

We currently expect the net asset value to increase by an average of around 10 percent in this financial year and in the next two financial years – with distributions that are at least on a par with the current amount.

THE DBAG INVESTMENT STRATEGY

MARKET SEGMENT

We invest in mid-market companies that generate revenues of between 20 million and 500 million euros a year. There are almost 9,000 companies in this category in Germany.

INVESTMENT SIZE

Depending on the transaction, we invest between ten million and 200 million euros in equity with our funds. This allows us to cover a significant part of the German M&A market that is accessible for private equity investments.

INVESTMENT APPROACH

We focus on companies that have dynamic management teams, enjoy a strong market position and offer development potential.

SECTORS

We are primarily interested in industrial business models. We can find such models in our core sectors and in selected other sectors.

REGIONS

We concentrate on the German-speaking world. We also invest in well-positioned mid-market companies beyond Germany's borders if they come from our core sectors.