EDISON Scale research report - Update

Deutsche Grundstücksauktionen

Lots to admire

Continued buoyancy in H217 has delivered another successful year for Deutsche Grundstücksauktionen (DGA). 2017 saw a double-digit increase in gross turnover comfortably exceed management expectations, while a 7% rise in an already generous dividend would have been significantly greater but for unusually high commission reversals on historic transactions. Positive prospects reflect sustained favourable macro factors and a record start to 2018 thanks to a bumper €15m Berlin auction lot and likely associated payout (surplus cash – DGA has no debt – allows profit to be distributed almost entirely by way of dividend).

H217 maintains high tempo

While not repeating the step-change in financials of H1, DGA's second half performance was nonetheless creditable, matching year-on-year gross turnover from autumn and winter auctions. Indeed, net commission rate almost held steady despite the change in mix of lots sold (average sales price up 10%, including the most valuable item then to date at €7m). Net profit was however a casualty (down by a third), albeit exceptionally depressed by the reversal of €0.3m net commission on several historic auction transactions. Also, major subsidiary, Westdeutsche, faced an outstanding comparative. The group lot selling quota fell again owing to concessions on minimum bids to secure orders but was still high at c 86%.

Set fair

Management has once again affirmed positive fundamentals for the business, notably interest rates, disposable income and employment. To that we should add demographic advantages such as supply shortages, a rising population and increasing homeownership rates. While early in the period, management's 2018 goal of reaching last year's gross turnover appears undemanding, given 40% higher gross turnover in Q1 and encouraging signs from imminent summer auctions. Consensus estimates (below) are more ambitious but justifiably regard the €15m Berlin area sale, which singly accounted for the Q1 boost, as exceptional, hence the return to more normal growth expectations in 2019.

Valuation: Bumper payout on the cards

Newly-received Federal government approval of that Q118 transaction improves the prospects of a substantially higher 2018 dividend, given DGA's policy of full profit distribution. A prospective yield of 7% (5% on more normalised 2019 earnings) is materially ahead of that of the small cap market (no direct listed peer).

Consensus estimates

Year end	Net commission (€m)	Net profit (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/16	10.6	1.17	0.73	0.72	23.8	4.1
12/17	11.2	1.22	0.76	0.77	22.9	4.4
12/18e	12.3	2.07	1.29	1.30	13.5	7.5
12/19e	11.5	1.54	0.96	0.95	18.1	5.5

Source: Company accounts, consensus estimates

Real estate

6 June 2018

Price	**€17.40**
Market cap	**€28m**

Share price graph

Share details

Code	DGR
Listing	Deutsche Börse Scale
Shares in issue	1.6m
Net cash (€m) at December 2017	3.3

Business description

Deutsche Grundstücksauktionen is market leader in the auctioning of properties in Germany. The company was founded in Berlin in 1984.

Bull

- Sustained demand for property thanks to favourable economic and interest rate outlook.
- Clear market leader with experienced management and wide client base.
- Sound finances, allowing generous, unbroken dividend record.

Bear

- Macroeconomic uncertainties; rising interest rates would diminish yield appeal of property.
- Intensely competitive.
- Potential supply shortage as a result of excess demand and unrealistic seller expectations.

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Edison profile page

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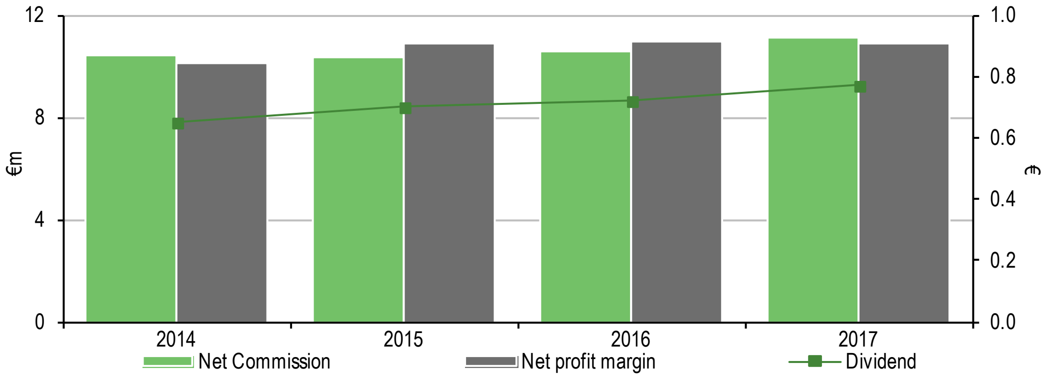
Review of 2017 results

Exhibit 1: Revenue, margin and dividend progression



Source: Edison Investment Research

The financial statements are in accordance with HGB. DGA, the parent company, is influenced to a considerable extent by the results of its fully owned subsidiaries but it is not obliged to present consolidated accounts and management reports. As a result of profit transfer agreements with its five subsidiaries, the total result of the group is therefore shown in the statements of the parent company.

Consequently, for the sake of clarity we show (shaded below) both gross turnover (auction sale proceeds) and net commission at the group level, as these drive the transferred profits. They are also regarded by management as key indicators. However, they are, of course, only proxies for the subsidiaries' revenue, which is not disclosed, so accurate top-line analysis is not possible.

Exhibit 2: Analysis of revenue and profit

Year end December (€m), HGB	H116	H216	FY16	H117	H217	FY17
Group:						
Turnover from auction sales	40.80	59.48	100.28	57.10	59.50	116.60
Change (%)	-9%	-1%	-5%	+40%	Flat	+16%
Net commission	4.64	5.95	10.59	5.49	5.67	11.16
Rate (%)	11.4%	10.0%	10.6%	9.6%	9.5%	9.6%
Change (%)	Flat	+5%	+2%	+18%	-5%	+5%
Revenue + other operating income	1.88	2.28	4.16	2.39	2.35	4.74
EBITDA	0.31	1.51	1.82	0.90	1.04	1.94
Parent company profit	(0.18)	0.24	0.06	(0.11)	0.20	0.09
Profit from subsidiaries	0.45	1.25	1.70	0.94	0.76	1.70
Pre-tax profit	0.27	1.49	1.76	0.83	0.98	1.81
Net profit	0.17	1.00	1.17	0.56	0.66	1.22

Source: DGA accounts

By any measure 2017 was a success for DGA. A sharp pickup (16%) in gross turnover after two years of consolidation, albeit at a high level (c €100m), drove further steady improvement in net commission and dividend, as shown in Exhibit 1.

However, it was a year of two halves as the exuberance of H1, termed "outstanding" by management ie gross turnover up 40% and a trebling of net profit, was reversed in the second half by top-line consolidation and net profit down by a third.

Given our H1 results review, we focus here on the second half performance. Notwithstanding the volatility of quarterly auctions (14% decline in Q3 gross turnover was fully recouped in subsequent winter auctions), total sale proceeds were maintained at the high level of the two previous second halves. Individual auction house businesses are inevitably volatile but they tend to compensate for each other; the subsidiaries' composite reduction of 8% in H2 was wholly offset by the parent company's c 20% higher outturn, driven by its €7m Berlin area lot sale in Q4, then a record for the group.

Second half net commission (effectively revenue in terms of company accounts) was down slightly (by 5%). This reflected the mix of lots sold (average sales price up 10% at €64,000) and consequently rates, which were lower and indeed potentially negotiable. Exhibit 2 shows also that the overall rate of 9.5% was on a par with that of H1.

In view of this relative buoyancy the blow to profit, as reported, is striking but can be attributed largely to €0.3m one-off costs relating to the reversal of net commission on auction transactions dating back over a decade (the main culprit was a €0.2m failed contract from 2014). Commission reversals are customary for DGA but the scale is not (NB: only €41k in 2016 and €79k in 2015, so the 2017 impact may reasonably be viewed as exceptional). Notionally adding back those costs, we may infer additional net profit of €0.2m and €0.12 boost to dividend, assuming full payout.

Strong momentum

Management guidance for 2018 remains understandably upbeat after record auction sale proceeds and net commission in Q1 and indications of the volume of deliveries for the summer auctions later this month. Not only was first quarter gross turnover up 40% at €37m but encouragingly there was little sacrifice in net commission (up 35% at €3.3m). This is all the more impressive as it included a new record lot sale of €15m, presumably at a lower than average commission rate. Apart from the immediate financial boost, the transaction brings DGA excellent publicity in terms of using the auction channel for such substantial items and as a reference sale in the valuable Berlin market. Consensus forecasts assume this transaction to be exceptional, hence the lower outturn in 2019, but DGA has a good relationship with the Federal Bundesanstalt (sales up strongly in 2017), so the offer of further high-value lots is not wishful thinking, in our view.

Balance sheet and cash flow

Finances remain sound with €3.3m net cash at December 2017. Surplus cash (the company has no debt) allows profit to be distributed almost entirely by way of dividend. Management is justifiably proud of its dividend record and well aware of investor demand for attractive dividend yield at a time of low interest rates.

Valuation

With no direct peer listed on the Frankfurt Stock Exchange, we look at the iShares MSCI Germany Small-Cap ETF, which seeks to track the investment results of an index composed of small-cap German equities. This shows a historical P/E ratio of 14.9x (DGA 23x) and 12-month trailing yield of 1.1% (DGA 4.4%). As noted above, the history of a sustained and attractive dividend should lend support to the shares.

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