

## German Startups Group

### Further buybacks likely

Following the successful disposal of Exozet in December 2019 as well as a few exits from its VC portfolio last year, German Startups Group (GSG) held a high net cash position of c €6.8m at end-2019. As the company's shares continue to trade at a wide discount to last reported NAV (currently at c 43%) and GSG continues its transition to an asset manager (largely focusing on realisations within its existing VC portfolio), management intends to utilise the liquidity for further share buybacks.

### Gain on Exozet disposal of €6.2m

GSG closed FY19 with an EPS of €0.26 (vs a €0.05 loss per share in FY18) on the back of the completed disposal of its 50.77% stake in digital agency Exozet. Excluding the gain on Exozet disposal, the net loss from the revaluation of financial assets amounted to €1.2m (vs €3.4m profit in FY18), mostly on the back of a full write-off of three holdings, partially offset by the write-up of five of its 12 major portfolio investments.

### A comfortable level of liquidity

GSG has greatly reduced its financial liabilities as a consequence of 1) Exozet's deconsolidation, 2) early repayment of €2.0m loans last year and 3) early redemption of half of its 2018 convertible bonds in April 2020. At end-2019, its net cash position stood at c €6.8m or €8.2m including purchase price receivables. In the latter approach, its gross liquidity of €11.3m represented 33% of its total assets (or €0.95 per share). Rather than being reinvested in the VC portfolio, it is likely to be utilised for share repurchases (the company already holds 9.4% of its outstanding shares in treasury).

### Valuation: Wide discount despite high cash position

GSG's current share price of €1.57 represents a c 43% discount to NAV at end-2019 (based on the book value of equity ex-minorities according to our estimates). While revaluation of minority holdings often occurs upon transactions (new funding rounds or secondary deals in particular), three of GSG's investments (making up c 52% of its VC portfolio's gross value) were valued using a peer method or blended DCF and peer method. If the last transaction values had been used (considered outdated for these three), the valuation of the whole portfolio would be 27% lower.

#### Historical financials

| Year end | Revenue (€m) | PBT (€m) | EPS (€) | DPS (€) | P/E (x) | Yield (%) |
|----------|--------------|----------|---------|---------|---------|-----------|
| 12/16    | 10.9         | (5.4)    | (0.29)  | 0.0     | N/A     | N/A       |
| 12/17    | 9.6          | 1.8      | 0.14    | 0.0     | 11.6    | N/A       |
| 12/18    | 12.5         | 1.2      | (0.05)  | 0.0     | N/A     | N/A       |
| 12/19    | 16.4         | 3.7      | 0.26    | 0.0     | 6.0     | N/A       |

Source: German Startups Group

#### Financials

29 June 2020

|            |       |
|------------|-------|
| Price      | €1.57 |
| Market cap | €19m  |

#### Share price graph



#### Share details

|   |                      |
|---|----------------------|
| Code                                    | GSG                  |
| Listing                                 | Deutsche Börse Scale |
| Shares in issue (incl. treasury shares) | 12.0m                |
| Last reported net cash at end-2019      | €6.8m                |

#### Business description

German Startups Group is a Berlin-based venture capital investment company primarily focused on providing investment to technology businesses in German-speaking countries. With the launch of its secondary shares trading platform and setup of an asset management subsidiary, the company started the transition to a wider business model.

#### Bull

- Potential success of new business model may result in narrowing/closing the valuation gap to NAV and realising additional shareholder value.
- Listed exposure to a diversified portfolio of technology start-ups in Germany.
- Successful sale of Exozet translated into significant cash proceeds, which may be used for share buybacks.

#### Bear

- Low liquidity.
- VC investments are inherently high risk.
- Longer periods when start-ups remain private may delay GSG's exits.

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## Profitable disposal of Exozet driving results

GSG reported a net profit of €3.4m in FY19 vs a €0.7m loss in FY18, primarily driven by the €6.2m gain from the disposal of its 50.77% stake in digital agency Exozet, announced in December 2019 (and discussed in more detail in our [previous update note](#) dated 19 December 2019). The net proceeds from the transaction amounted to €10.8m (or c €1.00 per GSG share). Excluding minority interests related to Exozet, GSG's net profit stood at €2.9m (€0.26 per share) in FY19 vs a €0.6m loss (€0.05 per share) in FY18. Group revenue stood at €16.4m in FY19 (up 31.2% y-o-y) but this was largely attributable to Exozet (€16.0m), which was deconsolidated upon its sale in late FY19. The remaining revenue was mostly related to costs recharged to GSG's general partner.

At the same time, GSG reported a net loss per share from continued operations (ie excluding Exozet's earnings in FY19 and gain on its disposal) of €0.32 compared to a loss of €0.04 in FY18. However, we need to note that the sale of the stake in Exozet could be considered a regular part of GSG's operations as an investment company. The transaction resulted in a €6.2m gain on disposal at the PBT level and supported GSG's overall EPS of €0.26. The company's net loss from the revaluation of financial assets of €1.2m (compared to a €3.4m net gain in FY18) was largely due to the full write-off of three portfolio companies, including Ceritech, which failed to execute its flagship project. The other two companies were not named in the company's annual report. One was written down due to persistent weak business performance, while the other was subject to an emergency sale at a low price. These three holdings represented around 82% of the overall loss from financial investments of €7.8m (comprising €6.98m losses from financial assets and €0.87m losses from sale of financial assets) in FY19. On the other hand, the company has recognised an upward revaluation in five out of its 12 main investments. These 12 holdings made up 92% of the value of its portfolio consisting of 30 holdings in total at end-2019.

### Exhibit 1: GSG FY19 results highlights (total operations)

| €000, unless otherwise stated   | FY19         | FY18          |
|---|--------------|---------------|
| Profits from financial assets valued at fair value with recognition in profit or loss | 5,768        | 6,764         |
| Losses from financial assets valued at fair value with recognition in profit or loss  | (6,975)      | (3,346)       |
| Profits from affiliated companies   | 0            | 75            |
| Losses from sale of financial assets  | (871)        | (226)         |
| Gain from disposal of Exozet  | 6,173        | 0             |
| <b>Result from investment business</b>  | <b>4,095</b> | <b>3,266</b>  |
| Revenues  | 16,447       | 12,534        |
| Change in inventories   | (1)          | 114           |
| Income from own work capitalized  | 347          | 470           |
| Other operating income  | 1,123        | 476           |
| Cost of materials and services received   | (4,304)      | (3,356)       |
| Personnel expenses  | (9,674)      | (7,722)       |
| Other operating expenses  | (3,183)      | (3,347)       |
| Incidental acquisition costs of investments   | (9)          | (99)          |
| Result from other components  | 95           | (1,547)       |
| <b>EBITDA</b>   | <b>4,840</b> | <b>2,336</b>  |
| Depreciation and amortization   | (651)        | (616)         |
| <b>EBIT</b>   | <b>4,190</b> | <b>1,720</b>  |
| Interest income   | 46           | 52            |
| Interest expense  | (575)        | (523)         |
| <b>Financial result</b>   | <b>(529)</b> | <b>(471)</b>  |
| <b>Pre-tax profit</b>   | <b>3,661</b> | <b>1,249</b>  |
| Income taxes  | (236)        | (1,925)       |
| Net profit  | 3,425        | (676)         |
| Minorities adjustment   | (487)        | 82            |
| <b>Net profit (ex-minorities)</b>   | <b>2,938</b> | <b>(593)</b>  |
| <b>EPS (€)</b>  | <b>0.26</b>  | <b>(0.05)</b> |

Source: German Startups Group accounts

GSG's new investment activity was limited in FY19 (cash outflow purchase of financial assets at just €0.8m in FY19) and consisted only of German Crypto Tech (where it acquired a 10% stake), an asset-backed tokenisation business GSG co-founded during the period, as well as a follow-on

investment in AuctionTech. Apart from the Exozet disposal, the company performed five full and partial exits in FY19 and reported a total cash inflow from the sale of financial assets in continued operations (ie excluding Exozet) of €5.2m. This includes two focus investments (Chrono24 and Mister Spex), which translated into sizeable disposal gains (according to the management), as well as several smaller disposals, such as Dalia Research, Datapine and Service Partner One.

GSG's net seller position is in line with its ongoing repositioning from an asset owner (focused on growing the value of its own balance sheet investments) to an asset manager (generating income from management fees and carried interest). This strategy is executed in particular through its subsidiaries German Startups Market, an online matchmaking platform for sellers and buyers of so-called secondary shares in German start-ups and VC funds, as well as German Startups Asset Management, see [our note from October 2018](#) for further details. Hence, GSG continues to prioritise profitable realisations of its VC investments, while making efforts to drive its asset management business beyond the early stage. As part of the realignment, the company has recently transferred its VC portfolio to a fully owned subsidiary. GSG has provided a limited update on the transition progress at this stage.

With respect to COVID-19, management has provided a general comment indicating that the impact was limited across its portfolio holdings, although its share price has followed the market decline, and has fallen 30%. Meanwhile two of its exits that were initially planned for early 2020 have been postponed.

## Ample liquidity for further buybacks

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Following the deconsolidation of Exozet and early repayment of €2.0m loans, GSG's total gross debt at end-2019 stood at €3.1m and consisted of €2.9m of outstanding 2018 convertible bonds, which have a coupon rate of 8% pa, as well as c €0.2m of short-term liabilities (mostly accrued interest). At the same time, the company's cash position at end-2019 was €4.9m, and was supported by €5.0m in near-cash items (money market investments), which translates into a net cash level of €6.8m at end-2019. If we also include the €1.4m of purchase price receivables at end-2019 (which could potentially be considered a near-cash item as well), GSG's net cash would stand at €8.2m while its gross liquidity would be €11.3m (or 33% of its total assets). We note that management recently announced that the company repurchased half of its outstanding convertible bond volume in April 2020.

Consequently, as the company has repaid most of its financial liabilities over 2019 and H120 and the shares continue to trade at a significant discount to NAV, it aims to distribute the disposal proceeds through further share repurchases. Last year, GSG launched a buyback programme covering up to 900.1k shares at a price of €1.50 per share, which was successfully completed on 8 July 2019. As a result, the company currently holds 1,130.4k treasury shares (or 9.4% of all outstanding shares).

## Valuation

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GSG's NAV (ex-minorities but including goodwill and intangibles) was €30.1m at end-2019, translating into €2.77 per share (based on share count excluding treasury shares, according to our estimate). The current share price of €1.57 implies a c 43% discount to this NAV. Based on the outstanding number of shares (including treasury stock), NAV per share would be €2.51 and the discount would stand at 37%, according to our calculations. We note, however, that the current NAV and discount are at least partially out of date, given that portfolio companies are normally valued, where possible, by independent third-party transactions, which reflect prices achieved in recent transactions and follow-on investment rounds. Having said that, among its 12 most important

investments at end-2019 (covering 92% of portfolio value), three of them (representing 57% of those important investments' value) were valued using other methods (two based on peer valuation and one based on a blended DCF and peer valuation). The company considers the last transaction values of these companies to be outdated but, had they been used, the end-2019 portfolio value would have been 27% lower.

Although the current discount to NAV is significant, we believe one of the reasons behind it may be the limited transparency on the performance of the portfolio companies, as GSG cannot disclose financial information on minority-held assets. A successful transition to an asset manager and full realisation of its VC portfolio could mitigate this issue.

We should also consider the structure of the company as it operates as a partnership limited by shares (KGaA), with the partner entitled to a preferential profit payment of 25% from the amount of earnings exceeding commercial losses. The company calculates the possible profit advance (assuming all portfolio components are sold at their IFRS fair values on 31 December 2019) is €1.0m, which translates to 9c per share.

In 2018 GSG issued €3m in convertible bonds maturing on 8 March 2023 and which can be converted into 1.2m new shares at maturity with a conversion price of €2.50 per share (which is 63% above the current share price). As highlighted above, the company redeemed half of the volume in April 2020. Moreover, as the conversion price is slightly below NAV per share at end-2019, the dilution should not translate into a significant change in our estimated NAV per share at the current portfolio valuation.

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