

Scherzer & Co

Asset management
30 April 2021

FY20 results assisted by AXA and Audi

Scherzer's (PZS) NAV per share at end-March 2021 stood at €3.12, 83% higher year-on-year. This was a result of strong FY20 income, with PZS's EPS at €0.42, vs an FY19 loss of €0.08 and an FY12–19 average of €0.12, paired with a low base effect from end-March 2020 (pandemic outbreak). Meanwhile, PZS's share price somewhat lagged the recovery and the discount to NAV widened to its current 10.9%, while PZS traded at par before the crisis. Following the profitable disposal of its AXA claims, PZS's extra compensatory claims (ECS) portfolio stood at €122m at end-March 2021 (12% lower year-on-year).

FY20 EPS at €0.42

In FY20, PZS realised a €12.7m net result on closed transactions (FY19: €1.1m), driven by active trading and the conclusion of two processes: disposal of AXA claims (€5.7m income) and squeeze-out at Audi (€6.6m). The unrealised losses booked in H120 were mostly reversed on the back of the equities rally in the later part of FY20 and as a result, PZS's net income was €12.6m (FY19 loss of €2.3m). Under German reporting standards, PZS can recognise an increase in the value of equity holdings only through realisations and reversals of former write-downs. Hence, the FY20 results do not fully reflect the positive share price developments of portfolio holdings.

More ECS to come

PZS's end March ECS portfolio was €122m (FY19: €139m) as AXA claims were sold (and some minor positions were concluded) and Audi was included. PZS also holds stakes in several squeeze-out candidates that are likely to strengthen its ECS portfolio, including the three largest 2020 investments: MAN (9.7% of end-March 2021 NAV), Rocket Internet (6.4%) and Kabel Deutschland (3.9%). The ECS cases are lengthy (the AXA case started in 2006) and their outcome is highly uncertain, but they constitute an important potential NAV kicker for PZS.

Valuation: Reinstating the dividend

The strong NAV development was not fully reflected in the share price performance, with the current discount to NAV at 10.9%, while PZS traded at par before the coronavirus outbreak, which we believe stemmed from the 'hidden value' in the ECS portfolio. The recommended €0.05 DPS implies a 1.8% yield and marks PZS's first dividend distribution since the FY17 profits distribution. Consensus expects that PZS will continue paying out a dividend next year.

Consensus estimates

Year end	Revenue* (€m)	EBITDA (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/19	5.2	(2.1)	(0.08)	0.00	N/A	0.0
12/20	21.2	9.3	0.42	0.05	5.6	0.0
12/21e	6.8	4.7	0.18	0.05	15.7	1.8
12/22e	7.2	4.9	0.19	0.05	14.6	1.9

Source: Scherzer & Co, Refinitiv consensus estimates. Note: Refinitiv consensus figures are based on the estimates of one (EBITDA) to three analysts as at 29 April 2021. *Gross gains from financial instruments.

Price €2.78
Market cap €83m

Share price graph



Share details

Code	PZS GY/PZSG
Listing	Deutsche Börse Scale
Shares in issue	29.9m
Last reported net debt as at end-FY20	€15.0m

Business description

Scherzer & Co (PZS) invests its funds mainly in domestic equities. PZS looks for companies that are unknown or unloved, and special situations. Its focus is on special situations, where the downside is perceived to be limited. In addition, it acquires value stocks, mainly below book value. These stocks need to demonstrate strong business models.

Bull

- Strong management, well known in the market.
- 'Hidden' NAV driver through extra compensatory claims, albeit with binary outcomes.
- Well diversified portfolio with attractive risk/return pattern, built over a number of years.

Bear

- Dependent on market environment.
- Still relatively small.
- For the strategy, market size is limited.

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FY20 financial highlights: Sale of AXA ECS

PZS reported a €12.6m net income in FY20 compared to a €2.3m loss in FY19. Major positive contributors include the successful conclusion of the AXA case (€8.5m positive pre-tax impact, including €5.7m reflected in the trading result, described in our [earlier note](#)) and the squeeze-out at Audi (adding €6.6m to the FY20 trading result). These have driven PZS's realised net result on trading in financial instruments to €12.7m compared to €1.1m in FY19. The trading in stocks overall yielded a €7.4m profit, while derivatives trading resulted in a €0.5m loss. The unrealised loss amounted to €1.7m, as most of the H120 write-offs were reversed in H220 (H120 loss at €4.9m). We note that under German reporting standards, PZS recognises valuation gains no sooner than upon disposal (the methodology is described in detail in our [April 2020 note](#)), and consequently the Q420 equity markets rally is likely only partially reflected in PZS's results.

The company received a significantly lower amount of dividends compared to FY19, as some companies decided to keep a liquidity buffer during the pandemic. Meanwhile, strong cash inflow from disposals and the ECS portfolio allowed PZS to reduce its leverage with end-2020 net debt of €15.0m (34% lower year-on-year). The strong results allowed management to recommend a €0.05 dividend per share to the AGM to be held on 27 May 2021.

The ECS portfolio as at end-March 2021 amounted to €122m vs €139m at end-FY19. The ECS portfolio represents positions where PZS was squeezed-out by majority shareholder, and PZS attempts to prove in court that a squeeze-out was performed at a price below fair value and receives compensation if successful. The value of the ECS portfolio is presented in the initial amount of the proceeds received, and PZS does not disclose its expectations of the settlement value. The company's ECS portfolio value declined in FY20 as the sale of the AXA claims (€25.6m) was not fully offset by the addition of Audi claims (€16.9m). During the year, some smaller cases (€8.0m in total) were concluded with no increase in settlement value over the initial price.

Exhibit 1: FY20 results highlights

€000s, unless otherwise stated	FY20	FY19	y-o-y
Gains from financial instruments	21,229	5,225	306%
Losses from financial instruments	(8,528)	(4,135)	106%
Result on financial instruments	12,701	1,090	1,065%
Other operating income (excluding value adjustments)	44	65	(33%)
Personnel expenses	(794)	(690)	15%
Other operating expenses	(1,528)	(700)	118%
Income from dividends	607	1,644	(63%)
Unrealized gains (losses)	(1,706)	(3,546)	(52%)
D&A	(24)	(18)	28%
EBIT	9,299	(2,155)	N/M
Other interest and similar income	3,486	86	N/M
Interest and similar expenses	(224)	(253)	(11%)
PBT	12,561	(2,322)	N/M
Income and other taxes	15	(8)	N/M
Net profit for the period	12,576	(2,330)	N/M
EPS (€)	0.42	(0.08)	N/M

Source: Scherzer & Co accounts

Portfolio development: New squeeze-out candidates

PZS invests in companies that management believes are undervalued due to a lack of understanding by the broader market. This encompasses stocks with little to no research coverage and business models that are difficult to assess, including ongoing restructurings and M&As. It also positions itself in potential squeeze-out targets to expand its ECS portfolio. PZS's investments may

take some time to unlock their value and as a result the portfolio has low turnover, with the majority of the top 10 positions at end-March 2021 being the same as a year ago. Investments are pooled into two categories: 'safe' – companies with high asset quality and sustainable earnings (52% of portfolio at end-FY20); and 'opportunistic' – growth stocks and companies in special situations (48%).

Exhibit 2: PZS's top 10 holdings list				
Company	% of total (Mar 21)	% of total (Mar 20)	Change (pp)	Opportunistic/safe
MAN	9.7%	N/A	N/A	Safe
freenet	8.5%	5.4%	3.17	Opportunistic
GK Software	6.9%	7.7%	(0.78)	Opportunistic
Rocket Internet	6.4%	N/A	N/A	Safe
Allerthal-Werke	5.9%	5.9%	0.00	Safe
Kabel Deutschland Holding	3.9%	N/A	N/A	Safe
ZEAL Network	3.9%	4.0%	(0.03)	Opportunistic
Weleda	3.9%	5.5%	(1.57)	Safe
Lotto24	3.8%	3.7%	0.09	Safe
RM Rheiner Management	3.5%	N/A	N/A	Safe
Total top-10 holdings	56.4%	54.5%*	-	-

Source: Scherzer & Co, Edison Investment Research. Note: *Top 10 holdings as at end of March 2020.

During FY20, PZS made three significant investments that are currently in its top 10: MAN, Rocket Internet and Kabel Deutschland Holding. All three positions represent potential ECS cases as squeeze-outs have been announced or are expected. We describe **MAN** investment in detail in our [previous note](#). **Rocket Internet** is a start-up incubator for internet-based companies with a market capitalisation of c €3.6bn. It currently holds stakes in more than 200 companies and an over €1bn portfolio of listed stocks. PZS invested in the company following its announcement that it will perform a mandatory buyback of all of its shares. The shares have been delisted from the regulated market and it is likely that Rocket Internet will be added to PZS's ECS portfolio once a squeeze out takes place. Scherzer considers Rocket Internet a value investment, as the latter's shares traded below its net asset value per share. **Kabel Deutschland Holding** represents a similar case, where Vodafone holds a 94% stake in the company. Vodafone first acquired a majority position back in 2013 and since then fully integrated the company into its structures. Vodafone attempted to acquire 100% of the company shares but entered into a legal dispute with three minority shareholders (17.1% in total) that was concluded in December 2020. This was followed by a squeeze-out announcement at a price agreed with the aforementioned minority shareholders. The shares have been delisted from the regulated market in 2016 and since then are traded solely on an OTC market.

Valuation

PZS's net asset value (NAV) per share stood at €3.12 at end-March 2021, translating into an 83% one-year total return. However, this comes from a low base in March 2020 when PZS's NAV was at a multi-year low due to the broad market sell-off caused by the coronavirus outbreak. Having said that, PZS's return since end-2019 is still a solid 36%. The performance is visibly ahead of the DAX, MDAX and SDAX indices, which delivered 51–67% y-o-y returns to end-March 2021 and 12–13% since end-2019.

PZS shares delivered a 90% return over the last year, as the discount to NAV narrowed from 16% in March 2020 (previously seen back in 2016) to 12.8% at end-March 2021 (10.9% currently). Nevertheless, we note that its shares on average traded close to par in 2017–19. It is possible that previously the market had already discounted the conclusion of the AXA case (20% of PZS's ECS portfolio at that time). Yet we would note that at present there are a number of ongoing litigations and the ECS portfolio value at end-March 2021 is only 12% lower than at end-FY19.

Exhibit 3: Comparable market P/E ratios (x)

	2016	2017	2018	2019	2020	2021e	2022e
DAX	19.0	14.6	12.9	22.7	42.8	16.2	14.4
MDAX	28.8	17.6	13.4	26.1	23.8	31.3	21.0
SDAX	23.5	23.4	13.8	32.1	76.6	21.1	16.4
Arithmetic average	23.8	18.5	13.4	27.0	47.7	22.9	17.3
PZS	13.6	10.0	loss	loss	5.6	15.7	14.6
PZS discount	43%	46%	N/A	N/A	88%	31%	15%

Source: Refinitiv as at 27 April 2021, PZS reports. Note: PZS forecast is Refinitiv consensus based on three analysts. P/E ratios based on year-end prices, forward ratios based on current prices.

PZS trades at a discount to German equity indices based on the P/E ratio in both 2021e and 2022e, though the discount is lower than in previous years. Based on the P/BV ratio, PZS's discount to the market narrowed between 2015 (60%) and 2018 (13%). However, the recent widening of its discount to NAV described above has led to a 37% discount to market based on 2021e Refinitiv consensus estimates. That said, we note PZS is not extensively covered by the sell-side as for example the book value per share consensus estimate is derived from the forecast of a single analyst only.

Exhibit 4: Comparable market P/BV ratios (x)

	2016	2017	2018	2019	2020	2021e	2022e
DAX	1.7	1.9	1.4	1.6	1.8	1.8	1.7
MDAX	1.9	2.1	1.6	2.1	2.3	2.2	2.1
SDAX	1.7	1.8	1.6	1.5	1.6	1.6	1.5
Arithmetic average	1.8	1.9	1.5	1.7	1.9	1.9	1.7
PZS	0.9	1.3	1.3	1.3	1.0	1.2	1.1
PZS discount	49%	32%	14%	24%	48%	37%	36%

Source: Refinitiv as at 27 April 2021, PZS reports. Note: PZS forecast is Refinitiv consensus based on one analyst. Historical P/BV ratios based on year-end prices, forward ratios based on current prices.

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