

DNICK plc

The share price is caught up in the stock market woes, but fundamentally the investment is as cheap as it has ever been

- Little-noticed press release from late December confirms 2008 projections
- Projections for 2009 are likely to come out better than the market currently expects
- The bid play has (for the time being) turned into a dividend play

This debt-free *Mittelstand* cash machine should turn into a dividend spinner while we wait for a lucrative bid

Dear Reader,

It pays to read up on every piece of information that you can get hold of about a company. At Undervalued-Shares.com, one of my tasks is to sift through the web and make sure that I get hold of anything and everything that is published about the companies that I report on.

The kind of official announcements that listed companies need to make, are the easiest to get hold of. They can be downloaded from just about any database offering stock market data. There is also a central place where to find them.

Another important, but more difficult to access source of information, is local newspapers. They often have information that they gathered, well, locally! Sometimes, there are developments that a listed company doesn't need to announce officially, but which are nonetheless of great interest for analysts and investors.

Such was the case, with a recent article in *Ruhrnachrichten*, a local newspaper published in the region where one of DNICK's important subsidiaries is located.

The journalists had noticed that something was going on at the company, and they even took a bunch of telling photos.

The Indian joint venture is progressing as planned

As I had written in my original 21st August 2008 report about DNICK, the company's management has been able to barter a set of old industrial machinery for a 33% stake in an Indian joint venture company. Together with Arcelor-Mittal (the world's largest steel manufacturer) and Shivalik Bimetalls (a privately held Indian company, that since 1986 has been providing solutions surrounding clad metals and similar products), the joint venture will start producing this year in India.

Ruhrnachrichten reported, that the entire machinery was de-installed and put into 27 sea containers (and they shot a few photos of the entire packing and loading affair). In other words, the plan to establish the joint venture seems to be going ahead as planned. It can now start producing in mid 2009, and 2010 will be the first year of full production. The new subsidiary is likely to add to earnings from 2010 onwards, and given that DNICK recycled a few old machines and put in very little actual cash, it should be a profitable stake indeed.

The much more important question, however, is how those divisions of DNICK that are already operating have been performing recently.

Judging from the share price, the market seems to see a considerable risk of the core business' figures not living up to expectations. Or why else should the share price have fallen from EUR9 in September 2008 to currently EUR6?

Here is a quick overview and update, to assess the situation.

Ruhr Nachrichten.de
Donnerstag, 15. Januar 2009

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Umzug: Deutsche Nickel schickt Walzwerk nach Indien

am 23. Dezember 2008 15:54 Uhr

HOLZEN Zu einer weiten Reise ist ein Kaltplattierwalzwerk der Deutschen Nickel angetreten. Es wurde nach Indien verschickt. In früheren Jahren hatte es in Schwerte seinen Dienst getan, um das Vormaterial für die kupferplattierten Pfennige und messingplattierten Zehn-Pfennig-Stücke zu walzen. Seit einigen Jahren stand es jedoch ungenutzt herum.



Nun ist es abgebaut und in 27 Container verpackt auf die Reise nach Indore in Indien geschickt worden.

Hier ist ein Gemeinschaftsunternehmen von der Dnick, ArcelorMittal und Shivalik gegründet worden, um den indischen, aber auch den amerikanischen Markt mit plattierten Bändern zu versorgen. Die Deutsche Nickel konnte somit ihre Aktivitäten weiter ausbauen.

Die gesamten Demontearbeiten sind fachgerecht von der 2007 gegründeten Schwerter Firma Technische Dienste Trompeter ausgeführt worden. Sie stellt auch den Wiederaufbau mit Schwerter Mitarbeitern in Indien sicher. Mit Stolz über die erbrachte Leistung standen die Unternehmer noch vor wenigen Tagen vor dem letzten "dicken Brocken" des Kaltplattierwalzwerks, einer 17 Tonnen schweren Bürstmaschine.

Stück für Stück wurde ein Kaltplattierwalzwerk der Deutschen Nickel abgebaut und nach Indore in Indien transportiert.
Foto: privat

The *Ruhrnachrichten* article dating 23 December 2008.

The 2008 earnings are in the bag

Seldom has it been that easy to make a judgement, on whether a company would reach the projections that I had set out for it.

On December 18th, DNICK published a little-noticed press release. The press release didn't enter the usual stock market databases, and instead was only intended to inform the business-press about a few changes at one of the subsidiaries.

However, it contained a paragraph stating that DNICK's management expects the central holding company's performance for 2008 to come out as expected. Nota bene, this was issued just 12 days before the year ended. And it confirmed the guidance that the management had provided in mid 2008. It also confirms the calculations in my original 28-page report and the 7th September 2008 update (both still available on my website).

Separately, I found out that DNICK's two key subsidiaries had been working between Christmas and New Year's Eve. It seems that the company – up to this point – hasn't been short of orders from its clients.

With projected earnings per share of about EUR1.40 for 2008 and projected EBITDA of EUR16m, the share is currently valued at a price/earnings ratio of 4.3 and an EV/EBITDA ratio of 3.5. In other word, the share is as cheap as they come.

The key question is, does the outlook hold up for 2009 – and what is the shareholders' perspective for seeing either a rise in share price or at least a substantial dividend (or both)?

Here is what I project for 2009

DNICK will provide its official guidance for 2009 when it publishes its 2008 figures. This will happen sometimes during Spring 2009, probably in March or April.

Up until that point, we need to draw conclusions from what we already know. At this stage, a number of positive and negative factors come into play.

Negative:

- The world economy is tanking, and with it the demand for certain goods will decrease. Some of these goods contain nickel alloys.

Positive:

- The recession also led to the price for nickel decreasing from \$54,000/ton in Spring 2007 to now \$10,450/ton (and a Autumn 2008 low of \$8,000/ton). The nickel used in DNICK's product is always separately paid-for by the company's clients, using the nickel price of the day the order was fixed. Put another way, DNICK does not carry any risk from the nickel price going up or down. However, because the company needs to pre-finance nickel purchases that it carries out on behalf of its clients, a lower nickel price leads to DNICK being able to reduce the interest costs on its working capital (the company has no long-term debt, but uses short-term arrangements to finance the nickel orders that it has to place once a client order is received).
- Every year, new applications for using nickel alloys are found (see page 25 of the original report). Even if demand from some areas that DNICK delivers nickel alloys to, were to fall, the widening use of nickel alloys might compensate for it.
- The latest available information was that DNICK's order books are full up until about March 2009 (and no change in orders had been detected yet). This is most likely also due to the fact that a considerable part of the group's business comes from areas that are relatively immune to the overall economy, such as producing materials and parts needed for producing coins and for building nuclear plants.

Is it possible, at this stage, to turn these rather broad statements into some more specific figures?

Some of this can indeed already be put into relatively specific figures. E.g., the recent decrease of the nickel price (70% compared to its record high, although the record high was only reached for a brief time) is

leading to savings in financing costs of about EUR0.7m on an annualized basis. This would translate into a positive earnings effect of EUR0.10 per share. It is quite a considerable effect.

Other factors are harder to gauge. E.g., the company also has to pay costs for energy, staff and transport. Generally, some of these costs actually should have decreased, thanks to the overall economic situation – especially, of course, energy costs.

All in all, it seems likely that for 2009, DNICK's management will provide guidance pointing to the earnings and the cashflow coming out at least on the same level as 2008. There does not currently appear to be a reason for any major downward revision. And if I were to throw caution overboard for a few seconds, I'd say that thanks to the effects of the last phase of the company's restructuring, there is even potential for DNICK surprising us on the positive side. However, given the overall situation, the management might also simply choose to be extremely cautious in its statements and predict flat earnings, only to then hopefully surprise shareholders in early 2010.

The fundamentals are extremely attractive for those who can sit out the current market panic

On the basis of zero earnings growth and cashflow growth in 2009, DNICK shares are still valued on an extremely low p/e of 4.3 and EV/EBITDA of 3.5.

And it is here, that a similar situation to that of Billing Services Group evolves – see my report of just a few days ago to read up more.

Just as in the case of BSG, I had expected DNICK to be put up for sale, or to potentially even receive an unsolicited bid. The company's major shareholders are, without exception, financial investors; the current management team's mission is to not just to restructure the company, but also to sell it one day (not the least as it's the only way for them to exit their stake). Furthermore, DNICK is such a gem of a *Mittelstand* company with a leading market position, that it's more likely than not that an industrial company from a similar area would be interested in snapping it up.

With the state that the capital markets (including the private equity industry) and the general economy are in, arranging such a deal has become much more difficult. This is the major revision of my initial report, where I had predicted a deal for Spring 2009. I can't rule out that something along that line is already being prepared and negotiated behind closed doors - but at the moment, I don't have any specific information about such a development being imminent.

So if my guess (from my original report last year) that the company will be sold during the next few months turns out to be wrong, what's the effect this will have on our investment?



Luckily, as in the case of BSG, there is an alternative route for all this to play out – and the current share price could well be an opportunity to buy more, at an attractive price.

Read on to see why DNICK is an investment with a safety net.

Dividends galore

The release of the 2008 figures will also show, that DNICK is now back in a position to pay out a dividend. What's more, the management has already promised to put a dividend for 2008 onto the agenda.

How much will be paid out, and when?

Share price:	€6
Book Value:	€11.50 (end of 2008)
Est. earnings 2008:	€1.40
Est. earnings 2009:	€1.40 (or higher)
P/E 2008:	4.3
P/E 2009:	4.3
EV/EBITDA 2008:	3.5
EV/EBITDA 2009:	3.5

Previously, the management's position was that they would not bother with too small a dividend. The company's official position has so far been, that a dividend for 2008 will not come out lower than EUR0.50 per share. At a share price of EUR6, this would give the investment an 8.3% yield.

Will DNICK stick to its earlier statement?

Given that 2008 earnings are likely to come out at around EUR1.40, a EUR0.50 dividend is equivalent to a mere 35% payout ratio. It wouldn't take the company much effort to part from a EUR0.50 dividend payment. A 50% payout ratio would be EUR0.70 per share (giving it a 11.6% yield). Besides that, the management holds quite a substantial stake itself and therefore has its interests aligned with those of the shareholders. The key financial investors behind DNICK are also likely to be interested in as high a payout as is possible. So quite possibly, it might even be higher than EUR0.50 per share.

When will we know?

Last year, DNICK released its preliminary figures on 31st March 2008. I'd expect the timing to be similar this year. As was the case with BSG, the share price rallied ahead of the release of the figures because the market anticipated that the share's sell-off had simply been overdone.

Will the same happen with DNICK?

If I had to take a bet, I'd say it will. And what I am sure about is, that on the current share price, this investment has an excellent risk-reward ratio (see box). There is little downside, and considerable upside. The risk of a longer than expected waiting for a bid, is effectively compensated if the company makes considerable dividend payments to shareholders in the meantime. And all that comes in the context of a company that is a global market leader in a highly attractive niche business, with high barriers to entry and a solid balance sheet that has no long-term debt.

Fancy buying some more? As ever, it's up to you to decide. Just don't say that you hadn't been told about it. And contrary to BSG, where I reported about a 90% rise within 4 weeks after it had happened, I wanted to get the update about DNICK out while the share price was still on its crisis-driven sell-out level. DNICK is unlikely to rise 90% in the next 4 weeks, but I doubt that the share will still be at the current bombed-out level in 3 months time when the management has released more information.

Small downside, large upside – and that's what I like.

Best wishes



Swen Lorenz

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