Equity Research

WestLB

29 May 2007

MBB Industries AG

BUY

Current price €8.1
Target price €12.7

Pan European Equity
Germany
Mid And Small Cap

INCREASE OF TARGET PRICE

Strong growth and deep value

DEUTSCHE BÖRSE
ENTRY STANDARD

Although MBB Industries kept the promises of the 2006 IPO, the stock has significantly underperformed. It has meanwhile developed into one of the cheapest stocks in our universe of 126 German mid & small caps. Our forecast of 28.1% net profit growth (CAGR 2006-09E), suggests it offers a very large upside potential of nearly 60% to our new target price of €12.7 (€11.3). Short term, we believe the recently successful holding exit and the expected authorisation to buy back 10% of the share capital at the AGM on 12 June could provide positive share price triggers.

Year end Dec	Sales (€m)	PBT (€m)	EPS (€)	P/E (x)	EV/EBITDA (x)	EV/EBIT (x)	Yield (%)
2006A	62.9	4.4	0.59	12.8	6.7	10.7	0.0
2007E	80.6	8.6	1.00	8.1	5.2	7.1	0.0
2008E	86.7	10.5	1.05	7.7	4.4	5.8	0.0
2009E	93.7	12.4	1.23	6.6	3.8	4.9	0.0

Source MBB Industries AG, WestLB Research estimates

- **Strong numbers for FY 2006.** The promises made at the time of the IPO in April 2006 were kept. In FY 2006, the EPS has more than doubled to €0.59, driven by both external and internal sales growth and margin expansion. The top-line growth amounted to 71%, and the EPS showed 123% growth.
- **Excellent prospects for FY 2007.** We expect to see further growth spurred on by the good state of the German economy. We expect the sale of the recycling activities on 23 May 2007 to boost MBB's earnings and have raised our EPS 2007E by 4%.
- **Between turnaround investor and SME investment holding.** MBB Industries focuses on "old economy" sectors and buys up companies in the throes of radical change. We believe that the company works in a profitable and relatively secure niche with moderate risk between turnaround investors like Arques Industries or SME holding companies like Gesco.
- **Unique combination of value and growth.** With an estimated 2007E PER of 8.1x and a PBV of 1.2x, MBB Industries is one of the cheapest shares in our universe of 126 German mid & small caps. At the same time, we believe the company will generate 28.1% EPS growth (CAGR 2006-09E).
- **Significant undervaluation.** The stock has significantly underperformed, and this is due, we feel, to its limited liquidity and small cap status. Based on our peer group analysis and book value multiplier valuation (for 2007/2008), we see a justifiable fair value range of between €12.33 and €13.01. Our target price is €12.7 (was €11.3).

Key data

in %	1m	3m	12m
Absolute	-4.1	0.5	-15.7
Relative	-5.5	-2.8	-32.1

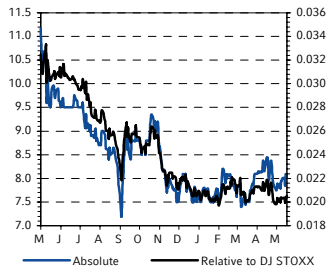
12 month price range	€9.96 - €7.20
Net cash/share YE	€-4.2
NAV/share YE	€5.5
No. shares in issue	6.6m
Free float	28.0%
Market cap	€53m
Next event	AGM
Reuters code	MBBG.DE
Bloomberg code	MBB GR
DJSTOXX	393.48

Unless otherwise stated, share prices are as of market close on 25 May 2007.

SRI rating N/A

Environment	n/a Stakeholder	n/a
Governance	n/a Controversy	n/a

Absolute & relative performance



Source JCF, WestLB Research (SRI data)

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Strong numbers for FY 2006

In FY 2006, MBB Industries was able to keep the promises it made at the time of its IPO in May 2006. The financial results for 2006 presented by the company were well above our expectations, especially H2.

FY 2006 analysis of differences

€m	2006A	2006E	+/- e/a	+/- e/a (%)	y-on-y. (%)
Sales	**62.9**	**60.0**	**2.9**	**5%**	**71%**
Delignit	27.3	27.5	-0.2	-1%	10%
OBO	9.5	9.5	0.0	0%	44%
Cildro	7.8	6.9	0.9	13%	43%
Huchtemeier Group*	18.4	16.0	2.4	15%	n.a.
EBIT	**5.7**	**5.8**	**-0.1**	**-1%**	**139%**
Net profit	**3.9**	**3.4**	**0.5**	**13%**	**97%**
EPS (€)	**0.59**	**0.52**	**0.1**	**13%**	**123%**
EBIT margin (%)	9.1	9.6	nm	nm	nm

*Huchtemeier, Hanke and Westfalia

Source MBB Industries, WestLB Research estimates

In H2, the reported revenues and net profit were 8% and 26% higher than our expectations. In terms of revenue performance, the Romanian veneer producer Cildro and the Huchtemeier Group (Huchtemeier, Hanke and Westfalia) in particular provided positive surprises, while Delignit, a specialist materials supplier, and OBO, a producer of polyurethane board, were in line with our expectations.

Disproportionate earnings growth

The strong earnings growth is all the more noteworthy given that MBB Industries had to absorb the IPO-related costs at the same time. Another extraordinary item in the P&L was a merger gain of €3.1m. This was set against a special write-down and the setting up of a special item with an equity reserve portion of €1.5m. The merger gain arose as the transferred balance sheet values of the subsidiaries were higher than the balance sheet value that the parent had in its books for the subsidiaries. It therefore represents a partial release of a bargain purchase component.

Operating cash flow negative as a result of the growth

The very strong increase in current assets in the form of inventories and trade receivables reduced cash flow by €12.7m and resulted in negative operating cash flow of €0.5m. This increase is due to strong organic growth and the acquisition of Huchtemeier. Current assets have hardly increased in terms of revenue days.

Fresh funds from capital increase have boosted equity ratio

The capital increase in connection with the IPO has given MBB Industries sufficient equity. We expect the equity ratio to rise from 47% at the end of 2006 to 57% by 2009 and net debt to fall at the same time.

Positive outlook for 2007, organic growth …

In its outlook for FY 2007, MBB Industries states that in addition to acquisition-related growth based on the consolidation of the Huchtemeier Group during the year, it expects further organic growth. This year, we believe Delignit in particular will be the earnings driver together with the acquisition-related growth in earnings provided by the Huchtemeier Group.

… and earnings contribution from successful exit

Having sold its 50% stake in DOREG (Dortmunder Recycling GmbH), which had been booked "at equity", back in December 2006, MBB Industries has now sold off its recycling activities (Westfalia) to Karl Tönsmeier Entsorgungswirtschaft on 23 May 2007. We estimate that MBB Industries has achieved a seven-digit profit through this sale, which has caused our earnings estimates for 2007 to rise.

Following the results and the exit from the recycling business through the sale of Westfalia, we have revised our estimates as follows:

Model revisions

	2006E			2007E			2008E		
	New	**Old**	**Delta**	**New**	**Old**	**Delta**	**New**	**Old**	**Delta**
Sales (€m)	62.9	60.0	5%	80.6	83.8	-4%	86.7	91.4	-5%
EPS (€)	0.59	0.52	12%	1.00	0.96	4%	1.05	1.05	0%

Source WestLB Research estimates

SWOT analysis

Strengths

- Generation of average yields >50% with achieved exits according to company management
- Experienced management team that has continuously developed MBB Industries for the past 12 years
- Successfully restructured investment portfolio of high-margin niche players with very good growth prospects
- Long-established network (specialist advisors, legal advisors, etc.)
- Streamlined structures with low holding costs

Weaknesses

- Hitherto modest portfolio size with long degree of diversification
- Sluggish acquisition activity in recent years
- Public profile is still modest compared to other listed players
- Limited share liquidity

Opportunities

- Successor issues, earnings and financing weakness of many SMEs and spin-offs from large conglomerates offer great potential for value enhancing acquisitions
- Significant underperformance of the shares to date indicates considerable upside potential
- Positive effects of the IPO on overall competitive position and public profile

Threats

- Investments in restructuring cases are associated with a high level of operating risk
- Limited management capacity can cause growth and restructuring management issues
- More competition in the acquisition of companies (e.g. as a result of market entries and high liquidity in private equity market)
- Foreign exchange risk

Business model in between turnaround investor and SME holding

MBB Industries' business model lies between that of a turnaround investor and traditional SME holding company. Within its market niche, we believe that it can be characterised as having high returns combined with relatively moderate risk. Most of its holdings are in the manufacturing sector. In terms of its revenue contribution, Delignit is by far the largest subsidiary, followed by OBO Modulan and Hanke Tissue. The portfolio also includes Cildro, Westfalia and the Huchtemeier Group.

The business model

Business model with limited risk

The investment holding company MBB Industries is neither a genuine turnaround investor such as Arques Industries nor a traditional holding company operating in the SMW market such as Gesco Holding. The business model lies right in the middle of these two extremes and in our view therefore offers high return opportunities combined with relatively moderate risk, which reflects the old economy and niche nature of all its business activities. MBB Industries focuses on companies in the throes of radical change, in particular:

- Succession problems, e.g. in owner-managed companies.
- Obsolete financing structures, above all a lack of equity.
- Groups that want to dispose of non-core operations.
- Businesses suffering from management errors.

Acquisition, management and sale of investments

MBB Industries' business model covers the acquisition, management and disposal of investments. MBB Industries does not hold its investments for any predefined period. As soon as an investment can be sold at a price that exceeds the potential added value that can be generated internally, it is sold.

Lean holding company and rapid decision-making processes

The holding company itself has a very lean structure with only seven employees. This means that decisions can be taken rapidly especially when businesses are acquired. In our opinion, this is a considerable competitive advantage given the increasing funds currently flowing into the German private equity market.

Network opens up buying opportunities

When acquiring businesses, MBB Industries makes use of a network it has built up over many years and only in exceptional cases does it draw upon the capacities of external consultants like the management consultancy Metropolitan for example. MBB can cover 90% of its financial due diligence and 50% of its legal due diligence with its own capacities.

Majority holdings in mid-sized businesses with revenues of more than €10m

MBB Industries concentrates on majority stakes in mid-sized businesses that offer considerable upside potential and revenues of more than €10m. Companies are considered to offer considerable upside potential if they meet the following criteria:

- They offer upside potential with an internal rate of return (IRR) of > 30%.
- They offer EBITDA margins upside of > 10%.
- They occupy a niche position.

Taking selective measures to enhance value

To raise the value of the individual companies, MBB Industries in particular exploits opportunities to cut costs that arise as a result of complicated decision-making and shareholder structures and of unfocused product portfolios. Such measures include:

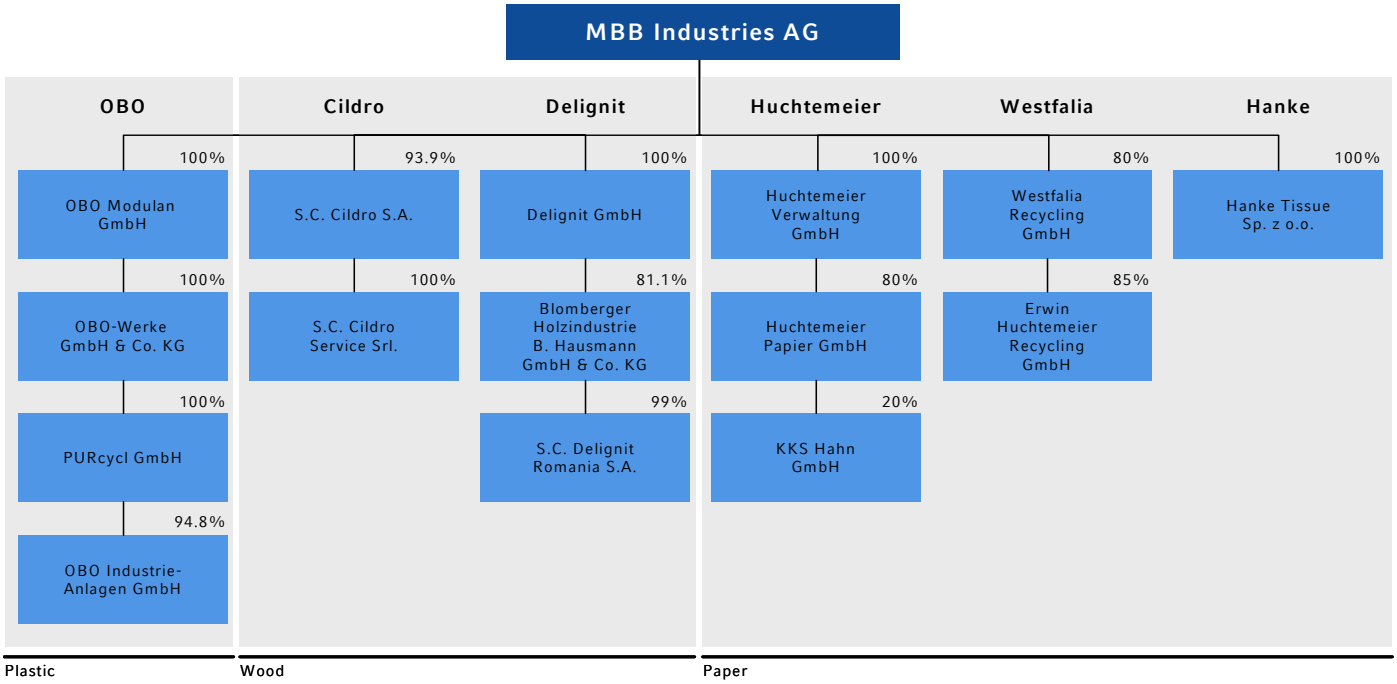
- Reducing overheads by up to 50% in the form of other operating expenses such as communications, insurance and logistics costs.
- Reducing non-operating overhead functions and optimisation of personnel costs.
- Improving production quality and raising machinery utilisation rates.
- Re-negotiating supplier terms and using new suppliers.

The investment portfolio

Investments in the producing sector

Although MBB Industries does not follow a sector approach, most of its companies in which it invests operate in the manufacturing sector. The company is currently divided into six sub-groups and operating units. The respective holdings are set out in the chart below.

Holding portfolio*



*before exit

Source MBB Industries

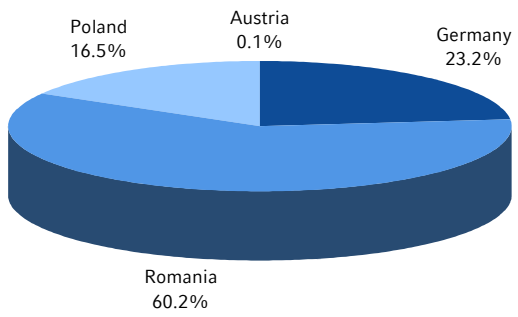
Delignit is by far the largest subsidiary of MBB Industries in terms of revenues, followed by OBO Modulan and Hanke Tissue.

Extremely competitive personnel structure

High share in Romania

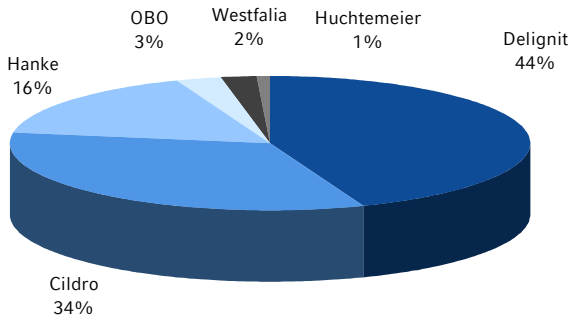
If one considers the number of employees, the high proportion of workers in Romania is striking. This is largely due to the subsidiaries Cildro and Delignit. The acquisition of Hanke Tissue as part of the Huchtemeier purchase in June 2006 established a workforce in Poland. The regional breakdown of the employees with a very high share in low-wage countries, notably Romania, gives MBB Industries a very competitive cost structure. Personnel costs consist of between 22% and 23% of operating costs and thus represent the second largest cost group.

Regional breakdown of employees



Source MBB Industries, WestLB Research estimates

Breakdown of employees by company



Source MBB Industries, WestLB Research estimates

Delignit

- Achieved a return of 43.5% on sales in 2006A.
- Produces the special-purpose material "Delignit"
- The company has increased its value by winning a second single-source OEM order for a leading light van and making productivity gains.

"Delignit" generates high value

Delignit produces "Delignit", a special material based on beech plywood used in motor vehicle construction (e.g. for VW and Daimler Chrysler Crafter/Sprinter vans), building construction, military technology and niche markets such as piano making and sports equipment construction. The high value-added of "Delignit" can best be illustrated by so-called panzerholz, which is used in military equipment. In this segment, a sales price in excess of €13,000 per cubic metre can be achieved in specific cases.

Company acquired after expansion-related crisis

MBB Industries acquired Delignit in 2002 after the previous owner ran into difficulties following the expansion into Romania with excessive financial leverage. Delignit produces both in Germany, where the company originated, and in Romania. The value-added share in both plants is about 50%. While the Romanian plant produced base board in the direct vicinity of the plentiful timber supplies in the past, the German site was primarily responsible for further processing.

Financially previous year affected by start-up problems

However, the ramp-up to series production for the DaimlerChrysler Sprinter created start-up problems in FY 2006 which depressed profitability. We assume that as a result of these problems Delignit only managed to generate an EBIT margin in the very low single-digit range last year. In our view, Delignit in particular could therefore assume the role of earnings driver this year. Besides the work it does for Daimler's Sprinter, Delignit also manufactures the interior fittings for VW's Crafter vans.

OEM supply contracts with VW and DaimlerChrysler for small vans

At present, the interior fitting of small vans represents most of the revenues and is the main revenue driver. The company has OEM supply contracts with VW and DaimlerChrysler to fit out the Sprinter/Crafter. In project business, Delignit also supplies products to parcel services such as the Royal Mail and UPS or trade fairs. Under the Vanycare name, Delignit also manages a business that produces "made-to-measure" flooring and panels for all the small vans available in Germany.

Volume estimate for Crafter & Sprinter vans

Model	VEH. TYPE: HCV / LCV	2004	2005	2006	2007E	2008E	2009E
Sprinter	LCV	0	0	0	27,434	31,000	30,000
Crafter		0	0	893	1,681	1,599	1,471
Crafter	LCV	0	0	16,843	33,083	35,000	34,000
Sprinter/T1(200-400)u	HCV	25,363	27,564	24,085	24,578	26,012	26,902
Total		**25,363**	**27,564**	**41,821**	**86,776**	**93,611**	**92,373**

Source WestLB Research estimates

Vehicle construction is a highly promising market for Delignit

In our view, a highly promising market for future expansion is car manufacturing plants. The material "Delignit" is good at discharging electrostatic charges. This property can be of immense significance when cars are conveyed along the production line. Problems can otherwise arise when electronic systems are fitted into new cars. At the same time, Delignit is a renewable and naturally degradable material. As such, it is an ecological material, which represents a clear competitive advantage in the current environment.

OBO Modulan

- Achieved a return of 15.1% on sales in 2006A.
- Produces polyurethane tooling board (PU board) mainly for automobile manufacturing.
- The strategic partnership with a US group since 2006 is creating value. Last year, this led to a jump in sales. In addition, the company has sharply trimmed the workforce from 135 to just 35 at the end of FY 2005 by focusing on PU-based modelling and mould construction.

Niche business

OBO Modulan's niche business emerged from an insolvency and has been part of the investment portfolio since 2003. The company operates in the €120m market for modelling above all in the automotive industry, where it has a market share of 8%. This covers producing model components, mould construction, models for tooling and auto models, for example to launch a mew model series. OBO Modulan's most important competitors are the Swiss company Sika and the Germany-based Rampf Group.

New markets tapped thanks to US alliance

We estimate that 85% of revenues are generated in the automotive industry. OBO Modulan has a blue chip customer base including carmakers such as Ford, GM, Volvo, Toyota, PSA, VW and DaimlerChrysler.

Customers from the automotive industry

By entering into a cooperation agreement with a US group, which has the necessary customer contacts but no technical PU know-how itself, OBO Modulan succeeded in raising revenues organically by 44% in FY 2006. In addition, it internationalised its businesses, expanding into new markets such as Japan, China and Turkey. By focusing consistently on the polyurethane board business, the company was able to concentrate on the profitable modelling and mould construction business.

Cildro

- Achieved a return of 12.4% on sales in 2006A.
- Produces sliced veneer.
- The company's value has been increased by investments to expand capacity in 2005 and 2006 followed by price rises in 2006 and 2007 after the focus on premium products.

In decorative furniture production genuine wood veneer is preferred because of its authenticity

While the Romanian subsidiary Cildro contributes only the third-largest contribution to group revenues, we assume that, in absolute terms, it is now responsible for the highest EBIT contribution. In our view, this conclusion can be drawn from the fact that Cildro acquired one of the most modern sliced veneer plants as a bargain. This keeps the interest and depreciation charges low compared to the costs of building a new plant – which any new competitor entering the market will have to shoulder. At the same time, Cildro operates close to the required precious timber supplies with a very low wage level. In Romania, the average wage costs are about one-tenth of those in Germany.

Greatest EBIT contribution thanks to highly modern production and low wages

Sliced veneer is the term used to describe in particular thin veneer, generally made from high-grade timber and used as covering/facing in the furniture industry and in interior decoration. As a service company, Cildro must be distinguished from furniture makers which are vertically integrated. Specialised veneer traders also operate in the market. Generally, high-grade timber veneer competes with plastic- or paper-based coverings, which are for example offered by Surteco AG for use in the kitchen industry. As kitchens are subject to heavy-duty use, high quality timber veneer is at a competitive disadvantage there. In the production of decorative furniture, high-grade timber veneer is preferred thanks to its authenticity.

Business successfully restructured

Cildro has been successfully restructured by MBB Industries, which has sharply cut the workforce, raised productivity and streamlined the portfolio to focus on sliced veneer. The huge 43% leap in revenues in FY 2006 was achieved organically with 15% capacity expansion combined with a 10% increase in prices in an otherwise very stable market environment. We believe that, given the attractive level of timber prices in 2006, Cildro also entered into spot transactions which boosted sales on a one-off basis, at the same time diluting margins on a one-off basis.

In 2007 we expect revenue growth of 10-12% and higher margins

In 2007, Cildro's capacity is booked out until August. Price negotiations for the following year are already in progress. We estimate that a further increase in a range of +5% and +7% with capacity expansion of some 5% is realistic in 2007. This gives rise to revenue growth between 10% and 12%. The fact that the company now focuses on higher-priced segments and products will help it in the price negotiations. A lower share of trading should also result in an increase in the margin.

Huchtemeier

- Achieved a return of 8.6% on sales in 2006A.
- Trades in quality paper, cellulose and waste paper.
- Increase in value: Huchtemeier is profitable and is part of the Huchtemeier Group acquired in June 2006. As a trading company, the company serves to maintain an industry network from which Hanke can profit. In our view, a sale is unlikely.

Weak margins, but highly significant for other activities

Although Huchtemeier accounts for 8.6% of group sales, we assume that its earnings contribution is minimal given the trading focus of the business. However, as this trading focus ensures very important industry contacts, we believe the activity will remain in the MBB Group although we expect Huchtemeier to dilute margins in the medium and long term.

Hanke

- Achieved a return of 13.9% on sales in 2006A.
- Produces paper rolls, tissue and napkins.
- Optimisation of the product mix and raising production capacity utilisation rate are increasing the value of the company.

Quality products and strong brand in Eastern Europe

Hanke Tissue produces mother tissue rolls and finished products such as napkins, both printed and unprinted. The quality characteristics of tissue paper for napkins are absorbency and printability. Hanke Tissue produces in Poland and has an established brand (Aha) in the Eastern European consumer goods market. It also makes white and coloured tissue paper for numerous retail brands.

The highest margins in the group

We estimate that Hanke generated the highest margins in the former Huchtemeier Group. By exiting the unprofitable toilet paper segment, MBB Industries has taken a further step towards raising profitability. To increase revenues further despite the high capacity utilisation, MBB Industries has renewed and expanded the production facilities. This investment was financed internally from the free cash flow. However, Hanke continues to operate with bank and leasing debts worth around €5m which stem from the company takeover.

Westfalia

- Achieved a return of 6.5% on sales in 2006A.
- Recycling activities for industrial and municipal waste paper and plastic waste.
- Increase in value achieved through exit on 23 May.

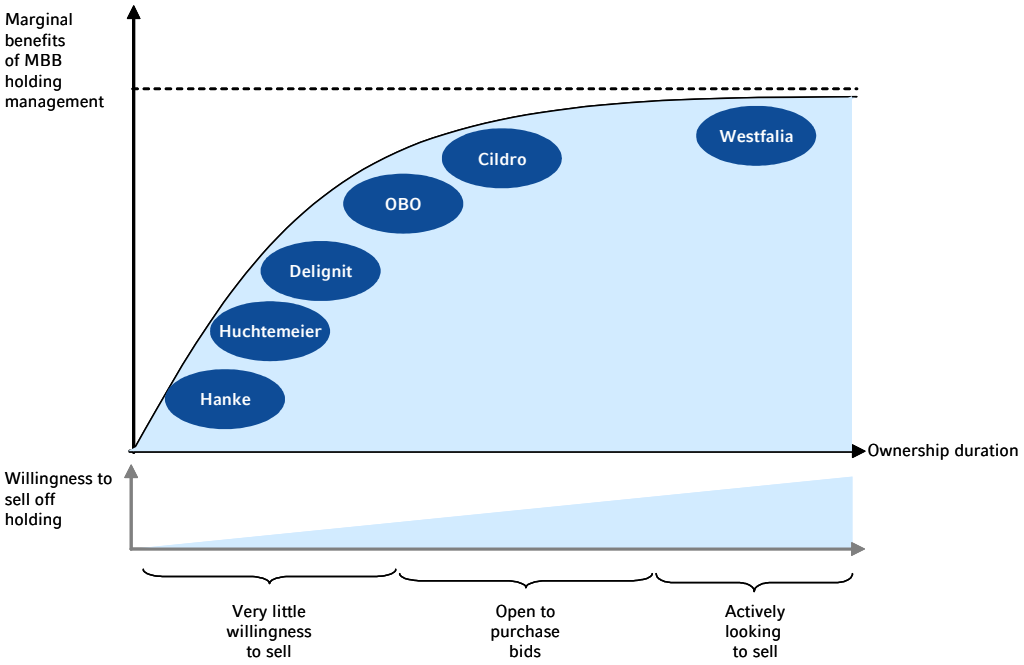
Recycling of waste paper and waste plastics

The Westfalia Group, also part of the former Huchtemeier Group, operates recycling sites for industrial and municipal waste paper and plastic waste. In addition, it is involved in the preparation of system solutions for waste disposal problems. The marketing and recording of recyclable material for which payments are made is also part of the value chain. The Westfalia Group has a regional focus and is headquartered in Hamm.

Exit completed

Having parted company with its 50% stake in DOREG (Dortmunder Recycling GmbH), which had been booked "at equity", back in December 2006, MBB Industries has now sold off its recycling activities (Westfalia) to Karl Tönsmeier Entsorgungswirtschaft on 23 May2007. We estimate that MBB Industries has achieved a seven-digit profit through this sale, which has caused our earnings estimates for 2007 to rise.

Exit ranking of MBB Industries business units



Source MBB Industries

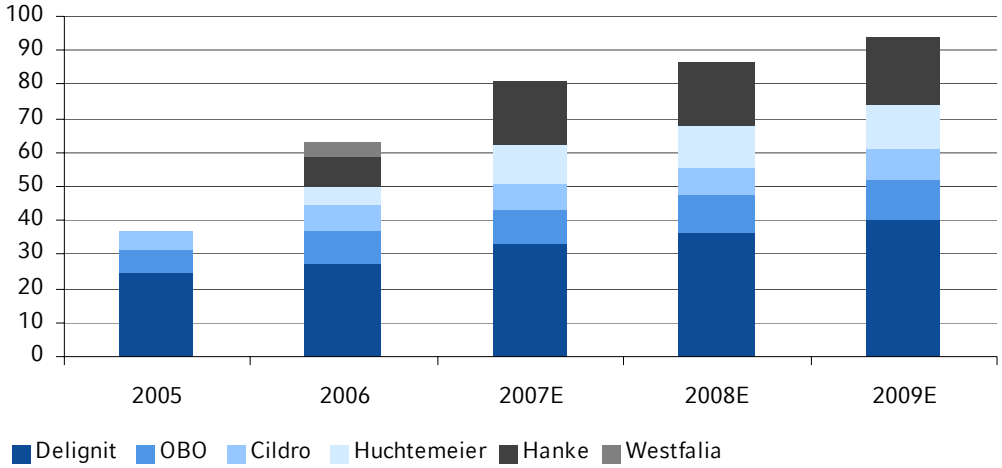
Further strong growth expected

We foresee growth opportunities for MBB Industries across a broad front. In FY 2007, growth should remain strong in our view. This is both due to strong organic growth and to the full-year consolidation of the companies in the Huchtemeier Group (Hanke, Huchtemeier, Westfalia). The sale of the former Huchtemeier recycling activities will also boost the company's earnings.

Consolidation effects and momentum at Delignit drive revenues

We estimate revenue growth of 42% in 2007. Of this, about 75% will stem from the full-year consolidation of the Huchtemeier Group (Hanke, Huchtemeier, Westfalia). We also predict organic growth of nearly 10%, driven largely by the subsidiary Delignit. This year, Delignit should, in our opinion, profit from the strong momentum of the Crafter/Sprinter models (see table on p. 9) and recover from the dip in earnings last year caused by the changeover to the one press operation. The revenue drivers are clearly set out in the following chart.

Revenues 2005-09E (€m)



Source MBB Industries, WestLB Research estimates

Exit from recycling activities could boost earnings

The exit from the recycling operations (Westfalia) will provide an additional boost to earnings. We have factored a gain from the sale of this holding of €1m into our estimates. However, the elimination of an EBIT contribution that we estimate to be worth €400,000 will reduce the company's earnings.

Operating margins should continue to rise

Overall, we expect that MBB Industries will continue to raise its operating margins against the backdrop of strong organic growth. In our estimates, we assume an increase of 270 basis points in the EBIT margin to 11.7% in FY 2007.

The German private equity market

The German private equity market remains underpenetrated relative to other European markets and, above all, to the German economy. This indicates scope for further growth. However, the upturn in recent years has already driven up acquisition multiples and there is now talk of a dearth of investment opportunities. Compared to other listed German private equity companies such as Arques Industries, Bavaria Industriekapital, Gesco and Indus, MBB Industries remains, however, uniquely positioned in our view.

German private equity market at a glance

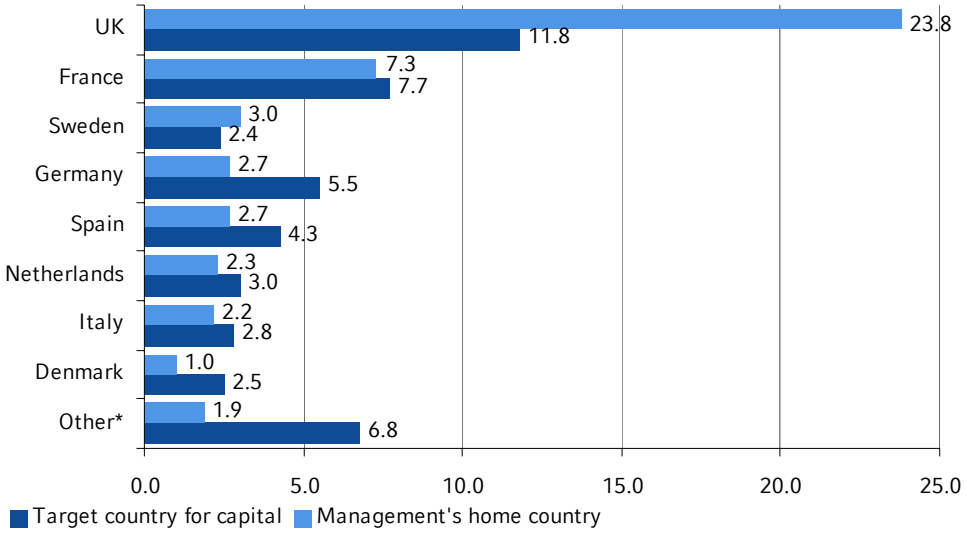
€bn	2005	2006	% y-o-y
Assets under management	26.5	28.7	8.3%
Fundraising	2.9	2.8	-3.4%
Investments	3.6	3.1	-13.9%
Portfolio	21.5	23.1	7.4%
Portfolio companies	5723	5986	4.6%

Source CEFS

Need to catch up with other European countries

The German private equity capital market remains small relative to other European markets and, above all, to the Germany economy. This indicates to us that there is scope for further growth. Private equity investments represent only 0.173% of GDP compared to an average 0.354% in Western Europe and 1.1% in the UK. We believe that this means that MBB Industries is clearly operating in a growth segment.

Private equity investments of European funds (€bn)



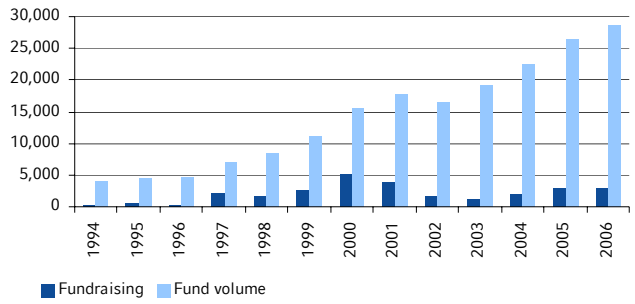
Source CEFS, EVCA

Since the 2003 low, market has shown good growth, …

In terms of assets under management and fundraising, the German private equity market has recovered since the tech bubble at the turn of the century and has in fact shown good growth since the low in 2003.

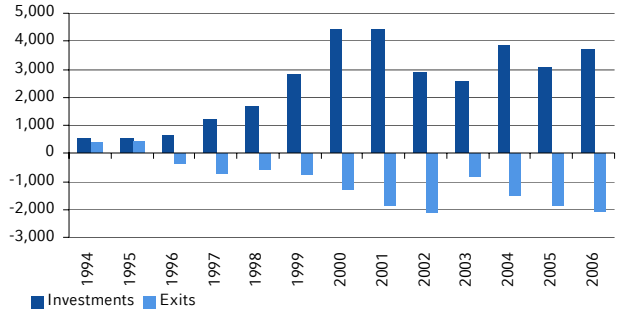
German private equity market

Fundraising & fund volume (€m)



Source BVK

Investments & exits (€bn)

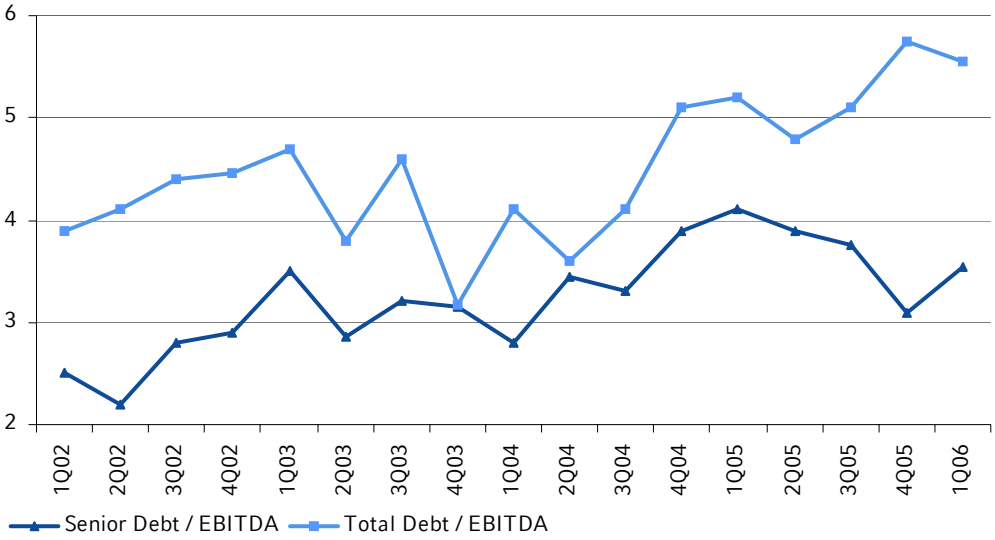


Source BVK

… which is also reflected in the multiples being paid

However, the high market liquidity, which is reflected in a more than doubling of the funds raised since the low of 2003, has resulted in high acquisition multiples. This is driven by the high liquidity in combination with a more aggressive gearing of acquisitions. Since the end of 2005, senior debt/EBITDA multiples have become clearly established at over 5x and in individual cases even exceed 6x. This compares to senior debt/EBITDA multiples of 3x to 4x when the market was in the doldrums in 2003 and 2004.

EBITDA multiples in the European private equity market



Source Ernst & Young

A lack of investment opportunities

In our discussions with MBB Industries, the company's management said that the current situation in the private equity market is marked by competitive bidding processes. We know that the high multiples now being demanded have deterred the company from making one large acquisition – an engineering company – in the recent past. In an auction process, MBB Industries was outbid by a competing private equity firm.

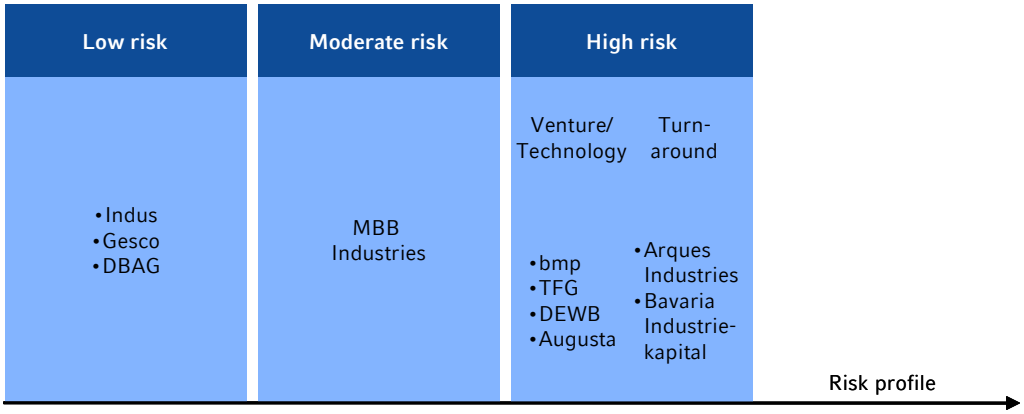
According to the company, MBB Industries still has plans to make between one and three acquisitions in FY 2007. Through moderate takeover multiples, these acquisitions are also required to meet MBB's target of a 30% IRR on the investment.

Positioning of MBB Industries

Attractive niche positions

Compared to other listed German private equity companies such as Arques Industries (AQUG.DE, €22.7), Bavaria Industriekapital (B8AG.F, €53.9), Gesco (CSCG.DE, €40.0) and Indus (INHG.F, €30.1), MBB Industries is uniquely positioned in our view. The company occupies a niche between the traditional low-risk industrial holding companies such as Gesco, DBAG (DBAG.DE, €27.26) and Indus and the riskier turnaround investors such as Arques Industries and Bavaria Industriekapital.

Private equity segments



Source WestLB Research

Mixture of value and growth

The numbers point to a growth stock …

We forecast that MBB Industries will achieve revenue growth of 14.2% (CAGR 2006-2009E), EBIT growth of 32.5% (CAGR 2006-209E) and net earnings growth of 28.1% (CAGR 2006-09E). Given these growth prospects and the revenue and net earnings growth of 70.7% and 120.8% respectively in FY 2006, we believe that MBB Industries can be viewed as a growth stock even though most of the company's investments are in the "old economy".

… with value character thanks to high FCF return

Despite the strong growth profile, we estimate a free cash flow return of 20.5% in FY 2008E and 18.2% in 2009E once MBB Industries has absorbed the acquisition-related increase in net working capital. In our opinion, the strong free cash flow return combined with the niche character of its units makes MBB Industries a value investment notwithstanding the growth profile.

Low valuation

Given its valuation, we believe that MBB Industries can be described as a value investment. In our universe of 126 German mid & small caps, MBB Industries is the cheapest stock on the basis of 2008E P/E, on our estimates. Based on our 2008E EV/EBITDA valuation multiples, MBB Industries is also one of the 10 cheapest shares although it still operates with a gearing of some 30% despite the IPO in 2006.

Shares illiquid

We believe that the significant underperformance of MBB Industries shares despite the high growth profile and, in our view, above-average earnings visibility, can mainly be explained by the stock's limited liquidity. In our view, this could be improved by actively contacting investors. In addition, the share is listed in the Entry Standard index, where average valuations are currently lower than is the case for the other German mid & small cap indexes.

Valuation and recommendation

For private equity companies with a buy-and-sell investment approach, valuation methods that are based directly on earnings multiples naturally play only a subordinate role, which is due to their inherently very high earnings volatility and low visibility.

NAV approach is suitable for investment companies

For this reason, we consider the net asset value approach to be the most suitable method for analysing how much investment companies are worth. The NAV approach applies valuations to holdings that are closely in line with market valuations, transaction prices in the individual sectors, concrete buying opportunities or peer group valuations based on earnings multiples.

In order to derive the NAV, we base our calculations in the following on a peer group valuation and the book value multiple model.

Peer group valuation

We choose two peer groups: German mid & small caps and companies from the wood processing and furniture industries

MBB's current portfolio focuses on industrial companies, and particularly on the wood processing industries. Due to the lack of peer group companies for the individual holdings, we consider a comparison of the overall portfolio against the market valuations of German mid & small cap industrial companies and a group of companies from the wood processing and furniture industries to be adequate.

We use the P/E ratio as the underlying earnings multiplier. Alongside this we take account of EV multipliers, although these do not consider the valuation effects arising from minority interests or MBB's consistently low tax rate.

MBB is undervalued compared to the peer groups

We have found that MBB shows a striking undervaluation compared to the two peer groups, both in terms of P/E ratio and enterprise value multiples. At the same time, MBB Industries is generating high net profit margins.

German Industrials peer group

	Reuters code	Closing price on 22/05/07	PER 2007E	PER 2008E	EV/EBITDA 2007E	EV/EBITDA 2008E	EV/sales 2007E	EV/sales 2008E	NP margin 2007E (%)	NP margin 2008E (%)	ROE 2007E
Deutz AG	DEZG.F	10.3	16.1	13.1	6.6	5.5	0.73	0.65	4.4%	5.0%	17.3%
Heidelberger Druck	HDDG.F	36.7	14.7	13.0	6.5	6.2	0.86	0.81	5.2%	5.2%	14.0%
Krones AG	KRNG.F	165.7	19.0	15.2	8.5	7.3	0.79	0.71	4.4%	5.1%	13.1%
IWKA AG	IWKG.F	25.9	17.2	14.5	7.0	5.4	0.46	0.41	6.3%	3.5%	18.9%
Rheinmetall AG	RHMG.F	72.0	15.8	13.0	6.3	5.6	0.70	0.65	4.2%	4.7%	15.9%
Vossloh AG	VOSG.F	83.1	18.6	15.9	9.4	7.8	1.16	1.02	5.7%	6.2%	16.2%
Gildemeister AG	GILG.F	15.2	17.2	13.3	6.5	5.8	0.60	0.56	2.8%	3.4%	10.9%
Jungheinrich AG	JUNG_p.F	30.5	14.5	12.2	4.3	3.8	0.56	0.50	3.7%	4.2%	13.3%
Masterflex AG	MZXG.F	25.3	13.3	11.5	8.2	7.4	1.18	1.06	6.4%	6.6%	23.0%
Rational AG	RAAG.F	147.3	27.3	22.4	16.2	13.8	4.93	4.28	18.5%	19.9%	49.5%
Technotrans AG	TTRG.F	22.5	13.3	11.3	6.6	5.7	0.89	0.76	6.9%	7.5%	19.1%
GEA Group AG	G1AG.F	23.0	20.6	17.2	9.4	7.9	0.87	0.78	4.5%	4.7%	12.8%
MBB Industries	**MBBG.F**	**7.8**	**8.1**	**7.7**	**5.2**	**4.4**	**0.83**	**0.76**	**8.2%**	**8.0%**	**15.5%**
AVERAGE			**17.3**	**14.4**	**8.0**	**6.9**	**1.14**	**1.02**	**6.1%**	**6.3%**	**18.7%**
MEDIAN			**16.6**	**13.2**	**6.8**	**6.0**	**0.83**	**0.74**	**4.8%**	**5.1%**	**16.1%**
+ premium / - discount (to average)			**-53%**	**-47%**	**-35%**	**-35%**	**-28%**	**-26%**			
+ premium / - discount (to median)			**-51%**	**-42%**	**-24%**	**-27%**	**0%**	**3%**			

Source JCF, WestLB Research estimates

German wood processing industry peer group

	Reuters code	Closing price on 22/05/07	PER 2007E	PER 2008E	EV/EBITDA 2007E	EV/EBITDA 2008E	EV/sales 2007E	EV/sales 2008E	NP margin 2007E (%)	NP margin 2008E (%)	ROE 2007E
Pfleiderer AG	PFD4.DE	24.9	17.4	13.4	7.2	6.0	1.03	0.93	4.0%	4.9%	14.9%
Surteco AG	SURG.DE	41.8	14.6	13.1	7.5	6.6	1.40	1.29	7.5%	8.1%	17.1%
Westag & Gelatit AG	WUGG.DE	23.5	12.8	na	na	na	na	na	na	na	na
MBB Industries	**MBBG.F**	**7.8**	**8.1**	**7.7**	**5.2**	**4.4**	**0.83**	**0.76**	**8.2%**	**8.0%**	**15.5%**
AVERAGE			**15.0**	**13.2**	**7.4**	**6.3**	**1.21**	**1.11**	**5.7%**	**6.5%**	**16.0%**
MEDIAN			**14.6**	**13.2**	**7.4**	**6.3**	**1.21**	**1.11**	**5.7%**	**6.5%**	**16.0%**
+ premium / - discount (to average)			**-46%**	**-42%**	**-29%**	**-30%**	**-32%**	**-32%**			
+ premium / - discount (to median)			**-45%**	**-42%**	**-29%**	**-30%**	**-32%**	**-32%**			

Source JCF, WestLB Research estimates

Peer group fair value ranges between €11.62 and €13.94

Based on the two peer groups, we calculate a fair value per share that ranges between €11.62 and €13.94 and which we derive from an average value for the two peer groups for FY 2007 and 2008. The lower end of the valuation range is set by the 2007E EBITDA multiple and the upper end is set by the 2007E PE ratio, to which we conservatively apply a 10% holding discount.

Range of fair value per share for MBB Industries

In €	Based on P/E 2007E	Based on EBITDA 2007E	Based on sales 2007E	Based on P/E 2008E	Based on EBITDA 2008E	Based on sales 2008E
MBB Industries valued using multiples for German "industrials" peer group	17.28	13.45	11.96	15.16	13.55	11.51
MBB Industries valued using multiples for German "wood processing industry" peer group	14.94	12.35	14.11	13.95	12.35	12.71
Average value for MBB Industries valuation	**16.11**	**12.90**	**13.03**	**14.56**	**12.95**	**12.11**
(-) 10% holding discount	1.61	1.29	1.30	1.46	1.29	1.21
Fair value per share for MBB Industries	**14.50**	**11.61**	**11.73**	**13.10**	**11.65**	**10.90**

Source WestLB Research estimates

Book value multiplier model

Alongside the peer-group valuation we have applied a book-value based valuation model, which calculates the fair value based on a book value multiplier into which the company's specific return ratios and costs of capital are considered directly. We take this valuation methodology from our banking team.

Cost of capital:

- Risk-free interest rate: 4.3% (10Y Bund)
- Market risk premium: 3.5%
- Beta coefficient: 1.3
- Cost of equity: 8.9%

Book value valuation model

	2007E	2008E
CoE	8.9%	8.9%
RoE	16.2%	16.2%
Return multiple	1.83	1.90
Equity value	80.30	97.30
Minority interests	4.00	4.87
Value per share	**11.60**	**14.01**

Source WestLB Research estimates

Fair value suggested by the book value multiple model ranges between €11.60 and €14.01

As an average value for 2007E and 2008E, our book value valuation model arrives at a value per share that ranges between €11.60 and €14.01.

Recommendation

We have raised our target price for MBB Industries from €11.3 to €12.7, which corresponds to the average for the fair value per share based on a peer group and book value multiple analysis. We believe that value-enhancing holding divestments and an active investor relations policy could act as share price triggers in the short and medium term.

Earnings forecast

(in €m)	2005	2006	2007E	2008E	2009E
Sales	**36.858**	**62.915**	**80.586**	**86.695**	**93.680**
Delta inventories finished goods & work in progress	0.090	3.418	3.850	4.004	4.164
Own work capitalized	0.056	0.382	0.000	0.000	0.000
Other operating income	2.495	4.426	3.821	3.624	3.916
Total income	**39.498**	**71.141**	**88.257**	**94.323**	**101.760**
Cost of raw materials	-16.124	-34.147	-44.564	-46.555	-50.587
Gross profit	**23.374**	**36.994**	**43.692**	**47.768**	**51.173**
Personnel cost	-11.587	-16.455	-18.535	-19.940	-23.420
Depreciation and amortisation	-2.238	-3.360	-3.385	-3.555	-3.841
Other operating expenses	-5.713	-11.511	-12.330	-13.004	-10.764
Non-operating expenses	-1.448	-0.022			
EBIT	**2.388**	**5.646**	**9.443**	**11.269**	**13.148**
Income from investments	0.000	0.031	0.100	0.200	0.200
Interest income	0.000	-1.327	-0.929	-1.000	-1.000
Extraordinary income					
PBT	**2.388**	**4.350**	**8.615**	**10.469**	**12.348**
Income taxes	-0.217	-0.128	-1.723	-3.245	-3.951
Net profit before minorities	**1.976**	**4.042**	**6.812**	**7.224**	**8.397**
Minorities	-0.226	-0.178	-0.221	-0.269	-0.269
Net profit	**1.750**	**3.863**	**6.591**	**6.954**	**8.127**
No. of shares	6.60	6.60	6.60	6.60	6.60
EPS (€)	**0.27**	**0.59**	**1.00**	**1.05**	**1.23**

Source MBB Industries, WestLB Research estimates

Cash flow forecast

(in €m)	2005	2006	2007E	2008E	2009E
Net profit	**1.976**	**4.042**	**6.812**	**7.224**	**8.397**
Depreciation and amortisation	2.238	3.360	3.385	3.555	3.841
Change in provisions	5.239	0.043	-0.055	0.000	-0.095
Other non-cash expenses/income & divestment gains/losses	0.732	-2.152	-4.000	-2.000	-2.000
Changes in inventories, trade receivables & other assets	-9.930	-12.782	-2.326	-1.949	-2.065
Changes in trade payables and other equity & liabilities	6.719	6.982	-1.801	4.066	1.643
Net cash from operations	**6.974**	**-0.508**	**2.014**	**10.895**	**9.720**
Proceeds from asset disposals	0.036	0.113	0.000		
Investment in non-current assets	-20.743	-2.043	-2.200	-2.500	-2.500
Investment in financial assets	-0.010	-0.726	0.381	0.199	0.766
Changes in cash and cash equivalents due to the acquisition of consolidated subsidiaries	-0.210	-6.286	-2.486	-7.500	-7.500
Net cash from investing activities	**-20.927**	**-8.942**	**-4.305**	**-9.801**	**-9.234**
Proceeds from additions to equity	0.162	15.200	0.000	0.000	0.000
Dividends paid to owners and minority interests	0.000	0.000	0.000	0.000	0.000
Proceeds from financing/repayment of debt	14.121	4.375	0.000	0.000	0.000
Repayment of borrowings					
Net cash from financing activities	**14.283**	**19.575**	**0.000**	**0.000**	**0.000**
Net change in cash & cash equivalents	0.330	10.125	-2.291	1.094	0.486
Changes due to exchange rates and other factors					
Cash at beginning of period	**0.008**	**0.338**	**10.463**	**8.172**	**9.266**
Cash at end of period	**0.338**	**10.463**	**8.172**	**9.266**	**9.753**

Source MBB Industries, WestLB Research estimates

Balance sheet

(in €m)	2005	2006	2007E	2008E	2009E
Intangible assets	**3.086**	**7.473**	**7.473**	**7.473**	**7.473**
Deferred taxes					
PP&E	**28.198**	**31.974**	**33.057**	**39.139**	**44.924**
Non-current financial assets	**0.010**	**0.741**	**0.741**	**0.741**	**0.741**
Total non-current assets	**31.294**	**40.189**	**41.272**	**47.354**	**53.139**
Inventories	**6.094**	**13.596**	**17.566**	**18.978**	**20.533**
Accounts receivable – trade	**3.322**	**8.074**	**8.830**	**9.454**	**10.050**
Trade receivables	2.284	6.894	7.330	7.854	8.450
Other assets	1.038	1.180	1.500	1.600	1.600
Cash and cash equivalents	0.338	10.463	6.970	8.794	9.617
Total current assets	**9.754**	**32.133**	**33.366**	**37.226**	**40.199**
Deferred taxes	0.000	0.000	0.000	0.000	0.000
Prepaid expenses	0.515	1.042	0.493	0.470	0.881
Total assets	**41.563**	**73.364**	**82.101**	**93.844**	**103.836**
Shareholders' equity and liabilities					
Share capital	0.162	6.600	6.600	6.600	6.600
Share premium	7.230	15.992	15.992	15.992	15.992
Retained earnings	1.749	6.267	12.707	19.742	27.823
Badwill	5.073	4.199	7.000	7.000	7.000
Revaluation reserve	0.000	0.000	0.000	0.000	0.000
Minority interests	1.270	1.322	1.543	1.811	2.079
Total shareholders' equity	**15.484**	**34.380**	**43.842**	**51.146**	**59.494**
Special item incl. reserves		**1.505**			
Pension provisions	2.179	2.077	2.000	1.900	1.805
Provisions for taxes	2.256	1.927	1.830	1.739	1.652
Other provisions	0.804	1.278	1.300	1.400	1.400
Current liabilities	**20.785**	**32.170**	**33.102**	**37.633**	**39.458**
Bank loans and overdrafts	14.121	18.496	18.496	18.496	18.496
Advances received from customers	0.144	0.479	0.575	0.604	0.634
Trade payables	4.134	10.893	11.729	16.231	18.026
Shareholder payables					
Other current liabilities	2.386	2.303	2.303	2.303	2.303
long-term liabilities					
Deferred tax liabilities	0.000	0.000	0.000	0.000	0.000
Deferred income	0.055	0.027	0.027	0.027	0.027
Total shareholders' equity and liabilities	**41.563**	**73.364**	**82.101**	**93.844**	**103.836**

Source MBB Industries, WestLB Research estimates

MBB BS, P&L and CF ratios

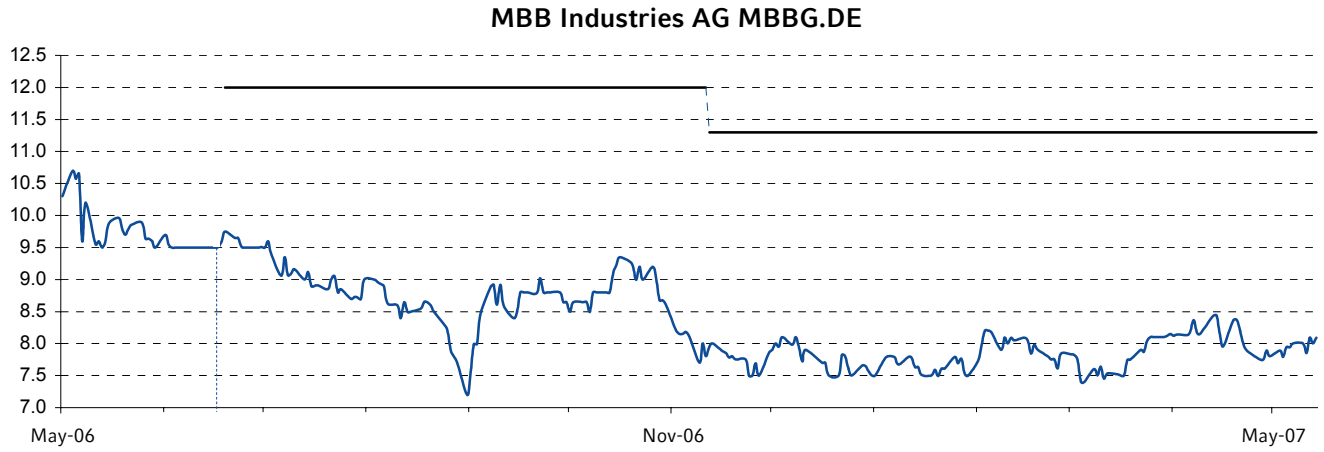
	2005	2006	2007E	2008E	2009E
Share price (in €)	n.a.	7.5	8.10	8.10	8.10
Number of outstanding shares (in m)	6.6	6.6	6.6	6.6	6.60
Market cap (in €m)	n.a.	49.500	53.460	53.460	53.460
Enterprise value (in €m)	16.961	60.609	66.783	65.589	65.008
Valuation multiples					
EV/EBIT	7.1	10.7	7.1	5.8	4.9
EV/EBITDA	3.7	6.7	5.2	4.4	3.8
EV/sales	0.5	1.0	0.8	0.8	0.7
EV/capital employed	0.5	1.2	1.2	1.1	1.0
PER	0.0	12.8	8.1	7.7	6.6
Price to book		1.4	1.2	1.0	0.9
Margins					
EBIT (in €m)	2.39	5.65	9.44	11.27	13.15
EBIT margin	6.5	9.0	*11.7*	*13.0*	*14.0*
EBITDA (in €m)	4.63	9.01	12.83	14.82	16.99
EBITDA margin	12.6	14.3	*15.9*	*17.1*	*18.1*
Capital returns (%)					
Return on capital employed (RoCE)	6.5	11.2	17.4	19.3	20.2
Return on equity (RoE)	11.3	11.2	15.0	13.6	13.6
Return on assets (RoA)	5.7	7.7	11.5	12.1	12.8
Equity return according to DuPont Model					
Pre-tax profit margin (PBT/sales)	6.5	6.9	10.7	12.1	13.2
Asset turnover (sales/assets) x	0.9	0.9	1.0	0.9	0.9
Financial leverage ratio (assets/equity) x	2.7	2.1	1.9	1.8	1.7
(1-tax rate)	82.7	92.9	79.1	69.0	68.0
= RoE	12.8	11.8	15.5	14.1	14.1
Balance sheet ratios					
Equity ratio (in %)	37.3	46.9	54.2	55.4	58.2
Book value per share (in €)	2.35	5.21	6.67	7.76	9.03
Net debt (+)/net cash (-)	16.961	11.109	13.323	12.129	11.548
Gearing (net debt/equity) (%) before pension funding gap	110	32	30	24	19
Net gearing (net debt/net equity) (%)	133.0	41.0	30.3	23.7	19.4
Current ratio (current assets/current liabilities) (%)	0.5	1.0	1.0	1.0	1.0
Net working capital					
Inventories (in €m)	6	14	16	17	19
(+) receivables (in €m)	3	8	8	9	9
(-) payables (in €m)	4	11	11	15	16
= net working capital (in €m)	5.282	10.777	13.398	11.218	11.584
Delta net working capital (in €m)	-5.282	-5.495	-2.621	2.180	-0.366
WC% of sales	14.3	17.1	16.6	12.9	12.4
Cash flow analysis					
Operating cash flow (in €m)	7.0	-0.5	2.0	10.9	9.7
- CAPEX (in €m)	-20.7	-2.0	-2.2	-2.5	-2.5
= free cash flow (in €m)	-13.769	-2.550	-0.186	8.395	7.220
Free cash flow (in % of sales)	-37.4	-4.1	-0.2	9.7	7.7
Operating cash flow (in % of sales)	18.9	-0.8	3.8	20.4	18.2

Source MBB Industries, WestLB Research estimates

MBB BS, P&L and CF ratios

	2005	2006	2007E	2008E	2009E
Management of net working capital					
DSOs	33	47	37	37	36
Inventory days	-138	-145	-130	-135	-135
Payable days	41	63	48	62	64
Inventory (in % of sales)	16.5	21.6	19.7	19.9	20.0
Receivables (in % of sales)	9.0	12.8	10.1	10.1	9.9
Payables (in % of sales)	11.2	17.3	13.2	17.0	17.5
Capital employed					
PP&E (in €m)	28.198	31.974	33.275	39.721	45.880
(+) intangible fixed assets (in €m)	3.086	7.473	7.473	7.473	7.473
(+) net working capital (in €m)	5.282	10.777	13.398	11.218	11.584
= capital employed (in €m)	36.566	50.224	54.147	58.413	64.937
Capital employed turnover	1.01	1.25	1.49	1.48	1.44
Enterprise value					
Market capitalisation (in €m)	0.000	49.500	53.460	53.460	53.460
(-) interest bearing assets (in €m)	0.339	10.463	8.172	9.266	9.753
(+) interest bearing liabilities (in €m)	16.300	20.573	20.496	20.396	20.301
(+) operating lease commitments	1.000	1.000	1.000	1.000	1.000
= enterprise value (in €m)	16.961	60.609	66.783	65.589	65.008

Source MBB Industries, WestLB Research estimates



Date	Price	Changed to...	Date	Price	Changed to...	Date	Price	Changed to...
30-Jun-06	9.75	Buy						

Coverage History No Rating as of 12/05/2006

Change of analyst as of 19 Sept 2006
Initiation of coverage as of 30 Juner 2006

Source FactSet/JCF, WestLB Research

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Sell/Reduce	29	11	Sell/Reduce	2	3

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