

5th January 2016

Food & Beverages

**Heineken**

Price EUR77.79

Slowdown expected for 2016 after buoyant 2015

Fair Value EUR80 vs. EUR85 (+3%)

**NEUTRAL**

**We have fine-tuned our expected earnings for 2015 and beyond, but have hardly changed our numbers. Nevertheless we are lowering the fair value of the company to EUR80 from EUR85 as we return to our previous long-term growth rate of 3.3% (as compared to 3.6% which underpinned the EUR85 fair value). At 19.5x 2016 earnings, the company trades at the average for 2015, but well ahead of the average 17.0x of the past five years.**

On 10 February, the company will report full-year 2016 figures. Overall, we are looking for organic revenue growth of 3.9% (2.8% volume and 1.1% price/mix), driving organic operating profit growth of 8.7%. Including the currency impact, we are expecting reported operating profit growth of 9.1%. For 2016, we expect organic revenue growth to slow down to 2.7% and organic operating profit growth to slow down to 6.5%.

**ANALYSIS**

- In Europe, we are expecting full-year organic revenue growth of 2.5%, of which 0.7% volume growth and 1.8% price/mix. This is a marked slowdown compared to the 1.9% volume growth after 9 months and assumes a decline of 2% in the fourth quarter after the strong weather-driven 6.8% growth in Q3. Q4 price/mix looks like to be in line with the previous quarters. The first indications are that volume in the UK remains positive, driven by strong off-premise performance. In Spain, the positive volume trend (over 5 quarters) continues but we would expect that the terrorist attacks in France will hold back the positive growth that the company had experienced in this country since the start of the year. In Poland, we do not expect the company to repeat the double-digit growth from Q3 (because of the relisting), but even a more flattish figure would already be more positive than the declines of the past years. Because of these relatively good performances in Q4 on top of a very strong Q3, we are increasing our margin expectation for the European business from 11.1% to 12.0% (compared to 11.4% in 2014).
- The region which seems to be worse off in the fourth quarter is Africa, Middle East & Eastern Europe as the flattish Q3 figures were helped by the mid single-digit increase in volumes in Nigeria, driven by the earlier promotional campaigns. This has a balance impact in Q4 on top of the harsher economic conditions (also price/mix will be lower than the 6% from Q3). In Russia, the decline in volumes seems to be decelerating from double-digit to high single-digit. For the remainder, Egypt, Tunisia and Algeria are all weaker because of terrorist treats whereas Ethiopia continues to grow double-digit. Overall, we are expecting for the year a volume decline of 2.5% (1.4% decline after 9 months) and a price/mix of 5% (5.9% after 9 months), which should be enough to allow for a 40bp margin expansion from 21.0% to 21.4%.
- In the Americas, the momentum (delivering 4.5% volume growth so far this year) seems to be continuing although not as strong as the 7.2% volume growth in Q3 itself, as Q3 benefited from some promotional activities in Mexico and Brazil was still growing double-digit. But despite the economic difficult conditions in Brazil, volume growth for Heineken still looks like being in a high single-digit. In the US, Q4 volumes look to be positive as the Mexican brands are improving and the Heineken brand is confirming the positive trends. Overall, we are expecting for the full year organic volume growth of 4% and price/mix of 3%, which should drive 100bp margin expansion to 17.7% from 16.7%.
- Also, in Asia, the strong momentum seems to be continuing and we are expecting organic volume growth for the full year of 7.5% with the strongest performance expected to be in Vietnam following the repositioning of the Heineken and Tiger brands which is driving strong Tiger volumes. The Tiger brand volumes also seem to be continuing to grow strongly in Cambodia and Malaysia. The volume decline in Indonesia, seems to be improving as the company is working with the supermarkets to counter the impact from the ban on the sale of alcoholic beverages in minimarts (convenience stores). Heineken's volumes in China continue to be impacted by the general slowdown in the economy and the impact from the anti-extravaganza measures on the consumption of beer (see our note on the Chinese promise). Because of the country mix, we are expecting a regional price/mix to be down by 1.8%, but still allowing for an operating profit margin of 27% (from 26.3% last year).

Bloomberg	HEIA NA
Reuters	HEIN.AS
12-month High / Low (EUR)	85.2 / 56.8
Market Cap (EUR)	44,807
Ev (BG Estimates) (EUR)	55,894
Avg. 6m daily volume (000)	853.0
3y EPS CAGR	12.3%

	1 M	3 M	6 M	31/12/14
Absolute perf.	-2.9%	6.9%	14.2%	32.0%
Food & Bev.	-3.0%	6.7%	4.5%	15.2%
DJ Stoxx 600	-3.8%	2.5%	-7.0%	4.1%

YEnd Dec. (EURm)	2014	2015e	2016e	2017e
Sales	19,257	20,361	20,984	21,712
% change		5.7%	3.1%	3.5%
EBITDA	4,566	4,852	5,152	5,509
EBIT	3,129	3,415	3,659	3,917
% change		9.1%	7.2%	7.0%
Net income	1,758	2,083	2,287	2,487
% change		18.5%	9.8%	8.8%

	2014	2015e	2016e	2017e
Operating margin	16.2	16.8	17.4	18.0
Net margin	9.1	10.2	10.9	11.5
ROE	14.2	15.1	15.3	15.3
ROCE	7.7	9.0	9.6	10.3
Gearing	89.3	66.8	54.0	41.5

(EUR)	2014	2015e	2016e	2017e
EPS	3.05	3.62	3.97	4.32
% change	-	18.5%	9.8%	8.8%
P/E	25.5x	21.5x	19.6x	18.0x
FCF yield (%)	3.5%	5.5%	4.7%	5.3%
Dividends (EUR)	0.94	1.11	1.18	1.28
Div yield (%)	1.2%	1.4%	1.5%	1.7%
EV/Sales	3.0x	2.7x	2.6x	2.5x
EV/EBITDA	12.5x	11.5x	10.7x	9.7x
EV/EBIT	18.3x	16.4x	15.0x	13.7x



## VALUATION

- The fine-tuning of our numbers 2015 and beyond hardly changes our earnings forecasts (less than 1% plus or minus depending on the year). However, we are lowering again our long-term growth rate for the company to 3.3% from 3.6%. In our last update, we had increased it from 3.3% to 3.6% showing that a more bullish stance was still resulting in an overvalued stock and hence deserved a downgrade. Applying a long-term growth rate of 3.3% (1.3% volume growth based on our market by market analysis of growth potential and a 2% standard inflation rate) leads to a fair value of EUR80, which is 4% higher than the current share price.
- The stock is trading at 19.5x 2016 earnings which is in line with the average 2015 rating of 19.6x but is still significantly higher than the average 17.0x that the company traded over the past 5 years. At EUR68 (12% lower than the current share price), the stock would be trading at 17.0x 2016 numbers.

## NEXT CATALYSTS

- On 10 February, the company will report full year 2016 figures and will also give guidance for 2016 where we believe that the message is likely to be of a challenging macro-economic environment (Brazil, Nigeria, Russia) and with organic revenue growth below the 2015 level (we are expecting 2.7% organic revenue growth in 2016 compared to 3.9% in 2015).

EURm	FY2015e				FY2016e			
	Old	New	% chge	% Incr.	Old	New	% chge	% Incr.
Revenues	20,429	20,361	-0.3%	5.7%	21,127	20,984	-0.7%	3.1%
Europe ex. Russia, Belarus	10,199	10,297	1.0%	37.7%	10,199	10,297	1.0%	0.0%
Americas	5,094	5,071	-0.5%	9.5%	5,537	5,511	-0.5%	8.7%
Africa, Middle East & Eastern Europe	3,285	3,221	-1.9%	21.9%	3,383	3,253	-3.8%	1.0%
Asia Pacific	2,516	2,437	-3.2%	16.7%	2,692	2,607	-3.2%	7.0%
Head office	-665	-665	0.0%	47.3%	-684	-684	0.0%	3.0%
Operating profit	3,371	3,415	1.3%	9.1%	3,700	3,659	-1.1%	7.2%
Europe ex. Russia, Belarus	1,131	1,240	9.7%	45.5%	1,141	1,250	9.6%	0.8%
Americas	903	899	-0.5%	15.3%	1,082	1,077	-0.5%	19.8%
Africa, Middle East & Eastern Europe	728	689	-5.4%	5.2%	830	707	-14.8%	2.6%
Asia Pacific	679	658	-3.2%	19.6%	719	697	-3.2%	5.9%
Head office	-71	-71	0.0%	-454.0%	-72	-72	0.0%	1.0%
Non recurring items	-239	-239	0.0%	18.7%	-220	-220	0.0%	-7.8%
Operating profit margin	16.5%	16.8%			17.5%	17.4%		
Europe ex. Russia, Belarus	11.1%	12.0%			11.2%	12.1%		
Americas	17.7%	17.7%			19.5%	19.5%		
Africa, Middle East & Eastern Europe	22.2%	21.4%			24.5%	21.7%		
Asia Pacific	27.0%	27.0%			26.7%	26.7%		
Net interest	-440	-440	-0.1%	-9.9%	-376	-375	-0.2%	-14.7%
PBT	2,692	2,736	1.7%	12.1%	3,104	3,064	-1.3%	12.0%
Tax	-829	-841	1.5%	15.0%	-820	-809	-1.4%	-3.9%
Minority interests	-221	-221	0.0%	15.0%	-254	-254	0.0%	15.0%
Net profit	1,642	1,674	2.0%	10.4%	2,030	2,001	-1.4%	19.5%
Net profit - adjusted	2,050	2,083	1.6%	18.5%	2,315	2,287	-1.2%	9.8%
Number of fully diluted shares	576	576	0.0%	0.0%	576	576	0.0%	0.0%
Diluted EPS - adjusted	3.56	3.62	1.6%	18.5%	4.02	3.97	-1.2%	9.8%
Net dividend (EUR)	1.09	1.11	1.6%	18.3%	1.20	1.18	-1.2%	6.7%

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