12th February 2016

Luxury & Consumer Goods

adidas Group

Price EUR89.05

FV adjusted to EUR104 vs. EUR102 following a more upbeat FY16 sales guidance

Fair Value EUR104 vs. EUR102 (+17%) **BUY**

Bloomberg	ADS GY
Reuters	ADSG.F
12-month High / Low (EUR)	95.6 / 63.6
Market Cap (EURm)	18,631
Ev (BG Estimates) (EURm)	19,550
Avg. 6m daily volume (000)	1 198
3y EPS CAGR	19.7%

	1 M	3 M	6 M	31/12/15
Absolute perf.	4.4%	-0.8%	24.8%	-1.0%
Consumer Gds	-5.7%	-13.9%	-12.8%	-11.8%
DJ Stoxx 600	-10.8%	-19.8%	-22.9%	-17.0%

YEnd Dec. (EURm)	2014	2015e	2016e	2017e
Sales	14,534	16,864	18,226	19,470
% change		*16.0%*	*8.1%*	*6.8%*
EBITDA	1,205	1,452	1,631	1,851
Reported EBIT	961.0	1,065	1,212	1,403
% change		*10.8%*	*13.8%*	*15.7%*
Net income	490.0	644.2	809.3	942.4
% change		*31.5%*	*25.6%*	*16.4%*

	2014	2015e	2016e	2017e
Rep. EBIT margin	6.6	6.3	6.6	7.2
Net margin	3.4	3.8	4.4	4.8
ROE	8.7	12.0	15.5	16.4
ROCE	9.7	10.8	12.2	13.6
Gearing	3.3	17.1	26.3	19.5

(EUR)	2014	2015e	2016e	2017e
EPS	2.72	3.33	4.01	4.67
% change	-	*22.5%*	*20.2%*	*16.4%*
P/E	32.7x	26.7x	22.2x	19.1x
FCF yield (%)	0.6%	0.9%	2.6%	3.5%
Dividends (EUR)	1.50	1.60	1.85	2.15
Div yield (%)	1.7%	1.8%	2.1%	2.4%
EV/Sales	1.3x	1.2x	1.1x	1.0x
EV/EBITDA	15.6x	13.5x	12.3x	10.7x
EV/EBIT	19.6x	18.4x	16.5x	14.1x

The better-than-expected top line growth in Q4 (BG: +12%e FX-n vs. CS of 9-10%e) enabled ADS to achieve 10% FX-n over 2015, beating its own target of a high single-digit increase. Like in the first 9M, the main driver was adidas brand (+14%e in Q4 and +12% in 2015) thanks to strong double-digit growths in Western Europe, Greater China, MEAA and in Latin America. Against this solid performance, ADS expects this momentum to remain in 2016, hence the increased sales guidance (double-digit growth vs. high single-digit initially) whilst earnings targets are reiterated. We revise up our top line assumption by ~2pp (+3pp FX-n) which leads to our new FV of EUR104 vs. EUR102.

ANALYSIS

- **A strong end to the year at the top line level (+12%e FX-n).** By brand, **adidas** grew by 14% FX-n (in line with Q3) boosted by the "usual suspects" (i.e. Western Europe, Greater China, MEEA at Latin America). The double-digit growth achieved in **Latin America** was broad-based between Argentina, Colombia, Chile, etc. which have more than offset softer trends in Brazil. Trends have accelerated in **North America**, mainly driven by Lifestyle whilst the ramp up of U.S sport categories and Running will mostly play positively in 2016. **Reebok** registered its eleventh consecutive quarter of growth (+5%e) despite the ongoing rationalisation of the US outlet store network.

- **Golf: slight decline expected in Q4 but no worries (yet).** We anticipate 4% FX-n decrease for Q4, which might appear as a concern following the 6% increase in Q3 and in light of the 19% FX-n increase achieved by Callaway (product launches) over Q4 but we remember that at Q3 results conference call, management insisted that TaylorMade was now cautiously monitoring sell out trends to avoid any excess inventory. The golf division continues to restructure the business and we remind investors that the strategic review on the golf business should be completed by Q1 16.

- **Minor adjustments to our FY15 earnings estimates. Marketing efforts** appear to have accelerated further in Q4 since brand-building investments were up over 20% over 2015 (vs. +19% in the first 9M), which is justified by significant promotional campaigns in the US and to support the robust momentum in Lifestyle, particularly considering the launch of the fifth footwear franchise (NMD). This leads us to nudge down our FY15 EBIT forecast by 2%, representing a 6.5% adjusted operating margin (vs. 6.6% previously). As the group could not benefit from deferred tax assets from TMaG, it provoked this temporary higher-than-expected **tax rate** of 32.9% (CS at 32.2%), which should come back to more normative levels in 2016 (30-30.5%).

- **Implications on our FY16 assumptions.** Following the sales guidance increase yesterday (double-digit growth vs. high single-digit initially), we are now anticipating a 10% FX-n for 2016 vs. ~7% previously, partly offset by a more adverse FX headwind (~2%). We expect double-digit increases in Western Europe, Greater China and in MEAA whilst we remain more conservative with regards to North America (+8% vs. double-digit growth guided by ADS) and we anticipate 7% growth in Latin America thanks to the Summer Olympics in Rio and the other countries (Mexico, Argentina, Colombia, etc.). As for the profitability, the operating profit guidance was reiterated ("at least stable vs. 2015") since the GM headwinds (labour cost inflation, unfavourable USD hedging rates) will be compensated by a positive operating leverage.

VALUATION

- Whilst a positive momentum was partly anticipated by investors given a solid 2015 performance and ahead of two major sporting events occurring this year, they will now look closely at improvements made by adidas in North America which should be a key catalyst for the stock.

- Following a 2% adjustment to our FY16 sales assumption, we increase our FV to EUR104 vs. EUR102. Buy recommendation reiterated.

NEXT CATALYSTS

- adidas Group will release its FY15 Results on 3rd March 2016.

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