

Bayer

Price EUR98.97

What does Covestro say about 2016 exactly?

Fair Value EUR126 (+27%)

NEUTRAL

Bloomberg	BAY GY
Reuters	BAYG.F
12-month High / Low (EUR)	146.2 / 92.8
Market Cap (EURm)	81,843
Avg. 6m daily volume (000)	2 439

	1 M	3 M	6 M	31/12/15
Absolute perf.	-6.2%	-21.6%	-16.3%	-14.5%
Healthcare	-5.3%	-12.5%	-9.0%	-10.8%
DJ Stoxx 600	-1.9%	-13.1%	-8.2%	-9.3%

	2014	2015e	2016e	2017e
P/E	16.4x	14.8x	15.3x	13.9x
Div yield (%)	2.3%	2.4%	2.6%	2.7%

ANALYSIS

- For its first fiscal year as a stand-alone company, Covestro has released unsurprising results for its parent group Bayer, that will report its own FY numbers on Thursday. Sales came in at EUR12.08bn (BG: EUR12.09bn) whereas adjusted EBITDA was EUR1.64bn (or 13.6% of sales) slightly below our expectations (BG: EUR1.72bn, 14.2% and 8.3% in Q4 2015). Despite this small miss, we would say the difference was not very meaningful as the last quarter is always difficult to predict and much lower than previous ones. Volumes picked up compared to Q3 (+3.3% in Q4). That said, we would stress that the price impact was negative by 12.4%.
- Based on this strong negative price impact that is unlikely to be interrupted as we move into 2016, it is worrying to see management only committing itself to a mid-single-digit percentage increase in core volume growth since it makes the type of growth that can be expected for revenues in general very uncertain. Not only could prices drop by more than mid-single digits but the FX effect is likely to turn negative this year in contrast to the significant positive effect of 2015. With the consensus currently at EUR12.09bn for 2016 i.e. slightly above actual 2015 numbers, we see the risk of a downward revision by a few percentage points. As far as EBITDA is concerned, Covestro has given no specific guidance and reference to FCF is voluntarily vague in our view as it suggests higher levels than the average of previous years. Should the same apply to EBITDA and taking the last two years as a reference (three?), the average would be 11.9% (but 11.1% taking a three-year average) vs 13.6% in 2015. Assuming 12.5% is a good first estimate to assess what "above average" means, and based on sales of EUR12bn, this would equal EUR1.5bn whereas we and the consensus were expecting EUR1.7bn i.e. implying a more than 10% downward revision to implement.

VALUATION

- While Covestro remains a significant part of Bayer's sales and EBITDA (26% and 16% respectively), it is of course a much lower part of its valuation as it is now calculated separately to determine FV. As such disappointing guidance for Covestro should translate into a downward revision of numbers for Bayer but not necessarily into a meaningful change of FV and TP in the market, except if the Covestro share price is significantly impacted too.

NEXT CATALYSTS

- 25th February 2016: Bayer FY 2015 results

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Distribution of stock ratings

BUY ratings 72%

NEUTRAL ratings 0%

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