15th March 2016

Luxury & Consumer Goods

Safilo

Price EUR8.69

Heading in the right direction but the road is still long

Fair Value EUR12,5 vs. EUR14 (+44%) **BUY**

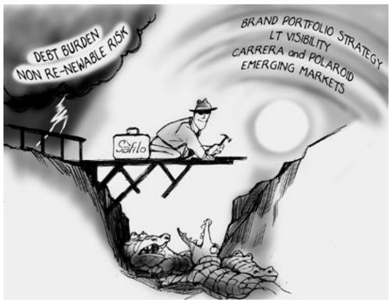
Bloomberg	SFL IM
Reuters	SFLG.MI
12-month High / Low (EUR)	15.1 / 7.4
Market Cap (EURm)	544
Ev (BG Estimates) (EURm)	724
Avg. 6m daily volume (000)	132.6
3y EPS CAGR	-9.9%

	1 M	3 M	6 M	31/12/15
Absolute perf.	13.0%	-12.8%	-20.2%	-18.9%
Consumer Gds	7.5%	0.4%	5.7%	-3.5%
DJ Stoxx 600	10.3%	-1.4%	-2.5%	-5.8%

YEnd Dec. (EURm)	2014	2015e	2016e	2017e
Sales	1,179	1,279	1,340	1,267
% change		*8.5%*	*4.7%*	*-5.4%*
EBITDA	111	82.4	114	97.6
EBIT	75.3	0.8	73.7	59.6
% change		*-98.9%*	*NM*	*-19.1%*
Net income	39.0	-52.3	40.2	34.6
% change		*NM*	*NS*	*-14.0%*

	2014	2015e	2016e	2017e
Operating margin	6.4	0.1	5.5	4.7
Net margin	3.3	-4.1	3.0	2.7
ROE	4.0	-5.6	4.1	3.4
ROCE	4.0	0.2	4.1	3.4
Gearing	16.8	19.2	14.1	10.2

(EUR)	2014	2015e	2016e	2017e
EPS	0.71	0.11	0.70	0.52
% change	-	*-84.5%*	*NM*	*-25.2%*
P/E	12.2x	78.4x	12.5x	16.7x
FCF yield (%)	NM	NM	4.6%	9.8%
Dividends (EUR)	0.10	0.13	0.16	0.20
Div yield (%)	1.2%	1.5%	1.8%	2.3%
EV/Sales	0.6x	0.6x	0.5x	0.5x
EV/EBITDA	6.4x	8.8x	6.0x	6.6x
EV/EBIT	9.4x	870.8x	9.3x	10.8x



At the analysts' meeting yesterday, Safilo reviewed the commercial reorganisation and transformation plan initiated in 2015. Although the measures are part of the 2020 Strategic Plan, they had a more painful impact than initially expected due to some headwinds (proprietary brands, Asia-Pacific). For 2016, further question marks remain (e.g.: relaunch of Carrera, normalisation in Asia-Pacific, Gucci transition), hence the 8% downward revision to our 2016 adj. assumptions, although we remain convinced that sales and earnings momentum will improve this year, thanks also to new catalysts (Givenchy, Swatch, Havaianas). FV reduced to EUR12.5 but Buy recommendation maintained.

ANALYSIS

- **Licensed brand PF (+15% FX-n) outperformed the proprietary brands (-2.5%).** Indeed this contraction partly explains the flat organic growth in 2015. The brand rebuild at **Carrera** (HSD decline) is proving to be more difficult than expected, especially in sunglasses (~50% of sales). **Polaroid** and **Smith** both posted low single-digit increases, the former suffering from distributor exits in China and Russia while the latter was hampered by the sluggish snow season in the US. Although it was only the first year of the Strategic Plan, this underperformance might cause concerns about the chances of reaching the 2020 target (proprietary brands to account for 40% of sales vs. 25% in 2014), especially since Safilo has welcomed four new licences over the past months.

- **Asia-Pacific: stabilisation expected for 2016 but visibility is still low.** Much of the 20.5% FX-n decrease in 2015 was a self-inflicted decline caused by the commercial and business reorganisation there. However the group was more sensitive to the market slowdown than Luxottica (+10% in Asia-Pacific excl. Australia, +15% in China) which cut prices by 10-15% in Q3 2015. **2016 outlook:** management confirmed that the reorganisation was complete and guided on a stabilisation even if he anticipates more challenging market conditions there, highlighting that visibility in this region is quite low.

- **Sunny outlook for the licensed brand PF.** Note that the 15% FX-n growth was broad-based between Dior, Fendi, Jimmy Choo and Céline (all of them grew DD), while Future Core (MaxMara, Hugo Boss, Kate Spade, etc.) increased low single-digit. Moreover, the new **Givenchy** license had a promising start to the year and this licence will alone offset the negative impact from the loss of Kering's three small licences. Safilo is ready to launch **Swatch** in April (first available at Solstice and in Swatch's own stores) and **Havainas** in H2 2016 (first in Brazil then global roll-out in 2017).

- **Transition year for Gucci:** in 2015, sales of the Gucci licence dropped double-digits (now less than 20% of group sales) and this trend will continue in 2016 as Kering Eyewear starts collecting orders from August '16 (US) and October '16 (RoW). We anticipated this decline but we might underestimate its impact on the group's performance if the momentum of proprietary brands does not accelerate in 2016, hence our more cautious organic growth forecast to ~5% vs. 6% previously.

- **Transformation projects weighed on 2015 margins, first signs of turnaround are for 2016.** Safilo already reaped fruits of its commercial reorganisation as the DSO reduction led to a positive inflow of EUR32.7m from NWC. The group has implemented numerous initiatives for a leaner and more efficient cost structure, and these are advancing according to plan (e.g.: five distribution centres are to be closed down in 2016 to 14, 2020 objective: six, integrated supply chain planning and *Eyeway* IT project, etc.) particularly weighed on the group's profitability in a context of a sales contraction at constant currency (= margin squeeze). **For 2016:** as a consequence of the 2015 performance and our more cautious 2016 LFL growth assumption, we are reducing our adj. EBITDA forecast by 7%. Yet it still implies 110pb improvement in the adj. EBITDA margin (to 9.1%) since some headwinds will gradually ease off such as obsolescence provisions or the FX impact (-70bp in 2015).

  Our 2016 reported EBITDA now factors one-off costs of EUR8m (total of EUR20m) relating to the cost-savings programme announced yesterday. The group expects cumulated savings of EUR25-30m by 2019, o/w EUR2-3m this year and EUR10-15m in 2017 (*see. graph overleaf*).

(Continued on next page)

VALUATION

- We appreciated the comprehensive review of 2015 achievements and the presentation of growth catalysts for 2016 but have reduced our FV to EUR12.5 vs. EUR14 to reflect adjustments to our 2016 assumptions in view of remaining question marks (rebound of Carrera, normalisation in Asia-Pacific and negative impact from the Gucci transition).
- Arguably, we upgraded our recommendation in order to play the first positive results of the initiatives implemented last year, but these were ultimately longer in coming. However we believe, like management, that top line and earning trends will improve this year, also driven by the four new licences (2016: Givenchy, Swatch, Havaianas / 2017: Elie Saab very limited volumes). We maintain our Buy recommendation.

NEXT CATALYSTS

- Safilo is due to release its Q1 2016 results on 10th May.

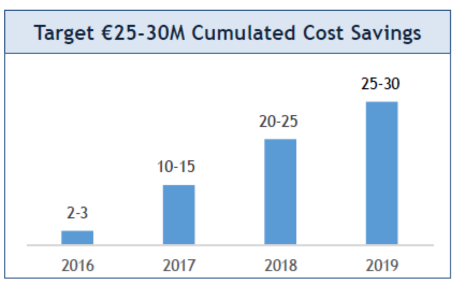
Table 1: "Going-forward" PF performance: breakdown between licensed and proprietary brands:

LICENSED BRANDS	NET SALES EVOLUTION +15%
FOUNDATION:	UP high double-digit
FUTURE CORE:	UP low single-digit
ROCKETS:	UP high double-digit

OWN CORE BRANDS	NET SALES EVOLUTION -2.5%
CARRERA:	DOWN high single-digit
POLAROID:	UP low single-digit
SMITH:	UP low single-digit

Source: Company Data

Table 2: Cost-savings target of the overhead productivity plan



Source: Company Data

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Analyst:
Cédric Rossi
33(0) 1 70 36 57 25
crossi@bryangarnier.com

Analyst Consumer Team:
Nikolaas Faes
Loïc Morvan
Antoine Parison
Virginie Roumage

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London
Beaufort House
15 St. Botolph Street
London EC3A 7BB
Tel: +44 (0) 207 332 2500
Fax: +44 (0) 207 332 2559
Authorised and regulated by the Financial Conduct Authority (FCA)

Paris
26 Avenue des Champs Elysées
75008 Paris
Tel: +33 (0) 1 56 68 75 00
Fax: +33 (0) 1 56 68 75 01
Regulated by the Financial Conduct Authority (FCA) and the Autorité de Contrôle prudential et de resolution (ACPR)

New York
750 Lexington Avenue
New York, NY 10022
Tel: +1 (0) 212 337 7000
Fax: +1 (0) 212 337 7002
FINRA and SIPC member

Geneva
rue de Grenus 7
CP 2113
Genève 1, CH 1211
Tel +4122 731 3263
Fax+4122731 3243
Regulated by the FINMA

New Delhi
The Imperial Hotel
Janpath
New Delhi 110 001
Tel +91 11 4132 6062
+91 98 1111 5119
Fax +91 11 2621 9062