

25th April 2016

Healthcare

Bayer

Price EUR110.30

Covestro's strange Q1: sales light, earnings good and cash flows down!

Fair Value EUR110 (0%)

NEUTRAL

Bloomberg	BAY GY
Reuters	BAYG.F
12-month High / Low (EUR)	138.4 / 92.8
Market Cap (EURm)	91,212
Avg. 6m daily volume (000)	2 448

	1 M	3 M	6 M	31/12/15
Absolute perf.	6.4%	4.5%	-1.2%	-4.7%
Healthcare	5.6%	-1.7%	-4.7%	-7.4%
DJ Stoxx 600	2.4%	3.0%	-5.8%	-4.7%

	2015	2016e	2017e	2018e
P/E	16.0x	15.2x	13.8x	12.9x
Div yield (%)	2.3%	2.4%	2.4%	2.5%

ANALYSIS

- A day earlier than its parent group Bayer, Covestro has released first-quarter results this morning that are actually substantially different to what we had included in our estimates for Bayer.
- At EUR2.875bn, sales were down 6% i.e. a couple of points worse than we had anticipated, on the back of a sharp 10.5% decline in prices during the period, which was especially reflected in the Polyurethanes business that was down 9.7% in the quarter.
- But actually, the real surprise came from the rest of the release with earnings and margins coming out very strong despite the difficult context. EBITDA increased 22% to EUR508m and EBIT by 65% to EUR340m. No proceeds artificially impacted first-quarter numbers this year whereas in the reference quarter in 2015 negative EUR45m and EUR23m one-offs lowered the respective EBITDA and EBIT numbers.
- If we stop here our comments would be very positive, but operating cash flows during the quarter decreased 33% to EUR124m and Covestro highlighted a significant increase in cash tied up in working capital (and also higher tax payments). In the balance sheet, we do not see high inventories or issues with trade accounts receivable but maybe more with trade accounts payable.
- In the end, free cash flows decreased from EUR90m to EUR77m and that is what really matters.

VALUATION

- Covestro's contribution to Bayer's earnings is set to be pretty good and we see a EUR0.10 positive impact on our estimated core EPS in Q1 from Covestro's actual numbers. Our core EPS for Bayer in Q1 now stands at EUR2.21 whereas the consensus expects EUR2.15.

NEXT CATALYSTS

- Tomorrow 26th April 2016 : First-quarter results

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Distribution of stock ratings

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NEUTRAL ratings 0%

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