

Cappgemini

Price EUR78.58

Q1 16 conference call feedback: more confidence in revenues and margins

Fair Value EUR96 vs. EUR90 (+22%)

BUY

Bloomberg	CAP FP
Reuters	CAPP.PA
12-month High / Low (EUR)	90.2 / 69.0
Market Cap (EUR)	13,530
Ev (BG Estimates) (EUR)	14,561
Avg. 6m daily volume (000)	665.1
3y EPS CAGR	11.5%

We reiterate our Buy rating and increase our DCF-derived Fair Value to EUR96 from EUR91 following yesterday's conference call. This factors in the increase in our adj. EPS ests. by 1-2% on fx (+EUR1) and our medium-term lfl sales growth assumption to 5% from 4% (+EUR5) as management reiterated its +5-7% target for 2018 or 2019. As synergies with Igate are delivered ahead of schedule, we expect Cappgemini to be able to reach the top-end of the FY16 margin guidance range (11.1-11.3%) at least.

ANALYSIS

	1 M	3 M	6 M	31/12/15
Absolute perf.	-2.5%	-7.0%	-4.5%	-8.2%
Softw. & Comp.	-0.5%	-0.5%	1.1%	-3.8%
DJ Stoxx 600	3.6%	2.4%	-7.6%	-5.1%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	11,915	12,743	13,202	13,707
% change		6.9%	3.6%	3.8%
EBITDA	1,577	1,721	1,853	1,979
EBIT	1,022	1,231	1,373	1,499
% change		20.4%	11.5%	9.2%
Net income	798.7	940.5	1,032	1,123
% change		17.8%	9.8%	8.8%

	2015	2016e	2017e	2018e
Operating margin	10.6	11.3	12.0	12.4
Net margin	9.4	6.0	6.5	6.9
ROE	16.3	10.3	10.7	11.0
ROCE	17.2	12.8	14.3	15.9
Gearing	25.3	13.9	2.3	-8.5

(EUR)	2015	2016e	2017e	2018e
EPS	4.66	5.44	5.93	6.45
% change	-	16.9%	9.0%	8.8%
P/E	16.9x	14.4x	13.3x	12.2x
FCF yield (%)	6.1%	6.6%	7.4%	7.9%
Dividends (EUR)	1.35	1.50	1.60	1.70
Div yield (%)	1.7%	1.9%	2.0%	2.2%
EV/Sales	1.3x	1.1x	1.0x	0.9x
EV/EBITDA	9.7x	8.5x	7.4x	6.5x
EV/EBIT	12.1x	10.1x	8.7x	7.5x

• **A bit more confidence in revenues, medium-term target reiterated.** While confirming 2.5-4.5% lfl growth guidance for 2016, management is a bit more confident in revenue trends, based on very solid demand for Digital & Cloud, while service automation helps gain market share. Management considers Cappgemini should be close to the middle of the range in H1, which implies nearly +4% lfl in Q2. For the medium-term (2018 or 2019), it is reiterating its 5-7% lfl growth target. France had a good start in Q1 (+2% lfl, driven by +6% in Application Services) and is expected to accelerate further in Q2. The UK posted positive lfl growth despite the fall in government-related revenues thanks to double-digit growth in commercial sectors, and is expected to grow over the full-year. North America was up 3.1% lfl including Energy & Utilities, but the latter (14% of regional revenues) was down in strong double-digits, and will not improve before H2. In the Rest of Europe region, Benelux was down slightly, but Cappgemini saw double-digit growth in Germany and Italy and mid-single digit growth in Nordic countries. Finally, Asia Pacific was up double-digit and Latin America shrunk in Q1, will keep declining in Q2 but may get stabilise in H2 as comps will be easier.

• **More optimism on margins.** Cappgemini reiterated op. margin guidance for 2016 (11.1-11.3%) but is more optimistic since synergies with Igate are being delivered ahead of schedule. Management admits this will have some impact on the margin. The integrated businesses and P&Ls are fully up and running, and 90% of the merger of legal entities should be complete by end 2016. The 0.3ppt headwind from growth investments to the FY16 margin has been reiterated, but the impact will be lower for H1 (-0.2ppt) than for H2. Despite the strong demand of digital and cloud skills, wage inflation is not a particular issue, and it is still 7-8% offshore, in line with the last 3-4 years. The offshore headcount was up 3.3% vs. end 2015, while onshore was down 1.1%. The offshore leverage of 55% reached 35% in Continental Europe, 60% in the UK, and 72% in North America, and this helps Cappgemini increasing its competitiveness. Finally, investments in service automation continue, especially in Infrastructure Services and Business Services (BPO+ITOPS), while IBM Watson artificial intelligence will be used to manage the demand and supply for people staffing.

• **Bigger acquisitions to resume, but not before H2.** Cappgemini intends to keep acquiring small companies like Oinio and Fahrenheit 212 in Digital & Cloud - other small deals of 50-100 staff are expected in Q2 and/or later this year. As private equity funds and stock markets are less hungry for high valuations, the company is more keen on acquiring bigger targets - several hundreds of million euros or more, but definitely not of the same size as Igate - with North America as the main priority -, but not before H2, once the bulk of the integration of Igate is complete.

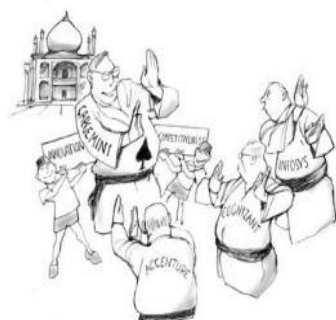
VALUATION

- Cappgemini's shares are trading at est. 10.1x 2016 and 8.7x 2017 EV/EBIT multiples.
- Net debt on 31st December 2015 was EUR1,747m (net gearing: 25%).

NEXT CATALYSTS

- AGM on 18th May. Capital Markets day on 1st June in Munich (Germany).
- H1 results on 27th July before markets open.

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