7th April 2016

Sector View

# Consumer

## Q2 16 TOP PICKS: we continue with Essilor and Ahold

| | 1 M | 3 M | 6 M | 31/12/15 |
|---|---|---|---|---|
| Pers & H/H Gds | -0.2% | 1.3% | 2.9% | -1.5% |
| DJ Stoxx 600 | -2.1% | -6.2% | -3.8% | -8.6% |

*Stoxx Sector Indices

**Companies covered**

| | | |
|---|---|---|
| ADIDAS GROUP | BUY | EUR108 vs. 104 |
| BEIERSDORF | NEUTRAL | EUR80 vs. 82 |
| BIC | NEUTRAL | EUR119 vs.122 |
| CHRISTIAN DIOR | BUY | EUR175 vs 177 |
| ESSILOR | BUY | EUR130 vs. 132 |
| GRANDVISION | BUY | EUR28 vs. 29 |
| GROUPE SEB | BUY | EUR102 vs.105 |
| HERMES Intl | BUY | EUR355 vs.360 |
| HUGO BOSS | NEUTRAL | EUR80 vs. 87 |
| KERING | NEUTRAL | EUR176 vs. 180 |
| L'OREAL | BUY | EUR177 vs.182 |
| LUXOTTICA | BUY | EUR61 vs. 63 |
| LVMH | BUY | EUR177 vs.182 |
| PRADA | NEUTRAL | HKD37 vs. 41 |
| RICHEMONT | BUY | CHF81 |
| SAFILO | BUY | EUR12 vs. 12.5 |
| SALVATORE FERRAGAMO | BUY | EUR25.8vs.26.5 |
| THE SWATCH GROUP | NEUTRAL | CHF410 vs. 420 |
| TOD'S GROUP | NEUTRAL | EUR78 vs.82 |
| | | |
| AB INBEV | NEUTRAL | EUR109 vs 111 |
| DANONE | BUY | EUR70 vs. 71 |
| CAMPARI | BUY | EUR9.3 vs. 9.4 |
| CARLSBERG | SELL | DKK500 vs. 520 |
| DIAGEO | NEUTRAL | 1790p |
| HEINEKEN | BUY | EUR79 vs. 83 |
| NESTLE | NEUTRAL | CHF72 vs. 73 |
| PERNOD RICARD | BUY | EUR113 |
| REMY COINTREAU | BUY | EUR72 |
| SABMILLER | NEUTRAL vs. BUY | 4400p |
| MOLSON COORS | NEUTRAL vs. BUY | USD97 vs 101 |
| | | |
| AHOLD | BUY | EUR21 |
| CARREFOUR | BUY | EUR31 |
| CASINO GUICHARD | BUY | EUR69 |
| DELHAIZE | BUY | EUR94 |
| DIA | NEUTRAL | EUR7.5 |
| JERONIMO MARTINS | NEUTRAL | EUR13.5 |
| METRO AG | SELL | NOK24 |
| RALLYE | BUY | EUR18.5 |
| TESCO | NEUTRAL | 166p |

### LOOKING BACK ON Q1 2016

Our **Consumer** "Top Picks" report encompasses all our global Consumer franchises: **Luxury**, **Consumer goods**, **Retail** and **Food & Beverages**. In Q1 16, our Consumer stocks sample delivered a very modest global performance (+0.5%), but nevertheless outperformed the DJ Stoxx index by 7%.

**Luxury goods stocks** share price remained almost unchanged during the period but **Prada** rebounded by 5.5%, whilst **LVMH** was up 4% (+13% vs DJ Stoxx) and even **Ferragamo** (+3%) which can appear as a great performance with the challenging luxury goods industry environment (still poor activity in HK, negative impact of the attacks in November in Paris and in Brussels on 22nd March for tourists flows in Europe). **Tod's** (-14%) and **Hugo Boss** (-25%) were the worst performers amongst the sample, the HB share price has suffered from the PW on 2016 outlook and the departure of the CEO last February.

Our **Optical & Eyewear sample** was impacted by profit-takings after the strong run over 2015 and disappointments with the profitability outlook as the four groups are spending significant capex investments to achieve a sustainable MT growth, which is particularly true for **Safilo** (-27%). **Luxottica** (-20%) was heavily impacted by the surprising departure of CEO for Markets Adil Khan last February, raising concerns about the governance structure and the succession plan on which Mr Del Vecchio is currently working on. **GrandVision** (-9%) and **Essilor** (-6%) resisted quite well, confirming their defensive profiles in a volatile environment.

Within the **HPC/Consumer Goods** sample, we highlight the **adidas** share price rally (+15%), fuelled by strong momentum, a supportive 2016 outlook and the appointment of Mr Rorsted as CEO from October. **SEB** remained broadly flat (-4%) whilst **BIC** (-13%) was impacted by conservative 2016 guidance. It is worth noting the outperformance of **L'Oréal** (+1%) vs. **Beiersdorf** (-6%).

**Food & Beverages**, in Q1 2016, with a global 1% increase, our Food & Beverages sample has outperformed the DJ Stoxx by almost 9%. The top three were **Campari** (+19% vs DJ Stoxx), **SAB Miller** (+13.3%), and **Molson Coors** (+11%). **Danone**, with a slight 0.4% increase, has outperformed DJ Stoxx by 9%. On the other hand, **Nestlé** has only outperformed the index by 4%.

Lastly, it is worth noting the clear rebound of our **Retail** sample (+3%) thanks to Casino which did very well (+19%) after several quarters of underperformance. Ahold and Delhaize were also very resilient during the period (close to +2%), but Carrefour was down 9%.

### WHAT WE SEE FOR Q2 2016

**With regards to luxury groups,** we remain cautious on the Q1 1 publications at least concerning the organic sales growth performances. Following the terrorist attacks in Paris on November 13th and the one in Brussels on March 22nd, activity in Paris for luxury goods brands has not recovered the levels pre-attacks and we argue that the trend has even likely recently deteriorated (Brussels impact) while since January 2016, the trend was progressively improving. On average, France accounts for 7% of the luxury goods industry and Paris alone 5%, being the world's second biggest city for the sector after NY (10%). It also appears that the situation is not improving in Hong Kong and in Macau (double digits sales decline) while it is normalizing in Mainland China (close to 10% Luxury Goods sales). In others Asia countries, the momentum is well oriented, particularly in Korea and Singapore, as it is also the case in Japan thanks to local consumers and Chinese tourists. On the other hand, revenues momentum in US is somewhat deteriorating (negative impact of strong USD for tourist's flows, despite recent weakness, poor financial markets and US elections to come…). Ahead of Q1 sales release, we are cautious, and anticipate some slowdown vs Q4 15. For instance, LVMH Q1 sales should be up close to 4% vs +5% in Q4 15 (+2% for F&L vs +3% in Q4 15) and Kering revenues should grow 5.8% organically vs +8% with Gucci at almost the same trend than in Q4 (+4.8% despite very undemanding comps (-8% in Q1 15).

**Food retail sector** remains penalised by the deflationary wave in Europe. This trend exacerbates a more fundamental issue which is the dilution of the growth potential in a fixed costs industry (structurally, the environment is that of a sluggish demography, deflation and very high penetration rate of modern food retail). So far, we do not foresee any reversing trend in 2016: 1/ deflation is still there in several major markets (France and UK especially) while 2/ there is no obvious thinning on the horizon in emerging markets (Brazil especially).

**Food & Beverages**: This is likely not to be the best quarter of all for the food and spirits companies in terms of organic sales growth. Their performance should be dragged down by the tough macro background in emerging countries (especially China and Brazil) and a number of technical effects. One exception is Rémy Cointreau which is likely to report an improving performance in its last fiscal quarter,

with organic sales expected to be up 7.6% after +3.2% in Q3.

**Consumer Groups: some opportunities after Q1 publications…** Indeed **GrandVision** faces a difficult comparison base in Q1 given successful promotional campaigns in G4 last year (SSSG: +6.8%), but we are convinced that this stock share numerous catalysts with Essilor and has an interesting defensive profile. **Luxottica** has already insisted on the tough comparison base this quarter. As this negative base effect is included in FY16 rule-of-thumbs, it implies a clear improvement in the sales and earnings momentum afterwards. **adidas Group**'s Q1 results will be marked by a strong top line performance and even if the USD and higher input costs hamper the profitability, the risk profile improves. <u>Hence we nudge down our beta assumption (5-yr average), justifying our slight increase in our FV to EUR108.</u>

## CONCLUSIONS AND TOP PICKS: Essilor and Ahold once again

**Consumer Goods: Essilor (Buy, FV: EUR130) reiterated.** We continue to favour **Essilor** since we have not identified major threats ahead of the Q1 publication, unlike Luxottica and GrandVision which cope with challenging comparison bases. The visibility remains good as we expect another slight LFL growth acceleration (BG: +5% in 2016 vs. +4.6% in 2015) supported by innovation, marketing campaigns and emerging markets (we are more cautious on Brazil). The market is now aligned with the group's prudent contribution margin outlook ("at least 18.8%" vs. 18.8% in 2015), leaving a limited downside risk for the remainder of the year. ***Next publication:*** *Q1 16 Sales on 21st April.*

**Food Retailing:** Against the sector backdrop, size provides a key asset for large players which can dilute fixed costs over a far denser store network and obtain additional ammunition for nurturing their price and non-price competitiveness (for as long as productivity gains are wisely reinvested back into the value proposition). In that respect, **Ahold** (Buy, FV: EUR22) and **Delhaize**, which are to merge in mid-2016, appear to be the best compromise within the sector as they are getting bigger. Moreover, both have: 1/ a very limited exposure to the emerging markets/forex together with a strong footprint in US (between 60% and 75% of the groups' respective EBIT); and 2/ a higher-than-average profit-to-cash conversion, we keep Ahold in our Top Picks list for Q2 2016, which, objectively, is to take the lead.

**Food & Beverages**: Regarding brewers, on the back of the changed BG research risk free rate and risk premium, we are lowering our DCF-based FV for brewers stocks (see table on page 1). For SABMiller the FV of GBp4,400 is driven by the ABI offer price and remains unchanged. As a result of these FV adjustments we have limited upside for the brewers. AB InBev Heineken and Molson Coors are trading at FV, SABMiller has an upside of 3% to FV and Carlsberg has a significant downside, in our view. Following on from that we lower our recommendation for SABMiller to Neutral (from Buy) and for Molson Coors to Neutral (from Buy). Although there is no upside to FV for Heineken shares and that's why we do not put it in our top pick list, we believe this stock is still worthwhile buying. Organically the company is growing well with last year delivering 3.5% organic sales growth. But on top of that HEIA is most likely to be the next brewer to make a significant acquisition. And acquisitions are the big value creator (or destructor in some cases) in the sector. With deals like FEMSA Cerveza and Asia Pacific Breweries, Heineken's recent acquisition track record has been good. Furthermore with net debt/EBITDA of 2.2xe at end of 2016, the company has the capability to gear up. If external growth opportunities would not come along, we can expect, Heineken to start buying back to 20% that FEMSA has in the company. FEMSA has always made it clear that although it is a happy shareholder of Heineken, the stake could be sold if an opportunity in its retail and bottling business would arrive. We neither chose a top pick in the sample of spirits and food stocks as the groups' releases should show a subdued performance in Q1. We think that the improving organic sales growth of Rémy Cointreau is partly already factored into market expectations.

**Luxury Goods:** Again we do not include any Luxury goods stocks this quarter. The visibility remains poor ahead of Q1 16 publications, as the situation in Europe has certainly deteriorated vs Q4 15 while the environment remains tough in H-K and Macau.

## NEXT CATALYSTS

- **Luxury Goods: LVMH** (Q1 sales) on April 11 and **Kering** (Q1 sales) on April 21st.
- **Consumer Goods (April): Essilor** (Q1 sales) on 21st / **BIC** (Q1 Results) on 27th / **SEB** (Q1 Sales) on 28th / **GrandVision** (Q1 Trading update) on 29th / **Luxottica** (Q1 Results) on 29th.
- **Food & Beverages: Nestlé** (Q1 16 sales) on Apr 14th**, Rémy Cointreau** (Q4 16 sales) on Apr 19th, **Danone** (Q1 16 sales) on Apr 19th**, Heineken** (Q1 16 sales) on Apr 20th, **Pernod Ricard** (T3 16 sales) on Apr 21st, **SAB** (Q4 16 sales) on Apr 21st**, ABI** on May 4th (Q1 16 results), **Campari** (Q1 16 results) on May 9th, **Carlsberg** (Q1 16 sales) on May 11th

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| | |
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