

Bayer

Price EUR96.42

Interested in buying Monsanto: Never say never!

Fair Value EUR110 (+14%)

NEUTRAL

Bloomberg	BAY GY
Reuters	BAYG.F
12-month High / Low (EUR)	137.8 / 92.8
Market Cap (EURm)	79,734
Ev (BG Estimates) (EURm)	96,910
Avg. 6m daily volume (000)	2 585
3y EPS CAGR	6.4%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-9.5%	-2.6%	-22.3%	-16.7%
Healthcare	-2.4%	1.2%	-11.3%	-10.3%
DJ Stoxx 600	-1.9%	2.6%	-11.0%	-7.7%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	46,325	45,860	47,452	49,008
% change		-1.0%	3.5%	3.3%
EBITDA	10,275	10,653	11,169	11,755
EBIT	8,851	9,274	9,752	10,291
% change		4.8%	5.1%	5.5%
Net income	5,687	5,827	6,399	6,852
% change		2.5%	9.8%	7.1%

	2015	2016e	2017e	2018e
Operating margin	19.1	20.2	20.6	21.0
Net margin	12.3	12.7	13.5	14.0
ROE	25.6	22.9	22.7	21.8
ROCE	11.6	12.4	13.1	13.9
Gearing	71.0	51.8	35.6	20.9

(EUR)	2015	2016e	2017e	2018e
EPS	6.88	7.05	7.74	8.29
% change	-	2.5%	9.8%	7.1%
P/E	14.0x	13.7x	12.5x	11.6x
FCF yield (%)	5.4%	7.5%	8.1%	8.6%
Dividends (EUR)	2.50	2.60	2.70	2.80
Div yield (%)	2.6%	2.7%	2.8%	2.9%
EV/Sales	2.2x	2.1x	2.0x	1.8x
EV/EBITDA	9.8x	9.1x	8.4x	7.6x
EV/EBIT	11.3x	10.4x	9.6x	8.7x

By way of press release, Monsanto and Bayer have confirmed preliminary discussions for a negotiated acquisition of the leading seeds company by Bayer. Monsanto is currently reviewing the non-binding proposal received and no further comment will be made until it is completed. We did not believe the rumour last week about this combination – and we were wrong. If consumated, it would create by far the leading company in Crop Sciences and, subject to divestments, this division would represent half of Bayer's total revenues. This is consistent with Bayer's strategy to grow in seeds and to be a life sciences company, but we did not assume that the mix could be so strongly balanced between human health and crop sciences. We would stay very neutral.

ANALYSIS

- Never say never. We must say that we did not believe in the rumours last week that Bayer may be interested in discussing a combination with Monsanto. It looked too big both from a financial perspective and afterwards for the question of balance between the two big activities within the group i.e. human health and crop sciences.
- But it was indeed very true and both companies have stated publicly that Bayer has initiated discussions with Monsanto about a proposed combination. Monsanto's Board of Directors is currently reviewing the unsolicited and non-binding offer made by Bayer and no further comments will be made until the process is completed.
- Monsanto achieved USD15bn in net sales in 2015 o/w USD10.2bn in the so-called seeds and genomics segment. This compares with sales of USD11.5bn achieved by Bayer CropSciences last year, with seeds representing only a small part although a very dynamic one (SeedGrowth was up 5.4% in Q1 and Seeds 11.9% in a division only up by 1%). For quite some time, Bayer made it clear that it wanted to grow especially within this segment of the Agrochemical business.
- At the end of the previous fiscal year, Monsanto had initiated a restructuring programme (at a cost of USD850-900m) to improve productivity and introduce additional operational discipline within the organisation with a target of USD275-300m of cost savings over two years. That said, EBITDA margin was already at a very high level of 32.5% in 2015, well ahead that of Bayer in Crop Sciences (23.3%) and actually even superior to that of Bayer in Life Sciences (25%). So a combination would not be dilutive margin-wise even before synergies.
- That said, an acquisition of Monsanto would represent a bid of circa USD40bn, excluding the existing USD5bn of net debt of Monsanto at the end of the previous fiscal year. Bayer had already EUR18bn in net debt at the end of 2015 and although corporates raise money easily and at a low interest rate, gearing would exceed 2x (although we might expect Bayer to have included paper in its offer and not only cash). No doubt Bayer could consider selling the rest of its stake in Covestro (less than USD5bn) and may be some smaller assets and may also have to divest some of Monsanto's assets to get antitrust approvals, but the bill is high.

VALUATION

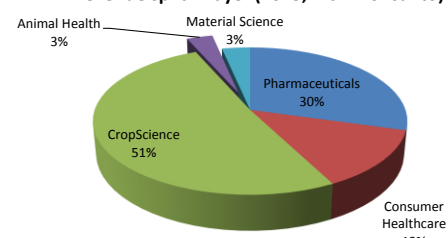
- Based on the product/franchise mix shown on the left, Bayer will no doubt be approached differently by the investment community. How much would it have to be compared with other pharmaceutical companies? Because the market and ourselves are questioning the pharma pipeline of Bayer and would expect the group to make acquisitions to strengthen it, this acquisition looks preventive to any further significant deal, which is not very good.
- That said, Bayer's share price has already suffered a lot in the recent past and P/E ratio may even appear attractive, so we would not suggest more than a cautious neutrality on the stock.

NEXT CATALYSTS

- Coming days: next step in the discussions between Bayer and Monsanto

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Revenue split - Bayer (2015, incl. Monsanto)



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