27th May 2016

Sector View

Business services

TIC : Worth being selective (full report published today)

	1 M	3 M	6 M	31/12/15
Inds Gds & Svs	1.2%	8.7%	-3.8%	1.8%
DJ Stoxx 600	0.5%	5.2%	-9.2%	-4.6%

*Stoxx Sector Indices

Companies covered			
BUREAU VERITAS		**NEUTRAL**	**EUR22**
Last Price	EUR19.425	*Market Cap.*	EUR8,586m
SGS SA		**BUY**	**CHF2400 vs.2150**
Last Price	CHF2152	*Market Cap.*	*CHF16,833m*
EUROFINS		**SELL**	**EUR340**
	COVERAGE INITIATED		
Last Price	EUR345.7	*Market Cap.*	*EUR5,317m*

Although the TIC market's medium/long-term outlook remains very positive, the short-term is a bit more challenging since no longer underpinned by the super cycle in commodities. Between the two main leaders, we confirm our hierarchy anticipating short-term outperformance from SGS (Buy) with a FV upgraded to CHF2,400 vs. Bureau Veritas (Neutral). Regarding Eurofins, the valuation reflects the strong operating performance and ambitious management but leaves no room for disappointment. At the current share price (not far from all-time high) we recommend taking profits and are initiating coverage with a Sell recommendation based on a FV of EUR340.

- **The fundamentals remain positive.** The huge TIC market is estimated at EUR200bn, o/w EUR80bn is addressable. As estimated by MarketsandMarkets, the outsourced market should grow by a 5% CAGR over 2015-2020 supported by structural drivers i.e. globalization which requires standards, scandals in sanitary and outsourcing potential notably in Greater China. Market consolidation is continuing with significant M&A activity by the leading companies.
- **Short-term more challenging for the two leaders ….** Mainly due to the weakness of commodity-related activities and no new short-term growth drivers to bridge the situation, growth is currently under pressure. This is the case for the two leaders with nevertheless a much better operating performance at **SGS** (lfl growth at least 2.5% in H1e) compared to **Bureau Veritas** (-0.6% in Q1).
- **…while Eurofins continues to report strong performance.** With no presence in commodities, Eurofins is the only one of the four major quoted companies which hasn't been impacted. In fact, Q1 revenue was up over 10% after a strong Q4 and Q3 2015 and we are anticipating 8% in 2016.
- **Valuation historically high.** All the companies are trading at high multiples based on strong long-term organic growth, positive M&A impacts and margin resilience (17.5x 2016e EV/EBIT for SGS, 13x for BVI and 20.2x for Eurofins). Taking into account each operator's short term challenges and perspectives, we confirm our Buy recommendation on **SGS** with a FV upgraded to CHF2,400 and our Neutral on **BVI** with EUR22. We initiate **Eurofins** at Sell with a FV of EUR340 due to the high valuation (justified) which leaves no room for disappointment concerning lfls and the EBITDA margin improvement; and a potential capital increase that cannot be ruled out.
- **EUROFINS SCIENTIFIC : (SELL, FV EUR340)**

  In the TIC sector, Eurofins focuses on testing with no inspection or certification activity unlike the other companies we follow. As the worldwide no.6 in terms of revenue, the group has a strong presence in food testing and now also in pharma and clinical diagnostics but no presence in commodities. The growth strategy is the same as the other players, split between organic growth and M&A, in which the group is particularly active. The current valuation with high multiples, reflecting a strong market track record and ambitious management, leaves no room for disappointment (lfl growth, M&A strategy in view of the group's financial constraints, EBITDA margin improvement).

- **SGS : (BUY, FV CHF2400 vs. 2150)**

  The strong re-rating, especially after the FY results publication in mid-January, confirms the group's cost flexibility in an environment lacking visibility (stock price up c.9% ytd in absolute terms, outperforming the DJ Stoxx in Euro by 17.5%). Although the "old" main growth sectors, i.e. Oil, Gas and chemicals, Minerals and Industrial services are not delivering at the moment, we nevertheless understand after our contact with the company that current trading is much better than for Bureau Veritas in all segments. Taking into account this situation, lfl revenue growth in H1 should be in line with the FY 2016 guidance (between 2.5% and 3.5%) and the top of the range seems now reachable for the full year. We upgrade our lfl revenue growth, maintaining a flat adjusted operating margin vs. last year at 16.1%. Our FV moves to CHF2,400 from CHF2,15**0.**

- **BUREAU VERITAS : (BUY, FV EUR22)**

  The TIC market's medium/long-term outlook remains very positive even if market growth is less sustained by trade globalisation, which has matured, or the super cycle in commodities. Moreover, Bureau Veritas is engaging in growth initiatives which should bring in at least 4% organic growth CAGR in the next five years even if we assume no market growth. Nevertheless, the short term is under pressure with a lack of visibility in some businesses and organic growth turning negative in Q1 2016 as expected but at a higher pace. Due to this situation with no improvement expected in Q2 and the lack of visibility due to macro-economic uncertainties, the share price should continue to be volatile.

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Stock rating

BUY	Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
NEUTRAL	Opinion recommending not to trade in a stock short-term, neither as a BUYER or a SELLER, due to a specific set of factors. This view is intended to be temporary. It may reflect different situations, but in particular those where a fair value shows no significant potential or where an upcoming binary event constitutes a high-risk that is difficult to quantify. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

Distribution of stock ratings

BUY ratings 72%　　NEUTRAL ratings 0%　　SELL ratings 28%

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