12th May 2016

Food retailing

DIA

Price EUR4.83

Q1 2016 (first take): it may be psychological, but still negative LFL in Iberia (-0.3% LFL)

Fair Value EUR6,5 (+35%) **NEUTRAL**

Bloomberg	DIA.SM
Reuters	DIA MC
12-month High / Low (EUR)	7.6 / 4.4
Market Cap (EURm)	3,005
Ev (BG Estimates) (EURm)	4,137
Avg. 6m daily volume (000)	4 113
3y EPS CAGR	8.1%

	1 M	3 M	6 M	31/12/15
Absolute perf.	5.6%	-2.0%	-17.5%	-11.3%
Food Retailing	-3.8%	2.5%	-7.7%	-1.6%
DJ Stoxx 600	1.3%	6.7%	-10.6%	-8.1%

YEnd Dec. (EURm)	2014	2015e	2016e	2017e
Sales	8,011	8,926	8,876	9,430
% change		*11.4%*	*-0.6%*	*6.2%*
EBITDA	585	610	628	686
EBIT	323.9	274.1	379.0	426.9
% change		*-15.4%*	*38.3%*	*12.7%*
Net income	262.4	254.1	271.3	310.6
% change		*-3.1%*	*6.8%*	*14.5%*

	2014	2015e	2016e	2017e
Operating margin	5.0	4.4	4.8	5.1
Net margin	3.3	2.8	3.1	3.3
ROE	NM	NM	NM	NM
ROCE	32.2	22.5	21.6	22.3
Gearing	141.3	361.8	221.3	143.4

(EUR)	2014	2015e	2016e	2017e
EPS	0.41	0.42	0.45	0.52
% change	-	*3.1%*	*7.2%*	*14.5%*
P/E	11.8x	11.5x	10.7x	9.4x
FCF yield (%)	1.7%	NM	6.8%	9.3%
Dividends (EUR)	0.18	0.19	0.20	0.21
Div yield (%)	3.7%	3.9%	4.1%	4.3%
EV/Sales	0.4x	0.5x	0.5x	0.4x
EV/EBITDA	6.0x	6.8x	6.6x	5.9x
EV/EBIT	10.9x	15.1x	10.9x	9.4x

LFL "ex-calendar" worked out at +7.0% in Q1 2016, , with strong double-digit rates in Emerging Markets (+15.7% / helped by inflation) and a -0.3% decline in Iberia. At -0.3% LFL, it may be psychological, but we are still negative on Iberia

Topline: In Iberia, LFL sales fell 0.3% excluding the calendar effect (~-1% / slightly positive in Portugal and more negative in Spain) and 1.3% including it (vs -1.3%e). This LFL rate excl. calendar is better than in Q4 (vs -0.9%). In emerging markets, given the difficult macro-economic context in LatAm, Dia's performances turned out to be very resilient (+15.6% LFL vs +12.7%e). Note that LFL figures moved from 9% to mid teens due to inflation acceleration in LatAm (especially in Argentina..). Dia is gaining market share both in Argentina and Brazil according to Nielsen.

Bottom line: this quarter, the forex impact was hugely negative (sales down 14.6% in emerging markets on account of a 38% negative forex impact). The margin mix was therefore favourable since the relative weight of emerging markets, far less profitable (2.4% EBITDA margin / up +13bp vs +7bp e) than Iberia (7.5% / down 3bp vs -23bp e), has decreased vs Q1 2015. As a consequence, the group's EBITDA margin was up 22bp (vs +7bp e) to 5.8% despite the margin in Iberia being roughly flat.

Outlook: 1/ in 2016, Dia expects high single-digit growth in gross sales at CC; 2/ management forcasts EBITDA growth (at cc) with a positive contribution from Iberia and Emerging markets; 3/ the consolidated EBITDA margin is expected to be stable in 2016 (vs +20bp in our estimates); 4/ strong FCF is expected.

ANALYSIS

- As a reminder, some observers are persuaded that Dia is unwisely implementing a margin rate policy. This type of strategy resulted in a "margin restatement" for Tesco (i.e. radical price cuts at the expense of the margin rate, in order to restore customer flows).
- As such, it seems easy to think the Spanish group could have the same fate. In our view, the situation at Dia is far different to that at Tesco and we believe the restatement is not the right issue to focus on (see: Anorexic growth... the bigger the better!).
- However, the fact is that others believe this and seem to have convinced the market. Since management has postponed several times the deadline for lfl sales in Spain returning to positive territory, we believe the market has been scalded.
- In our view, only clear proof of this restored lfl growth could help significantly reverse momentum. This is not the case at this stage. Hence our Neutral rating on the stock despite the wide upside potential relative our Fair Value.
- Note that during the quarter, remodelling activites were particularly intense in Iberia (106 upgrades to new Dia formats). This impacted sales growth and could hopefully help strengthen topline momentum in the coming quarters.

VALUATION

- Dia is showing a 9x 2017 P/E vs 16x on average for the panel excl. Tesco

NEXT CATALYSTS

- Positive LFL in Iberia and further evidence that a margin restatement is not on the agenda

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