

10th May 2016

Food retailing

Metro AG

Price EUR27.33

Q2 earnings statement (first take)

Fair Value EUR26 (-5%)

NEUTRAL

Bloomberg	MEO GY
Reuters	MEOG.DE
12-month High / Low (EUR)	32.2 / 21.9
Market Cap (EURm)	8,856
Ev (BG Estimates) (EURm)	11,734
Avg. 6m daily volume (000)	1 278
3y EPS CAGR	12.3%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-1.5%	11.3%	-2.3%	-7.6%
Food Retailing	-4.9%	2.6%	-9.3%	-2.8%
DJ Stoxx 600	0.4%	7.7%	-11.3%	-8.9%

YEnd Sept. (EURm)	09/15	09/16e	09/17e	09/18e
Sales	59,220	58,320	59,835	61,396
% change		-1.5%	2.6%	2.6%
EBITDA	2,457	2,460	2,544	2,631
EBIT	711.0	1,497	1,557	1,618
% change		110.6%	4.0%	3.9%
Net income	502.3	597.5	652.5	711.0
% change		18.9%	9.2%	9.0%

	09/15	09/16e	09/17e	09/18e
Operating margin	2.6	2.6	2.6	2.6
Net margin	0.8	1.0	1.1	1.2
ROE	NM	NM	NM	NM
ROCE	10.5	10.2	9.8	9.6
Gearing	48.9	44.4	45.9	46.4

(EUR)	09/15	09/16e	09/17e	09/18e
EPS	1.54	1.83	2.00	2.18
% change	-	18.9%	9.2%	9.0%
P/E	17.8x	14.9x	13.7x	12.6x
FCF yield (%)	NM	NM	NM	NM
Dividends (EUR)	1.00	0.98	1.02	1.05
Div yield (%)	3.7%	3.6%	3.7%	3.8%
EV/Sales	0.2x	0.2x	0.2x	0.2x
EV/EBITDA	4.8x	4.8x	4.7x	4.7x
EV/EBIT	16.6x	7.8x	7.7x	7.6x

Given the seasonal nature of the business, we would conclude that better than expected bottom line performances (+EUR11m EBIT BSI vs -EUR11me) do not allow us to draw strong conclusions. The fact remains that the LFL (+0.6%) performance (certainly below the normative natural cost inflation) remained soft and prevents us from talking about a commercial recovery. At this stage, we continue to think that hype surrounding the spin-off (details on which would be very much appreciated especially regarding the ex-post credit situation of both separately listed entities) has underpinned the share price rather than a commercial recovery whose strength remains unproven.

Q2 2015/16 sales grew 0.6% LFL to EUR13.6bn (vs EUR13.5bn e). As a whole, business seems to have been better in Germany (+1.1% LFL) than in other regions (+0.3% LFL). The picture is mixed at the international level (very sparse details provided) especially with Russia (which management expects to gradually bottom out during Q4), which was penalised by strong comps. In detail, LFL sales rose +0.5% in C&C (48% of sales), +0.7% at MMS (39% of sales) and +0.5% at Real (13% of sales).

EBIT before special items (EBIT BSI) worked out above expectations at +EUR11m (vs -EUR11m expected by the consensus) i.e. a +26bp increase in margin. In detail, EBIT BSI came out at EUR38m at Metro C&C vs EUR33m e (i.e. flat margin), EUR43m at Media Saturn vs EUR23m e (i.e. +43bp in margin), -EUR16m at Real vs -EUR32m e (i.e. +108bp improvement in margin). Other activities worked out at -EUR53m (vs minus EUR34m e).

Given the seasonality of the business, we would conclude that these above than expected bottom line performances do not allow to draw strong conclusions. The fact remains that LFL performance (certainly below the normative natural cost inflation) remains soft and prevent us from talking about a commercial recovery.

On the whole, Q2 15/16 EPS BSI works out at minus EURO0.18 (vs -EURO0.16 e), on account of a 46% tax rate BSI in H1. For FY15/16, Metro continues to expect a slight increase in overall sales, in a persistently challenging environment. In LFL terms, management foresees a slight increase (vs +1.5% in the previous year). It expects EBIT before special items to rise slightly above the EUR1,511m (vs EUR 1,497m in our own estimates) achieved in financial year 2014/15, including income from real estate sales.

ANALYSIS & INVESTMENT CASE

- Metro share is supported since the beginning of April by the buzz surrounding the announcement of a spin-off by mid 2017. Hence, we upgraded our recommendation while stressing that: 1/ the spin-off makes sense from a strategic point of view, 2/ separate listings would help gain operational flexibility, 3/ a pure player is far more valuable than a patchwork of different BU. But we also layed the emphasis on fundamental issues that remain harsh facts:
- The favorable tax lever (shifting of costs out of Germany, in a bid to boost the domestic operating result at Metro C&C and thus activate the loss carry forward) should not eclipse soft commercial trends (evidenced in Q2). In 2015, Metro beat the consensus thanks to property development revenues (~EUR150m) that are incorporated in EBITDA. In the end, it is not so much Metro's commercial potential which seems to be acclaimed but rather the tax engineering potential.
- So far, in view of EBIT margin at around 10% (!), Russia accounts for ~25/30% of EBIT whereas its share of sales stands at less than 10%. In a restricted consumer spending environment, and with the market stigmatising and harshly punishing margin rate policies, a margin rate at this level leaves us somewhat perplexed. Moreover, we are concerned by the situation of Media Saturn outside Russia given that it is in the front row concerning the ramp-up of e-commerce.

VALUATION

- 2017 P/E stands at 14x vs 16x on average for the panel excl. Tesco

NEXT CATALYSTS

- Spin-off by mid 2017



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