15th June 2016

Luxury & Consumer Goods

Luxottica

Price EUR43.95

Cloudy trading, but fundamentals remain intact

Fair Value EUR58 vs. EUR61 (+32%) **BUY**

Bloomberg	LUX IM
Reuters	LUX.MI
12-month High / Low (EUR)	67.5 / 44.0
Market Cap (EUR)	21,264
Ev (BG Estimates) (EUR)	21,978
Avg. 6m daily volume (000)	965.3
3y EPS CAGR	11.7%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-7.8%	-13.2%	-24.4%	-27.2%
Consumer Gds	-3.9%	-4.7%	-4.3%	-8.0%
DJ Stoxx 600	-4.2%	-7.0%	-8.3%	-12.4%

YEnd Dec. (€m)	2015 *	2016e	2017e	2018e
Sales	8,837	9,325	9,927	10,574
% change		*5.5%*	*6.5%*	*6.5%*
EBITDA	1,853	2,018	2,183	2,369
EBIT	1,376	1,517	1,648	1,800
% change		*10.2%*	*8.7%*	*9.2%*
Net income	804.1	916.5	1,017	1,121
% change		*14.0%*	*10.9%*	*10.3%*

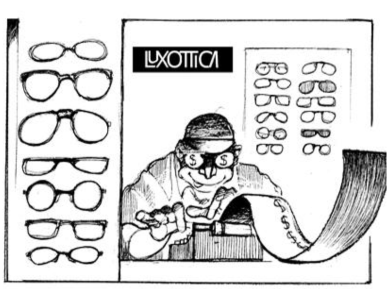
** Reported figures*

	2015 *	2016e	2017e	2018e
Operating margin	15.6	16.3	16.6	17.0
Net margin	9.1	9.8	10.2	10.6
ROE	14.6	15.4	15.9	16.2
ROCE	12.0	13.2	14.3	15.8
Gearing	18.2	12.0	5.0	-3.8

** Reported figures*

(€)	2015 *	2016e	2017e	2018e
EPS	1.68	1.91	2.12	2.33
% change	-	*13.9%*	*10.9%*	*10.3%*
P/E	26.2x	23.0x	20.8x	18.8x
FCF yield (%)	3.5%	4.1%	4.8%	6.0%
Dividends (€)	0.89	1.00	1.10	1.22
Div yield (%)	2.0%	2.3%	2.5%	2.8%
EV/Sales	2.5x	2.4x	2.2x	2.0x
EV/EBITDA	12.0x	10.9x	9.9x	8.9x
EV/EBIT	16.2x	14.4x	13.0x	11.6x

** Reported figures*



It seems that Luxottica's soft start to the sun peak season was solely due to a rainy May across Europe and in some parts of the US. Consequently, we anticipate slower FX-n sales growth in Q2 (+4%e vs. +5%e) and in 2016 (+4.5%e vs. +5%e), slightly shy of the group's "rule-of-thumb" (+5-6%). We believe the market has already anticipated these soft trends, which do not call into question our investment case over the MT/LT. FV adjusted to EUR58 vs. EUR61 but Buy recommendation confirmed.

ANALYSIS

- **What has changed since the Q1 sales? The wet weather…** At the Q1 sales conference call (29 April), management was satisfied by the acceleration in April after the soft Q1. However, it did not continue into May due to very wet weather conditions across Europe and in some parts of the US, limiting reorders from wholesalers. Note that European Wholesale accounts for approx. 42% of the Wholesale Division and ~18% of total sales. These unfavourable weather conditions are also partly impacting Sunglass Hut (100% exposed to the sunglasses category).

- **Luxottica still guides on a robust H2 16.** Even if the month of May was softer than the group's expectations, it remains quite optimistic on the strong acceleration expected in H2 as the latter was be mainly driven by the **contribution from optical store openings across the U.S.** (~80 LensCrafters stores at Macy's and 80 Target Optical) **which should bring ~2-4pp on Luxottica's H2 FX-n top line growth** and ~1-2pp over FY16. Last but not least, the **calendar effect** that played negatively in H1 will be positive in H2. Should LUX report a 3% FX-n growth in H1 (o/w +4%e FX-n in Q2), +7% in H2 would be required to reach the lower end of the FY guidance (+5%), which is a bit challenging in our view.

- **Implications of our assumptions.** The group has often insisted on the importance of the months of May, June and July, which represent the sun peak season. Since the weather has not shown any improvement over the first days of June (BG ests: ~10% of FY sales), we prefer to adopt a more cautious stance: for Q2, we now anticipate a FX-n growth of ~4% vs. ~5% previously whilst leaving our H2 forecast unchanged at +6%. We expect the contribution from new stores to be at the lower end of the range (i.e. +2pp in H2 and +1pp in FY16). **Our new FY16 assumption (+4.5%e vs. +5% initially) would then become slightly more conservative than the group's guidance of +5-6%.**

- **Luxottica is also comfortable on margin upside potential.** Despite this expected softer top line performance, the group can still benefit from its scale effect (BG ests: >+3% FX-n) and efficiency gains and it is continuously identifying new areas of opex reduction. Hence the group is quite optimistic about achieving its "rule-of-thumb" over 2016-18, but as indicated in the table below, we remain more prudent at this stage.

Our forecasts vs. guidance (≥1.5x sales growth in 2016 and >1.5x sales growth in 2017-18):

FX-n	2016e	2017e	2018e
Sales growth (%)	4.5	6.5	6.5
EBIT growth (%)	5.1	8.7	9.2
Ratio (x)	**1.1x**	**1.3x**	**1.4x**

Source: Bryan, Garnier & Co ests.

VALUATION

- Our new FV of EUR58 vs. EUR61 reflects our revised assumptions over 2016-18.

- Following the significant derating of the stock in February-March mostly caused by governance issues, the share price (1M: -8%/ 3M: -13%) performed globally in line with the FTSE MIB index (-8.3% and -14.3% respectively). Despite these ST headwinds, we are still convinced by the group's sound fundamentals (ability to capture the industry's structural drivers, improving sales and earnings momentum thanks to the EUR1.5bn capex plan, etc.), supported by an attractive valuation (2017e EV/EBIT of 13x => 20% discount to 2004-16 historical average).

NEXT CATALYSTS: H1 16 Results on 25 July. ***Click here to download document***

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