

Capgemini

Price EUR85.02

Feedback from Capital Markets Day

Fair Value EUR97 vs. EUR96 (+14%)

BUY

Bloomberg	CAP FP
Reuters	CAPP.PA
12-month High / Low (EUR)	90.2 / 69.0
Market Cap (EUR)	14,639
Ev (BG Estimates) (EUR)	15,678
Avg. 6m daily volume (000)	645.8
3y EPS CAGR	11.7%

We reiterate our Buy rating and fine-tune our DCF-derived fair value to EUR97 from EUR96 (on fx updates, especially EUR/USD and EUR/GBP) following the Capital Markets Day held yesterday in Munich (Germany). The positive key message from this event is that: 1). Management is increasingly confident on FY16 guidance and medium-term goals; 2). Capgemini is a bit ahead of schedule on synergies with Igate; 3). Acquisitions are at the agenda.

ANALYSIS

- Confidence in FY16 guidance.** Unsurprisingly, management reiterated FY16 guidance, i.e. sales up 7.5-9.5% at cc (up 2.5-4.5% lfl), a non-IFRS operating margin of 11.1-11.3% and a free cash flow above EUR850m. The strong double-digit decline in the Energy sector in the US is not expected to trigger significant restructuring, as many staff are on the sideline due to lack of contract and can be redeployed to more buoyant areas (High-tech, Automotive, Banking). In France, there is growth but management does not expect any acceleration going forward, while Sogeti's Application Services business is facing a significant re-skilling program over 2016-18. In Benelux, market conditions remain tough, but Capgemini is doing well in Digital & Cloud.
- Medium-term levers remain intact.** Medium-term objectives are also unchanged, i.e. reaching 5-7% lfl revenue growth and a non-IFRS operating margin of 12.5-13% by the end of the decade. The achievement of these goals is not tributary to better economic conditions. On growth, Capgemini is already close to +5% excluding Brazil and Energy in the US. Digital & Cloud (22% of sales) grew by 28% in Q1 16 while management expected 20-25%, and a lot of initiatives have been launched (Applied Innovation Exchange, Digital Manufacturing) or reinforced (Cloud Choice, Cybersecurity, DCX), helped by the ecosystem of partners. The global account management program presented two year ago has been extended to 22 customers from 14. On the margin, all the levers to reach 12.5-13% remain unchanged (competitiveness, innovation, industrialisation), but service automation and industrialisation (up to machine learning and artificial intelligence) is becoming more than ever a top priority in areas where offshoring has reached maturity, is not possible or is irrelevant – essentially in application testing, managed services and BPO/BPS.
- Synergies with Igate ahead of schedule.** This is not breaking news as management mentioned it with Q1 16 sales, but today it put some numbers on these synergies. When the acquisition of Igate was announced (April 2015), the goal was to generate over 3 years USD30-40m cost synergies from G&A cost optimisation, USD45-65m cost synergies from the operating model and USD100-150m revenue synergies. As of today, already USD40m G&A cost synergies have been delivered, while revenue synergies already amount USD60m (15 in Q4 15 + 45 in Q1 16), of which half were in Financial Services sector. The joint deal pipeline is above USD500m, with 7 deals above USD20m. Synergies on the operating model (people supply chain, etc) have started to be implemented, but will be visible on the P&L in H2 16 and 2017.
- Update on the M&A strategy.** Management is not ready for a large acquisition before the integration of Igate has been completed and the acquisition-related debt has been retired, i.e. not before 2018-19. However, the company is ready for small acquisitions essentially focused on Cloud & Digital. Like for Oinio and Fahrenheit 212, the target would remain autonomous. That said, if a sizeable opportunity arises, the CFO Aiman Ezzat admits Capgemini could be more leveraged.

VALUATION

- Capgemini's shares are trading at est. 10.9x 2016 and 9.3x 2017 EV/EBIT multiples.
- Net debt on 31st December 2015 was EUR1,747m (net gearing: 25%).

NEXT CATALYSTS

H1 15 results on 27th July before markets open.

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BUY ratings 55,9%

NEUTRAL ratings 34,3%

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