

Essilor

Price EUR121.60

Q2 LFL growth miss due to very weak trends in sun and photochromic lenses

Fair Value EUR130 (+7%)

BUY

Bloomberg	EF FP
Reuters	ESSI.PA
12-month High / Low (EUR)	123.6 / 100.4
Market Cap (EUR)	26,520
Ev (BG Estimates) (EUR)	28,239
Avg. 6m daily volume (000)	497.1
3y EPS CAGR	10.7%

	1 M	3 M	6 M	31/12/15
Absolute perf.	4.7%	5.7%	9.3%	5.7%
Consumer Gds	6.1%	1.1%	4.2%	-1.7%
DJ Stoxx 600	7.2%	-2.7%	1.4%	-7.2%

YEnd Dec. (€m)	2015	2016e	2017e	2018e
Sales	6,716	7,187	7,688	8,229
% change		7.0%	7.0%	7.0%
EBITDA	1,263	1,358	1,461	1,580
EBIT	1,183	1,288	1,391	1,515
% change		8.9%	7.9%	8.9%
Net income	757.1	844.5	932.1	1,027
% change		11.5%	10.4%	10.2%

	2015	2016e	2017e	2018e
Operating margin	17.6	17.9	18.1	18.4
Net margin	11.3	11.8	12.1	12.5
ROE	13.3	13.2	13.3	13.9
ROCE	20.0	20.4	20.9	21.6
Gearing	34.7	25.3	19.3	16.7

(€)	2015	2016e	2017e	2018e
EPS	3.57	3.98	4.39	4.84
% change	-	11.5%	10.4%	10.2%
P/E	34.1x	30.6x	27.7x	25.1x
FCF yield (%)	3.3%	3.4%	3.9%	4.1%
Dividends (€)	1.15	2.15	3.15	4.15
Div yield (%)	0.9%	1.8%	2.6%	3.4%
EV/Sales	4.3x	3.9x	3.6x	3.4x
EV/EBITDA	22.7x	20.8x	19.1x	17.6x
EV/EBIT	24.2x	21.9x	20.1x	18.4x

Essilor unveiled H1 sales of EUR3,583m (CS: EUR3,645m), up 5.1% reported and 4.1% LFL (CS: +5%). In Q2 alone, LFL growth was only 3.2% (CS: +5%) given a poor performance of the sunglasses business (-5.8% vs. +5.5%e => -1.3pp impact on LFL growth) and in North America (only Transitions is affected). In H1 the contribution margin contracted 20bp to 18.9% (CS: 19%). Ahead of the conference call today at 10.30am (CET), FY LFL growth target has been adjusted slightly to 4.5% vs. "around 5%" but the CM guidance is untouched ("at least 18.8"%).

ANALYSIS

- **Q2 sales grew 2.9% in reported terms (Q1: +7.5%).** The deceleration vs. Q1 firstly comes from a lower-than-expected LFL growth (+3.2% vs. +5%e vs. +5% in Q1), but also due to a more harmful FX impact (-4% in Q2 vs. -1.9% in Q1). The scope effect contributed for +3.7% (Q1: +4.4%).
- **Slowdown in North America but solid Europe.** Apparently this weak performance in **North America** (+1.5% LFL vs. +4.7% in Q1) is mainly explained by the significant sales decline to third parties at Transitions (photochromic lenses = affected by the bad weather?) since the other categories remain were well-oriented in Q2. On the positive side, **Europe** was strong again with +4.5% LFL (Q1: +4.7%), driven by the Nordic countries and Russia, whilst the Benelux countries returned to growth. The slight deceleration in the UK and Spain only due to demanding comparison bases.
- **Robust trends in LatAm and in Asia-Pacific.** Sales in **Latin America** were up 11.4% LFL (Q1: +9%) as sales in **Brazil** have picked up in Q2 (drivers: mid-tier Kodak brand, online business) whilst the activity in **Mexico, Colombia and Central America** remained strong. Sales in the **AMEA** region increased by 8.7% (Q1: +8.9%) driven by strong domestic demand in China and in India but also across S-K and Southeast Asia.
- **Bad weather conditions have significantly affected the S&R division (-5.8%).** In North America the unfavourable weather conditions have clearly impacted the sales of **Costa** and **FGX** (readers), the latter being also affected by the same headwind in Europe. Moreover the expected rebound of **Bolon** in China was longer-than-expected after the 33% sales drop in Q1 because of the implementation of the new ARTEMIS dealer fulfilment system at Bolon. Although we were anticipating a negative impact from the bad weather conditions, especially after the publication of Luxottica earlier this week, the magnitude is clearly more significant than we thought, causing almost a 1.3pp deviation on LFL growth (reported LFL growth vs. CS expectations). Sales in **Equipment** posted a second consecutive quarter of growth (+4.3% vs. +3.5%).
- **The contribution from operations came in at EUR677m (CS: EUR694.5m) in H1 (cf. details overleaf).** The product-mix (innovation, media push on the most profitable brands) and efficiency gains continued to play positively but the GM was impacted by the weak performance of Transitions (higher margins) as well as the dilutive impact from acquisitions, causing a 30bp contraction in the GM to 59.6%. Thanks to a tight opex cost control, **the CM only narrowed 20bp to 18.9% (CS: 19%).** EPS increased by 6.4% to EUR1.95, driven by a favourable tax rate (26.1% vs. 29% the prior year).
- **FY16 LFL growth target slightly revised down to 4.5% vs. "around +5%".** Against the miss in Q2 caused by the disappointing performance in sunwear and a significant sales drop at Transitions, the Group **has decided to adjust moderately the LFL growth target to +4.5% vs. "around +5%" previously, which still implies a 5% LFL growth over H2.** As for the profitability, the group reiterates the CM target of "around 18.8%", hence a possible stable margin vs. 2015 (BG ests: +10bp to 18.9%).

VALUATION

- Following a good outperformance ytd (+10% vs. the CAC40 index) and in light of this Q2 miss/LFL growth target adjustment, we expect the share price to be under pressure today. However we would consider it as a buy opportunity over the MT since: (i) the miss is mostly due to temporary factors (bad weather), (ii) the lowered guidance still requires a 5% LFL growth in H2, representing an acceleration vs. H1 (+4.1%) and (iii) Group fundamentals are intact.

NEXT CATALYSTS

- Conference call today at 10.30am (CET) // Q3 sales on 22 October.

(To be continued next page)



LFL Quarterly Sales:

% change	Q1 15	Q2 15	Q1 16	Q2 16	Q2 16 - CS
North America	4.5	3.7	4.7	1.5	5.0
Europe	2.5	5.0	4.7	4.5	3.5
Asia-Pacific-Middle-East- Africa	5.6	5.2	8.9	8.5	8.7
Latin America	10.0	10.5	9.0	11.4	7.4
Lenses & Optical Instruments	4.4	4.9	5.7	4.4	5.2
Equipment	-2.1	-7.1	3.5	4.3	1.0
Readers & Sun	1.8	3.2	-1.5	-5.8	5.5
Total group	4.0	4.4	5.0	3.2	5.0

Source: Company Data

H1 16 Results:

EURm	H1 15	H1 16	% change
Sales	3,408	3,583	5.1
Gross Profit	2,041	2,135	4.6
Gross Margin (%)	59.9	59.6	-30bp
Contribution from operations	651	677	4.0
As a % of sales	19.1	18.9	-20bp
Operating Profit	614	646	5.3
Net result attributable to shareholders	388	416	7.3
EPS	1.83	1.95	6.4

Source: Company Data

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