BRYAN, GARNIER & CO

INDEPENDENT RESEARCH UPDATE

8th July 2016

Molson Coors

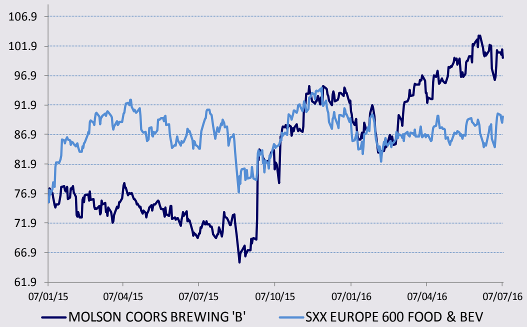
Good call!

Food & Beverages

Fair Value USD110 vs. USD97 (price USD99.85) **BUY vs. NEUTRAL**

Bloomberg	TAP US
Reuters	TAP.N
12-month High / Low (USD)	103.7 / 65.2
Market capitalisation (USDm)	21,435
Enterprise Value (BG estimates USDm)	15,470
Avg. 6m daily volume ('000 shares)	1,856
Free Float	82.0%
3y EPS CAGR	16.7%
Gearing (12/15)	38%
Dividend yield (12/16e)	1.81%

YE December	12/15	12/16e	12/17e	12/18e
Revenue (USDm)	3,568	3,248	11,503	11,675
EBIT (USDm)	352.20	356.40	1,914	2,059
Basic EPS (USD)	1.93	3.28	5.45	5.97
Diluted EPS (USD)	3.76	3.28	5.45	5.97
EV/Sales	5.33x	4.76x	2.72x	2.57x
EV/EBITDA	29.2x	23.5x	12.2x	11.1x
EV/EBIT	53.9x	43.4x	16.3x	14.6x
P/E	26.6x	30.5x	18.3x	16.7x
ROCE	2.7	2.7	8.9	7.1



As the acquisition of the remaining 58% of MillerCoors becomes more likely and its earnings enhancement becomes more clear, coupled with the continued strong price inflation for beer in the US and Canada, we are increasing our fair value of the company to USD110 and move our recommendation to Buy

- The USD12bn acquisition to gain full control of MillerCoors is a game changer for Molson Coors. Not only is there the immediate EPS accretion with 2017 EPS of USD5.45, which is an increase of 43% from a stand-alone EPS of USD3.81 in 2016e. But the strategic impact is likely to be even bigger. With the acquisition, the company is gaining a fully-integrated stable number two position in the North American market. As a result, the company's free cash flow profile is changing dramatically from on average USD800m p.a. over the past five years (2012-2016e) to nearly USD2bn p.a. from 2017 onwards. This should provide the company with the ammunition to accelerate acquisition-driven growth.

- Existing efficiency plans at MillerCoors and Molson Coors, together with the synergy estimates from the acquisition, should combine into an annual USD150-200m of efficiency improvements (1.3% to 1.7% of net revenue) for the coming 3-4 years. We would expect the company to keep most of these savings in its North American operations helped by the quasi-duopoly shared between Molson Coors and AB InBev. Indeed, despite the global commodity price deflation, beer price inflation in both the US and Canada is currently over 2%.

- The high-end beer segments are highly profitable and growing. However, in the US, MillerCoors's high-end brands are only 10% of its total volumes, whereas it is 1/3rd of the market. Getting full control of the profits generated by import brands Peroni, Pilsner Urquell and Foster's (more money available to motivate distributors) will help and add to the investments behind Blue Moon, Leinenkugel , Redd's, Henry's hard soda and, the recently acquired, Saint Archer craft brewer. On top of this, the company has been rejuvenating its mainstream Miller Lite and Coors Light brands.

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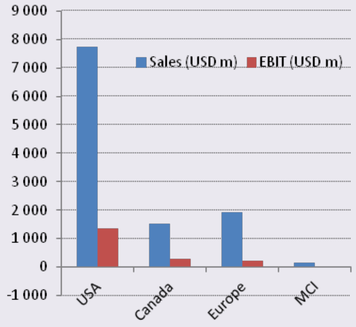

Company description

Molson Coors was created on 9 February 2005 by the merger of two of North America's largest breweries: Molson of Canada and Coors of the United States. After taking full control of MillerCoors (2016 H2e) Molson Coors is the world fifth largest brewer by volume with 102m hl and the third largest in terms of profits. In all its main markets: US, Canada, UK, it is the number two brewer with market shares of 27%, 37% and 18% respectively.

Simplified Profit & Loss Account (USDm)	**2013**	**2014**	**2015**	**2016e**	**2017e**	**2018e**
Revenues	4,206	4,146	3,568	3,248	11,503	11,675
Change (%)	*7.4%*	*-1.4%*	*-14.0%*	*-9.0%*	*254%*	*1.5%*
Adjusted EBITDA	756	856	651	659	2,569	2,714
EBIT	467	489	352	356	1,914	2,059
Change (%)	*6.6%*	*4.8%*	*-28.0%*	*1.2%*	*437%*	*7.6%*
Financial results	(170)	(134)	(112)	(50.1)	(341)	(316)
Pre-Tax profits	297	355	240	306	1,573	1,744
Exceptionals	(179)	(330)	(342)	0.0	0.0	0.0
Profits from associates	539	562	516	579	0.0	0.0
Tax	(84.0)	(69.0)	(51.8)	(177)	(393)	(453)
Minority interests	(5.2)	(3.8)	(3.3)	0.0	0.0	0.0
Net profit	567	514	360	708	1,180	1,290
Restated net profit	727	769	700	708	1,180	1,290
Change (%)	*2.3%*	*5.7%*	*-8.9%*	*1.2%*	*66.5%*	*9.4%*
Cash Flow Statement (USDm)						
Operating cash flows	1,326	1,460	838	1,239	2,569	2,714
Change in working capital	96.4	15.0	22.6	0.16	1,032	138
Capex, net	(240)	(251)	(263)	(271)	(722)	(641)
Financial investments, net	(36.7)	11.3	(71.5)	0.0	(12,000)	0.0
Dividends	(239)	(278)	(303)	(390)	(429)	(472)
Other	(171)	(199)	(313)	2,273	(484)	(519)
Net debt	3,358	2,562	2,507	(395)	9,631	8,400
Free Cash flow	928	1,022	433	741	2,395	1,692
Balance Sheet (USDm)						
Tangible fixed assets	1,970	1,798	1,591	1,559	1,625	1,611
Intangibles assets	8,314	7,245	6,235	6,235	6,235	6,235
Cash & equivalents	442	625	431	2,882	382	382
current assets	1,095	954	828	737	2,554	2,534
Other assets	3,758	3,375	3,192	3,192	15,192	15,192
Total assets	15,580	13,996	12,276	14,605	25,988	25,954
L & ST Debt	3,800	3,187	2,937	2,487	10,012	8,781
Others liabilities	3,175	2,947	2,296	2,256	5,114	5,242
Shareholders' funds	8,605	7,863	7,043	9,861	10,862	11,930
Total Liabilities	15,580	13,996	12,276	14,605	25,988	25,954
Capital employed	13,899	12,729	11,275	10,616	16,087	21,518
Ratios						
Operating margin	11.10	11.80	9.87	10.97	16.64	17.64
Tax rate	12.83	11.77	12.61	20.00	25.00	26.00
Net margin	17.29	18.53	19.63	21.81	10.26	11.05
ROE (after tax)	8.45	9.77	9.94	7.18	10.86	10.82
ROCE (after tax)	2.93	3.39	2.73	2.69	8.92	7.08
Gearing	44.27	39.37	38.35	(1.95)	90.36	71.98
Pay out ratio	41.56	53.59	85.03	55.08	36.38	36.59
Number of shares, diluted	184	186	186	216	216	216
Data per Share (USD)						
EPS	3.08	2.76	1.93	3.28	5.45	5.97
Restated EPS	3.95	4.13	3.76	3.28	5.45	5.97
% change	*1.0%*	*4.6%*	*-9.0%*	*-12.8%*	*66.5%*	*9.4%*
EPS bef. GDW	3.95	4.13	3.76	3.28	5.45	5.97
BVPS	47.02	42.53	38.01	45.82	50.47	55.44
Operating cash flows	7.20	7.85	4.49	5.73	11.88	12.55
FCF	4.51	5.41	2.20	3.42	6.30	7.19
Net dividend	1.28	1.48	1.64	1.80	1.98	2.18

Source: Company Data; Bryan, Garnier & Co ests.

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1. Valuation

1.1. DCF Valuation

DCF based fair value of USD110 per share

Our fair value of USD110 for Molson Coors is based on a DCF analysis. We employ a consistent method to value the shares of our beverages universe and our fair values are generated using a standardised DCF model. Following this, our valuations are compared against a peer group in order to formulate our final investment view.

Our standardised DCF model incorporates the following:

- The WACCs are calculated using a levered beta which allows us to adjust for the companies' different financial structures. The unlevered beta for Molson Coors is set at 0.95.
- The WACCs are calculated using cost of debt forecasts which account for the differing tax rates and interest charges of the companies under our coverage.
- The long-term growth rates for the companies reflect their geographic spread and potential growth of their markets.
- The cost of equity is based on a BG standardised 1.6% risk free rate and 7.0% equity risk premium.

For Molson Coors, given its increased financial gearing (but low tax benefit from financial leverage due to its lower tax rate), the WACC that we compute varies from 7.8% in 2016 to 7.5% in 2017 (the assumed first year of the MillerCoors acquisition) to 8.3% in the long term (equal to its cost of equity).

Fig. 1: DCF- based fair value of USD110 per share

DCF Valuation	Dec-16e	Dec-17e	Dec-18e	Dec-19e	Dec-20e	Dec-21e	Dec-22e	Dec-23e	Dec-24e
Sales	11,027	11,503	11,675	11,866	12,073	12,285	12,501	12,721	12,945
EBIT	1,746	1,914	2,059	2,204	2,311	2,389	2,470	2,553	2,637
Tax rate	20.0%	20.0%	26.0%	27.0%	28.0%	28.0%	28.0%	28.0%	28.0%
Taxes	(349)	(133)	(285)	(345)	(397)	(419)	(442)	(465)	(488)
Operating profit after taxes	1,397	1,781	1,774	1,859	1,914	1,970	2,028	2,088	2,149
+ Depreciations	303	655	655	655	653	305	307	310	313
-Investments in fixed assets	(271)	(722)	(641)	(647)	(653)	(305)	(307)	(310)	(313)
Total net investments in fixed assets	28	32	(67)	14	8	0	0	0	0
-Investments in WC	0	1,032	138	138	138	138	138	138	138
=Operating cash flow	1,429	2,746	1,926	2,005	2,051	2,108	2,166	2,225	2,287
Discount factor	0.98	0.92	0.85	0.79	0.73	0.67	0.62	0.57	0.53
Present value of FCF	1,404	2,513	1,640	1,577	1,491	1,415	1,343	1,275	1,210
Cum. present value of free cash flow	13,870								
+Pres. value of terminal value	19,751								
=Enterprise value	33,621								
Adjusted net debt incl pension provisions (restated cash)	(9,832)								
Revalued minority interests	(20)								
=Fair value	23,768								
Fair value fully diluted/share	110								

Source: Company Data; Bryan, Garnier & Co ests.

Peer group comparison

A comparative multiples table is shown below, with all companies' results annualised to a December year-end in order to enable direct analysis across the portfolio of stocks. On a 2016 P/E, Molson Coors is one of the more expensive beverages companies, but, looking at 2017, when the earnings enhancement of the Miller acquisition should flow through to the bottom line, the stock is one of the cheaper ones. The same goes for its free cash flow yield. For 2017, we calculated its free cash flow yield at 6.3%, partially reflecting profitability but also the gearing of the business to more mature markets where investment levels are lower.

Fig. 2: Ratio valuation…

	local c'cy	Share price	Market Cap (EURbn)	P/E		EV/EBIT		EV/EBITDA not adj.		FCF yield	Net yield		5yr EPS CAGR	PEGD
				2016e	2017e	2016e	2017e	2016e	2017e	2016e	2016e	2017e		
Brewers														
AB InBev	EUR	115.8	170.5	27.8	23.6	21.2	19.3	17.4	16.1	3.1%	5.3%	1.9%	11%	2.12
Carlsberg	DKK	634.0	11.4	20.6	19.3	18.7	16.5	11.4	10.5	3.0%	5.9%	1.0%	10%	1.88
Heineken	EUR	82.9	40.7	20.6	18.7	16.8	15.1	12.7	11.3	4.1%	5.1%	1.4%	9%	1.90
Molson Coors	USD	100.0	13.3	30.5	18.3	44.0	16.4	23.8	12.3	3.4%	6.3%	1.8%	2%	8.32
SABMiller	GBp	4,317.0	86.4	29.5	26.8	25.5	23.0	19.7	18.0	3.1%	3.9%	2.1%	7%	3.15
Royal Unibrew	DKK	295.0	2.1	20.3	19.1	16.5	15.6	12.6	12.0	6.0%	5.7%	2.1%	7%	2.19

Source: Company Data; Bryan, Garnier & Co ests.

2. A place at the consolidation table

Molson Coors' vision is to become a top global brewer in profitability and its strategy rests on three pillars: 1) maximising the profitable growth opportunities in its core markets through a focus on brands, innovation, and cost management; 2) accelerating its push into new and emerging markets to grow its brands globally; and 3) looking for M&A opportunities that meet its criteria for generating shareholder value and that provide solid growth platforms for its business and brands. In what follows, we tackle its progress in each of these three pillars

2.1. A history of acquisitions

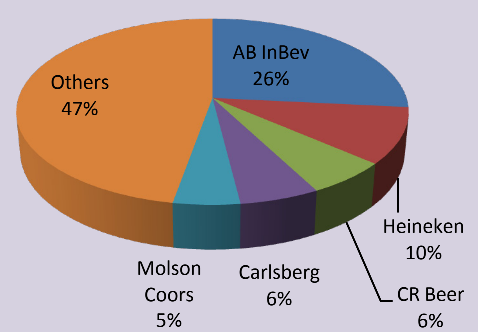
M&A is in its DNA. And now it will have the money to participate properly in the consolidation

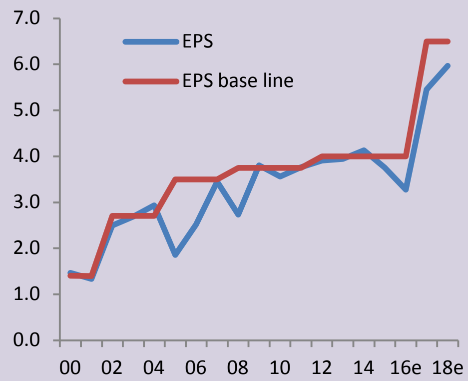
Molson Coors has gradually built itself into the third largest brewer in the world (in terms of revenues) and the fifth largest in terms of volumes. In the last 10 years, there have been significant step-ups in size, with the latest 58% acquisition of MillerCoors being truly transformational. This has mainly been driven by the acquisitions the company has made since 2000, 6.7% annual revenue growth (2000-2016e) and 6.8% EPS growth. We expect the acquisition of the 58% of MillerCoors to accelerate (acquisition-driven) growth as the company's free cash flow profile is changing dramatically from on average USD800m p.a. over the past five years (2012-2016e) to nearly USD2bn p.a. from 2017 onwards. Given the company's track-record and desire to participate in the consolidation of the industry, we expect more acquisitions. However, initially, the free cash flow will be used to pay down debt, but by the end of 2019, we expect the net debt/EBITDA ratio to decline to 2.6x from 3.8x at the end of 2017. In terms of EPS, we expect the acquisition to lift 2017 figures by 66% to USD5.45 (from USD3.28 in 2016) and another 9% in 2018 to USD5.97 (for the purpose of easier computation, we assume that the acquisition is completed on 1 January 2017).

Acquisitions bring step-ups in size and profits

Fig. 3: With acquisitions come increases in profit

Global beer market (2015 – 1965m hl) | **Growth in EPS (USD), 2000-2018e**





Source: Canadean; Bryan, Garnier & Co ests.

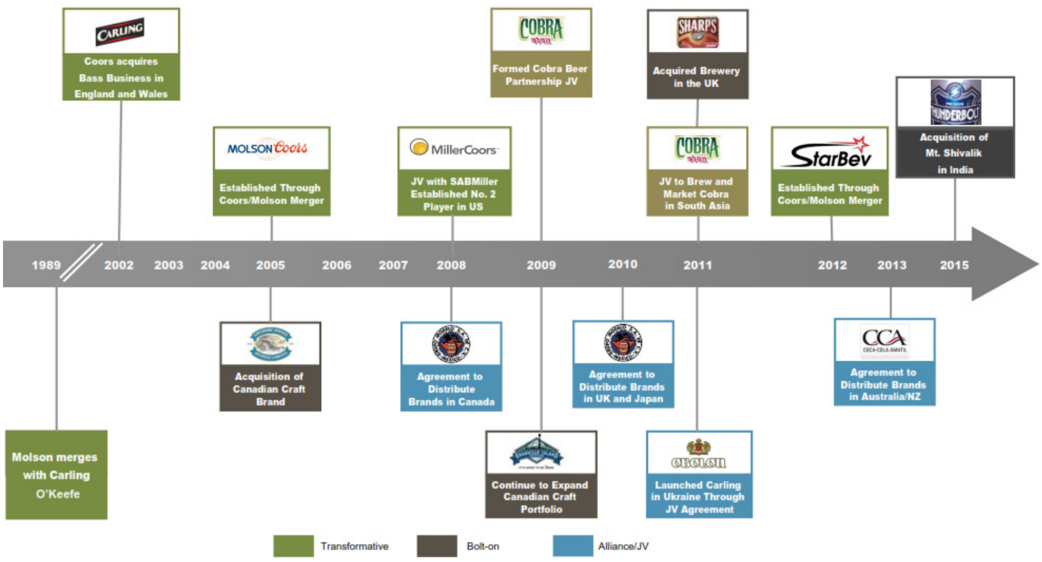
The acquisitions that brought about the transformation of the company were mainly:

- Back in 1989, Molson, the second largest brewer in Canada merged with Carling O'Keefe which was third. The merger put the combined company ahead of former market leader Labatt, and made it at that time the sixth largest North America brewery.

- In 2005, Molson Coors was formed by the merger of Molson of Canada, and Coors of the United States. Three years earlier, in 2002, Coors had bought Bass Breweries in the UK, which Interbrew (now AB InBev) had bought in 2000 but was forced to sell.
- In late 2007, SABMiller and Molson Coors announced that they were creating a joint venture, MillerCoors, for their US operations that was going to market all of their products and in which SABMiller held a 58% economic interest and Molson Coors a 42% economic interest, although management was organised 50/50.
- In early 2012, the company expanded into the Central and Eastern Europe markets by acquiring StarBev from CVC Capital Partners, which it had bought from AB InBev in 2009 (which was looking to finance the Anheuser-Busch acquisition).
- And, in the second half of 2016, the company is expected to complete the acquisition of the 58% in MillerCoors that it does not own.

Next to these step-ups in size, the company has been adding smaller companies to its portfolio. In 2005, the company entered the growing Canadian craft beer market with the acquisition of Creemore Springs Brewery and, in 2009, it added the Granville Island Brewing Co. In England, it bought in 2011 the real ale Sharp's Brewery of Cornwall and added, in 2015, 'Rekorderlig UK' giving it the exclusive rights in the on- and off-trade to distribute, sell and market the full Rekorderlig cider portfolio across the UK, Ireland and the Channel Islands. Furthermore, Molson Coors entered India in June 2011, purchasing a controlling stake of 51% in Cobra India, which owns a brewery in Bihar, and, in 2015, it added Mount Shivalik Brewing Ltd which has brewing operations in the Punjab and Haryana with a combined brewing capacity of 600k hectolitres and has a strong brand presence across a number of northern states in India, including the Punjab, Haryana, Jharkhand, Bengal and UP.

Fig. 4: Time line of acquisitions by Molson Coors



Source: Molson Coors; Bryan, Garnier & Co ests.

Buying 58% in MillerCoors

On 11th November 2015, Molson Coors agreed with AB InBev to buy the remaining 58% in the MillerCoors joint venture plus the global Miller brand portfolio. Molson Coors agreed to pay USD12bn for these assets (20-25% financed by the issuance in new equity) which comes down to an implied headline valuation multiple of 11.5x 2014 EV/EBITDA. Furthermore, adjusting the purchase price for an estimated USD2.4bn present value of cash tax benefits, the multiple comes down to 9.2x. Indeed, the acquisition provides, according to Molson Coors, access to more than USD250m of anticipated cash tax benefits in the first 15 years. Molson Coors expects USD200m of annualised cost synergies delivered by the fourth year, which it plans to a large extent to reinvest in growing its brands.

US to account for 3/4trs of profits

With the acquisition, the weight of the business at Molson Coors shifts even more to the US, which will account for 68% of net revenues and 73% of underlying pre-tax profit (2017e).

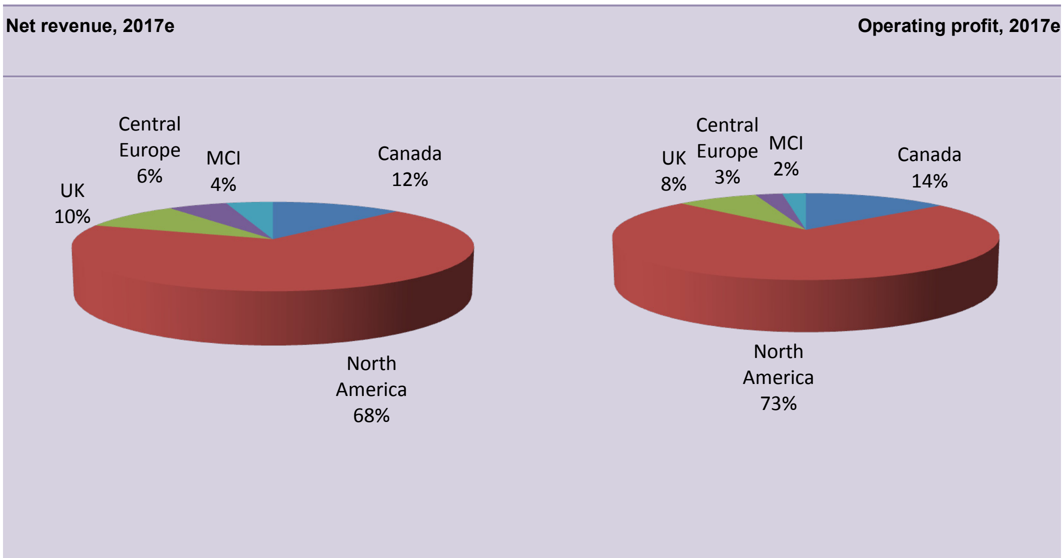
After the acquisition the size of the company will significantly expand. For example, in 2015, the company's underlying EBIT, including 42% of MillerCoors, was USD919m and that increases to USD1.6bn pro-forma. Worldwide beer volume increases to 94m hl from 58m hl, net revenue increases to USD11.2bn from USD6.8bn and EBITDA to USD2.3bn from USD1.3bn. And these figures do not include the USD200m annualised costs savings by year 4 and the USD100-150m lower annual interest expense (vs pro forma); and do not reflect the USD250m annual cash tax benefit for 15 years.

Free cash flow to double to USD1.6bn p.a. from USD0.8bn

After the acquisition, the free cash flow of the company is expected to double to USD1.6bn p.a. from around USD0.8bn previously, providing significant flows for deleveraging and new initiatives to widen the footprint of the company.

In terms of EPS, we expect the increase in profit, financial leverage, cost savings and tax benefits, will significantly outweigh the increased number of shares. Indeed, we expect USD5.45 EPS for 2017, which is an increase of 43% from a stand-alone EPS of USD3.81 in 2016e (which is excluding the capital raising and an increased contribution from MillerCoors).

Fig. 5: Pro forma geographical split of the Molson Coors business



Source: Molson Coors, Bryan, Garnier & Co estimates

2.2. Efficiency improvements to accelerate

With Molson Coors mainly active in mature markets where top-line growth is slow and volumes in mainstream and discount tend to be under pressure, the company has to focus on improving efficiency. Indeed, over the past 10 years, the company has realised a total of USD1.4bn of cost savings. But only about 1/3rd of these savings flew through to the operating profit, which improved to USD919m in 2015 from USD422m in 2005.

Despite a decade of cost cutting, US and Canadian margins are half those of AB InBev

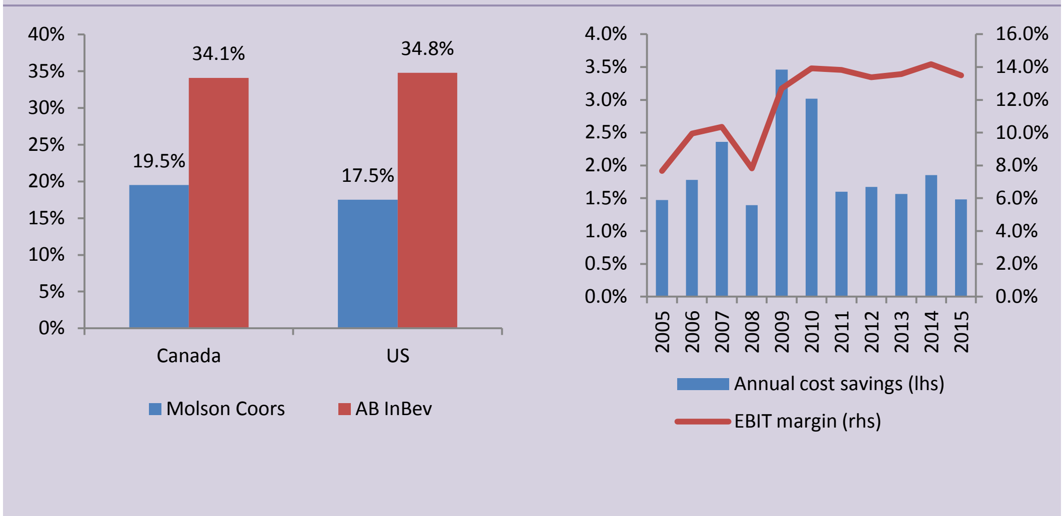
The trend of cutting costs is likely to continue in the foreseeable future as the company faces increased challenges in its Canadian market (shift from returnable bottles to cans) and, in the US, craft beers continue to take share from mainstream lager, putting pressure on volumes. Nonetheless, however impressive the Molson Coors efforts might seem, the EBIT margins in the US and Canada are about half those of AB InBev. Indeed in Canada, Molson Coors's EBIT margin of 19.5% (2015) is 14.6% below AB InBev's 34.1% (BGe). And in the US, its 17.5% EBIT margin is about 17.3% below AB InBev's 34.8% (BGe).

As always, there is some underlying explanation for the large gap, i.e. Molson Coors has a larger declining returnable beer bottle business in Canada, it has more value brands in both the US and Canada, it has a large network of breweries, advertising costs have to be spread over smaller volumes, etc. But part of the margin gap is also the upside that there still is at Molson Coors to improve. And the budgeted USD200m of cost savings from gaining full control over MillerCoors, might help to close the gap (i.e. the improvement could add about a 2.5% EBIT margin) but even then there is more to do.

Fig. 6: Margins and cost savings

Comparing Canadian and US margins

Molson Coors' annual savings and EBIT margin



Source: Company Data; Bryan, Garnier & Co ests.

Looking for USD150-USD200m annual efficiency improvements

Currently, Molson Coors is targeting USD50-70m of cost savings for at least two years on top of the MillerCoors savings which has not been quantified but which are reported on quarterly. In the first quarter these savings totalled USD18m (they were USD88m for financial year 2015) and we expect them to come in at USD80m for the years ahead, which would bring the total to USD130-USD150m, of which we expect 1/3rd to be retained in operating profit growth. But, on top of these savings, the company is expecting an additional USD200m savings by the fourth year from gaining full control of

MillerCoors and we expect these to flow fully through to the bottom line. Once the MillerCoors acquisition is finalised, the company will publish an all-in multi-year savings target and will not report on the different components. We expect the company to indicate an annual USD150-200m cost savings target for the coming 3 to 4 years.

Fig. 7: Cost savings reporting

Current reporting	Future reporting
Molson Coors' annual cost savings	All-in multi-year savings target
• USD50-70 million/year for at least 2 years	
Deal-related synergies	Annual cost savings reporting
• USD200 million by year 4(annualised)	
MillerCoors' cost savings	
• No forward targets	
• Quarterly historical reporting	

Source: Company Data; Bryan, Garnier & Co ests.

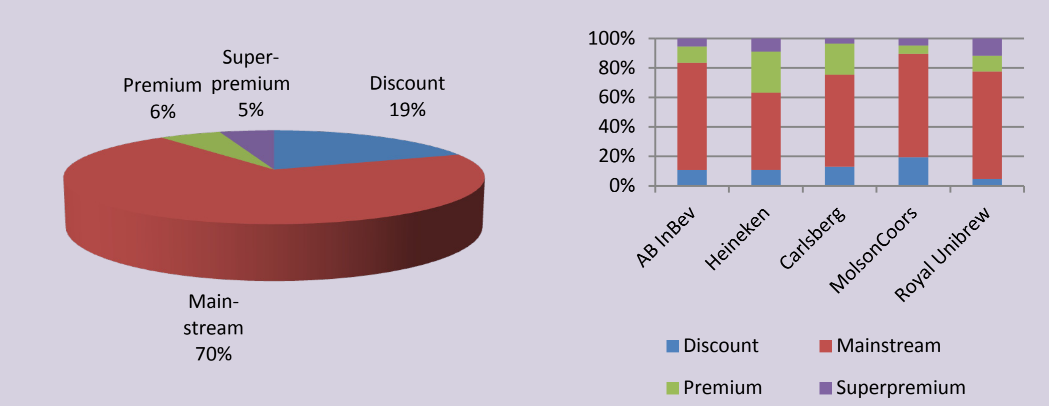
3. Increasing high-end exposure

Pretty low exposure to high margin, high growth high-end segment

From all global brewers, Molson Coors' product portfolio is most geared towards lower-end products. We calculate that high-end beer (premium and super premium) accounts for only 11% of volumes, 18% of revenues and 28% of operating profit. In terms of volume contribution, we calculate that for 2015, at AB InBev high-end beer is 17%, at Carlsberg 25%, Royal Unibrew 26% and at Heineken 36%.

Fig. 8: Molson Coors' volume by price segment compared

Molson Coors volume breakdown by price segment (2015 including 100% MillerCoors) | **Relative weight of the different categories, 2015 volume**



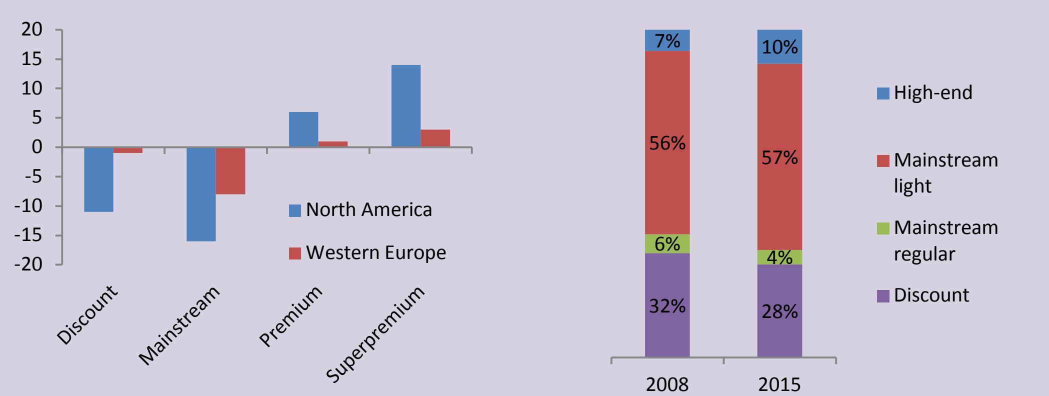
Source: Canadean; Bryan, Garnier & Co ests.

In the US, 10% of its volumes are in the high-end compared to 1/3rd for the market as a whole

For Molson Coors, its poor presence in high-end beers is especially in North America where this segment is only 10% of its total volumes (but it is 1/3rd of the market) and because of the gearing towards the discount and mainstream, Molson Coors' volume growth remains lacklustre.

Fig. 9: MillerCoors' portfolio and different growth rates by price segment

Regional growth/decline in different price segments (2010-2015, in m hl) | **MillerCoors portfolio by price segment**



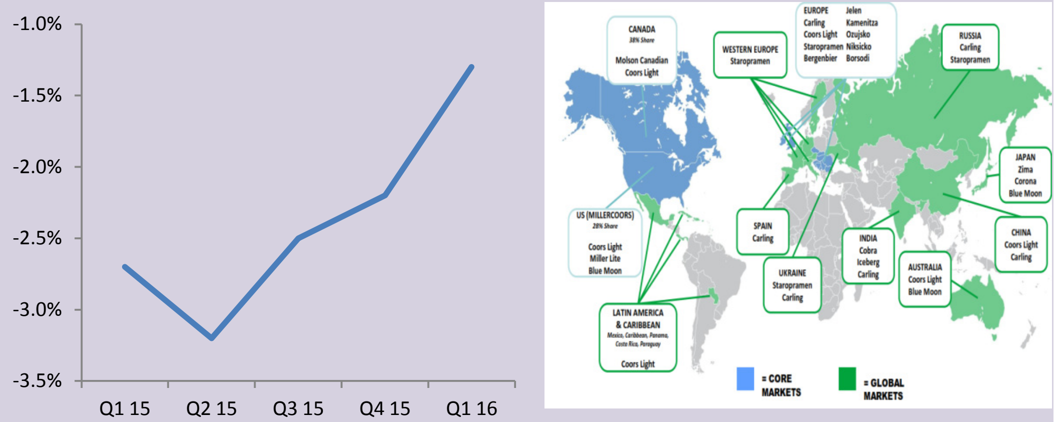
Source: Canadean; Bryan, Garnier & Co ests.

More effort is needed to address the portfolio's underperformance

So, if Molson Coors has the ambition to stabilise its US volumes in 2018 and return to growth in 2019, the company will have to work really hard in increasing its exposure to the high-end US beer segments. But the portfolio transformation is happening and, in 2015, high-end beers were already 10% of its US volumes compared to 7% in 2008 and the discount had fallen back to 28% from 32%. And we believe that by acquiring full control of MillerCoors and retaining the perpetual rights to all of the brands currently in the MillerCoors portfolio for the US market, including Redd's and import brands such as Peroni, Pilsner Urquell and Foster's, the return to growth might get an extra boost. As there will be no more licence fee paid, more money becomes available to motivate distributors to grow its import brands faster. Also investments behind Blue Moon, Leinenkugel, Redd's and Henry's hard soda is helping the growth of these high-end brands. Furthermore, MillerCoors has recently acquired the Saint Archer craft brewer and is planning to expand its reach to the rest of California and Arizona. Next to working on its portfolio composition, MillerCoors has also rejuvenated the Miller Lite brand and further developed the Coors Light identity.

Fig. 10: Molson Coors' main brands and MillerCoors' sales performance

MillerCoors' sales to retailers volume | **Molson Coors' main brands**



Source: Molson Coors

4. Financial forecasts

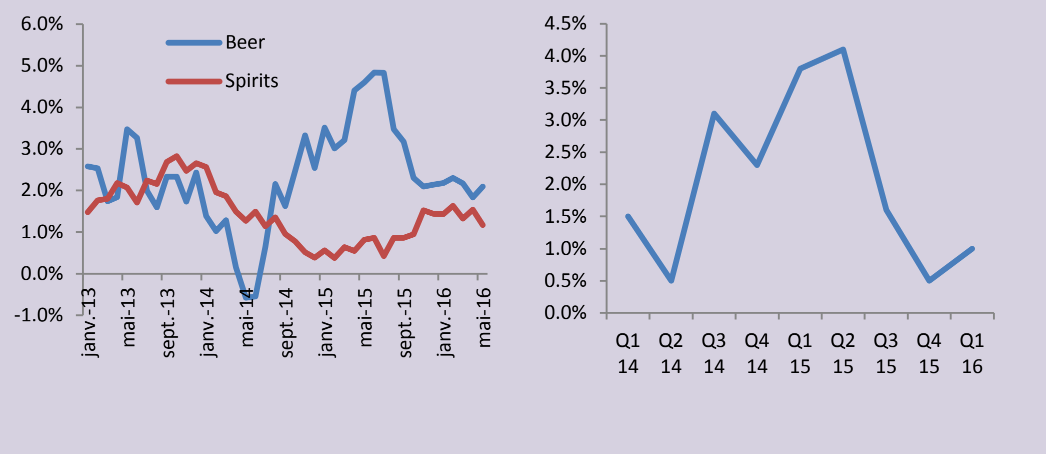
Molson Coors operates in the following segments: Canada, the US, Europe and Molson Coors International.

The replacement of a returnable bottle system with one-way packaging is putting Canadian margins under pressure

• In Canada, the company operates seven breweries, strategically located throughout Canada. And because there are plenty of import taxes between the provinces, it is likely that this structure will stay. Canada used to be a returnable bottle market but bottles are losing share (from 56% of the market in 2010 to 40% in 2014) at the expense of cans (from 34% to 49% over the same period). This process is just about finished in the west of the country but in the east, where Molson Coors has its strongest positions, the process has only started. For Molson Coors, it means that next to investing in can production, the company still needs to support the returnable bottling system and this will weigh on margin progression in the years ahead. Furthermore, there is strong competition from small brewers which do not have the same tax treatment (excise) as the larger brewers. Nevertheless, the efficiency improvement measures are expected to pay off and we look for a significant improved efficiency from 2018 onwards (after the start-up costs of the new brewery in Vancouver in 2017). Furthermore, the full ownership of the MillerCoors business should allow for some cross-border efficiency improvements. We look for an operating margin of 19.9% in 2016 and 20.1% in 2017, up from 19.5% in 2015. Although beer price inflation remains good in Canada (running at over 2%, the mix is deteriorating, resulting in only a 0.5% increase in revenue per hl in Q4 2015 and 1% in Q1 2016.

Fig. 11: Canadian price/mix growth

Canadian beer and spirits inflation (Jan 2016- June 2015) **Molson Coors Canadian revenue per hl growth (yoy)**



Source: StatCan and Molson Coors

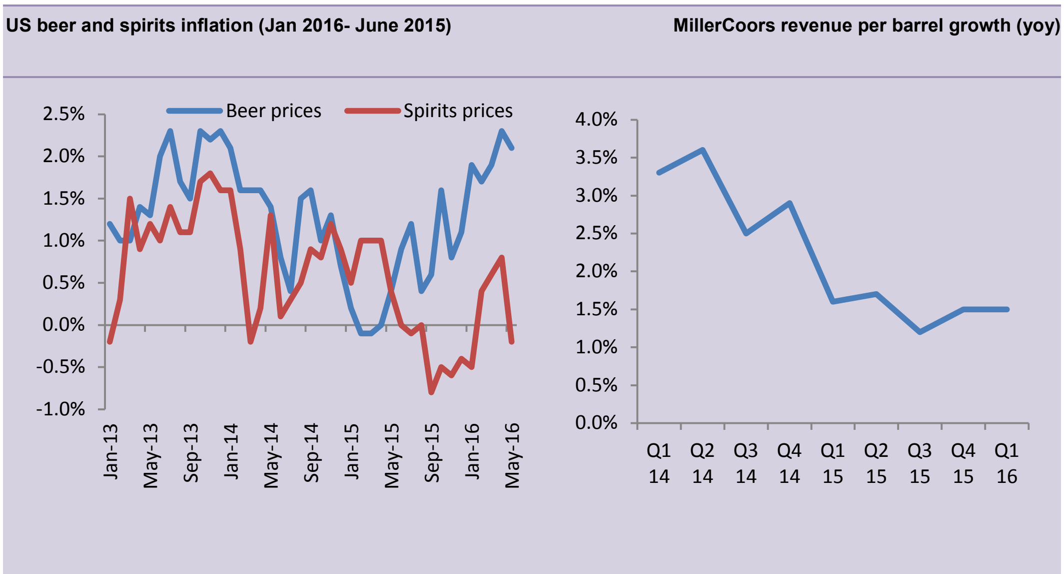
US margin progression by 30-60 bps p.a. driven by premiumisation of the portfolio but USD200m of cost savings from the MillerCoors acquisition to flow fully through to the bottom line

• In the US, MillerCoors operates nine breweries, two packaging facilities and one cidery, which produce MillerCoors' products. MillerCoors imports Molson brands and Worthington's from MolsonCoors, and Peroni Nastro Azzurro, Pilsner Urquell, Grolsch and other import brands from SABMiller. In the US, MillerCoors' guidance was for medium-term growth of 30-60 bps p.a. with volume flat to down by 1%. In our forecasts, we take on board these expectations and include on top of this the expected USD200m of cost savings from the combination. Indeed, with beer price inflation developing positively (and indicating the less price aggressive nature of the market), we believe that most of these additional savings will flow through to the bottom line.

On the other hand recent data from StatBureau indicate that US beer prices have accelerated in the second quarter to an average of 2.1% compared to 1.6% in the first quarter. This should be good news for both AB InBev and Molson Coors whose revenue per barrel mirrors the beer price inflation. Indeed, in Q1, revenue per barrel at AB InBev's US business increased 1.3% and at Molson Coors' by 1.5%.

Look at the benefit from living in a duopoly situation

Fig. 12: US price/mix growth

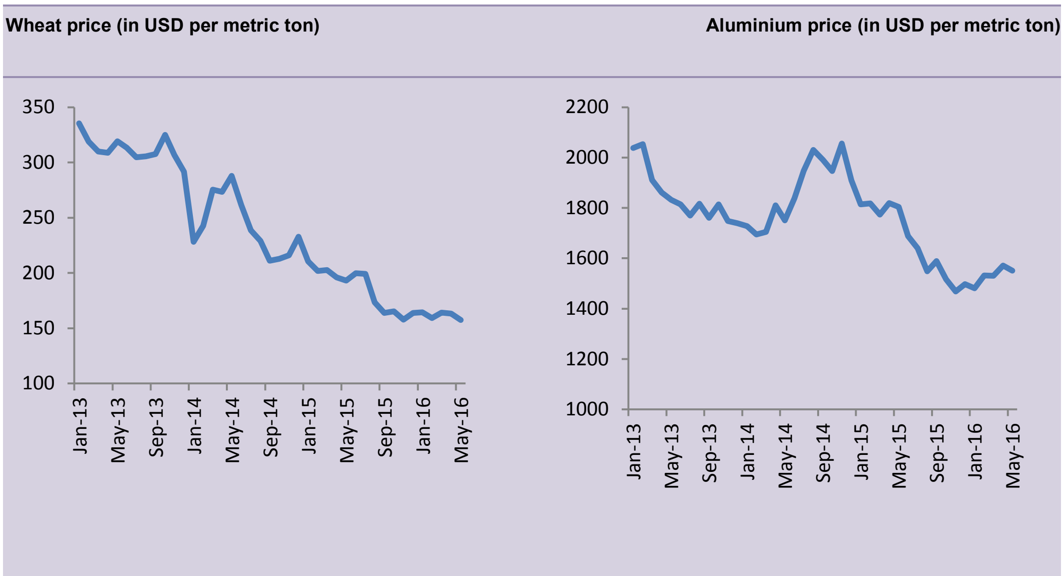


Source: StatBureau, Molson Coors

The decent price inflation for beer products compares with a cost of goods sold that continues to decrease, helped by cost savings but also by the strength of the USD and the global price weakness for some of the inputs (e.g. barley, wheat, aluminium, etc.). Indeed, in 2015, COGS per barrel for MillerCoors was down 1.3% and the trend is accelerating with a 3.4% decline in Q4 2015 and 5% in Q1 2016. The decline in COGS was in 2015 and will also be in 2016 partially offset by the investments in marketing and systems that the US subsidiary is making. But, on average, we are expecting US operating profit margins to increase to 17.7% in 2016 and 18.6% in 2017 from 17.5% in 2015. 2017 is also benefiting from the Eden brewery closure which is expected to be completed in Q3 2016.

Commodity prices in free fall

Fig. 13: Wheat and aluminium commodity prices



Source: World Bank

Restructurings in the UK are paying off

- In the UK, we expect significant progress in profitability as the company is rationalising its production footprint (closing Tadcaster and moving production from Burton-upon-Trent North to South) following the loss of the Heineken outsourcing business. Last year, profits slid because of the termination of the Modelo licencing agreement and the loss of the Heineken contract for brewing, but this year we expect some rebound. Furthermore, the USD strength leads to significant negative currency movements in the European division.

For the group as a whole, the integration of 100% of MillerCoors will have a significant impact on revenue and earnings. For ease of computation, we assume that the consolidation will happen on 1 January 2017, but in reality it will be somewhere in the second half of 2016. For 2017, we expect EPS to leap by 66.5% to USD5.45 from USD3.28 in 2016. Afterwards we are expecting relatively mediocre revenue growth of 1.7% p.a. over the next five years and 5.7% annual growth in EBIT. With a persistent low tax rate (15% this year and guided for 20-24% in the years after), we are looking for a high single-digit growth in net profit (8%).

5. Company profile

Molson Coors Brewing Company (Molson Coors) was formed on 9 February 2005, by the merger of Adolph Coors Company and Molson Inc, which were founded in 1873 and 1786, respectively. With pro forma operating profits of USD1.9bn, the company is the third largest brewer in the world in terms of profits behind ABI/SABMiller and Heineken. The Molson and Coors family shareholders still own 18% of the capital of the company, but, with different class A and B shareholdings, they control 93% of the A shares, which have most of the voting rights. Shareholders of the mostly widely traded class B shares only have voting rights in certain situations.

The company has a portfolio of owned and partner brands, including core brands Carling, Coors Light, Molson Canadian and Staropramen, as well as craft and speciality beers such as Blue Moon, Creemore Springs, Cobra and Sharp's Doom Bar. The company operates in Canada, the US, the UK & Ireland and in a series of Central European countries (Bosnia-Herzegovina, Bulgaria, Croatia, Czech Republic, Hungary, Montenegro, Romania, Serbia and Slovakia). Furthermore, it has an exporting business to various other countries (Japan, Mexico, Panama, Germany, Sweden, India, China, the Caribbean).

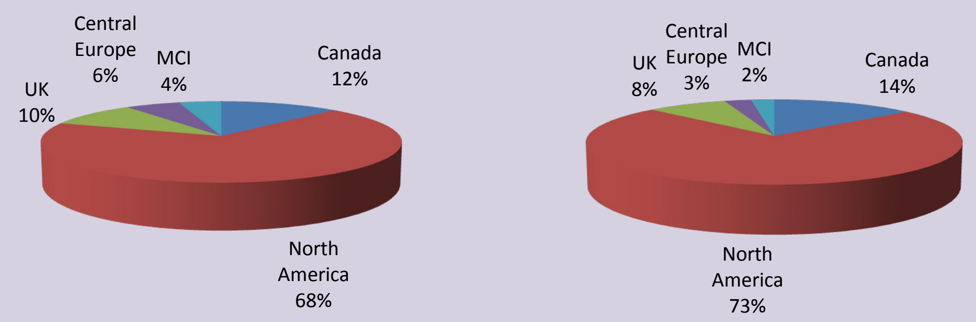
Molson Coors' brewing operations are mainly in mature markets: Canada, the US and the UK. In all three markets, the company takes second position in terms of market share. In Canada, the company has a 37% share of the market behind market leader Labatt (AB InBev) which has 43%; in the US, the company has a 42% economic interest in the MillerCoors joint venture with SABMiller (and it is planning to buy the latter's 58% economic interest) and has a 27% share behind the market leader AB InBev (46%). And, in the UK, it has an 18% share which is the same as AB InBev's and just behind market leader Heineken which has 20%.

After the full integration of MillerCoors, in 2017e, we expect that, in terms of revenues, the US is the largest contributor with 68%, followed by Canada 12% and the UK with an estimated 10%. On the basis of operating profits, we expect the US to be good for 73% and Canada for 14%. We estimate that the UK will account for around 8%.

Nearly 3/4trs of profit will be from the US

Fig. 14: Portfolio composition by geographic area

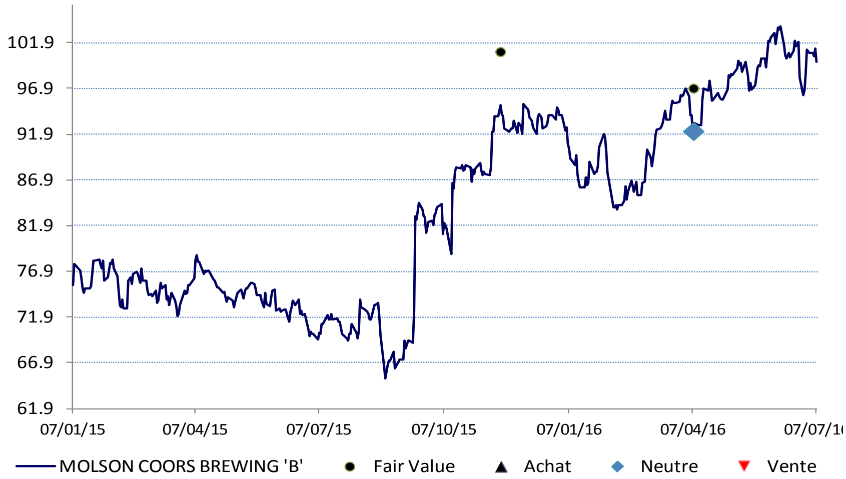
Net revenue, 2017e | **Operating profit, 2017e**



Source: Bryan, Garnier & Co ests.

Price Chart and Rating History

Molson Coors



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Ratings		
Date	**Ratings**	**Price**
07/04/16	NEUTRAL	USD93.99

Target Price	
Date	**Target price**
07/04/16	USD97
17/11/15	USD101

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Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

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Distribution of stock ratings

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