

18th July 2016

Business Services

SGS SA

Price CHF2,314

H1 results: Sustained top-line growth, but disappointed on margin

Fair Value CHF2400 (+4%)

BUY

Bloomberg	SGS VX
Reuters	SGS.VX
12-month High / Low (CHF)	2,314 / 1,626
Market Cap (CHF)	18,100
Avg. 6m daily volume (000)	22.30

ANALYSIS

- **Sustained top-line despite trading conditions remaining challenging...:** Total revenue reached CHF2,901m, in line with consensus (CHF2,896m) and slightly lower than our estimate of CHF2,927m, up 7% on a pro-forma basis with strong organic of 3.4% vs. 2.6% anticipated; organic growth particularly sustained despite trading conditions that remain challenging in the energy and mining industries due to reduced and delayed expenditure by clients. In fact, organic in **Mineral** (10.5% of consolidated revenue) was down 0.3%, -2.1% in **Oil, Gas and Chemicals** (18.9%) and -0.1% in **Industrial** (15%). On the other hand, sustained organic in **Certification** (5.4%) up 10.9%, in **Environment, Health & Safety** (7.8%) up 9.6% or in **Agriculture Food and Life** (15.3%) up 6.5%.
- **But disappointed on margin:** With an adjusted operating margin of EUR411m, this is clearly lower than our anticipation (consensus CHF435m and BG estimate of CHF439m). Actually adjusted operating margin was down 60bps at 14.2% vs. 14.8% last year. According to management, the decline was mainly attributable to the impact of investments in IT systems governing both laboratory operations and human resource management and the build-out of shared services infrastructure. Acquisitions as anticipated weighed on margins too. Nevertheless, **operating cash flow** was strong up CHF70m vs last year at CHF366m and net debt was down CHF179m vs. last year at CHF990m.
- **Management remains confident for the rest of the year:** For the FY, Management expects to deliver organic revenue growth of between 2.5% and 3.5% (our estimate is 3.3%). Regarding adjusted operating result, management announced that margin will be impacted “temporarily” as it was the case in H1 by additional corporate costs (our current estimate on adjusted operating margin 2016e is flat vs. last year at 16%).

VALUATION

- At the current share price, the stock is trading at 18.9x EV/EBIT 2016e and 17.9x 2017e which compares with a median historic multiple of 14.8x and CAGR 2015-2018 of 6.2%.

NEXT CATALYSTS

- Meeting/Conference call at 2.00pm (Geneva)
- Capital market days on 27th & 28th October (Krakow-Poland)

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