

15th July 2016

Luxury & Consumer Goods

The Swatch Group

Price CHF289.50

H1 preliminary results far worse than expected

Fair Value CHF270 vs. CHF370 (-7%)

SELL vs. NEUTRAL

Bloomberg	UHR.VX
Reuters	UHR.VX
12-month High / Low (CHF)	432.9 / 269.7
Market Cap (CHFm)	15,962
Avg. 6m daily volume (000)	260.2

	1 M	3 M	6 M	31/12/15
Absolute perf.	3.6%	-13.3%	-11.9%	-17.3%
Pers & H/H				
Gds	6.7%	2.2%	8.5%	1.9%
DJ Stoxx 600	5.6%	-1.6%	-0.3%	-7.5%

	2014	2015e	2016e	2017e
P/E	11.3x	14.4x	26.2x	22.3x
Div yield (%)	2.6%	2.6%	2.7%	2.9%

ANALYSIS

- The Swatch Group will release its H1 profits on July 21st. However, this morning the group has issued a press release highlighting that sales should be down 12% (we were expecting -5%) during this first semester to close to CHF3.7bn with very severe EBIT deterioration (expected to be down 50%). This implies EBIT at around CHF410m (CS:CHF550m) and an EBIT margin at 11.2% or 700bp decline. There is no more information in the press release except that, unsurprisingly, management rules out any job cuts despite the very challenging environment, in line with its long-term philosophy of considering employees as "investments".
- Consequently, we lower our FY 16 earnings by 25%, and currently expect FY sales to decline 8% vs a slight decrease previously. More importantly, while we were expecting FY profitability to be down by 170bp, we expect the EBIT margin to be down 450bp to 12.9%. These figures highlight again the clear operating impact on Swatch group of any sales reduction given the group policy of not adjusting costs even in a very difficult period as it is the case this year (and the situation in Europe will certainly not improved given last night's attack in Nice). Furthermore, we also question the group's communication policy as the CEO, Mr Hayek, was, even last March, expecting at least 5% organic sales growth in 2016 and was optimistic about the group's FY performance.

VALUATION

- Given these earning adjustments, we lower our FV from CHF370 to CHF270 and we downgrade our recommendation to Sell from Neutral.

NEXT CATALYSTS

- H1 release on July 21st.

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