Sector View

Construction & Materials

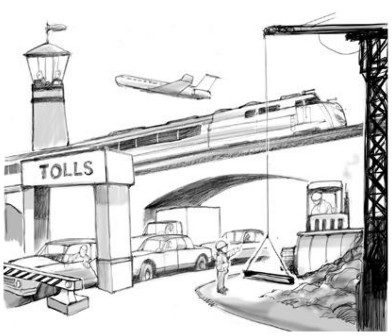
Q2 earning seasons review - Where is my upside gone?

	1 M	3 M	6 M	31/12/15
Cons & Mat	6.9%	6.4%	16.5%	4.5%
DJ Stoxx 600	1.6%	2.6%	7.2%	-6.1%

*Stoxx Sector Indices

Companies covered

CRH		**BUY**	**EUR30**
Last Price	EUR29.06	*Market Cap.*	EUR24,112m
EIFFAGE		**BUY**	**EUR73**
Last Price	EUR69.89	*Market Cap.*	*EUR6,855m*
HEIDELBERGCEMENT		**BUY**	**EUR86**
Last Price	EUR81.14	*Market Cap.*	*EUR16,099m*
IMERYS		**BUY**	**EUR72**
Last Price	EUR64.05	*Market Cap.*	*EUR5,097m*
LAFARGEHOLCIM		**BUY**	**CHF50**
Last Price	CHF51.4	*Market Cap.*	*CHF31,195m*
SAINT GOBAIN		**BUY**	**EUR46**
Last Price	EUR39.035	*Market Cap.*	*EUR21,661m*
VICAT		**NEUTRAL**	**EUR56**
Last Price	EUR57	*Market Cap.*	*EUR2,559m*
VINCI		**BUY**	**EUR72**
Last Price	EUR67.6	*Market Cap.*	*EUR40,262m*



Earning season for the sector has been positive, so far, for our coverage. Companies appeared to be properly managed, with usually improved profitability. Difficulties have not disappeared though, like macro uncertainties in Europe, a deflationist environment and sometimes poor volumes – but companies can deal with them. While French Contractors remain safe harbour, cement majors might benefit from a better momentum from some Emerging Markets. Saint-Gobain offers the most upside.

ANALYSIS

- French contractors remain a specific type of investment within the sector, with a significant exposure to toll roads (two thirds of EBIT) and infrastructures (half of sales or more). Toll roads traffic at end June is strong (+3.3% for Vinci Autoroutes, +4.1% for APRR) and Vinci has recently lift its FY guidance to 2.5% (vs less than 2% implicit previously). Even with limited price effect (less than 1.5%e for cars on 1st February 2016), EBITDA margin are likely to continue to improve. On the Contracting side, Vinci said to stand now at the trough of the cycle for French roadworks, while it might appear relatively soon for the other segments. On the valuation side, upsides are more limited but Vinci newsflow is likely to be filled with new M&A in energy and new concession projects. All in all, French Contractors remain safe harbours in difficult times.
- Unlike most of the cement players, CRH has not reported interim figures yet but has already indicated H1 2016 EBITDA should be close to cEUR1.1bn vs EUR1bn previously guided, presumably benefited from its unique exposure to North America (c60% of the EBITDA PF). Recent rumours regarding the possible inclusion of CRH into the EuroStoxx50 index has helped too. Hence share price has been strong this year (+9%), significantly reducing the upside. The three other cement players under coverage have all reported good Q2 figures, with usually significant EBITDA margin improvement. Comments on the US markets are usually positive (cement shipments up 7.3% at end June, housing starts up 5.6% y/y at end July), with good momentum for prices. In LatAm, situation is more contrasted, with some positive trends in Mexico and some prices increase in Colombia or Argentina but of course situation is complicated for Brazil. Africa-Middle East region trends are mixed, with some difficulties in Nigeria (currency, security), illustrated by very poor figure for Dangote Cement in Q2 2016 (EBITDA margin at 40% vs 59% in Q2 2015) but better trends in some country like Egypt or Algeria. Finally, in Asia, India market continue to recover with good volumes in H1 for Vicat (+28%) but more subdued for LHN (+1.5%) due to pricing policy, and overall decent outlook. Indonesia looks more complicated with volumes increase but not everywhere (not within the Heidelberg footprint for instance). It worth underlying Italcementi H1 2016 EBITDA performance was poor, down 7.6% at EUR300m, which is a negative read-across for HEI. It worth underlying however than HEI has announced this morning the disposal of the Martinsburg Cement Plant in the US, in order to comply with anti-trust demands and its EUR1bn disposal target has been now exceeded.
- Both Saint-Gobain and Imerys have reported well-oriented Q2 results, although Imerys is still penalised by very modest volumes trends (-3.3% in Q2). We have been reassured by comments of SGO regarding the new-built activity in France, which "showed the first signs of improvement" (Nexity has reported reservations up +38% in H1 2016, housing starts are up 5% rolling-12 months at end June), but the share price reaction has been limited (1.7% on 29 July), probably penalised by unchanged comments for the French renovation and a disappointing publication for the French GDP in Q2 (0%) on the same day. France represents a quarter of SGO sales. SGO and NK are the two stocks for which we still got some decent upside.

Revenues organic growth and operating margin in the first two quarters

y/y	HEI	NK	LHN	SGO	VCT	DG
Q1 sales organic growth (%)	1.0%	-1.8%	0.1%	1.8%	6.5%	-3.3%
Q2 sales organic growth (%)	1.0%	-2.6%	-2.1%	3.8%	2.5%	-1.9%
Q1 EBITDA/EBIT margin (bps)*	70	30	-280	nc	nc	nc
Q2 EBITDA/EBIT margin (bps)*	140	100	210	nc	nc	nc
H1 EBITDA/EBIT margin (bps)*	110	70	-10	60	50	120

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

NEXT CATALYSTS

- CRH to report interim results on 25 August and Eiffage on 31th August.

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BUY ratings 55.7% NEUTRAL ratings 33.6% SELL ratings 10.7%

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