Fresenius SE

Price EUR67.05

KABI weak NA sales surprised but margins are keeping-up

Fair Value EUR73 (+9%) **BUY-Top Picks**

Bloomberg	FRE GR
Reuters	FREG.DE
12-month High / Low (EUR)	69.8 / 53.1
Market Cap (EURm)	36,633
Ev (BG Estimates) (EURm)	51,931
Avg. 6m daily volume (000)	1 204
3y EPS CAGR	9.0%

	1 M	3 M	6 M	31/12/15
Absolute perf.	1.2%	5.6%	10.4%	1.6%
Healthcare	2.2%	8.3%	3.7%	-2.9%
DJ Stoxx 600	2.3%	-0.5%	-0.5%	-7.1%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	27,626	29,070	30,963	33,250
% change		*5.2%*	*6.5%*	*7.4%*
EBITDA	4,990	5,432	5,799	6,287
EBIT	3,875	4,269	4,561	4,957
% change		*10.2%*	*6.8%*	*8.7%*
Net income	1,358	1,576	1,681	1,843
% change		*16.1%*	*6.6%*	*9.6%*

	2015	2016e	2017e	2018e
Operating margin	14.0	14.7	14.7	14.9
Net margin	4.9	5.4	5.4	5.5
ROE	7.2	7.6	7.5	7.6
ROCE	3.8	4.2	4.3	4.6
Gearing	118.4	107.5	99.2	90.1

(EUR)	2015	2016e	2017e	2018e
EPS	2.62	2.90	3.09	3.39
% change	*-*	*10.8%*	*6.6%*	*9.6%*
P/E	25.6x	23.1x	21.7x	19.8x
FCF yield (%)	2.0%	4.2%	4.2%	4.5%
Dividends (EUR)	1.69	1.87	2.00	2.19
Div yield (%)	2.5%	2.8%	3.0%	3.3%
EV/Sales	1.8x	1.8x	1.7x	1.6x
EV/EBITDA	10.1x	9.6x	9.0x	8.3x
EV/EBIT	12.9x	12.2x	11.4x	10.6x

KABI sales surprised with a -6% organic deline in NA. However, increased sales and EBIT guidance highlighted management's ability to monitor an easing drug shortage situation. We remain at Buy and maintain our EUR73 target price.

ANALYSIS

- While KABI sales appeared mixed and notably in NA affected by IV Gx, they were clearly above management's conservative estimates as organic sales guidance has been raised from roughly flat to low single-digit. Indeed, while KABI North America performed well in H1 with a 6% organic increase, Q2 numbers reflected a settling of dust with 1/ organic growth down -6% QoQ to EUR510m (35% of sales) after 2/ 20% organic growth in Q1 2016. While this might be seen as a U-turn in the group's ability to generate growth at divisional level as neither we nor the consensus were expecting organic growth to be in negative territory for the region, it was the result of an underperformance by the IV Gx business. We believe that this weak NA performance over the quarter should be put in the context of 1/ high comparison basis with organic growth of 24% in Q2 2015 2/ three IV generic drugs launched in Q1, none in Q2 and 3/ Neostigmine's (IV Gx) sales decrease with competition entrance over the first half of the year. Entering H2, both back-end loaded drug launches (at least three expected; 6-10 drugs launches guidance reiterated by management) and stabilisation of Neostigmine sales should act as a support to organic sales growth, which we would expect in the 1-3% range (both in Q2 and Q4). This bodes well with updated FY2016 sales guidance for low single-digit organic sales growth (vs roughly flat) and our estimates of 4% organic growth for the year. Management commented on conservative internal estimates, which might well be a sign of confidence in reaching this new guidance without concerns.
- In Europe, the low-end of guidance should be targeted now (i.e. low single-digit) while a dynamic trend in emerging markets should enable the group to deliver low double-digit organic sales growth (vs. mid/high single-digit). Note that in emerging markets, price reductions should be offset by a strong volume increase. Moreover, we see the infusion therapy business (up 8% organic in Q2), helped by the recently penned 10-year contract with Becton Dickinson as further supporting sales in NA and EM for the remainder of the year. Note that overall sales performance and growth prospects triggered a sales guidance increase for KABI i.e. 3-5% organic growth vs. low single-digit.
- Margin-wise, we were pleased to see an improvement in Fresenius KABI margins in North America (up 210bp to 43.1%) despite an easing of the drug shortage situation. KABI has a strong comp basis for the remainder of the year. However, we believe that management's ability to keep-up with high margins in the US which triggered an increase in guidance (3-5% vs roughly flat) is reassuring as it should be done in the context of higher R&D expenditures in H2 (incurred from investment in the recently acquired BD plant).
- Note that HELIOS progressed well in H1 with a 4.5% organic growth and that this is already in the high range of the 3-5% anticipated organic growth rate for the year while HELIOS historically performed better in H2.
- On the M&A front, the CEO mentioned that a few strategic blanks might be filed overtime. We do not rule out that this might concern the infusion device space as competition intensifies and there is a need for a differenciated offer.

VALUATION

- We reiterate our BUY recommendation and EUR79 Fair Value

NEXT CATALYSTS

- H2 2016 : ≥3 injectable product launches at KABI / Q3 results on 27th October

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