23rd August 2016

Food & Beverages

Heineken

Price EUR79.51

On the road with Anna

Fair Value EUR88 vs. EUR90 (+11%) **BUY**

Bloomberg	HEIA NA
Reuters	HEIN.AS
12-month High / Low (EUR)	85.2 / 67.9
Market Cap (EUR)	45,798
Ev (BG Estimates) (EUR)	59,649
Avg. 6m daily volume (000)	631.8
3y EPS CAGR	8.1%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-5.5%	-3.1%	6.5%	0.9%
Food & Bev.	-1.0%	4.0%	5.4%	0.0%
DJ Stoxx 600	0.0%	0.7%	2.6%	-6.9%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	20,511	20,530	21,033	21,595
% change		*0.1%*	*2.4%*	*2.7%*
EBITDA	4,975	5,080	5,412	5,760
EBIT	3,381	3,486	3,694	3,932
% change		*3.1%*	*6.0%*	*6.4%*
Net income	2,048	2,158	2,385	2,586
% change		*5.4%*	*10.5%*	*8.4%*

	2015	2016e	2017e	2018e
Operating margin	16.5	17.0	17.6	18.2
Net margin	10.0	10.5	11.3	12.0
ROE	15.1	14.7	15.0	14.9
ROCE	8.2	8.3	8.8	9.4
Gearing	86.0	74.8	61.9	49.4

(EUR)	2015	2016e	2017e	2018e
EPS	3.57	3.77	4.16	4.51
% change	-	*5.4%*	*10.5%*	*8.4%*
P/E	22.2x	21.1x	19.1x	17.6x
FCF yield (%)	3.7%	3.8%	5.1%	5.7%
Dividends (EUR)	1.11	1.12	1.24	1.34
Div yield (%)	1.4%	1.4%	1.6%	1.7%
EV/Sales	2.9x	2.9x	2.7x	2.6x
EV/EBITDA	12.1x	11.7x	10.7x	9.7x
EV/EBIT	17.8x	17.1x	15.6x	14.2x

Heineken's stock has shown some weakness since first half figures were published, with the company guiding towards a tougher second half in terms of comparables and currencies. However, nothing has changed in terms of fundamentals (well diversified, high emerging markets exposure, most premium portfolio) and we believe the current share price is an attractive Buy opportunity.

On 1st August when Heineken published excellent first half figures (4.2% organic revenue growth and 12.6% organic operating profit growth) we updated provisionally our numbers and increased our Fair Value to EUR90 from EUR83. We have now worked the numbers more in detail and shaved our 2016 and 2017 profit forecasts by about 2% and also lowered our FV to EUR88 (fromEUR90). However this is all just fine-tuning and there is no change in the company's underlying strong fundamentals.

ANALYSIS

- **Currency drag:** Our forecasts take into account a EUR200m drag on operating profit from adverse currency movements in the Mexican Peso, the Brazilian Real, the British Pound, the Russian Rouble, and the Nigerian Naira. Most of these currency movements shold work themselves through by the end of the year, but the impact of the Nigerian Naira, will continue to be felt in 2017 (especially H1). In addition to the impact on operating profit, the Naira devaluation also impacts "Other net financial expenses" by about EUR40m due to its impact on outstanding foreign payables (revaluation of accumulated payables at the floating rate).

- **All-in margin expansion of 40bps might prove too conservative**: The company is guiding for operating margin expansion of 40bp (including currency movements and new acquisitions). We are slightly more positive and estimate full year margin expansion at 50bp to 17% from 16.5% as we expect good top-line growth in the high margin Asian business (estimated 31.8% operating margin) and premiumisation in the Americas, to offset margin pressure in the African operations. A 50bp margin expansion over the full year takes into account some margin pressure in the second half (margins were up 124bp in the first half) stemming from 1) tough comps in Europe where volumes surged by 7% in Q3 2015 on the back of excellent weather, 2) tougher comps in the Americas where organic volume growth in Mexico and US started accelerating in the second half of the year, 3) a low single-digit volume decline in Nigeria in the second half compared to mid-single digit growth (as in Q1 2015, volumes declined sharply with the presidential elections). (Of course as Heineken owns only 54% of the Nigerian operations the negative impact of the Naira devaluation and volume weakness is also reflected in lower minorities). Our 50bp growth forecast compares with a 50bp decline in our model for AB InBev and a 10bp decline for Carlsberg.

- **Investment thesis confirmed:** Heineken has a well diversified geographic footprint providing balanced growth. For 2016 (and this was also the case in H1), underlying trading conditions in Nigeria (est. 10% of 2015 EBIT) are difficult, but Mexico (est. 11% of 2015 EBIT) is benefiting from a positive economic environment, which high consumer confidence in Vietnam (est. 12% 2015 EBIT) is more than offsetting low consumer confidence in Brazil (est. 1% of 2015 EBIT). The company is also highly geared towards developing markets, which in H1 represented 66% of group volumes, 51% of revenue and 60% of operating profit. Furthermore, the company is number one in high-end beers that account (BG est.) for 36% of volumes and 60% of operating profit compared with 25%/37% at Carlsberg,17%/30% at AB InBev and 11%/28% at Molson Coors.

VALUATION

- Our Fair Value of EUR88 is based on a risk-free rate of 1.6%, an equity risk premium of 7%, a beta of 0.95x and a long terms growth rate of 3.3%

NEXT CATALYSTS

- 26th October 2016: trading update Q3

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