

**Hermès Intl.**

Price EUR353.00

Share price decline offers a buy opportunity!

Fair Value EUR370 (+5%)

BUY

Bloomberg	RMS FP
Reuters	HRMS.PA
12-month High / Low (EUR)	398.6 / 291.6
Market Cap (EURm)	37,266
Ev (BG Estimates) (EURm)	35,494
Avg. 6m daily volume (000)	56.10
3y EPS CAGR	13.4%

**H1 results were quite reassuring, with a 140bp EBIT margin gain to 33.9%. Nevertheless, management still anticipates a “slight” FY EBIT margin improvement. We are slightly more optimistic and we expect a 80bp profitability improvement to 32.6%, implying +30bp in H2 as positive FX impact will be less positive than in H1. We leave unchanged our estimates, our EUR370 FV and our Buy recommendation. Yesterday’s share price decline (-9%) is, in our view, a good buying opportunity for medium term.**

**ANALYSIS**

	1 M	3 M	6 M	31/12/15
Absolute perf.	-11.3%	9.6%	7.5%	13.2%
Pers & H/H Gds	-4.3%	4.4%	-0.4%	-0.3%
DJ Stoxx 600	-2.2%	5.6%	-1.8%	-7.5%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	4,841	5,165	5,630	6,100
% change		6.7%	9.0%	8.3%
EBITDA	1,605	1,746	2,040	2,265
EBIT	1,541	1,683	1,880	2,095
% change		9.2%	11.7%	11.4%
Net income	973.0	1,106	1,255	1,418
% change		13.7%	13.5%	13.0%

	2015	2016e	2017e	2018e
Operating margin	31.8	32.6	33.4	34.3
Net margin	20.1	21.4	22.3	23.2
ROE	26.0	25.9	24.2	22.7
ROCE	43.8	43.4	43.0	43.2
Gearing	4.3	3.7	3.1	2.6

(EUR)	2015	2016e	2017e	2018e
EPS	9.26	10.52	11.94	13.49
% change	-	13.7%	13.5%	13.0%
P/E	38.1x	33.5x	29.6x	26.2x
FCF yield (%)	2.5%	2.4%	2.7%	3.0%
Dividends (EUR)	3.35	3.80	9.00	4.80
Div yield (%)	0.9%	1.1%	2.5%	1.4%
EV/Sales	7.4x	6.9x	6.2x	5.6x
EV/EBITDA	22.3x	20.3x	17.1x	15.1x
EV/EBIT	23.2x	21.1x	18.6x	16.3x

- H1 16 sales grew 7% organically, of which +8% in Q2. The most important information was the strong revenue increase in leather goods (+16% in H1 of which +17% in Q2). Silk sales were affected by poor activity in Hong Kong and less tourists in France despite a less negative trend in Q2 vs Q1 (-4.3% vs -9.2%). By geographical area, Hermès achieved a reassuring performance in France versus its peers with a 8.8% sales increase in Q2. Paris stores were slightly up despite lower traffic, as a higher average basket offset fewer tourists. In H1, we highlight that sales in Mainland China were still growing while they remained stable in HK and down HSD in Macau, which again means an outperformance versus peers. Furthermore, Hermès saw more activity in the UK in Q2 and even in recent months, thanks to GBP erosion (consequence of Brexit).
- H1 2016 results were slightly above market expectations, with an EBIT margin up 140bp to 33.9% with a EUR827m EBIT (consensus was at EUR820m). The profitability improvement comes mainly from gross margin, which gained 200bp to 68.4%. This positive trend has been achieved thanks to a hedging gain, of which 100bp is one off and will not recur in H2. Beyond FX effect, Hermès benefited from favourable distribution mix (outperformance of retail sales which grew 8% versus +3% for wholesale) and more importantly from positive product mix thanks to 16% Leather Goods sales increase. On the other hand, upstream activity integration in Leather Goods affected group gross margin, as this business is not yet profitable. In H1, communication costs grew no more than 3%, which implies 4.1% of sales vs 4.2% in H1 2015.
- For full year 2016, Hermès management expects sales to grow slightly below 8%. We anticipate a 7% increase, in line with H1 performance and Hermès CEO added during yesterday’s analysts meeting that he is quite optimistic on Q3 sales momentum, despite some uncertainties. Concerning profitability, management expects a “slight” EBIT margin improvement adding that in H2, the group will spend more on communication than in H1 as more stores will open or reopen (after renovation and extension) in the coming months and particularly in Q4. FY 16 Cap ex will reach around EUR280m (5.5% of sales) versus EUR250m last year, of which half will be dedicated to stores renovation or openings. For instance, a flagship store will be opened in October in Rome after the one in Singapore (Liat Towers) in H1. Each year, Hermès opens on average three to four stores including one in Mainland China, but renovates and extends around 15 stores.
- Hermès management does not want to quantify anymore its goal of annual sales growth, adding that it will remain ambitious. Furthermore, target for internal purpose has not been changed. Therefore, we do not change our expectations both for 2016 and 2017. Furthermore, leather goods volume annual growth target remains at 8% thanks to production capacity increase. This implies around 10% sales increase for this activity which accounts for 49% of group sales.

**VALUATION**

- Despite yesterday’s 9% share price decline, the stock has gained 14% YTD, but has lost more than 10% versus its mid-August peak (EUR399). We remain at Buy on the stock with an unchanged EUR370 FV and we still see RMS as one of the best investments among our luxury stocks sample. Take the opportunity of yesterday share price decline to buy the share with a medium-term view.

**NEXT CATALYSTS**

- Q3 sales to be reported on 3<sup>rd</sup> of November.

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