BRYAN, GARNIER & CO

INDEPENDENT RESEARCH

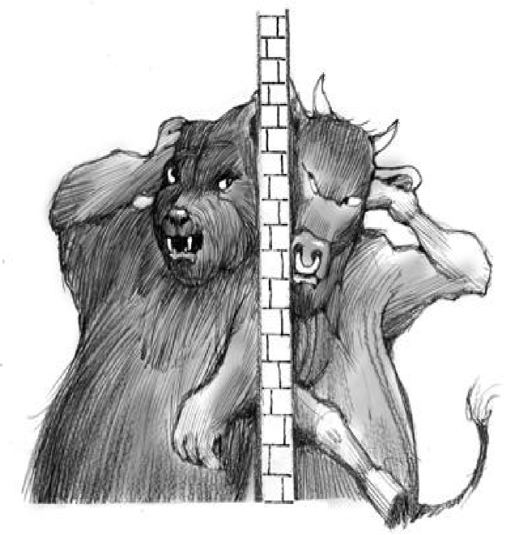
Top Picks

7th July 2016

Top Picks Q3 2016

Top Picks

ABLYNX		**BUY**	**EUR18**
Last Price	EUR11.505	*Market Cap.*	EUR700m
AHOLD		**BUY**	**EUR22**
Last Price	EUR20.465	*Market Cap.*	EUR17,075m
ELIOR		**BUY**	**EUR23**
Last Price	EUR19.57	*Market Cap.*	EUR3,372m
FRESENIUS SE		**BUY**	**EUR73**
Last Price	EUR65.56	*Market Cap.*	EUR35,804m
IMERYS		**BUY**	**EUR72**
Last Price	EUR56.76	*Market Cap.*	EUR4,517m
INFINEON		**BUY**	**EUR15**
Last Price	EUR12.64	*Market Cap.*	EUR14,310m
IPSEN		**BUY**	**EUR63**
Last Price	EUR55.15	*Market Cap.*	EUR4,591m
LVMH		**BUY**	**EUR171**
Last Price	EUR134.55	*Market Cap.*	EUR68,304m
MELIA HOTELS		**BUY**	**EUR15**
Last Price	EUR9.65	*Market Cap.*	EUR2,217m
MONCLER		**BUY**	**EUR17**
Last Price	EUR14.14	*Market Cap.*	EUR3,537m
SHIRE PLC		**BUY**	**6500p**
Last Price	4762p	*Market Cap.*	GBP42,805m
VEOLIA ENVIRONNEMENT		**BUY**	**EUR23**
Last Price	EUR19.11	*Market Cap.*	EUR10,766m
VINCI		**BUY**	**EUR72**
Last Price	EUR62.67	*Market Cap.*	EUR37,267m
WIRECARD		**BUY**	**EUR54**
Last Price	EUR38.71	*Market Cap.*	EUR4,783m

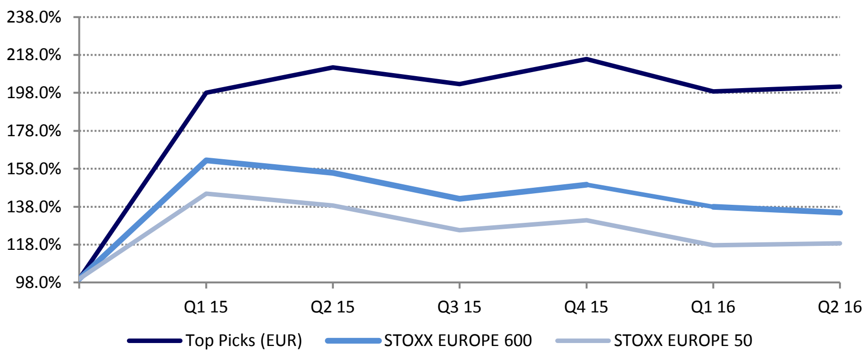


This is the third volume of our quarterly 'Top Picks' for 2016. This list is not intended to be a model portfolio, but simply reflects a pure stock-picking exercise in our coverage universe. It reflects a bias towards themes that we believe fit best with the current very uncertain, volatile market environment: self-helped businesses, robust organic growth, limited outside interference, earnings momentum and/or secure shareholders' returns.

- Even if the DJ Stoxx600 dipped only 2.3% in Q2 2016, we experienced an even more challenging market environment than in Q1, especially due to the Brexit drama. In this context, the performance of our list has been pretty decent, down 0.8% (and up 0.8% including dividends). Since the creation of our list in Q1 2012, our cumulative performance has been +100% vs. +35% for the Stoxx600.
- We have started Q3 just like we ended Q2: full of uncertainties, including on potential macro impacts, market disruptions, money flows and FX. And this makes it one of the toughest quarters to assess. On top of that, we all know how dumpy financial markets can be during summer…
- So for our Q3 list, we have tried to remain selective inside our ongoing growing coverage (14 stocks out of 144), and focus on companies that offer better-than-average, short-term visibility (which is why we refrain from including any insurance stock for example): self-helped drivers, robust organic growth, limited outside interference, earnings momentum and/or secure shareholders' returns.

This document is a compilation of the notes written to update our Top Pick list

	Perf Q1 16	Perf Q2 16	Perf Historique
Top Picks (EUR)	-7.93%	1.28%	101.34%
STOXX EUROPE 600	-7.73%	-2.27%	34.93%
STOXX EUROPE 50	-10.00%	0.83%	18.72%



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Our top picks for 3Q 2016 are

Changes :

+ABLYNX
+IMERYS
+INFINEON
+SHIRE
+VEOLIA ENV.
+VINCI
+WIRECARD

-ACTELION
Out 24th June
-ATOS
-ACCORHOTELS
-ABLYNX
-AXA
-HEIDELBERGCEMENT
-WIRECARD

Fig. 1: Valuation ratios: 3Q 2016 Top Picks

	Market Cap. (EUR)	EV/EBIT(x)		PER (x)		RDT (%)			
		2015e	2016e	2015e	2016e	2015e	2016e	Reco	FV
ABLYNX	702	-36.5	-36.6	-11.4	-10.2	0.0%	0.0%	BUY	18.0
AHOLD	17 013	14.6	13.8	20.6	18.0	2.6%	2.7%	BUY	22.0
ELIOR	3 350	15.2	13.8	24.4	17.2	1.6%	2.1%	BUY	23.0
FRESENIUS SE	35 537	12.7	11.9	24.9	22.5	2.6%	2.9%	BUY	73.0
IMERYS	4 421	13.2	11.8	15.6	13.6	3.1%	3.4%	BUY	72.0
INFINEON	13 597	14.9	12.6	19.9	15.0	1.5%	1.7%	BUY	15.0
IPSEN	4 515	13.7	13.6	19.5	18.9	1.6%	1.6%	BUY	63.0
LVMH	67 266	10.8	10.3	18.6	16.6	2.7%	2.9%	BUY	171.0
MELIA HOTELS	2 168	17.9	15.3	48.7	27.7	0.3%	0.6%	BUY	15.0
MONCLER	3 515	14.1	12.3	20.5	18.6	1.0%	1.2%	BUY	17.0
SHIRE PLC	43 227	23.1	19.7	18.0	17.1	0.3%	0.3%	BUY	6500.0
VEOLIA ENV	10 569	16.5	13.0	27.7	19.2	3.9%	4.5%	BUY	23.0
VINCI	36 993	13.0	12.0	17.4	16.2	3.0%	3.3%	BUY	72.0
WIRECARD	4 708	20.3	15.5	28.7	20.8	0.3%	0.4%	BUY	54.0

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

Fig. 2: Dividend payments: 3Q 2016 Top Picks

Top Picks	Ex-Dividend date	Amount
MELIA	14th July	€0.032

Source: THOMSON REUTERS

Our Top Picks are updated and published every quarter.

Top picks for 2Q 2016 performances

	2Q 2016 perf.		incl. Div.	
	Euro	Local Ccy	Euro	Local Ccy
ABLYNX	-17.8%	-17.8%	-9.88%	-9.9%
ACCOR)	-6.6%	-6.6%	-3.02%	-3.0%
ACTELION	14.5%	13.6%	14.91%	24.3%
AHOLD KON	0.7%	0.7%	6.22%	6.2%
ATOS	4.5%	4.5%	6.05%	6.0%
AXA	-13.0%	-13.0%	-11.41%	-11.4%
ELIOR GROUP	1.8%	1.8%	7.60%	7.6%
ESSILOR INTL	9.5%	9.5%	10.00%	10.0%
FRESENIUS (XET)	2.5%	2.5%	4.53%	4.5%
HEIDELBERGCEMENT (XET)	-9.6%	-9.6%	-8.49%	-8.5%
IPSEN	9.83%	9.83%	9.83%	9.8%
MELIA HOTELS INT	-6.53%	-6.53%	-6.53%	-6.5%
WIRECARD (XET)	-0.30%	-0.30%	0.12%	0.1%
2Q 2016* Top picks average Perf.	**-0.80%**	**-0.87%**	**1.53%**	**2.26%**
STOXX EUROPE 600	-2.27		-0.36	
STOXX EUROPE 50	0.83		2.82	

Source : Bryan Garnier

**calculation based on the opening prices of the day the stock has been removed.*

Stocks removed on 24th June

Ablynx, Accor, Atos, AXA, Heidelbergcement, Wirecard.

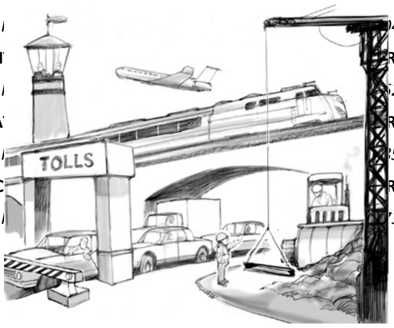
Construction & Materials : TOP PICKS Q3 16: A combination of decent visibility (VINCI) and a bit of cyclicality (Imerys)

	1 M	3 M	6 M	31/12/15
Cons & Mat	-7.4%	-4.9%	-5.9%	-5.9%
DJ Stoxx 600	-5.1%	-2.3%	-9.8%	-9.8%

*Stoxx Sector Indices

Companies covered

CRH		**BUY**	**EUR30**
Last Price	EUR26	*Market Cap.*	EUR21,571m
EIFFAGE		**BUY**	**EUR73**
Last Price	EUR64.21	*Market Cap.*	*EUR6,298m*
HEIDELBERGCEMENT		**BUY**	**EUR86**
Last Price	EUR67.47	*Market Cap.*	*EUR12,679m*
IMERYS		**BUY**	**EUR72**
Last Price	EUR57.53	*Market Cap.*	*EUR4,578m*
LAFA			**F50**
Last I			*4m*
SAIN			**R46**
Last I			*2m*
VICA			**R56**
Last I			*5m*
VINC			**R72**
Last I			*3m*



LOOKING BACK ON Q2 2016

Q2 has been a disappointing quarter for stocks in the construction and building materials sector. Apart from CRH (up 3.7%), no genuinely positive performance was noted. Cyclical players have been under pressure since roughly the second half of April and of course Brexit has taken its toll more recently.

In addition, investors have taken profits on Eiffage and VINCI, after a very good performance in 2015 and in Q1 2016 - despite an impressive start to the year on the toll roads traffic side (6.5% APRR, 7.2% VINCI Autoroutes).

WHAT WE SEE FOR Q3 2016

The first quarter is usually not the most relevant one for construction and building materials financial performance, as it is usually polluted by calendar and weather effects. It is a modest quarter too, especially for cement players. Second quarter publications, expected in late July/early August for most companies in the sector, should be much more representative of underlying business trends. We expect a satisfactory performance here: further improvements in key cement markets, in particular the US and India, while prices might gradually improve.

Nevertheless, due to the Brexit vote, we expect investors to be much more sensitive to risk and cyclicality, especially for companies exposed to Europe. Therefore, we would be cautious during the third quarter on Saint-Gobain (67% of 2015 sales exposed to Western Europe - 12% to the UK), Vicat (c50% of 2015 sales), CRH (c36% of EBITDA), HeidelbergCement (around 30% of sales exp. to Western & Northern Europe). On the currencies side however, the riskiest stock is probably LafargeHolcim, which reports in CHF while most revenues are generated outside of Switzerland, while CRH should benefit from its US exposure (c38% of EBITDA)

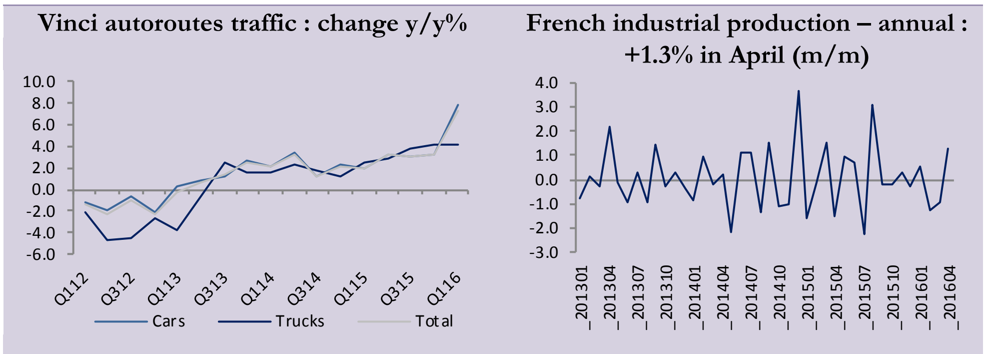
CONCLUSIONS AND TOP PICKS

Following the Brexit vote, we have withdrawn HeidelbergCement from the Top Pick list, due to its cyclical profile. In a more cautious approach, we have chosen VINCI and Imerys as Top Picks for the Q3 period:

- Alongside Eiffage, VINCI is the least cyclical stock in our coverage. 63% of 2015 EBITDA was generated by toll roads and 8% by airports. We see no obvious risks on toll roads traffic, on the contrary. Light vehicles traffic might continue to benefit from macro uncertainties (cheaper local holidays favoured) and geopolitical risks (public transport avoided) and heavy vehicle traffic from slightly positive industrial production (+1.3% in April, +0.6% on 12 months). We foresee 2% y/y traffic growth in Q2, while players could actually report stronger figures. On the contracting side, the group is mostly exposed to non-residential (c25% est. of total sales) and civil works (c55% est.) and to France (c60% of sales). We are presumably close to the trough in France for Construction and we see no risk of negative newsflow during the Summer: The Grand Paris is not likely to be disturbed by Brexit and VINCI order intakes were up 12% in Q1. Finally, 7% of VINCI sales are generated in the UK but we doubt strong earnings will be reported this year, due to VINCI Construction UK woes on a tramway project (losses last year, close to breakeven this year). VINCI reports H1 figures on 28th July post market and we expect a 1.2% decline for sales at EUR17.7bn and Operating income (from ordinary activities) at EUR1.63bn (9.2% margin, up 60bps, partly due to a mix effect).

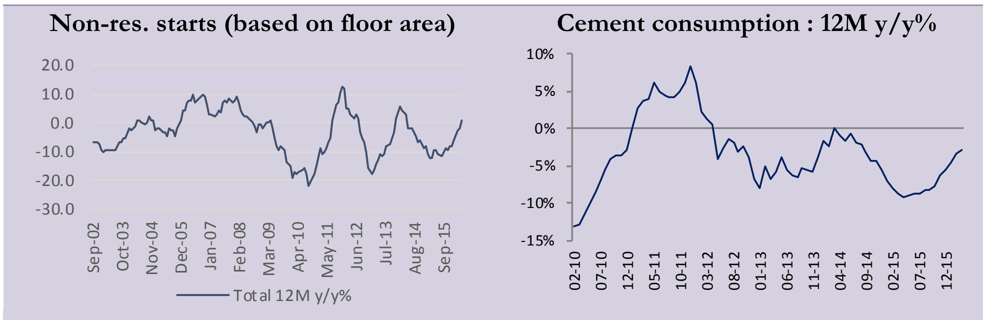
- We have added Imerys to the Top Pick list for the third quarter in order to shake it up somewhat. Imerys is cyclical yet much more resilient than Saint-Gobain for instance, or a cement player. We have therefore introduced some cyclicality but not too much (Imerys' Beta stands at 0.9): it is very well diversified (in term of markets and countries), has numerous leadership positions and operating margins are more than decent at 13%. Timing looks fine: Q1 2016 was good, with a lower volume decline (-2.6% vs -5.9% in 2015) and margin improvement (+30bps on reported current EBIT) while the comparison basis will remain easier. Proppant sales of EUR22m were mostly generated in Q1 and this division mostly reported losses as of Q2 2015. H1 figures will be reported on 27th July and we expect sales at EUR1.1bn for Q2 2016 (-1.5% lfl) and current operating income at EUR158m (14.3% margin).

Fig. 3: Vinci: Traffic performance and industrial production



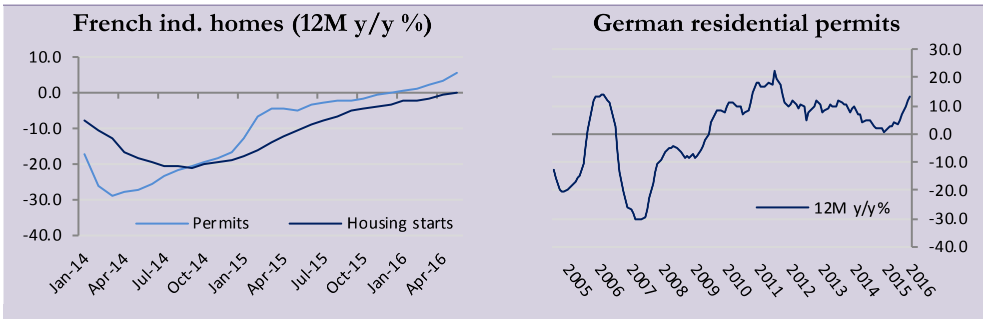
Sources: Vinci, Insee, Bryan, Garnier & co

Fig. 4: Vinci: French non-residential statistics and French cement volumes



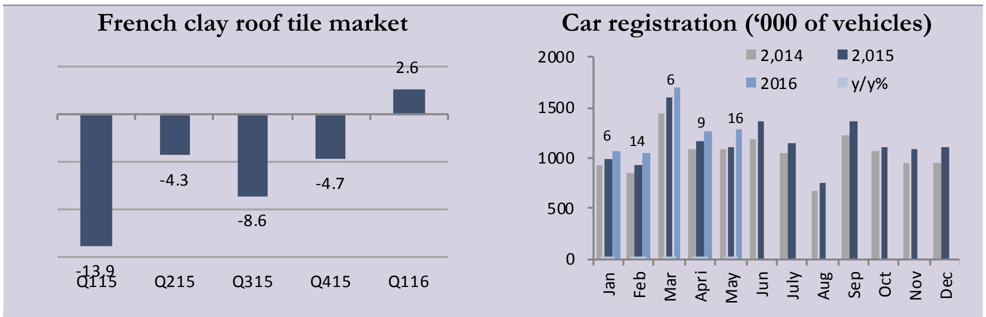
Sources: French government, SFIC, Bryan, Garnier & co

Fig. 5: Imerys: French individual homes market, German permits



Sources: French government, Destatis.com, Bryan, Garnier & co

Fig. 6: Imerys: French clay roof tile market – European autos



Sources: Unicem, ACEA, Bryan, Garnier & co

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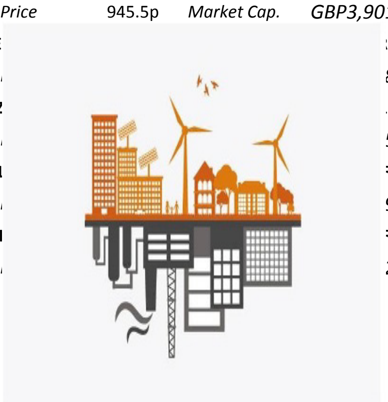
Utilities : TOP PICKS Q3 2016: VEOLIA

	1 M	3 M	6 M	31/12/15
Utilities	-0.2%	2.8%	-2.6%	-2.6%
DJ Stoxx 600	-5.1%	-2.3%	-9.8%	-9.8%

*Stoxx Sector Indices

Companies covered			
ALBIOMA		**BUY**	**EUR16**
Last Price	EUR13.85	*Market Cap.*	EUR413m
AMOEBA			
Last Price	EUR25.7	*Market Cap.*	*EUR154m*
E.ON		**BUY**	**EUR10.2**
Last Price	EUR9.026	*Market Cap.*	*EUR18,061m*
EDF		**BUY**	**EUR13.8**
Last Price	EUR10.97	*Market Cap.*	*EUR22,085m*
EDP RENOVAVEIS		**NEUTRAL**	**EUR7.5**
Last Price	EUR6.78	*Market Cap.*	*EUR5,914m*
ENGIE		**BUY**	**EUR16.8**
Last Price	EUR14.51	*Market Cap.*	*EUR35,336m*
PENNON GROUP		**SELL**	**830p**
Last Price	945.5p	*Market Cap.*	*GBP3,901m*
RWE			**9.5**
Last			*8m*
SUEZ			**7.5**
Last			*5m*
VEOL			**23**
Last			*9m*
VOLT			**13**
Last			*2m*



LOOKING BACK ON Q2 2016

The **Utilities sector** performed better than the **Stoxx 600** during Q2 2016 *(2.8% for SX6P vs. -2.3% for the Stoxx 600*). Since the beginning of the year, the Stoxx 600 Utilities has dropped 2.6% vs. a 9.8% decline for the Stoxx 600. Since our initiation of coverage in July 2014, we have recommended staying out of the sector as a whole and playing it safe through stocks offering strong earnings growth stories based on restructuring efforts. As a reminder, after having played Suez for Q1 2016, **we decided not to put any utilities stocks on the BG Top Picks List for Q2 2016 as we saw limited positive catalysts**. Inside the BG utilities universe (*Albioma, EDF, EDPR, Engie, E.ON, Pennon, RWE, Suez, Veolia and Voltalia)* the top performers were RWE *(+24.7%)* followed by Pennon *(+16.6%)* and Voltalia *(+13.6%)* while the worst performers were the two French environmental services companies we cover: Suez *(-12.7%)* and Veolia *(-8.0%)*. Overall, integrated utilities outperformed environmental services companies. **Both the increase in power prices and positive newsflow** *(potential agreements on nuclear dismantling in Germany, potential carbon floor prices implementation in France)* **have contributed to this performance**. During the quarter, **European power prices** *(forward FY1 power prices for France, Germany, the UK and the Netherlands)* **surged by 26.7% on average** *(vs. a 20% drop in Q1-16)* **while gas *(TTF)* and coal prices increased by 23.5%** *(vs. -12% in Q1-16)* **and c.28%** *(vs. -4% in Q1-16)* **respectively over the period**.

WHAT WE SEE FOR Q3 2016

As for Q2 2016, during the summer we expect no short term recovery in commodity prices in Europe. As a reminder our **models are marked-to-market** and therefore integrate no upside from any price recovery as yet. Except the traditional H2 earnings publications for almost all our stocks we do not **expect any precise catalysts.** All major events (*investor day, workshop cession*) occurred during Q2-16 and affected positively Engie and RWE. **We remain cautious on the sector** given the lack of visibility on the macro and commodity prices environment, but have to admit that the sector could be played by investors as a defensive means of protecting against Brexit risks given that utilities remain poorly exposed to UK and the sector is not so cyclical.

At this stage we remain Neutral.

CONCLUSIONS AND TOP PICKS

In our last reports, **we updated our models with our latest macro data assumptions** *(update on integrated utilities: Potential upside from higher Brent for EDF & Engie and report on environmental services companies: Haste makes waste, it's upside time!*) which implies no further changes in our FV and estimates today.

We have chosen to put Veolia *(Buy, FV @ EUR23)* **on our BG Top Pick list for Q3 2016** as **1) the stock's derating** over the past quarter *(-8.0% in Q2-16 vs. 2.8% for the Stoxx 600 Utilities)* now implies a **6.5x 2017e EV/EBITDA multiple** - a 4% discount vs. its 6-year historical average – and a 5% discount vs. Suez on comparable basis. **2) Following Brexit, we believe Veolia's exposure to the UK is rather limited today** *(c. 9% of revenues of Group's revenues i.e. EUR2.3bn out of which 80% coming from the waste business)* as GBP headwinds could be partly offset by USD tailwinds for an overall fairly **limited FX impact**. In addition, **Veolia appears well-protected in case of a potential macro downturn in the UK** as around one third of its UK waste revenues are generated by PFI contracts *(around 50% EBITDA margin)* whereas about 70-75% of **volumes are guaranteed**. **3)** Despite, a potential weak sales performance in H1 2016 *(due to FX headwinds, unsupportive weather as well as the downsizing of Veolia Water Technologies)*, **we think Veolia will post a strong and resilient EBITDA performance in line with its 5% organic growth objective**, notably thanks to its ability to **deliver cost-savings measures** *(EUR600m over 2016/2017/2018 i.e. EUR200m per year).* **4)** Finally, we believe the **Transdev's disposal** – *Transdev is 50% owned by Veolia* – could be a **positive catalyst** in the upcoming quarter. More than the financial part of the disposal *(EUR0.1 positive impact on our FV according to our estimates, assuming a mere 10% capital gain*), **we believe the disposal should be well received by investors as 1) this is a long-lasting story; and 2) proceeds could be used to fund future organic growth and contribute to ensuring the company's dividends target.**

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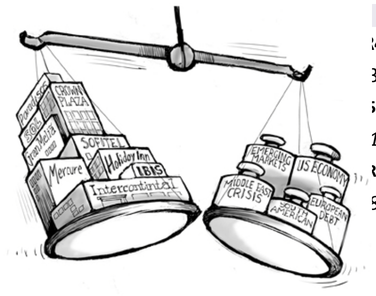
Hotels & Tourism : Top picks: Melia Hotels!

	1 M	3 M	6 M	31/12/15
Travel&Leisure	-9.9%	-9.4%	-17.8%	-17.8%
DJ Stoxx 600	-3.5%	-0.3%	-9.2%	-9.2%

*Stox

Comp	
ACCC	45
Last I	3m
Inter	50p
Last I	1m
MELI	15
Last I	3m



LOOKING BACK ON Q2 2016

In the hotel sector, volatility has remained high due to rumours and/or specific situations for each player in an uncertain economic environment. In Q2, **AccorHotels** was down 6.8% in absolute terms after losing 6.2% in Q1 and -4.7% vs. the DJ Stoxx (+0.5% in Q1), same performance for **Melia Hotels** (after the worst one in Q1) down -6.5% and 4.4% vs. the DJ Stoxx, while **IHG** reported the worst one (after the best one in Q1) down -8.9% in absolute terms in euros and -6.7% vs. the DJ Stoxx.

In **dependence care**, after **Korian's** hefty underperformance in Q1 (-25.9% and -20.6% vs. DJ Stoxx) rebounded in Q2 with the share price up 12.4% and 15% vs. the DJ Stoxx while **Orpea's** share price was slightly up 1.2% in Q2 and 3.6% vs. the DJ Stoxx after respectively -2.2% and +4.9% in Q1.

WHAT WE SEE FOR Q3 2016

Brexit opens a new long period of uncertainty especially as Great Britain is in no hurry to trigger the procedure to withdraw from the EUR under Art. 50 of the Treaty of Lisbon.

The United Kingdom is a key source market for many international tourist destinations. In fact, the UK is the second largest European source market for hoteliers and **British citizens spent 215 million overnight stays in hotels** (and similar accommodations) in the European Union representing c.8% of total overnight stays (2.7m), including 110 million outside their own territory and the depreciation of the GBP/EUR exchange rate will clearly have an impact on British decisions when it comes to travelling abroad.

The breakdown of overnights across Europe shows that **British tourists** are especially fond of Mediterranean destinations. After the islands of **Cyprus** and **Malta** which appear to be the most sensitive markets when it comes to exposure to British tourist arrivals, as they account for respectively 31.2% and 30.7% of total overnight stays in hotels, **Portugal**, **Spain** and **Greece** are the three next countries exposed to British tourist arrivals for respectively 16.2%, 16.1% and 11.9% (source Eurostat). **France** is also exposed with Britishs tourist representing around 9.5% of total overnights.

In this context, **Melia Hotels** would be one of the most affected with British citizens representing 12% of total room nights. With over 33% of the total number of rooms, Spanish resorts generate 25% of consolidated EBIT. On a positive note, we would highlight the high level of occupancy (73.1% in Q1 o/w 78.1% on owned & leased) which could decline without affecting profitability.

AccorHotels should be mainly affected by a consolidation impact of its business in the UK representing c.6% of the group's offer in number of rooms but around 10% of consolidated EBIT based on currency sensitivity. Remember that we have removed AccorHotels from our top picks list mainly due to the group's exposure to France and particularly Paris/Ile de France.

A bit more complex, but a limited impact on **IHG**. Actually as a UK company, the main quotation is in GBP but reporting is in USD. The Americas represented 64.4% of the total number of rooms at the end of 2015 having generated 71.8% of consolidated EBIT before central costs. In Europe (14.3% of number of rooms generating 9.4% of consolidated EBIT), UK is the main European country representing 47% of the group's offer.

CONCLUSIONS AND TOP PICKS

Despite **Melia Hotels** exposures to British citizens, we are maintaining the stock in our top picks list.

Brexit is definitely not good news, but Spain remains one of the main Mediterranean destinations preferred by tourists given the geopolitical environment in North Africa and the Middle East etc. Moreover, as stated above, Spanish resorts reported a very high level of occupancy which leaves room for some decrease without affecting profitability by increasing ADR to optimise RevPAR as done in America.

Thereafter, as stated in our last note on 15th June, the improvement in operating results over three years (EBIT 2015-2018 CAGR of c.13%) is primarily set to be driven by Spanish cities (EUR30m), Asia (EUR10m) and the Americas (EUR10m from Cuba).

In addition, after the early redemption of convertible bonds, the group has restored some financial health with estimated net debt/EBITDA w/o asset rotation estimated at 1.7x at the end of 2016. In this situation, assuming that normal financial leverage should be around 2.5x and taking into account non-core asset disposals, Melia has potentially EUR500m for new expansion in fully-owned property ahead of the current pipeline mostly under management contracts.

NEXT CATALYSTS

Accorhotels: H1 results on 28th July (before market)

IHG: Investor event on 7th July; H1 results on 2nd August (before market)

Melia Hotels: H1 results on 1st August (after market)

Orpea: H1 revenue on 20th July (before market)

Korian: H1 revenue on 20th July (after market)

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TMT : Q2 2016 review and our TMT Top Picks for Q3: Wirecard and Infineon.

	1 M	3 M	6 M	31/12/15
Softw.& Comp. SVS	-6.5%	-4.2%	-7.3%	-7.3%
DJ Stoxx 600	-3.5%	-0.3%	-9.2%	-9.2%

*Stoxx Sector Indices

Companies covered

ALTEN		**SELL**	**EUR48**
Last Price	EUR53.25	*Market Cap.*	*EUR1,793m*
ALTICE		**BUY**	**EUR16.3**
Last Price	EUR13.595	*Market Cap.*	*EUR14,877m*
ALTRAN TECHNOLOGIES		**NEUTRAL**	**EUR13**
Last Price	EUR12.175	*Market Cap.*	*EUR2,140m*
ARM HOLDINGS		**BUY**	**1340p**
Last Price	1131p	*Market Cap.*	*GBP15,917m*
ASML		**SELL**	**EUR81**
Last Price	EUR88.09	*Market Cap.*	*EUR38,172m*
ATOS		**BUY**	**EUR92 vs. 93**
Last Price	EUR75.01	*Market Cap.*	*EUR7,850m*
AXWAY SOFTWARE		**NEUTRAL**	**EUR20**
Last Price	EUR20.65	*Market Cap.*	*EUR429m*
CAPGEMINI		**BUY**	**EUR95 vs. 97**
Last Price	EUR77.85	*Market Cap.*	*EUR13,404m*
CAST		**NEUTRAL**	**EUR3.6**
Last Price	EUR3.35	*Market Cap.*	*EUR54m*
DASSAULT SYSTEMES		**SELL**	**EUR64 vs. 63**
Last Price	EUR68.56	*Market Cap.*	*EUR17,637m*
DIALOG SEMICONDUCTOR		**BUY**	**EUR35**
Last Price	EUR27.165	*Market Cap.*	*EUR2,115m*
GEMALTO		**NEUTRAL**	**EUR62**
Last Price	EUR55.87	*Market Cap.*	*EUR4,979m*
ILIAD		**BUY**	**EUR212**
Last Price	EUR182.4	*Market Cap.*	*EUR10,709m*
INDRA SISTEMAS		**NEUTRAL**	**EUR10**
Last Price	EUR9.637	*Market Cap.*	*EUR1,582m*
INFINEON		**BUY**	**EUR15**
Last Price	EUR13.075	*Market Cap.*	*EUR14,803m*
INGENICO GROUP		**BUY**	**EUR144**
Last Price	EUR106	*Market Cap.*	*EUR6,518m*
NUMERICABLE SFR		**NEUTRAL**	**EUR28.4**
Last Price	EUR22.75	*Market Cap.*	*EUR9,970m*
ORANGE		**BUY**	**EUR13.59**
Last Price	EUR14.585	*Market Cap.*	*EUR38,797m*
SAGE GROUP		**SELL**	**575p vs.555**
Last Price	625p	*Market Cap.*	*GBP6,747m*
SAP		**NEUTRAL**	**EUR74 vs. 73**
Last Price	EUR67.4	*Market Cap.*	*EUR82,801m*

LOOKING BACK ON Q2 2016

In Q2 2016, the TMT sector had a negative performance in bear stock markets amidst the vote in favour of Brexit. Over the period, the DJ STOXX Europe technology index fell 4.9% and underperformed the DJ STOXX Europe 600 index by 2.7%.

During the period, **the best performers were Ubisoft** (+20%, increasing speculative appeal), **Wirecard** (+18%, rebound after fraud allegations by Zatarra), and **Worldline** (+16%, good Q1 organic sales growth). **The worst performers were Numericable-SFR** (-39%, breakdown of merger talks between Bouygues and Orange), **Dialog Semiconductor** (-23%, downward revision of FY guidance), **and Iliad** (-19%, same as for Numericable SFR). **Our sector Q2 Top Picks Atos and Wirecard, that we removed from the Top Pick list on 24th June after the vote for Brexit were up respectively 4.5% (+6.0% dividend included) and 1.5% (+1.9% dividend included).**

NEW ESTIMATES AND FAIR VALUES

We have taken the opportunity to update our 2016-2018 forecasts and our DCF-derived Fair Values, due to new fx assumptions, especially due to the weakness in the British pound and the strength of the US dollar and the Japanese yen against the euro.

On that basis, **we have adjusted our DCF-derived Fair Values for Atos (to EUR92 from EUR93**, headwinds on GBP), **Capgemini (to EUR95 from EUR97**, headwinds on GBP), **Dassault Systèmes (to EUR64 from EUR63**, tailwinds on JPY and USD), **Sage Group (to 575p from 555p**, tailwinds on USD and EUR), **SAP (to EUR74 from EUR73**, tailwinds on USD), **and Sopra Steria Group (to EUR127 from EUR130**, headwinds on GBP).

WHAT WE SEE FOR Q3 2016

For Software & IT Services, based on industry analysts' forecasts, at this stage we are still anticipating stable growth or a slight slowdown in global IT spending for 2016, with est. growth of 5-6% for software (vs. +6% for 2015), still driven by the now established SaaS model, and est. growth of 3-4% for IT Services (vs. +4%) driven by digital transformation projects. **However, we cannot ignore Brexit and the negative consequences it may generate short-term** (essentially on licence sales for software vendors), **so we consider these estimates are now at risk** - yet very challenging to quantify as of today - due to several unknowns: 1) **Political uncertainty** - how the "divorce" between the UK and the UE will be managed and what kind of partnership will replace the UK's membership in the EU, and we cannot rule out that political manoeuvres to slow the Brexit process are likely to generate a 'wait-and-see' attitude for decision makers, so some IT projects could be postponed or cancelled if they are concerned by a lack of visibility; 2). **Some industries like Banking and Government are at the frontline for potential cuts in IT budgets** as foreign banks may be led to relocate their businesses outside the UK if they lose the "European passport", which allows them to make transactions in euros in the UK, and as the Cabinet Office may decide to freeze new government IT projects before envisaging more efficiency in order to avoid increasing deficits; 3). **Concerns about an economic recession in the UK**; 4). **A contagion effect to other geographies**. **We consider the companies in our coverage with the highest risk of downward revisions to forecasts are Sopra Steria** (27% of revenues in the UK), **Capgemini** (17% of revenues in the UK), **Atos** (16% of revenues in the UK) and **Temenos** (100% of revenues in Banking). In addition, a decline in UK long-term interest rates may have an adverse impact on pension deficits for IT Services firms having significant exposure to the UK (Sopra Steria, Atos, Capgemini).

The payments sector should continue to benefit fully from EMV migration in the US (50% still to be upgraded), equipping emerging markets (notably in China), as well as rising demand for payment services outsourcing (notably e-commerce) and for security in electronic payments. Regarding Brexit, the companies we cover in this segment are extremely flexible and see Brexit in a very relaxed manner and without implications for their businesses (GBP is below 9% of their revenue on average and they have a natural hedge with the respective currency). **1) Ingenico Group (Buy – FV of EUR144, 100% of sales in payment)** has the best commercial multi-channel offer available today. We are still confident in Q2 sales (BG est.: +13/14% lfl vs. consensus of +10%) despite VeriFone's comments (facing company-specific issues), and see the FY16 guidance as too cautious (>=10% lfl sales and ~21% Ebitda margin). **2) Wirecard (Buy – FV of EUR54, pure player in online payments)** is now a global issuing and acquiring payment service provider (all continents are now covered). It

SOFTWARE AG		**BUY**	**EUR40**
Last Price	EUR31.045	*Market Cap.*	*EUR2,453m*
SOITEC		**NEUTRAL**	**EUR0.45**
Last Price	EUR0.54	*Market Cap.*	*EUR327m*
SOPRA STERIA GROUP		**BUY**	**EUR127 vs. 130**
Last Price	EUR95.05	*Market Cap.*	*EUR1,943m*
STMICROELECTRONICS		**NEUTRAL**	**EUR6.3**
Last Price	EUR5.28	*Market Cap.*	*EUR4,810m*
SWORD GROUP		**BUY**	**EUR26**
Last Price	EUR24.35	*Market Cap.*	*EUR230m*
TEMENOS GROUP		**NEUTRAL**	**CHF52**
Last Price	CHF50	*Market Cap.*	*CHF3,477m*
UBISOFT		**BUY**	**EUR34**
Last Price	EUR33.775	*Market Cap.*	*EUR3,756m*
WIRECARD		**BUY**	**EUR54**
Last Price	EUR39.78	*Market Cap.*	*EUR4,915m*
WORLDLINE		**BUY**	**EUR29**
Last Price	EUR25.425	*Market Cap.*	*EUR3,358m*
WORLDPAY		**NEUTRAL**	**278p**
Last Price	274.3p	*Market Cap.*	*GBP5,486m*

should post FY16 organic sales growth of over 20%, driven notably by south-east Asia, which should translate into 2016 EPS growth of 38%. Its Q2 organic sales growth should continue to accelerate (i.e. over 20% lfl, much the same way as growth in transaction volumes processed). **3) Worldline (Buy – FV of EUR29, 78% of 2016 sales in payment)** is not yet fully considered as a PSP (whereas it is #1 in Europe since the acquisition of Equens vs. #3 before). We expect the group to post ~5% organic sales growth in Q2 (taking into account the termination of the public sector contract in the UK at the end of last year). **4) Gemalto (Neutral – FV of EUR62; less than 25% of its sales in payment**) should post again weak lfl sales growth in Q2 (after -2.5% lfl in Q1). We believe there are still too many risks in the SIM and related services businesses. Shorter term, we do not view the bid on Morpho as positive for the share price as it should be not so easy to integrate given size and profitability levels (Morpho is half the size of Gemalto's sales and half its EBIT margin level). **5) Worldpay (Neutral – FV 278p; 100% of its sales in payment**) is struggling in the US (half of group sales), such that the associated poor lfl top-line growth cannot create any leverage to its proprietary platform. We expect the group to post 7% organic sales growth at best over the FY…, so disappointments cannot be ruled out in our opinion.

For Semiconductors, the environment remains tough with cumulative WW sales from January to April down by 5.9% yoy. Nevertheless, we expect global 2016 sales to be broadly flat thanks to improving momentum in H2 (Q1 was tough for almost all sub-segments) and easier comparison basis. During Q2 2016, we observed a stable environment in smartphones, which was a weak spot in Q1. The PC segment remains penalised by lacklustre sales and shows no sign of rebound. Regarding the other semiconductor end-markets, in which the automotive and industrial sector falls, we note that momentum is continuously improving. As expected, automotive production was particularly dynamic during the first two months of Q2 with aggregated production of US, Europe and China up 6% yoy (5m aggregated sales also up +6%). In addition, the industrial sector is said to be healthy according to industry sources. As for Q1, in our coverage, this should translate into positive momentum for **Infineon (Buy, FV EUR15)** and **STMicroelectronics (Neutral, FV EUR6.3)**. Regarding semi equipment makers, Q2 was the quarter of the 10nm ramp-up at Logic IDM and foundries, triggering equipment orders. We also expect 10nm ramp to act as a tailwind over Q3. However, we remain convinced that most of the positive impact from 10nm investments are already priced in, and particularly for **ASML (Sell, FV EUR81)**.

For Video Games: We are optimistic on fundamentals (no game delays expected) and momentum for the Ubisoft share price. By taking equity stakes in **Ubisoft (Buy – FV EUR34)**, Vivendi has encouraged investors to change the way they look at the share. For this group, speculation will be the main driver behind share price. We would therefore not be surprised if the share started to reflect its speculative premium (in 2017?). As a reminder we estimate a fair offer in the EUR40-51 range.

In Telecom, consolidation hopes on the French market should be over for quite some time now. Nevertheless, the first signs of spontaneous market repair are visible: Orange, SFR and Bouygues Telecom have increased their prices lately, both in fixed and mobile, and Iliad has the opportunity to do so with the launch of its Freebox v7 before the end of the year. While ARPUs are on the way to stabilising, the CAPEX war is in full swing in fibre deployment and 4G coverage. Visibility has increased for **Iliad (Buy - FV EUR212)**, since the 2G/3Groaming agreement with Orange has been extended, growth will continue, supported by strong marketing and direct distribution, although competing on fiber and increasing mobile ARPUs remain a challenge. **SFR (Neutral - FV EUR28.4)** should still struggle for several months with operational and commercial issues, waiting for the effects of increased investment and new management to kick in. Following the closing of Cablevision's acquisition in the US, **Altice (Buy – FV EUR16.3)** should be able to offset the poor performance at SFR with good results at the international level, especially in the US and in Portugal. **Orange (Buy – FV EUR17.1)**, taking advantage of SFR's difficulties, will still be in a good position to steam ahead as the only all-around premium telecom provider on the market.

CONCLUSIONS AND TOP PICKS

In Software & IT Services, due to the environment caused by Brexit and political uncertainties, we have had no pick for Q3 2016 since 24th June when we removed Atos from the list.

In Payments, we expect investors to show an increasing appetite for the rising momentum of eCommerce. As such, **we have placed Wirecard (Buy, FV EUR54) on our Q3 Top Pick list to benefit from** extremely good fundamentals (pure player in ePayment, exposure to South-East Asia) and a still attractive entry-point following the Zatarra story. As a reminder, we expect organic sales growth of more than 20% in FY16e with EBITDA of EUR306.4m i.e. a margin of 30.1% (vs. an increased guidance range to EUR290-310m, which is still cautious in our view). **Wirecard's PEG is still very appealing with a PE of 21.8x vs. EPS growth of 37.9% in 2016e.**

In Semiconductors, given the current supportive environment in the automotive segment within the semiconductor market, we believe that investors' appetite for auto players will increase as June quarterly publications should be robust. As a result, **we add Infineon (Buy, FV EUR15) to our Q3 Top Pick list** to benefit from an attractive entry point as the stock has recently suffered from 1/ a downward FY16 guidance revision in May due to a move in the EUR/USD exchange rate (from 1.10 to 1.15), and 2/ the negative impact of Brexit on European stocks. With a supportive environment, we are confident about FQ3 results (to be posted on 2nd August) and given that Brexit caused the EUR/USD to move back to the ~1.10 level, we believe that there are also good chances that the group shows a great confidence for FQ4 and posts a stronger than expected guidance.

In Video Games, 2016 should be buoyant thanks to speculation concerning Ubisoft. This main theme is set to drive the share price in 2016e. However, and despite our buy rating, we find it difficult to predict the exact timing of an increase in Ubisoft's capital by Vivendi and/or a formal takeover bid for the whole company. As a result, **we are not including this name in our Q3 2016 Top Pick list.**

In Telecoms, although market trends are improving**, we are not including any stock in our Q3 Top pick list.** Regarding **Altice (Buy – FV EUR16.3)**, tension in high yield markets related to the Brexit impact and difficulties in France should still weigh on the stock performance, although we expect good trends on the international side. Regarding **Iliad (Buy, FV EUR212)**, the entry point is not as good as it was only a few days ago, having recovered much of the Brexit loss, and we see no specific catalyst for high short term performance. **Orange (Buy - FV EUR17.1)** should maintain its good commercial and financial trend, but with no major catalyst in Q2 justifying adding it to our top pick list.

NEXT CATALYSTS

Software & IT Services: Infosys' Q1 FY17 results next week. TCS' Q1 FY17 results on 14th July after the Indian markets close. IBM's Q2 2016 results on 18th July after US markets close. Q2 2016 and H1 2016 sales and results for European companies start on 20th July (SAP, Software AG).

Payments: Worldline's and Ingenico's H1 earnings on 26th July (after trading), Worldpay's H1 earnings on 9th August (before trading), Wirecard's H1 earnings on 11th August (before trading), Gemalto's H1 earnings on 26th August (before trading), and).

Semiconductors: TSMC's Q2 2016 results on 14th July, ASML's Q2 2016 results on 20th July, STMicroelectronics Q2 results on 22th July, ARM's Q2 results on 27th July, Dialog's Q2 results on 28th July and Infineon's Q3 results on 2nd August.

Video Games: Ubisoft's Q1 sales in July.

Telecom: Orange H1 results on July 27th[t], SFR and Altice H1 results on August 9th, Iliad's H1 results at the end of August.

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Healthcare : Top Picks Q3 2016: Shire jumps in and takes Actelion's seat, others remain

	1 M	3 M	6 M	31/12/15
Healthcare	1.3%	9.6%	-5.0%	-5.0%
DJ Stoxx 600	-3.5%	-0.3%	-9.2%	-9.2%

*Stoxx Sector Indices

Companies covered			
ABLYNX		**BUY**	**EUR18**
Last Price	EUR11,89	*Market Cap.*	EUR724m
ACTELION		**BUY**	**CHF173**
Last Price	CHF165,5	*Market Cap.*	*CHF18,888m*
ADOCIA		**BUY**	**EUR100**
Last Price	EUR46,16	*Market Cap.*	*EUR316m*
ASTRAZENECA		**BUY**	**5100p**
Last Price	4502,5p	*Market Cap.*	*GBP56,939m*
BAYER		**NEUTRAL**	**U.R.**
Last Price	EUR90,69	*Market Cap.*	*EUR74,996m*
BIOMERIEUX		**BUY**	**EUR122**
Last Price	EUR122,25	*Market Cap.*	*EUR4,823m*
BONE THERAPEUTICS		**BUY**	**EUR30**
Last Price	EUR16,745	*Market Cap.*	*EUR115m*
CELLECTIS		**BUY**	**EUR37**
Last Price	EUR24,14	*Market Cap.*	*EUR853m*
CELYAD		**NEUTRAL**	**EUR20**
Last Price	EUR21,79	*Market Cap.*	*EUR203m*
DBV TECHNOLOGIES		**BUY**	**EUR91**
Last Price	EUR59,46	*Market Cap.*	*EUR1,433m*
ERYTECH		**BUY**	**EUR48**
Last Price	EUR21,29	*Market Cap.*	*EUR169m*
FRESENIUS MED.CARE		**BUY**	**EUR94**
Last Price	EUR78,16	*Market Cap.*	*EUR23,976m*
FRESENIUS SE		**BUY**	**EUR73**
Last Price	EUR66,23	*Market Cap.*	*EUR36,170m*
GALAPAGOS		**BUY**	**EUR64**
Last Price	EUR49,345	*Market Cap.*	*EUR2,275m*
GENEURO		**BUY**	**EUR18,2**
Last Price	EUR8,8	*Market Cap.*	*EUR129m*
GENMAB		**BUY**	**DKK1600**
Last Price	DKK1237	*Market Cap.*	*DKK74,015m*
GLAXOSMITHKLINE		**BUY**	**1740p**
Last Price	1600p	*Market Cap.*	*GBP77,958m*
INNATE PHARMA		**BUY**	**EUR18**
Last Price	EUR10,41	*Market Cap.*	*EUR560m*
IPSEN		**BUY**	**EUR63**
Last Price	EUR56,06	*Market Cap.*	*EUR4,667m*
KORIAN		**NEUTRAL**	**EUR29**
Last Price	EUR29,29	*Market Cap.*	*EUR2,328m*
LDR HOLDING		**Tender to the offer**	
Last Price	USD36,99	*Market Cap.*	*USD1,081m*
MORPHOSYS		**BUY**	**EUR62**
Last Price	EUR37,685	*Market Cap.*	*EUR1,000m*
NICOX		**CORPORATE**	**EUR14**
Last Price	EUR12,19	*Market Cap.*	*EUR279m*
NOVARTIS		**NEUTRAL**	**CHF89**
Last Price	CHF80,45	*Market Cap.*	*CHF211,351*

LOOKING BACK ON Q2 2016

Q2 2016 was a strange quarter actually and if Healthcare performed very well in the end, this was largely because it appeared to be the safest heaven over the few days following the Brexit vote. UK healthcare stocks in particular skyrocketed by more than 10% in a single week. Before that, healthcare stocks did not show particularly strong momentum and simply showed signs of a stabilisation after a difficult start to the year.

So, thanks to the Brexit vote, Healthcare achieved an outstanding relative performance of more than 11% compared to the Stoxx Europe 600, meaning +8.7% in absolute terms. As always, some of the large cap pharmaceutical stocks were behind the performance considering their weight in the overall index but it was also supported by stellar performances from some small to mid-cap healthcare stocks this time. In the first category are the three UK names as previously highlighted (Shire +17.2%, AZN +14.5%, GSK +13.6%) but also Novartis, up 15%. Of course, when reported in EUR, the performances are not so good but nevertheless remain strong and positive. In the second category are Galapagos, Nicox and Genmab all up by more than 30% during the quarter. However, it is also worth mentioning that some small biotech companies did not fully recover from a difficult quarter which also includes one specific large cap name, Bayer, for obvious reasons (bid over Monsanto).

To note also in our coverage the bid over LDR by Zimmer Biomet at USD37 per share (+45% in Q2). Genmab (+33%) benefited from strong daratumumab data whereas Celyad (-43%) suffered from disappointingly negative results for its lead stem cell therapy product candidate, C-CURE, in CHF (CHART-1 trial). Lastly, Novo-Nordisk did not benefit from positive data for SUSTAIN-6 (to be presented at EASD) and LEADER (presented at ADA) and stock was flat over the quarter (+0.8%).

WHAT WE SEE FOR Q3 2016

Since inception of the Top Pick List in 2012, this is one of the toughest quarters to assess in our view because macro trends are quite difficult to handle and to predict for the coming weeks and months.

In particular, we are fundamentally positive on UK names but we do question how they are going to perform in the post-Brexit environment as we might finally see some cash-out from UK funds, impacting healthcare stocks in the end. We also see moving parts if not binary events for non-UK stocks which we are not fully comfortable with like the final outcome for Bayer in Monsanto's bid, for Roche with APHINITY's phase III results or for Novartis with Entresto and Alcon at mid-year. Obviously, PDUFA dates for both lixisenatide and iGlarLixi during the quarter will be key events for Sanofi but even more substantially for Zealand.

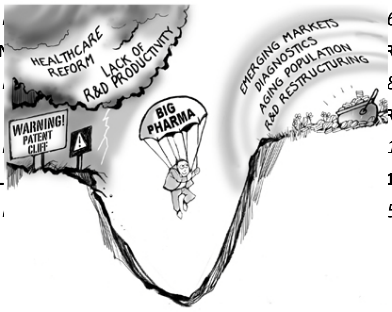
As such, we have tried to take reasonable risks while keeping our exposure to the healthcare sector unchanged i.e. with four stocks included in the List for the quarter to come. This results in one change with the inclusion of Shire and exit of Actelion.

CONCLUSIONS AND TOP PICKS

Here is the list of healthcare stocks included in BG's Top Pick List for Q3 2016: Ablynx, Fresenius SE, Ipsen and Shire.

ACTELION (BUY – FV CHF173): we have decided not to include the stock this quarter after a strong performance over the last two quarters although we expect another strong set of quarterly numbers to be released on 21st July with another highly likely increase in guidance for core EBIT in 2016. With Opsumit still performing very well (driven by the US), the increasing likelihood of not seeing US generic bosentan this year and a strong take-off of Uptravi in the US, we believe that Actelion will upgrade its guidance to low-to-mid teen's growth. And we do not see this reflected yet into CS figures as Bloomberg suggests expectations are for a modest 11.4% core operating income growth in reported terms whereas we cautiously (in our view) expect Actelion to report 13.1%. As a reminder,

NOVO NORDISK		**NEUTRAL**	**DKK400**
Last Price	DKK363,5	*Market Cap.*	*DKK731,567*
ORPEA		**BUY**	**EUR79**
Last Price	EUR74,49	*Market Cap.*	*EUR4,474m*
QIAGEN		**NEUTRAL**	**EUR22**
Last Price	EUR19,845	*Market Cap.*	*EUR4,757m*
ROCHE HOLDING		**BUY**	**CHF293**
Last Price	CHF256,7	*Market Cap.*	*CHF180,348*
SANOFI		**NEUTRAL**	**EUR83**
Last Price	EUR75,02	*Market Cap.*	*EUR96,549m*
SHIR			**)0p**
Last			*6m*
TRA			**R12**
Last			*8m*
UCB			**R80**
Last			*1m*
ZEAL			**176**
Last			*5m*



in Q1, currencies played positively by 6pp (+8% underlying, +14% reported) with Uptravi just starting. Although we expect the positive currency impact to reduce somewhat, we believe it will remain positive by at least 3-4%. Now, we also expect investors to pay increasing attention to the mid-term over the short-term and we do not see a lot coming through in Q3 to help from that perspective.

SHIRE (BUY – FV GBp6,500): We believe Shire displays an outstandingly attractive risk-reward as 1/ we expect an above-industry average EPS growth of 14% over the 2015-2020e period; 2/ nearly 85% of our 2020 sales estimate is derived from already commercialised products; 3/ at current levels, SHP trades on a 55% discount to CSL on 2017e P/E (30% compared with the European sector as a whole). In our view, this gap will be significantly reduced thanks to the very next catalysts… and namely (i) the approval of lifitegrast as a treatment for dry-eye disease on the 22nd July (impact on our FV: -GBp150 if negative / +GBp150 if positive); 2/ the (likely) increase in anticipated cost synergies with Baxalta on 2nd August (FV: +GBp200 assuming an updated guidance of USD750m vs USD500m previously).

IPSEN (BUY – FV EUR63): We still consider Ipsen well placed to take advantage of the next quarter to convince an increasing number of investors that it is worth looking at the ongoing deep change taking place within the group. Not only will second-quarter figures show an overall improvement in momentum vs the poor first-quarter impacted by tender phasing and wholesaler inventories with the exception of a solid continuing trend for Somatuline in the US but we also anticipate the quarter to result in two key triggering events: (i) CHMP positive opinion for cabozantinib in second-line renal cell carcinoma is expected in September whereas new data might be disclosed ahead of the ESMO meeting both in first and second line; (ii) arrival of new CEO by September is also likely. If Somatuline has the potential to surprise CS on the upside with its US peak sales and maybe more with its influence on profits, we think that cabozantinib is even less well captured by CS. Recently unveiled data in RCC carry strong potential for the drug and maybe stronger than initially thought although competition with IO (including Opdivo) is expected to be fierce. Last but not least, our understanding is that position of Marc de Garidel has clarified over the last few months and we expect his influence at the head of the Board, in close collaboration with Anne Beaufour and the new CEO, to help Ipsen's perspectives over the medium and long term.

ABLYNX (BUY – FV EUR18). We maintain Ablynx in our top pick list as Q2 should be a turning point with the publication results from the two trials evaluating ALX-0061 in rheumatoid arthritis' patients. While results from the first trial expected in July, should give a good trend of the product's efficacy, we would not look at statistical significance (no placebo arm). The second however should provide us with data enabling us to better assess the company's IL-6, hence its potential in the RA space. As a reminder, we have assumed EUR1.5bn in peak sales for the product candidate. We believe that interactions with AbbVie have been reinforced over the past weeks and should the latter decide to opt-in, Ablynx would be eligible for a USD75m milestone payment. Positive results would add EUR3 to our Fair Value.

FRESENIUS SE (BUY – FV EUR73). Fresenius SE also stays in. While comps should be stronger in Q2 for Fresenius SE, we see no short term threat to the company's ability to maintain 1/ top line trends and 2/ profitability, mainly for KABI in the US. Monitoring of the US drug shortages situation show us that although the number of shortages shrank in the US since June 2015 (50 to 44), KABI still benefits from more than 20 of them, which should enable the division keep up with strong growth margins in Q2. The recent appreciation in the USD against the EUR should also benefit KABI which generates 56% of its EBIT in the US compared with around 1/3rd of sales. The promotion of Stephan Sturm to CEO following Ulf Mark Schneider's departure does not change the equity story and we expect the transition to be seamless with no operative shake-up. Our numbers for the year are within the high end of the company's guidance which we view as conservative (organic topline growth BGe7.4% vs. guidance 6-8%, Net Income growth BGe 12.3% vs guidance 8-12%).

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Luxury & Consumer Goods : Q3 2016 TOP PICKS: We remove Essilor, add Moncler and LVMH and continue with Ahold!

	1 M	3 M	6 M	31/12/15
Pers & H/H Gds	0.8%	4.0%	1.9%	1.9%
DJ Stoxx 600	-3.5%	-0.3%	-9.2%	-9.2%

*Stoxx Sector Indices

Companies covered

ADIDAS GROUP		**BUY**	**EUR124**
Last Price	EUR128,2	*Market Cap.*	EUR26,821m
BEIERSDORF		**NEUTRAL**	**EUR80**
Last Price	EUR84	*Market Cap.*	*EUR19,051m*
BIC		**NEUTRAL**	**EUR119**
Last Price	EUR128	*Market Cap.*	*EUR6,136m*
BURBERRY		**NEUTRAL**	**1200p**
Last Price	1166p	*Market Cap.*	*GBP5,189m*
CHRISTIAN DIOR		**BUY**	**EUR175**
Last Price	EUR145,3	*Market Cap.*	*EUR26,405m*
ESSILOR		**BUY**	**EUR130**
Last Price	EUR119,55	*Market Cap.*	*EUR26,069m*
GRANDVISION		**BUY**	**EUR28**
Last Price	EUR23,91	*Market Cap.*	*EUR6,084m*
GROUPE SEB		**BUY**	**EUR125**
Last Price	EUR111,1	*Market Cap.*	*EUR5,574m*
HERMES Intl		**BUY**	**EUR355**
Last Price	EUR340,8	*Market Cap.*	*EUR35,978m*
HUGO BOSS		**NEUTRAL**	**EUR77**
Last Price	EUR50,21	*Market Cap.*	*EUR3,535m*
KERING		**BUY**	**EUR174**
Last Price	EUR148,2	*Market Cap.*	*EUR18,713m*
L'OREAL		**BUY**	**EUR177**
Last Price	EUR172,45	*Market Cap.*	*EUR96,572m*
LUXOTTICA		**BUY**	**EUR58**
Last Price	EUR44,61	*Market Cap.*	*EUR21,583m*
LVMH		**BUY**	**EUR171**
Last Price	EUR136,15	*Market Cap.*	*EUR69,116m*
MONCLER		**BUY**	**EUR17**
Last Price	EUR14,64	*Market Cap.*	*EUR3,663m*
PRADA		**NEUTRAL**	**HKD35**
Last Price	EUR23,95	*Market Cap.*	*EUR61,284m*
RICHEMONT		**NEUTRAL**	**CHF63**
Last Price	CHF57,35	*Market Cap.*	*CHF32,116m*
SAFILO		**NEUTRAL**	**EUR11**
Last Price	EUR6,77	*Market Cap.*	*EUR424m*
SALVATORE FERRAGAMO		**BUY**	**EUR25**
Last Price	EUR18,34	*Market Cap.*	*EUR3,096m*
THE SWATCH GROUP		**NEUTRAL**	**CHF370**
Last Price	CHF286,1	*Market Cap.*	*CHF15,788m*
TOD'S GROUP		**SELL**	**EUR53 vs.60**
Last Price	EUR49,66	*Market Cap.*	*EUR1,643m*

LOOKING BACK ON Q2 2016

Our **Consumer** "Top Picks" encompass all our global Consumer franchises: **Luxury**, **Consumer goods**, **Retail**, **Spirits** & **Brewers** and **Food**. In Q2, our Consumer sample was slightly down (-4% globally in line with DJ Stoxx) but again with a mixed situation with -11% for our luxury goods sample while the HPC segment was more resilient (+3%) as was the case for beverages (+4%). In all, Retail stocks remained almost stable.

Luxury goods stocks were again strongly penalised (-11% on 3m) among others factors by still poor activity in Hong Kong, a slowdown in US, the lack of tourists in Europe and especially in France. Nevertheless, the best performer was **Hermès** (+6%) thanks to its fairly resilient status among peers (Q1 sales up 6% vs no growth for the sector average), while **Tod's** was the worst (-25%), due to very poor Q1 results with same-store sales down 12%. **LVMH** and **Kering** achieved the same kind of performance (around -10%).

Our **Optical & Eyewear sample** had a mixed performance: on the negative side **Luxottica** and **Safilo** fell by 13% and 15% respectively as both groups posted unhelpful Q1 numbers. As highlighted recently in our latest comment on **Luxottica**, the second quarter should be affected by rainy weather conditions across Europe during the sun peak season and **Safilo** should still be partly impacted by production bottlenecks that already played negatively in Q1. Consequently we believe that investors still prefer to "wait-and-see" ahead of H1 results. The **GrandVision** share price only contracted ~7% in the absence of any major catalyst but we do not think that the consensus has factored in the dilutive impact from M&A. Last but not least, **Essilor** remained the best-performer in our sample with a 9% increase over the quarter. Indeed, in a volatile environment, Essilor's defensive profile was sought after by the market given a solid Q1 publication combined with a reassuring MT outlook, confirming the group's strong fundamentals.
Among the **HPC/Consumer goods** stocks, we would highlight the relative outperformance of this segment with a particularly good move for **L'Oréal** (+7% or +11% vs the DJ Stoxx). Once again **adidas Group** led our **HPC/Consumer** sample with a rally of 23% over the quarter, fuelled by an astonishing Q1 publication (+22% FX-n), FY guidance that was revised up and a healthy global sporting goods market. **Groupe SEB** increased by 20% following better-than-expected Q1 results but also after the game-changing acquisition of WMF Group that was announced at the end of May.

Food & Beverages: In Q2, our Food & Beverage stocks rose 6.9% vs the DJ Stoxx as investors favoured their defensive profile. The best performers were Rémy Cointreau (+19% vs DJ Stoxx) which guided for a return to growth in China in 2016/17 and Diageo (+14% vs DJ Stoxx), which benefited from the weaker GBP. Given their defensive qualities (high cash generation, steady top line growth, self-help restructuring and efficiency improvements) share prices of the brewers held up very well over the quarter. AB InBev was the best performer over the quarter with a 7.6% increase in the share price outperforming the DJ Stoxx by 10.1% and Royal Unibrew was the worst performer with a 5.7% decline.

Retail: Over the last quarter, newsflow was rather poor in food retailing. There was no good news, except for Dia (+9%) whose message turned out to be more positive following its latest publication (hence our new Buy rating), which would have allowed us to amend our conviction that the sector is not attractive, both in absolute (16x average PE for 2017 and anorexic growth vs 14x 10Y average) and relative terms (~20% premium vs stoxx 600). On the contrary, the profit warning from TESCO (mid-April) along with CARREFOUR being punished by the market (-9% in absolute terms in Q2) for not having a clear post-turnaround commercial strategy, does not allow us to amend our view. At this stage, we also believe that the upcoming trading statements will be rather febrile.

WHAT WE SEE FOR Q3 2016

Concerning **Luxury groups**, we remain cautious on Q2 and H1 results publications. Actually, after no organic sales growth in Q1, we argue that the trend should be almost the same despite a likely improvement in Asia-Pacific, thanks to a better Mainland China (8 to 10% of sales) and Korea, but not yet in Hong Kong (8% of luxury sales), but clearly affected in Western Europe as tourists are still lacking. For instance, in April Duty Free shopping by Chinese clientele in Europe fell 18% and in Q1 the number of Japanese tourists in Paris was down around 50% and we do not expect any clear improvement in Q2. France accounts for 7% of luxury sales (and 5% in Paris alone). Moreover, comps in Q2 were slightly more demanding than in Q1. Actually, for LVMH, we expect 2-3% organic sales growth in Q2 following +3% in Q1 (no growth at F&L). LVMH's H1 EBIT margin should be slightly under pressure (-30bp of which -70bp for F&L). Concerning Kering, for Q2 we anticipate 4%

Companies covered			
AB INBEV		NEUTRAL	EUR109
Last Price	EUR115.85	*Market Cap.*	EUR186,315
CAMPARI		BUY	EUR9.7
Last Price	EUR8.81	*Market Cap.*	*EUR5,117m*
CARLSBERG		NEUTRAL	DKK600
Last Price	DKK632.5	*Market Cap.*	*DKK96,711m*
DANONE		BUY	EUR71
Last Price	EUR63.83	*Market Cap.*	*EUR41,866m*
DIAGEO		NEUTRAL	1840p
Last Price	2139.5p	*Market Cap.*	*GBP53,861m*
HEINEKEN		BUY	EUR83
Last Price	EUR83.38	*Market Cap.*	*EUR48,027m*
MOLSON COORS		NEUTRAL	
Last Price	USD100.44	*Market Cap.*	*USD21,562m*
NESTLE		BUY	CHF80
Last Price	EUR75.6	*Market Cap.*	*EUR235,279*
PERNOD RICARD		NEUTRAL	EUR107
Last Price	EUR99.68	*Market Cap.*	*EUR26,457m*
REMY COINTREAU		BUY	EUR80
Last Price	EUR77.45	*Market Cap.*	*EUR3,775m*
ROYAL UNIBREW		BUY	DKK325
Last Price	DKK295.8	*Market Cap.*	*DKK16,003m*
SABMILLER		NEUTRAL	4400p
Last Price	4353p	*Market Cap.*	*GBP70,612m*
UNILEVER		NEUTRAL	EUR43
Last Price	EUR42.14	*Market Cap.*	*EUR121,263*
UNILEVER Plc		NEUTRAL	3350p
Last Price	3678.5p	*Market Cap.*	*GBP47,212m*

Companies covered			
AHOLD		BUY	EUR22
Last Price	EUR20.465	*Market Cap.*	EUR17,075m
CARREFOUR		BUY	EUR30
Last Price	EUR22.02	*Market Cap.*	*EUR16,652m*
CASINO GUICHARD		BUY	EUR57
Last Price	EUR48.55	*Market Cap.*	*EUR5,462m*
DELHAIZE		BUY	EUR104.5
Last Price	EUR96.88	*Market Cap.*	*EUR10,132m*
DIA		BUY	EUR6.5
Last Price	EUR5.15	*Market Cap.*	*EUR3,206m*
JERONIMO MARTINS		NEUTRAL	EUR13.5
Last Price	EUR14.27	*Market Cap.*	*EUR8,980m*
METRO AG		SELL	EUR26
Last Price	EUR26.84	*Market Cap.*	*EUR8,699m*
RALLYE		BUY	EUR18.5
Last Price	EUR15.08	*Market Cap.*	*EUR736m*
TESCO		SELL	166p
Last Price	175.75p	*Market Cap.*	*GBP14,366m*

organic sales growth including +1% for the Luxury division. Gucci brand sales are expected to grow slightly in Q2 (+1.5%) after +3% in Q1 despite much more demanding comparison (-8% in Q1 15 but +4.6% in Q2 15). Gucci brand recovery is underway despite a challenging environment. Furthermore, Puma should achieve a very significant sales increase (close to 10%) partly thanks to the positive EUR impact.

Food retail: We continue to think the commercial equation of retailers remains somewhat weakened in Continental Europe and in the UK, in view of: **1/** apathetic demographical factors, **2/** the de(dis)flationary backdrop and **3/** the strong penetration of modern retail. In this context, it has become challenging for retailers to generate a sufficient LFL growth to cover natural cost inflation, amortise their fixed costs base and increase their cash margin.

Food & Beverages. Despite a tough trading environment with weak pricing power and pressure on volumes in emerging countries, food companies should report solid organic sales growth in Q2 partly thanks to easy comps. We are also confident in the reporting of spirits groups as momentum remains healthy in the US and China is improving on the back of a return to normal in private consumption.

Consumer Groups. **Play the "feel good" factor…** Indeed, given this volatile environment, we believe that investors will continue to favour groups that enjoy olid momentum (=> hence a low risk of disappointing H1 results) such as **adidas Group**, **Essilor** or **Groupe SEB**. As mentioned above, we remain cautious ahead of **Luxottica**'s H1 results given poor current trading and significant capex investments to launch the 2018 Strategic Plan although the stock is currently at a very attractive entry point.

CONCLUSIONS AND TOP PICKS

We have removed Essilor… Let's be clear, our decision has nothing to do with potential concerns on H1 results or on the group's sound fundamentals but the decision to remove Essilor is based on two main reasons: **(i)** securing the capital gain following a very satisfying quarter (+9%) and **(ii)** playing a more aggressive scenario with more "cyclical stocks" and more attractive upside. Fundamentally, Essilor remains one of our favurite buy ideas for a MT/LT investment horizon.

… and added Moncler. In a context of a subdued organic growth in our luxury goods sample, Moncler clearly outpaces its peers as we anticipate 13% FX-n growth for Q2. Moncler's strong brand appeal enables it to outperform the fragmented and dynamic outerwear segment (~5% growth per year) and its selective retail expansion limits the risks of overexposure (= brand dilution) despite an expected 10% sales CAGR during 2015-18. The group should maintain its high margin level (34.1% adj. EBITDA margin in 2015e) thanks to its "Retail Excellence" (one of the highest sales/m² ratio in the sector with EUR30k/m², focus on SSSG, limited store size formats, etc.) and improve its FCF generation in the MT. The stock proved to be more resilient than our luxury sample in Q2 (flat vs. -11%) but was affected by Brexit (-14% over 24-27th June). Any easing of these concerns implies attractive rebound potential given these strong fundamentals, this is why we add Moncler in our Top Picks list.

Food retailing: **Ahold** (Buy, FV: EUR22): In this apathetic environment and post Brexit, we continue to favour AHOLD (Buy, FV @EUR22) which boasts a very defensive profile and attractive comparative edges for scalded investors: **1/** strong exposure to the US (~60% of EBIT) and no exposure to the UK, **2/** best FCF generation within the panel (~7% FCF yield vs ~3.5% on average for the sector); **3/** the upcoming merger with Delhaize (mid-July) that will allow the Dutch retailer to share its costs with the Belgian banner; **4/** as a general rule, very strong momentum. As such, we believe that Ahold deserves to remain on BG's top pick list.

Food & Beverages: Despite the upcoming good reporting season, we have not chosen a top pick as many of our stocks are trading at an historical high and we have limited upside.

Luxury goods: We add **LVMH (Buy- FV: EUR170).** Despite a clearly challenging environment for luxury goods industry (lack of tourists in Europe) and a potentially risky H1 publication (no sales growth at LV in Q2, likely Fashion & Leather margin erosion including for LV), we have added LVMH in our Q3 Top Picks given i/ attractive valuation (10.6x 16 EV/EBIT or 8% discount vs peers) and ii/ recent underperformance (-9% vs DJ Stoxx on 3m). Actually, we argue that poor expectations for H1 are already, at least partly, taken into account by investors, hence the current share price that dropped 1% on last month vs +3% for our luxury stocks sample average. Furthermore, we are convinced that other divisions such as W&S, P&C and W&J should report better trends that could offset potential disappointments at F&L.

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Business Services : Top picks: We are maintaining Elior

	1 M	3 M	6 M	31/12/15
Inds Gds & Svs	-6.6%	-2.6%	-4.6%	-6.9%
DJ Stoxx 600	-5.0%	-1.2%	-9.7%	-11.4%

*Stoxx Sector Indices

Companies covered			
BUREAU VERITAS		**NEUTRAL**	**EUR21**
Last Price	EUR18.535	*Market Cap.*	EUR8,192m
COMPASS GROUP		**NEUTRAL**	**1200p**
Last Price	1445p	*Market Cap.*	*GBP23,737m*
EDENRED		**NEUTRAL**	**EUR19**
Last Price	EUR19.07	*Market Cap.*	*EUR4,457m*
ELIOR		**BUY**	**EUR23**
Last Price	EUR19.57	*Market Cap.*	*EUR3,372m*
EUROFINS SCIENTIFIC		**SELL**	**EUR340**
Last Price	EUR329.75	*Market Cap.*	*EUR5,275m*
SGS SA		**BUY**	**CHF2400**
Last Price	CHF2204	*Market Cap.*	*CHF17,240m*
SODEXO		**NEUTRAL**	**EUR88**
Last Price	EUR96.9	*Market Cap.*	*EUR14,898m*

LOOKING BACK ON Q2 2016

Bureau Veritas was the only group to report negative performances in Q2 with a share price down 2.9% in absolute terms and -0.7% vs. the DJ Stoxx i.e. consolidating after a strong Q1 up respectively 6.4% and 14.1%. Main competitor **SGS** maintained its Q1 positive trend in Q2, up 10.5% in absolute terms (+5.7% in Q1) and 13% in Euros vs. the DJ Stoxx (+13.3% in Q1). **Eurofins Scientific** (coverage initiated on 27th May, 2016 at Sell with a FV of EUR340) was up 3.5% in absolute terms and 5.9% vs. the DJ Stoxx.

The picture was mixed again in **Foodservices**. After the best performance in Q1 due to positive newsflow, some consolidation was seen on **Sodexo,** up 2.1% in absolute terms and 4.5% vs. the DJ Stoxx. For **Elior**, our top pick, stock price consolidation continued in Q2 (+1.8% in absolute terms) as as the case in Q1 after the strong outperformance in 2015 (up 56.9%) and despite positive newsflow, which makes us increasingly confident in management's expectations. The best performances stemmed from **Compass Group** and **Edenred** (after the worst ones in Q1), up respectively 10.5% and 8.3% in absolute terms and in euros (+13% and 10.9% vs. DJ Stoxx) with Edenred benefiting notably from the re-appreciation of BRL/EUR exchange rate.

WHAT WE SEE FOR Q3 2016

In **Foodservices**, **Sodexo** is due to report 9m revenue on Friday 8th July for which we forecast total revenue of EUR15.603bn up 3.4% in reported terms implying -1.3% in Q3 (after +3.6% in Q2 and +9.6% in Q1) impacted by negative currencies of -3.7%. Lfl growth should be largely in line with FY guidance (3% after RWC) estimated at 3.4% implying 2.3% in Q3 after 2.7% in Q2 and 4.7% in Q1. Visibility on **Edenred** remains limited and the current main driver i.e. the BRL parity difficult to anticipate. For H1 results, we do not expect many surprises pending the investor day in October. Regarding H1 results, we anticipate EUR524m in total revenue down 2.7% in reported terms with lfl growth of 5.4% implying 5.5% in Q2 and an EBIT of EUR153m vs. EUR165m last year. Management will guide on FY results (our estimate is EUR372m). No major surprises are anticipated for **Compass Group** Q3 IMS after the recent investor day: we anticipate lfl growth of 5.5% slightly lower in H1 at 5.7% mainly due to RoW. During the investor day, management confirmed its medium-term guidance for lfl revenue growth of between 4% and 6% with some margin improvement albeit “modest” and further cash returns. In fact, we estimate that between 2 to 3% of the group's equity capital can be bought back each year when net debt/EBITDA will be back to below 1.5x i.e. in 2016 based on our forecast of 1.3x.

Regarding **TIC**, having downgraded our estimates on **Bureau Veritas** (see our note on 1st July), we confirm that H1 numbers (especially lfl revenue growth down 0.6%) will greatly contrast with those of **SGS** with more FY guidance that could be at risk. Remember that for **SGS** we anticipate lfl revenue growth of 2.6% in H1 and 3.3% for the FY. Following the conference call on private equity issuance, no major surprises on **Eurofins Scientific's** H1 results are expected, management having confirmed that Q2 was robust even if lfl growth should be lower than in Q1 up over 10%.

CONCLUSIONS AND TOP PICKS

We are maintaining **Elior** as our top pick.(see our note on 22nd June :*On track with 2020 Ambitions)*

Actually, following H1 2015-16 results on 27th May, management is clearly stepping up the roll-out of its 2020 Ambitions plan. It is particularly focused on the group’s expansion via acquisitions, which is gaining momentum with around EUR400m in annualised revenue added since the beginning of the year, 50% of which stemming from Preferred Meals in the US acquired at the end of last May.

Having reported H1 revenue growth of 3.5% with organic growth of 1.5% taking into account the 1.9% negative effect of voluntary contract exits (vs. 1.5% initially anticipated) with an EBITDA margin up 20bp to 7.4%, management confirmed its full year objectives with: 1) organic growth of "more than 3%" excluding the impact of voluntary contract exits which is expected to be less than 200bp vs. 150bp previously announced, 2) EBITDA margin of over 8.6% i.e. at least a 20bp improvement taking into account some penalties from contract cancellations or the negative impact of acquisitions on margin. The full benefits, especially from contract exits, is expected in 2016-17 and

management has confirmed its target for a 40bp EBITDA margin improvement to reach 9%.
In addition, early last May, the group undertook the early redemption of all the outstanding high yield 6.5% May 2020 Senior Secured Notes for a total amount of EUR186m. Simultaneously, the group raised the same amount from investors via a seven-year private placement at a variable rate plus 250bp. In all, taking into account recent M&A, we estimate net debt 2015-16 at around EUR1.6bn up EUR150m vs. last year with an average cost of 2.8% (vs. 3.3%).
In all, these actions make us increasingly confident in management's short and medium-term guidance. Our DCF valuation using a leverage beta of 1.3x yields our FV of EUR23. Our SOTP yields a valuation of EUR24 per share.

NEXT CATALYSTS

Sodexo: 9m 2015-16 Revenue on 8th July (before market)

SGS: H1 results on 18th July (before market). Capital market days on 27 & 28 October (Geneva)

Edenred: H1 results on 22nd July (before market). Capital market day on 19th October (London)

Bureau Veritas: H1 results on 28th July (before market)

Compass Group: 9m 2015-16 Trading update on 28th July (before market)

Elior: 9m 2015-16 Revenue on 28th July (before market)

Eurofins Scientific: H1 results on 2nd August (before market)

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Insurance : Top Picks Q3: Blind spot

	1 M	3 M	6 M	31/12/15
Insurance	-17.2%	-14.5%	-25.4%	-28.4%
DJ Stoxx 600	-6.9%	-3.6%	-10.0%	-12.9%

*Stoxx Sector Indices

Companies covered

AEGON		**NEUTRAL**	**EUR6**
Last Price	EUR3.036	*Market Cap.*	EUR6,546m
ALLIANZ		**BUY**	**EUR180**
Last Price	EUR119.2	*Market Cap.*	*EUR54,474m*
AXA		**BUY**	**EUR29**
Last Price	EUR16.305	*Market Cap.*	*EUR39,527m*
CNP ASSURANCES		**NEUTRAL**	**EUR15**
Last Price	EUR12.375	*Market Cap.*	*EUR8,497m*
COFACE		**NEUTRAL**	**U.R.**
Last Price	EUR4.336	*Market Cap.*	*EUR682m*
EULER HERMES		**BUY**	**EUR99**
Last Price	EUR70.6	*Market Cap.*	*EUR3,011m*
HANNOVER RE		**SELL**	**EUR110**
Last Price	EUR89.35	*Market Cap.*	*EUR10,775m*
MUNICH RE		**SELL**	**EUR185**
Last Price	EUR141.2	*Market Cap.*	*EUR22,741m*
SCOR		**BUY**	**EUR38**
Last Price	EUR25.365	*Market Cap.*	*EUR4,870m*
SWISS RE		**NEUTRAL**	**CHF100**
Last Price	CHF80.55	*Market Cap.*	*CHF29,860m*
ZURICH INSURANCE GROUP		**NEUTRAL**	**CHF270**
Last Price	CHF226.6	*Market Cap.*	*CHF34,110m*

LOOKING BACK ON Q2 2016

The DJ Stoxx Insurance lost 11% over the quarter, underperforming the market by more than 800bps (DJ Stoxx600 down 2.3%). Companies we cover have lost 10% on average, and 5% including dividends. The top performers were Zurich, CNP, Swiss Re and Euler Hermes whereas the worst performers were Aegon, Munich Re, Coface and Scor.

Of course the major event of Q2 was market turbulence associated with Brexit, which overnight disrupted most financial markets around the world and created a massive flight to quality (lower rates on major benchmarks, stress on credit spreads and equities, higher volatility).

The strong market reaction by insurance stocks we cover was not based primarily on potential operating issues (UK is not a central part of the business of the companies we cover, basically between 5% and 10% of operating profit), nor due to FX (in most cases the potential negative impact of the drop in the GBP was more than offset by the rise in the USD, where the share of business is much higher, up to 45%), nor earnings (potential losses on assets are minimal at this stage), but due to solvency.

Indeed, flight to quality and stress on more risky assets represent a major stress scenario for solvency margins in a Solvency II environment, which only came into force a few months ago (i.e. still a limited market education and back-testing). And of course potential pressure on solvency margins means potential pressure on dividend prospects, which have acted as a powerful catalyst for the sector in the last years. Remember most insurance companies gave precise dividend guidance as long as their solvency margin remains in a comfort area. Should they break it, dividends might be at risk.

Considering Q1 solvency margins levels and Q2 market events, our view is that the impact on solvency margins is only limited, at this stage. But the more rates go down, the higher the pressure will be…

WHAT WE SEE FOR Q3 2016

Please tell me about financial markets… Q3 2016 is a particularly tough call in general, and more particularly for insurance, as it remains very sensitive to very nervous financial markets.

Since Brexit, we experienced a few days of intense market stress, followed by some relief (screaming buys, hope of central bank interventions…), and then another round of market pressure. In this context, the insurance sector should remain very volatile, which is consistent with the mountain of uncertainties we are currently facing. And we all know how scary financial markets could be during the summer …

On top of that, Q2 2016 results should come under pressure across the board. Underwriting results should suffer from i/ higher claims experience, mainly driven by higher natcats, with significant earthquakes in Japan and Ecuador, a devastating fire in Canada, and major flooding in western Europe and ii/ lower commissions on asset management and unit-linked products (S&P500 down only 1% yoy on average but Stoxx50 down 18% yoy on average). We may also see lower capital gains and some equity impairments.

CONCLUSIONS AND TOP PICKS

Considering poor short-term visibility, at least until companies report their Q2 numbers (starting end-July), we believe it is wise to restrain from any insurance companies in our quarterly Top Pick list.

For longer term investors, and provided the stress on financial markets does not increase too much, we believe current prices offer very attractive (re)entry points, especially for AXA and Allianz. On the other side, if the markets remain bumpy during the summer, reinsurers, Zurich and Allianz offer more defensive profiles than average.

Bryan Garnier stock rating system

For the purposes of this Report, the Bryan Garnier stock rating system is defined as follows:

Stock rating

BUY	Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
NEUTRAL	Opinion recommending not to trade in a stock short-term, neither as a BUYER or a SELLER, due to a specific set of factors. This view is intended to be temporary. It may reflect different situations, but in particular those where a fair value shows no significant potential or where an upcoming binary event constitutes a high-risk that is difficult to quantify. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

Distribution of stock ratings

BUY ratings 56.8%　　NEUTRAL ratings 33.8%　　SELL ratings 9.5%

Research Disclosure Legend

1	Bryan Garnier shareholding in Issuer	Bryan Garnier & Co Limited or another company in its group (together, the "Bryan Garnier Group") has a shareholding that, individually or combined, exceeds 5% of the paid up and issued share capital of a company that is the subject of this Report (the "Issuer").	No
2	Issuer shareholding in Bryan Garnier	The Issuer has a shareholding that exceeds 5% of the paid up and issued share capital of one or more members of the Bryan Garnier Group.	No
3	Financial interest	A member of the Bryan Garnier Group holds one or more financial interests in relation to the Issuer which are significant in relation to this report	No
4	Market maker or liquidity provider	A member of the Bryan Garnier Group is a market maker or liquidity provider in the securities of the Issuer or in any related derivatives.	No
5	Lead/co-lead manager	In the past twelve months, a member of the Bryan Garnier Group has been lead manager or co-lead manager of one or more publicly disclosed offers of securities of the Issuer or in any related derivatives.	No
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