

## Essilor

Price EUR114.80

In sun Essilor is replicating the successful recipe from the Rx lens business

Fair Value EUR130 (+13%)

BUY

|                            |               |
|----------------------------|---------------|
| Bloomberg                  | EF FP         |
| Reuters                    | ESSI.PA       |
| 12-month High / Low (EUR)  | 123.6 / 103.0 |
| Market Cap (EURm)          | 25,037        |
| Ev (BG Estimates) (EURm)   | 26,706        |
| Avg. 6m daily volume (000) | 447.1         |
| 3y EPS CAGR                | 10.1%         |

|                | 1 M   | 3 M   | 6 M  | 31/12/15 |
|----------------|-------|-------|------|----------|
| Absolute perf. | 0.8%  | -3.4% | 5.8% | -0.2%    |
| Consumer Gds   | 0.2%  | 2.5%  | 2.5% | -1.4%    |
| DJ Stoxx 600   | -0.2% | 4.0%  | 1.6% | -6.3%    |

| YEnd Dec. (€m) | 2015  | 2016e | 2017e | 2018e |
|----------------|-------|-------|-------|-------|
| Sales          | 6,716 | 7,132 | 7,625 | 8,157 |
| % change       |       | 6.2%  | 6.9%  | 7.0%  |
| EBITDA         | 1,263 | 1,341 | 1,449 | 1,566 |
| EBIT           | 1,183 | 1,271 | 1,379 | 1,501 |
| % change       |       | 7.5%  | 8.5%  | 8.9%  |
| Net income     | 757.1 | 846.6 | 923.3 | 1,017 |
| % change       |       | 11.8% | 9.1%  | 10.1% |

|                  | 2015 | 2016e | 2017e | 2018e |
|------------------|------|-------|-------|-------|
| Operating margin | 17.6 | 17.8  | 18.1  | 18.4  |
| Net margin       | 11.3 | 11.9  | 12.1  | 12.5  |
| ROE              | 13.3 | 13.2  | 12.9  | 13.4  |
| ROCE             | 20.0 | 20.1  | 20.9  | 21.5  |
| Gearing          | 34.7 | 24.5  | 15.9  | 13.7  |

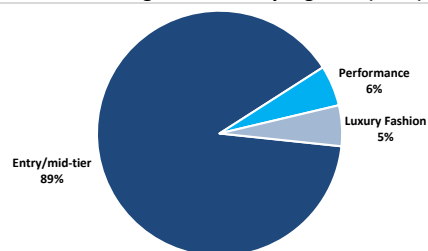
| (€)           | 2015  | 2016e | 2017e | 2018e |
|---------------|-------|-------|-------|-------|
| EPS           | 3.57  | 3.96  | 4.32  | 4.76  |
| % change      | -     | 11.0% | 9.1%  | 10.1% |
| P/E           | 32.2x | 29.0x | 26.6x | 24.1x |
| FCF yield (%) | 3.5%  | 3.7%  | 4.0%  | 4.3%  |
| Dividends (€) | 1.15  | 1.30  | 3.15  | 4.15  |
| Div yield (%) | 1.0%  | 1.1%  | 2.7%  | 3.6%  |
| EV/Sales      | 4.0x  | 3.7x  | 3.4x  | 3.2x  |
| EV/EBITDA     | 21.5x | 19.9x | 18.1x | 16.7x |
| EV/EBIT       | 23.0x | 21.0x | 19.0x | 17.4x |

The third and last day of this Field Trip took place at FGX headquarters (Smithfield, RI) to present more in details the Group's sun strategy in the US and worldwide. In a highly fragmented sun market expected to grow at a healthy 5-7% p.a., Essilor anticipates sales CAGR of ~9% over 2015-18, o/w 7% organically to reach a revenue of EUR1.1-1.2bn by 2018 (vs. ~EUR860m in 2015). This outperformance will be driven by: (i) increasing the quality of sun lenses and bringing innovation in all price points (premiumisation), (ii) expanding geographically its global brands (Foster Grand, Bolon, Costa, etc.) and (iii) M&A to enlarge the brand portfolio.

## ANALYSIS

- **Sunglasses industry harbours solid growth drivers. 1/ This category is quite under-penetrated:** just 30% of the world population and more importantly, only 10% of eyeglasses wearers are equipped with sunglasses (potential to reach 50% of eyeglasses wearers), **2/ Closing the technological gap:** in our view this gap is more significant than for Rx lenses as most of the eyewear manufacturers' R&D was spent on frames rather than sun lenses: as such polarized lenses only equip 30% of plano sunglasses, whilst there is a potential to 90%, **3/ Favorable demographic trends:** ageing population, growing awareness among the emerging middle-class and the fashion image that leads to shorter replacement rates (~12-18 months on average). Against these structural drivers, **Essilor expects this sunglass segment to grow at 5-7% p.a.**, the lower end of this bracket being within range even when adverse macro conditions, or unfavourable weather conditions occur like this year.
- **Essilor is already a key player in sunglasses.** Last year, EI reached sales of ~EUR860m in sun excl. Readers (~13% of total revenue) and sold 69m pairs of sunglasses, mostly below a retail price of USD30. As a comparison Luxottica produced more than 93m premium/luxury frames last year (Rx and sunglasses combined). As shown on the table next page, **EI owns 4 of the top 15 sun brands in volumes:** three of them belong to the entry/mid-tier price points (**Foster Grant, Bolon, Molsion**) and **Costa** which is part of the performance segment.

Global Plano sunglass market by segment (units):



Essilor Sun Sales Breakdown by segment:



Source: Essilor

- **Sun strategy: replicate a proven success recipe.** Indeed Essilor will use several levers to support its growth strategy: (i) **introducing higher quality** and innovative sun lenses to favour premiumisation (e.g.: Bolon average retail selling price increased by 20% over 2013-15), (ii) **encouraging sunwear prescription** to leverage its expertise from its core activity (+ positive impact on ASP and margins), (iii) **channel expansion** like online (~10% of EI sunwear sales), travel retail (Bolon, Costa) and independent opticians, (iv) **geographical expansion**, particularly for Bolon and Costa.
- **Foster Grant at the forefront in the segment >USD30.** FG (12m units) is US' largest sunglass brand and the No.2 in the world (after Ray-Ban), almost exclusively positioned within the price point >USD30. Yet, FGX continue to strengthen the brand equity by: (i) bringing unmatched innovations in this price point (e.g.: Eyezen, e.Reader with the anti-harmful blue light filter, etc.), (ii) increasing the shopping experience (merchandising and retail expertise). Thanks to these levers, FGX is now legitimate enough to start penetrating the USD30-50 price point.
- **Essilor's Chinese sun brands own 40% of the mid-tier segment in China.** The Chinese sunglass market is #1 in volume and #2 in value (~9% of global market). Essilor's PF encompasses **Bolon** (~70%), **Molsion** (~20%) and **Prosun** (~10%). Although Bolon was particularly affected by the implementation of the ARTEMIS inventory management system in H1, its growth in China relies on its strong brand equity and brand awareness (85% absolute awareness), not to forget a broad network of 30,000 retailers in Tier 2-4 cities. In parallel of an ongoing domestic development, Bolon is now rolled out internationally (Singapore, Malaysia, etc.) and in new channels such as travel retail and optical chains.
- **Costa is US' fastest-growing sun brand.** In 2015 the brand achieved sales over USD120m, leading



to a sales CAGR of 20% over 2012-15. Under the new management of Holly Rush, former President of LUX's Wholesale North America, Costa on its unique positioning (seaside communities, fishermen) to maintain this robust pace of growth: **(i)** interestingly Costa has the youngest customer base, especially the key "Millennial generation" (see table 3 below), **(ii)** expand the distribution in the US (Southeastern US: ~70% of sales) and enlarge its customer base to up to 150m consumers vs. 47m currently with a more lifestyle image, **(iii)** this rebalancing will also help Costa to expand internationally (Europe, Australia-NZ, Asia). Consequently, the product portfolio should be 50/50 between core and lifestyle in the MT vs. 80/20 today.

- **Will it increase the group's cyclicity? Not significantly in our view.** Admittedly the unhelpful H1 performance of the Sun & Readers division (-3.9% LFL) has not calmed some investors' fears about Essilor becoming more cyclical than previously. Yet, CEO Hubert Sagnières recalled that: **(i)** the poor performance was also due to a company-specific initiative (e.g. ARTEMIS in China), **(ii)** the global sunglasses market should slightly outgrow the lens segment this year despite unfavourable weather conditions and a more challenging macro environment, and **(ii)** the Group's exposure to sun in 2018 should amount to ~14-15% of total sales (EUR1.1-1.2bn vs. overall revenue target of EUR8.2bn), not materially higher than in 2015 (~13% of total sales).

#### VALUATION

- The stock trades at 26.6x 2017e P/E, implying a 11% premium to its 2004-16 historical average.

#### NEXT CATALYSTS

- Essilor will release its Q3 sales on 21st October. [Click here to download](#)

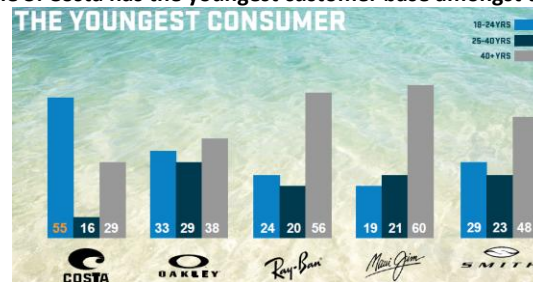
**Table 1: Breakdown of total sun revenues of Essilor (2015):**



**Table 2: Essilor leads the sunglasses industry in volumes**

| We own 4 of the top 15 sun brands worldwide                                    | Volume (in million of pairs) | Global/Regional/Local |
|--|------------------------------|-----------------------|
| Ray-Ban  | >25                          | G                     |
| Foster Grant   | >12                          | R                     |
| Oakley   | ~10                          | G                     |
| Maui Jim   | ~4                           | R/G                   |
| Bolon, Armani  | >2.5                         | L/R                   |
| Chilli Beans   | ~2.5                         | L                     |
| Polaroid, Gucci, Carrera, Dolce & Gabbana, Prada, Police, Dior, Costa, Molsion | 1 to 2                       | G/L                   |
| Small selective/Small local/Fast-growing brands                                |                              | G/L/R                 |
| TOTAL  | ~600                         |                       |

**Table 3: Costa has the youngest customer base amongst the premium/performance sun brands:**



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**Analyst :**  
Cédric Rossi  
33(0) 1 70 36 57 25  
crossi@bryangarnier.com

**Sector Team :**  
Nikolaas Faes  
Loïc Morvan  
Antoine Parison  
Virginie Roumage

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|         |   |
|---------|---|
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| 15 St. Botolph Street             | 75008 Paris                               | New York, NY 10022       | 80538 Munich         | New Delhi 110 001          |
| London EC3A 7BB                   | Tel: +33 (0) 1 56 68 75 00                | Tel: +1 (0) 212 337 7000 | Germany              | Tel +91 11 4132 6062       |
| Tel: +44 (0) 207 332 2500         | Fax: +33 (0) 1 56 68 75 01                | Fax: +1 (0) 212 337 7002 | +49 89 2422 62 11    | +91 98 1111 5119           |
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|                                   | resolution (ACPR)                         |                          |                      | CP 2113                    |
|                                   |   |                          |                      | Genève 1, CH 1211          |
|                                   |   |                          |                      | Tel +4122 731 3263         |
|                                   |   |                          |                      | Fax+4122731 3243           |
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