BRYAN, GARNIER & CO

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11th October 2016

# BG's Wake Up Call

|  | Last close | Daily chg (%) | Chg YTD (%) |
|---|---|---|---|
| **Indices** |  |  |  |
| Dow Jones | 18329.04 | +0.49% | +5.19% |
| S&P 500 | 2163.66 | +0.46% | +5.86% |
| Nasdaq | 5328.67 | +0.69% | +6.42% |
| Nikkei | 17024.76 | +0.98% | -11.42% |
| Stoxx 600 | 341.977 | +0.69% | -6.52% |
| CAC 40 | 4497.26 | +1.06% | -3.01% |
| **Oil /Gold** |  |  |  |
| Crude WTI | 51.35 | +3.09% | +38.04% |
| Gold (once) | 1259.81 | +0.51% | +18.58% |
| **Currencies/Rates** |  |  |  |
| EUR/USD | 1.1157 | -0.17% | +2.71% |
| EUR/CHF | 1.09715 | +0.22% | +0.90% |
| German 10 years | -0.011 | -78.03% | -101.69% |
| French 10 years | 0.293 | +15.81% | -70.17% |
| Euribor | - | +-% | +-% |

**Economic releases :**

| Date | |
|---|---|
| 11th-Oct | EUR - Euro Zone ZEW Survey (Economic Sentiment - OCT)<br>CAD - Housing Stats (SEP) |

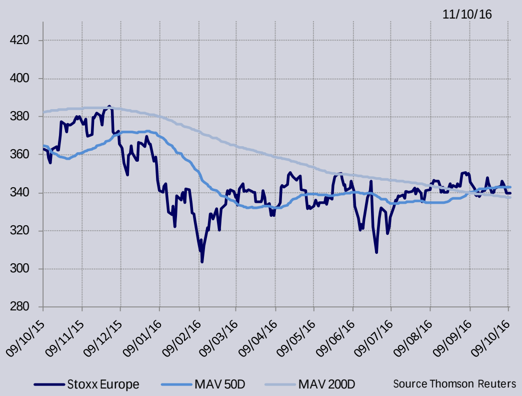
**Upcoming BG events :**

| Date | |
|---|---|
| 21st-Oct | KORIAN (BG Geneva roadshow with CFO) |
| 28th-Oct | IMERYS (Paris roadshow) |
| 8th-Nov | LVMH (BG Luxembourg roadshow with IR) |
| 14th-Nov/ 15th-Nov | 4th Paris Healthcare Conference |
| 18th-Nov | ENGIE (BG Luxembourg roadshow with IR) |
| 24th-Nov | IMERYS (BG London roadshow with IR) |

**Recent reports :**

| Date | |
|---|---|
| 7th-Oct | ALTICE Lower risk profile |
| 7th-Oct | SAINT GOBAIN : Endless sluggishness is not our scenario (report released today) |
| 4th-Oct | CASINO We are cautious ahead of Q3 figures |
| 4th-Oct | LAFARGE HOLCIM This is still a Buy |
| 15th-Sept | Remy Cointreau : It keeps getting better |
| 14th-Sept | Automotive Innovation: the only way to stand out! |

List of our Reco & Fair Value : Please click here to download




## AB INBEV — BUY vs. NEUTRAL, Fair Value EUR124 vs. EUR109 (+8%)

*Fox in the Hen House (report released today)*

As the acquisition of SABMiller is finalised, there is already speculation on what the next target could be for AB InBev (AB InBev has an internal target to reach USD100bn in revenues by 2022). Although we believe that the case for Coca-Cola is stronger than that for PepsiCo, investors wanting to benefit from the transformation of AB InBev into a drinks company (from a brewer) are probably best to buy shares in AB InBev rather than those of any potential targets.

## IPSEN — BUY-Top Picks, Fair Value EUR67 (+6%)

*A full case vs a single sentence*

At ESMO principal investigator presented quite convincing phase II data for cabozantinib in 1L RCC that could be the base of a supplement filing … despite a more balanced view from discussant.

## LVMH — BUY, Fair Value EUR171 (+9%)

*Q3 sales grew 6% organically, significantly above consensus*

LVMH reported Q3 sales of EUR9.14bn yesterday (cs: EUR8.93bn), up 4% and 6% organically (cs:+4%). This highlighted a clear acceleration versus Q2 and H1 (both at +4% organically). Note the very good performance by the F&L division (+5% in Q3). We are maintaining our Buy recommendation with an unchanged EUR171 FV.

## *In brief...*

**SPIRITS, *LVMH's Q3 sales ( what read-across for European spirits groups?***

Food & Beverages

# AB InBev

Price EUR115.05

## Fox in the Hen House (report released today)

**Fair Value EUR124 vs. EUR109 (+8%)** **BUY vs. NEUTRAL**

| | |
|---|---|
| Bloomberg | ABI BB |
| Reuters | ABI.BR |
| 12-month High / Low (EUR) | 123.3 / 98.4 |
| Market Cap (EURm) | 185,028 |
| Ev (BG Estimates) (EURm) | 265,171 |
| Avg. 6m daily volume (000) | 1,420 |
| 3y EPS CAGR | 6.3% |

| | 1 M | 3 M | 6 M | 31/12/15 |
|---|---|---|---|---|
| Absolute perf. | 3.6% | -0.8% | 7.7% | 0.6% |
| Food & Bev. | -1.4% | -1.7% | 2.2% | -1.8% |
| DJ Stoxx 600 | -1.0% | 4.5% | 3.1% | -6.5% |

| YEnd Dec. (USDm) | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| Sales | 43,604 | 43,044 | 58,284 | 60,870 |
| *% change* | | *-1.3%* | *35.4%* | *4.4%* |
| EBITDA | 16,921 | 16,643 | 23,847 | 25,688 |
| EBIT | 13,768 | 13,565 | 19,891 | 21,609 |
| *% change* | | *-1.5%* | *46.6%* | *8.6%* |
| Net income | 8,513 | 7,532 | 11,123 | 12,210 |
| *% change* | | *-11.5%* | *47.7%* | *9.8%* |

| | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| Operating margin | 31.6 | 31.5 | 34.1 | 35.5 |
| Net margin | 19.5 | 17.5 | 19.1 | 20.1 |
| ROE | 20.2 | 17.5 | 12.9 | 13.5 |
| ROCE | 10.1 | 10.1 | 10.4 | 8.6 |
| Gearing | 98.7 | 101.7 | 97.0 | 89.5 |

| (USD) | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| EPS | 5.10 | 4.52 | 5.58 | 6.12 |
| *% change* | - | *-11.5%* | *23.5%* | *9.8%* |
| P/E | 25.2x | 28.4x | 23.0x | 21.0x |
| FCF yield (%) | 3.6% | 3.0% | 5.4% | 4.9% |
| Dividends (USD) | 2.68 | 2.37 | 2.93 | 3.21 |
| Div yield (%) | 2.1% | 1.8% | 2.3% | 2.5% |
| EV/Sales | 6.7x | 6.9x | 5.8x | 5.5x |
| EV/EBITDA | 17.2x | 17.8x | 14.1x | 13.0x |
| EV/EBIT | 21.1x | 21.8x | 16.9x | 15.4x |


**As the acquisition of SABMiller is finalised, there is already speculation on what the next target could be for AB InBev (AB InBev has an internal target to reach USD100bn in revenues by 2022). Although we believe that the case for Coca-Cola is stronger than that for PepsiCo, investors wanting to benefit from the transformation of AB InBev into a drinks company (from a brewer) are probably best to buy shares in AB InBev rather than those of any potential targets.**

### ANALYSIS

- Given the obvious strengths of AB InBev in cost-cutting and distribution, and the limited remaining possibilities in beer, consolidation in soft drinks might be the next step for the company. AB InBev would become a drinks business, rather than just a brewer, delivering more self-help with the potential cost and revenue benefits of selling beer and soft drinks through the same distribution system.
- Soft drinks and beer seem to have the same profile in terms of growth (i.e. 5% p.a. over the medium term), drivers (population growth, rising incomes and middle classes) and profitability (PepsiCo Beverages and the Coca-Cola system has operating margins of respectively 14% and 16%, which compares well with any brewer). However, AB InBev does better with an operating margin of 31% in beer and has already the credentials to do the same in soft drinks (Brazil's soft drinks margin of 44%).
- We believe that the case for The Coca-Cola Company is more convincing than that for PepsiCo, as Coca-Cola is the stronger soft drinks brand and has plenty of opportunities to drive share growth in still non-alcoholic beverages. Furthermore, it offers additional prospects of buying out the bottlers (which have been separated from the main company) at much lower valuations. Integrating the entire Coca-Cola system sets AB InBev on its way to USD300bn in revenues by 2030.
- We are increasing our 2017 operating profit and EPS by about 4% to take into account the resurgence of some emerging market currencies against the USD (ytd BRL +25%, ZAR +20%, COP+15%). Our DCF-based fair value of EUR124 is computed using a risk free rate of 1.6%, a risk premium of 7.0% and a Beta of 0.95.

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Healthcare

# Ipsen

Price EUR63.22

## A full case vs a single sentence

**Fair Value EUR67 (+6%)** **BUY-Top Picks**

| | |
|---|---|
| Bloomberg | IPN FP |
| Reuters | IPN.PA |
| 12-month High / Low (EUR) | 63.6 / 47.1 |
| Market Cap (EUR) | 5,264 |
| Ev (BG Estimates) (EUR) | 5,352 |
| Avg. 6m daily volume (000) | 75.50 |
| 3y EPS CAGR | 13.8% |

| | 1 M | 3 M | 6 M | 31/12/15 |
|---|---|---|---|---|
| Absolute perf. | 8.3% | 20.9% | 21.3% | 3.6% |
| Healthcare | -0.6% | -4.9% | 0.6% | -9.5% |
| DJ Stoxx 600 | -1.0% | 4.5% | 3.1% | -6.5% |

| YEnd Dec. (€m) | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| Sales | 1,444 | 1,566 | 1,714 | 1,866 |
| *% change* | | *8.5%* | *9.4%* | *8.9%* |
| EBITDA | 366 | 407 | 462 | 544 |
| EBIT | 322.5 | 340.9 | 390.0 | 466.3 |
| *% change* | | *5.7%* | *14.4%* | *19.5%* |
| Net income | 228.0 | 237.3 | 278.0 | 335.6 |
| *% change* | | *4.1%* | *17.2%* | *20.7%* |

| | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| Operating margin | 22.3 | 21.8 | 22.8 | 25.0 |
| Net margin | 12.5 | 14.0 | 14.1 | 15.9 |
| ROE | 15.5 | 16.9 | 16.7 | 17.8 |
| ROCE | 22.6 | 17.6 | 19.6 | 22.8 |
| Gearing | -8.3 | 6.4 | -0.2 | -9.2 |

| (€) | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| EPS | 2.78 | 2.89 | 3.39 | 4.09 |
| *% change* | *-* | *4.1%* | *17.2%* | *20.7%* |
| P/E | 22.7x | 21.8x | 18.6x | 15.4x |
| FCF yield (%) | 3.4% | 3.7% | 4.5% | 5.5% |
| Dividends (€) | 0.85 | 0.85 | 1.10 | 1.20 |
| Div yield (%) | 1.3% | 1.3% | 1.7% | 1.9% |
| EV/Sales | 3.6x | 3.4x | 3.1x | 2.7x |
| EV/EBITDA | 14.1x | 13.2x | 11.4x | 9.4x |
| EV/EBIT | 16.0x | 15.7x | 13.5x | 10.9x |


**At ESMO principal investigator presented quite convincing phase II data for cabozantinib in 1L RCC that could be the base of a supplement filing … despite a more balanced view from discussant.**

### ANALYSIS

- What we are doing here is the summarized feedback from the third day at ESMO since CABOSUN phase II data were in highlight at the Presidential session.
- CABOSUN recruited 150 patients with clear-cell RCC naïve to therapy and having a poor or intermediate risk i.e. having the poorer prognosis (in 2L they will have between 5.4 and 16.6 months median survival rate), including 37% with bone metastases. This population represents between 70 and 75% of the overall RCC population.
- The primary endpoint was median PFS and it was expanded from 5.6 to 8.2 months (HR=0.69, p=0.012), with benefit across all subgroups, although it is fair to say that those with bone metastases benefited the most. The difference in ORR was also outstanding at 46% vs 18% (when assessed by investigator). Dose reductions occurred in 58% and 49% respectively in the cabo arm and the sunitinib arm and grade 3-4 side effects appeared very comparable across the two arms (65% vs 68%) and grade 5 AEs unfrequent (5% vs 4%). So these are very strong and consistent data in a setting where nothing has emerged since a long time.
- Everything was good until the last part of the presenter's speech when he stated that, based on the absence of median OS benefit (HR=0.80 with 30.3 months vs 21.8 but p=NS), he would not be comfortable prescribing the drug in 1L until confirmatory data from a phase III trial. This has come as a very unexpected comment from one of the most respected specialists in Europe. Exactly at that time, Exelixis's share price collapsed in the US.
- Asked similarly about what they would do, three US specialists invited by Ipsen and Exelixis went against this conclusion. They showed that sunitinib very much did as expected in this trial and like in previous ones and despite a limited follow-up, OS benefit is likely to be confirmed later. In any case, with a clear benefit on mPFS and ORR, cabozantinib proves superior to sunitinib and time will tell about nivolumab and others in this setting. In PC trials, it has been showed that cabozantinib might well prepare the milieu or make the environment permissive for a better effect of an IO drug. So cabo first makes a lot of sense, even though safety can be called into question. But patients might prefer an oral drug. Lastly, some preliminary phase I data, mostly in bladder cancers, showed interesting efficacy and safety data in heavily pre-treated patients that are reassuring for the safety of the combination and convinced Exelixis to start a phase II trial in bladder cancer. Cabo+Nivo vs Cabo then Nivo looks like an interesting phase III to perform.
- So, in the end, our belief is that cabozantinib, whatever its precise setting, is here to play a key role in RCC. Because of its mode of action that not only involves VEGFR pathway but also MET and AXL, it is now the TKi of choice and it is a bit too early to say how IO will navigate around. Moreover, 5-10% of patients that have immune diseases are not eligible to IO and those with bone mets are also clear candidates for cabo. So, the size of the market opportunity remains to be carefully measured but CABOSUN data are clearly helpful to give cabozantinib a central place in RCC.

### VALUATION

- What can now happen with 1L RCC? Well, the optimism to be able to file on phase II data has clearly increased at Exelixis and Ipsen. The ability to file by the end of H1 2017 and to have a variation procedure in Europe making it possible to get an approval by year-end 2018 is real. This would be a major upside to our scenario and although the median duration of treatment based on mPFS might not be massively increased by getting in 1L, it is said that about 40% of patients are lost between 1L and 2L, thus reducing dramatically the target population.
- We will reassess our main asumptions at a later stage.

### NEXT CATALYSTS

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## LVMH

Price EUR157.05

### Q3 sales grew 6% organically, significantly above consensus

**Fair Value EUR171 (+9%)** **BUY**

| | |
|---|---|
| Bloomberg | MC FP |
| Reuters | LVMH.PA |
| 12-month High / Low (EUR) | 173.5 / 131.4 |
| Market Cap (EUR) | 79,741 |
| Ev (BG Estimates) (EUR) | 82,861 |
| Avg. 6m daily volume (000) | 773.3 |
| 3y EPS CAGR | 11.2% |

| 9.14 | 1 M | 3 M | 6 M | 31/12/15 |
|---|---|---|---|---|
| Absolute perf. | 3.2% | 16.9% | 7.8% | 8.4% |
| Pers & H/H Gds | -1.5% | -0.6% | 2.0% | -0.3% |
| DJ Stoxx 600 | -1.0% | 4.5% | 3.1% | -6.5% |

| YEnd Dec. (EURm) | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| Sales | 35,664 | 36,960 | 39,070 | 41,380 |
| *% change* | | *3.6%* | *5.7%* | *5.9%* |
| EBITDA | 7,505 | 7,800 | 8,530 | 9,260 |
| EBIT | 6,605 | 6,850 | 7,530 | 8,210 |
| *% change* | | *3.7%* | *9.9%* | *9.0%* |
| Net income | 3,573 | 4,010 | 4,470 | 4,912 |
| *% change* | | *12.2%* | *11.5%* | *9.9%* |

| | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| Operating margin | 18.5 | 18.5 | 19.3 | 19.8 |
| Net margin | 10.0 | 10.8 | 11.4 | 11.9 |
| ROE | 12.7 | 13.1 | 13.4 | 13.4 |
| ROCE | 10.1 | 10.0 | 10.6 | 11.0 |
| Gearing | 13.4 | 10.2 | 6.5 | 3.6 |

| (EUR) | 2015 | 2016e | 2017e | 2018e |
|---|---|---|---|---|
| EPS | 7.11 | 7.98 | 8.90 | 9.78 |
| *% change* | - | *12.2%* | *11.5%* | *9.9%* |
| P/E | 22.1x | 19.7x | 17.6x | 16.1x |
| FCF yield (%) | 2.9% | 3.2% | 3.8% | 4.0% |
| Dividends (EUR) | 3.55 | 3.90 | 4.30 | 4.70 |
| Div yield (%) | 2.3% | 2.5% | 2.7% | 3.0% |
| EV/Sales | 2.3x | 2.2x | 2.1x | 2.0x |
| EV/EBITDA | 11.1x | 10.6x | 9.6x | 8.8x |
| EV/EBIT | 12.6x | 12.1x | 10.9x | 9.9x |

**LVMH reported Q3 sales of EUR9.14bn yesterday (cs: EUR8.93bn), up 4% and 6% organically (cs:+4%). This highlighted a clear acceleration versus Q2 and H1 (both at +4% organically). Note the very good performance by the F&L division (+5% in Q3). We are maintaining our Buy recommendation with an unchanged EUR171 FV.**

**ANALYSIS**

- **Q3 2016 sales grew 6% organically to EUR9.14bn (consensus: EUR8.93bn and +4% organic growth)**, implying a 5% increase over 9M (EUR26.3bn). Note the 4% sales increase of the **Wines & Spirits** division (13% of group sales) following +13% in Q2 and +9% in H1. This expected slowdown was due to a very demanding comparison basis particularly at Hennessy (+16% in Q3 2015 of which +23% for Cognac). Hennessy volumes grew 9% over 9m vs +13% in H1. The very welcome news from the release stemmed from **Fashion & Leather goods** (34% of LVMH sales), which grew 5% in Q3 following +1% in Q2 and even +0% in H1. We guess that Louis Vuitton revenues increased at least 4%, a level which allows the brand to improve its profitability, and the F&L performance was achieved despite the negative impact of the US brands (Marc Jacobs and Donna Karan). And Fendi continued to perform very well.
- **Performances by the three other businesses were also very strong on the whole** with for instance, +10% for **Perfumes & Cosmetics in Q3** (after +6% in Q2 and +8% in H1) thanks to market share gains particularly at Christian Dior Parfums in all geographical areas, while **Watches & Jewelry** sales (9% of Group sales) were up 2% during the quarter, with no acceleration vs Q2, driven by Bulgari and Tag Heuer's positive performances, despite a tough watches environment. Lastly, **Selective Retail** activity (32% of revenues) enjoyed an 8% increase in Q3 (+7% in Q2), despite the decline in DFS sales (Hong Kong and Macau had a strong negative impact) but thanks to Sephora's clear dynamism (double digit sales increase) and market share gains in almost every region.

**Quarterly organic sales growth by division**

| in % | Q4 15 | Q1 16 | Q2 16 | H1 16 | Q3 16 | 9M 16 |
|---|---|---|---|---|---|---|
| Wines & Spirits | 4 | 6 | 13 | 9 | 4 | 7 |
| Fashion & Leather | 3 | 0 | 1 | 0 | 5 | 2 |
| Perfumes & Cosmetics | 7 | 9 | 6 | 8 | 10 | 8 |
| Watches & Jewelry | 3 | 7 | 2 | 4 | 2 | 4 |
| Selective Retail | 5 | 4 | 7 | 5 | 8 | 6 |
| **Group** | **5** | **3** | **4** | **4** | **6** | **5** |

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

- Although the group's management did not disclose **sales momentum by geographical area** yesterday (this should be done today during the conference call at 3pm), we guess that revenues were globally well oriented in **North America**, in line with Q2 (+7%), thanks especially to Hennessy, Sephora and Tag Heuer while **Europe** should grow modestly (+3% in Q2), penalised by France despite some improvement in others European countries, not to mention the UK (GBP decline). Momentum in **Japan** (7% of sales) was probably still very poor (-5% in Q2) since the strength of the JPY means fewer Chinese tourist are visiting Japan and the Japanese are buying more overseas (mainly in Korea and Hawaii for instance). We anticipate a significant acceleration in **APAC** (27% of sales). Momentum should have improved for F&L while Hennessy's slowdown clearly had a negative impact. Globally, the situation in **Mainland China** is improving (the Chinese are buying more at home than before) although it remains very challenging both in Hong Kong and Macao. APAC sales were down 2% in Q1 and up 3% in Q2.

**VALUATION**

- The LVMH share has gained 9% YTD (+0% for luxury average) and the stock is trading at 12.1x 2016 EV/EBIT, an 11% discount vs the peer average. We are maintaining our buy recommendation with an unchanged EUR171 FV.

**NEXT CATALYSTS**

- Today conference call at 3pm

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Sector View

## Spirits

| | 1 M | 3 M | 6 M | 31/12/15 |
|---|---|---|---|---|
| Food & Bev. | -1.4% | -1.7% | 2.2% | -1.8% |
| DJ Stoxx 600 | -1.0% | 4.5% | 3.1% | -6.5% |

*Stoxx Sector Indices

**Companies covered**

| | | |
|---|---|---|
| CAMPARI | BUY | EUR10,5 |
| DIAGEO | NEUTRAL | 2100p |
| PERNOD RICARD | NEUTRAL | EUR112 |
| REMY COINTREAU | BUY | EUR84 |

### LVMH's Q3 sales à what read-across for European spirits groups?

**ANALYSIS**

- Yesterday LVMH reported that its Wine & Spirits division increased 4% organically in Q3, implying a deceleration vs Q2 (+13%) and Q1 (+6%). This reflected the basis of comparison (+16% in Q3 2015) and was mainly due to cognac, while the trend in champagne remained globally unchanged. Hennessy volumes only grew 9% over 9M vs +13% in H1. The group mentioned good growth in the US and improved momentum in China. It will provide the individual organic sales growth levels for cognac & spirits and champagne during the conference call due to be held at 3pm CET.
- The slowdown in the Wine & Spirits division should not be extrapolated to European spirits groups. Rémy Cointreau is set to publish its Q2 2016/17 sales on 18th October and should see a return to growth driven by its Cognac division. We expect total sales to rise 3.3% (+5% for Rémy Martin), accelerating vs Q1 (flat), which had been impacted by destocking. The performance by Pernod Ricard which is due to release its Q1 2016/17 sales on 20th October should also improve in China thanks to easy comps (-9% in Q1 2015/16) but is expected to remain in negative territory (an estimated -5%).

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# 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 56.5% NEUTRAL ratings 31.8% SELL ratings 11.7%

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