20th October 2016

Business Services

Edenred

Price EUR21.77

CMD feedback: Sustainable growth with "Fast Forward" but less predictable cash return

Fair Value EUR22 (+1%) **NEUTRAL**

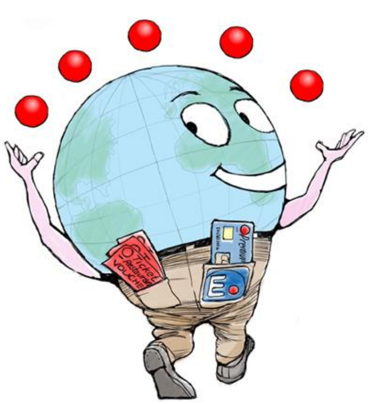
Bloomberg	EDEN FP
Reuters	EDEN.PA
12-month High / Low (EUR)	21.8 / 13.9
Market Cap (EUR)	5,089
Ev (BG Estimates) (EUR)	5,954
Avg. 6m daily volume (000)	741.9
3y EPS CAGR	11.3%

	1 M	3 M	6 M	31/12/15
Absolute perf.	7.0%	10.4%	15.3%	24.8%
Travel&Leisure	-4.1%	-2.2%	-9.2%	-17.4%
DJ Stoxx 600	0.7%	1.9%	-1.6%	-6.1%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	1,069	1,129	1,242	1,317
% change		*5.6%*	*10.1%*	*6.0%*
EBITDA	388	421	488	527
EBIT	341.0	372.5	433.8	470.2
% change		*9.2%*	*16.5%*	*8.4%*
Net income	206.0	220.4	256.9	280.6
% change		*7.0%*	*16.5%*	*9.2%*

	2015	2016e	2017e	2018e
Operating margin	31.9	33.0	34.9	35.7
Net margin	16.6	18.0	20.2	20.8
ROE	-12.2	-11.5	-13.6	-14.8
ROCE	-44.8	-44.2	-46.6	-49.3
Gearing	NM	NM	NM	NM

(EUR)	2015	2016e	2017e	2018e
EPS	0.87	0.94	1.10	1.20
% change	-	*8.4%*	*16.5%*	*9.2%*
P/E	25.0x	23.1x	19.8x	18.1x
FCF yield (%)	5.7%	8.3%	10.0%	8.9%
Dividends (EUR)	0.84	0.84	0.86	0.94
Div yield (%)	3.9%	3.9%	3.9%	4.3%
EV/Sales	5.4x	5.3x	4.8x	4.5x
EV/EBITDA	14.8x	14.1x	12.2x	11.2x
EV/EBIT	16.8x	16.0x	13.7x	12.6x



The 2016-2019 "Fast Forward" strategic plan has put in place actions to pursue the acceleration of the group's transformation. Under a new simplified organisation and capitalising on Edenred's expertise, the plan is to leverage growth opportunities resulting from higher digitalisation of Employee benefit, to become a leader in Expense management and develop solutions for new B2B transactional ecosystems such as Corporate payments. On financials, new metrics better reflect the product mix on a consolidated base with at least 7% lfl operating revenue growth, 9% lfl operating EBIT growth and above 10% lfl FFO growth to maintain a strong investment grade rating. The main changes concern capital allocation with a new objective for cash, which should be returned to shareholders to preserve the group's financial flexibility to seize growth opportunities. In fact, dividends will be based on a P/O ratio of at least 80% of reported net profit (less predictable) vs. a dividend based on at least 90% of net current profit previously.

ANALYSIS

- **Leveraging growth opportunities in Employee benefits from increased digitalisation:** Management confirmed that the business representing 79% of Issue Volume in 2015 but less than 70% by 2020, should continue to deliver mid-single digit lfl revenue growth. In fact, the market is still underpenetrated and digitalisation (digital solutions will move to over 80% of IV vs. 60% today) should provide new solutions and opportunities notably to further penetrate SMEs.
- **Increase Expense Management contribution…:** Expense Management is the second engine for the group and the aim is still to become a global leader. In Latam, the group now has solid positions notably in Brazil after the acquisition of Embratec in 2016 or in Mexico. In Europe, with the acquisition of a 34% srake in Germany-based UTA in 2015, the group entered the fuel card market. The target is to generate double digit growth with a contribution of over 25%.
- **…and leverage technological expertise in particular Corporate Payments:** With PrePay Solutions (PPS), the jointly-owned subsidiary with MasterCard, Edenred operates payment systems using virtual card technology in the hotel industry and in the e-commerce segment. During the CMD, the group announced that it had won a major tender to set up and manage a global prepaid private network in the travel industry. The contract will be signed in early 2017 and will represent a transaction volume of over USD20bn.
- **Cash returns to shareholders less predictable than before but the right decision to preserve growth opportunities:** Cash flow allocation is the main change decided by management on financials. In fact, after the takeover of 65% of **Embratec** equity capital and the group's decision to exercise its call option as of 2017 on an additional 17% in **UTA** (cash out of EUR70m plus UTA net debt which should be consolidated on Edenred balance sheet), a strong investment grade rating will be maintained (at least BBB vs. BBB+,) but with no further room for growth opportunities. As such, management's decision to rebase the dividend on reported net earnings rather than net current earnings is a way of preserving flexibility for growth opportunities but definitely reduces visibility on cash that could be returned to shareholders.

VALUATION

- At the current share price, the stock is trading at 16x EV/EBIT 2016e and 13.7x 2017e which compares with a 2015-2018 CAGR in EBIT of 11.3%.
- For dividends, we have reduced our estimate, anticipating that at the best the group would maintain the same level as last year, representing a payout ratio of 97% of net profit (vs. 108% in 2015 on the same metric and 115% in 2014). For 2017e, using a payout ratio of 80%, dividend per share moves to EUR0.86.

NEXT CATALYSTS

- FY results on 23rd February 2017

Analyst :
Bruno de La Rochebrochard
33(0) 1 56 68 75 88
bdelarochebrochard@bryangarnier.com

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London
Beaufort House
15 St. Botolph Street
London EC3A 7BB
Tel: +44 (0) 207 332 2500
Fax: +44 (0) 207 332 2559
Authorised and regulated by the
Financial Conduct Authority (FCA)

Paris
26 Avenue des Champs Elysées
75008 Paris
Tel: +33 (0) 1 56 68 75 00
Fax: +33 (0) 1 56 68 75 01
Regulated by the
Financial Conduct Authority (FCA) and the
Autorité de Contrôle prudential et de
resolution (ACPR)

New York
750 Lexington Avenue
New York, NY 10022
Tel: +1 (0) 212 337 7000
Fax: +1 (0) 212 337 7002
FINRA and SIPC member

Munich
Widenmayerstrasse 29
80538 Munich
Germany
+49 89 2422 62 11

New Delhi
The Imperial Hotel Janpath
New Delhi 110 001
Tel +91 11 4132 6062
+91 98 1111 5119
Fax +91 11 2621 9062

Geneva
rue de Grenus 7
CP 2113
Genève 1, CH 1211
Tel +4122 731 3263
Fax+4122731 3243
Regulated by the FINMA

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