

Sodexo

Price EUR98.81

First take FY results: Disappointing top line growth but operating in line. New share buyback. Short term challenging.

Fair Value EUR92 (-7%)

NEUTRAL

| | |
|----------------------------|--------------|
| Bloomberg | SW FP |
| Reuters | EXHO.PA |
| 12-month High / Low (EUR) | 107.7 / 79.9 |
| Market Cap (EUR) | 15,191 |
| Ev (BG Estimates) (EUR) | 15,916 |
| Avg. 6m daily volume (000) | 199.7 |
| 3y EPS CAGR | 7.4% |

| | 1 M | 3 M | 6 M | 31/12/15 |
|----------------|-------|-------|-------|----------|
| Absolute perf. | -4.1% | -5.5% | 10.3% | 9.6% |
| Travel&Leisure | 2.4% | -2.5% | -6.2% | -16.8% |
| DJ Stoxx 600 | -0.4% | -1.4% | 1.1% | -7.5% |

| YEnd Aug. (EURm) | 08/15 | 08/16e | 08/17e | 08/18e |
|------------------|--------|--------|--------|--------|
| Sales | 19,815 | 20,386 | 21,481 | 22,305 |
| % change | | 2.9% | 5.4% | 3.8% |
| EBITDA | 1,396 | 1,470 | 1,589 | 1,685 |
| EBIT | 1,143 | 1,205 | 1,309 | 1,396 |
| % change | | 5.5% | 8.6% | 6.6% |
| Net income | 700.0 | 707.6 | 776.0 | 850.6 |
| % change | | 1.1% | 9.7% | 9.6% |

| | 08/15 | 08/16e | 08/17e | 08/18e |
|------------------|-------|--------|--------|--------|
| Operating margin | 5.8 | 5.9 | 6.1 | 6.3 |
| Net margin | 3.5 | 3.5 | 3.6 | 3.8 |
| ROE | 19.5 | 23.3 | 18.4 | 19.1 |
| ROCE | 28.6 | 29.6 | 31.7 | 33.0 |
| Gearing | 10.2 | 23.0 | -5.9 | -11.2 |

| (EUR) | 08/15 | 08/16e | 08/17e | 08/18e |
|-----------------|-------|--------|--------|--------|
| EPS | 4.60 | 4.75 | 5.21 | 5.71 |
| % change | - | 3.2% | 9.7% | 9.6% |
| P/E | 21.5x | 20.8x | 19.0x | 17.3x |
| FCF yield (%) | 4.5% | 4.2% | 4.8% | 5.8% |
| Dividends (EUR) | 2.20 | 2.37 | 2.60 | 2.85 |
| Div yield (%) | 2.2% | 2.4% | 2.6% | 2.9% |
| EV/Sales | 0.8x | 0.8x | 0.7x | 0.7x |
| EV/EBITDA | 11.2x | 10.8x | 9.4x | 8.7x |
| EV/EBIT | 13.6x | 13.2x | 11.4x | 10.5x |

Top line growth disappointed with organic growth at 2.5% vs around 3% guidance and expected by consensus i.e. broadly flat in Q4 alone. Nevertheless, underlying operating result was in line representing an operating margin of 5.9%, up 30bps a reflecting positive impact from the Adaptation and Simplification programme. With a still comfortable balance sheet and cash flow generation, management will propose a new share buyback programme of EUR300m. The short-term outlook remains challenging but management is confident it can generate 3% organic revenue growth and 8-9% growth in underlying operating result. Medium term guidance confirmed (organic revenue growth between 4% and 7% with growth in underlying operating result of 8-10%. Neutral opinion confirmed.

ANALYSIS

- **Disappointing top line growth:** With FY revenue of EUR20,245m up 2.2% in reported terms with organic growth of 2.5%, this is definitely lower than management's guidance for organic growth of around 3% provided after 9m revenue in early July (the consensus was at 3% with consolidated revenue of EUR20,386m). This result implies a significant slowdown in Q4 with organic growth of -0.1% after 2.6% in Q3 and Q2 after 4.7% in Q1 with a positive impact from RWC (positive impact of 0.6% on FY growth). By business, FY organic growth for the **OSS** reached 2.4% i.e. down 0.2% in Q4 alone and up 4.7% in **Benefits & Rewards Services** i.e.1.4% in Q4.
- **An adaptation and simplification programme that delivers results:** In fact, despite lower revenue growth, underlying operating result amounted to EUR1,203m up 8.2% in line with expectations (consensus at EUR1,193m and BG at EUR1,206m) representing an operating margin of 5.9% up 30bps. In fact, the Adaptation and Simplification plan is paying off having delivered EUR32m in savings in its first year. Note that the plan is being implemented over the period from September 2015 to February 2017 at a total cost of EUR200m with 100% annual payback in FY2018.
- **Strong cash flow generation:** Despite the share buyback programme of EUR300m announced last year and completed at the end of 9m 2016 and investments, the group's financial leverage is broadly stable at 0.3x (0.2x in 2015). As such, management will propose a new share buyback programme of EUR300m.
- **Outlook challenging especially in H1:** Following the disappointing Q4 and comps, H1 2016-17 is set to be challenging. Nevertheless, management is guiding for organic growth of around 3% for FY (BG at 3.3% as consensus). Regarding underlying operating profit, growth is expected between 8% to 9% i.e. around EUR1.300m (BG at EUR1,297m and consensus at EUR1,285m).

VALUATION

- At the current share price, the stock is trading on 2017e and 2018e EV/EBIT multiples of 11.4x and 10.5x compared with a median historical level of 10.9x and 2016-18 CAGR of EBIT of 7.6%. 2017e and 2018e EPS capitalise at respectively 19x and 17.3x compared with 2016-18 CAGR of EPS of 9.6%.
- Having announced that the share buyback programme launched in November 2015 for EUR300m was completed in Q3 2016, management will propose a new one of the same amount of EUR300m (1.9% on current market capitalisation) for cancellation purposes. With financial leverage of 0.3x and debt coverage of 2.5years, the group would have room to return more cash.

NEXT CATALYSTS

- Conference call at 9.00am (Paris time)
- Q1 2016-17 revenue on 12th January 2017

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Analyst :

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

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| | |
|---------|---|
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|-----------------------------------|---|--------------------------|----------------------|----------------------------|
| Beaufort House | 26 Avenue des Champs Elysées | 750 Lexington Avenue | Widenmayerstrasse 29 | The Imperial Hotel Janpath |
| 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 |
| Fax: +44 (0) 207 332 2559 | Regulated by the | FINRA and SIPC member | | Fax +91 11 2621 9062 |
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| | resolution (ACPR) | | | CP 2113 |
| | | | | Genève 1, CH 1211 |
| | | | | Tel +4122 731 3263 |
| | | | | Fax+4122731 3243 |
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