

Valeo

Price EUR52.38

A deal that makes sense

Fair Value EUR49 (-6%)

NEUTRAL

Bloomberg	FR FP
Reuters	VLOF.PA
12-month High / Low (EUR)	54.4 / 34.9
Market Cap (EURm)	12,526
Ev (BG Estimates) (EURm)	14,609
Avg. 6m daily volume (000)	788.1
3y EPS CAGR	14.6%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-2.4%	14.1%	19.1%	-62.7%
Auto & Parts	1.1%	4.1%	6.5%	-11.7%
DJ Stoxx 600	-1.2%	0.0%	0.7%	-7.0%

YEnd Dec. (EURm)	2015	2016e	2017e	2018e
Sales	14,544	16,372	17,942	19,045
% change		12.6%	9.6%	6.2%
EBITDA	1,847	2,071	2,364	2,523
EBIT	1,060	1,260	1,421	1,532
% change		18.8%	12.8%	7.8%
Net income	729.0	880.4	1,011	1,102
% change		20.8%	14.9%	8.9%

	2015	2016e	2017e	2018e
Operating margin	7.3	7.7	7.9	8.0
Net margin	5.0	5.4	5.6	5.8
ROE	21.0	21.7	21.3	20.1
ROCE	23.7	20.1	21.0	21.2
Gearing	0.5	27.0	17.4	8.6

(EUR)	2015	2016e	2017e	2018e
EPS	3.11	3.74	4.29	4.68
% change	-	20.1%	14.9%	8.9%
P/E	16.8x	14.0x	12.2x	11.2x
FCF yield (%)	4.4%	4.0%	4.3%	5.2%
Dividends (EUR)	1.00	1.12	1.29	1.40
Div yield (%)	1.9%	2.1%	2.5%	2.7%
EV/Sales	0.9x	0.9x	0.8x	0.7x
EV/EBITDA	7.3x	7.1x	6.0x	5.5x
EV/EBIT	12.7x	11.6x	10.1x	9.1x

Yesterday morning the group unveiled it had launched a takeover bid for the shares of Ichikoh, the Japanese automotive lighting specialist, to raise its current 31.58% stake to a maximum of 55.08%. The group believes it can restructure the entity as it did with Sylvania, by progressively improving industrial efficiency and gross margin to the profit of EBIT margin. Dilutive on Valeo's margin in the short term, this deal therefore makes sense in our view yet could be a risky challenge assuming margin improvement takes longer than anticipated, putting at risk the group's 2020 EBIT margin target (8-9%). Positive.

ANALYSIS

- A deal that makes sense?** Valeo currently holds **31.58%** of the capital of Ichikoh, a Japanese automotive lighting specialist and aims to increase its stake to at least **50.09%** and to a maximum of **55.08%** (in order to maintain the liquidity of the Ichikoh share which will continue to be listed on the Tokyo Stock Exchange), to get control of this Japanese group. With an offer at **JPY408/sh**, Valeo is offering a **25% premium to Ichikoh's shareholders**, valuing the Japanese automotive supplier at around **EUR340m (market cap)**. Based on 2017 net debt estimates, and on Valeo's price offer, this deal values Ichikoh at **44% its N+1 sales** and at **18x its N+1 EBIT (and at 9x its N+2 EBIT)**. Getting control of a well-known industrial partner is not new for Valeo which made a similar deal in 2014 with the purchasing of a **50% stake in Sylvania (back then the group already owned 50% of the entity)**. Valeo's good track record in this type of operation combined with the low impact on group's net debt (*less than EUR200m, or 15% of Valeo BG estimated net debt*) makes this deal credible in our view. By acquiring Ichikoh Valeo it will then reinforce its presence in Japan, (*7% of group's sales*) with Japanese carmakers.
- Dilutive margin impact in the short term:** This deal will however have a **20-30bp negative impact** on Valeo's EBIT margin in the short term (2017) as Ichikoh is at this stage still generating poor operating margin (2-3%), far from Valeo's margin on the lighting business (7-8%). To progressively improve Ichikoh's gross margin and EBIT margin (*close to the groups' lighting business profitability*), Valeo and Ichikoh will be leveraging **1/sales synergies** that could develop out of a worldwide product offering (*by notably raising the share of LED within Ichikoh product mix*), will **2/optimize manufacturing footprint**, will generate **3/R&D synergies** as well as **4/purchasing synergies**, in particular for electronics, which represent a growing proportion of the value of innovative lighting products, and **5/administrative synergies**. We estimated the integration of Ichikoh (*not before February 2017*) could have an accretive impact on group's EPS close to **1%** while raising group's sales by around **5%**.
- This deal therefore makes sense in our view yet could be a risky challenge assuming margin improvement takes longer than anticipated, putting at risk the group's 2020 EBIT margin target (8-9%).**
- At this stage we still do not integrate this deal into our model:** As this transaction is still subject to approval by the relevant anti-trust authorities and as the takeover bid will run until 12th January 2017, we have decided not to integrate it into our model yet.

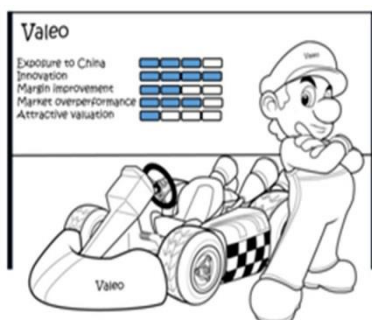
VALUATION

- At the current share price the stock is trading at **10x** its 2017e EBITDA and at **12.2x** its 2017e EPS
- Neutral, FV @ EUR49/sh**

NEXT CATALYSTS

- 30th November** - Lunch with IR @ Bryan Garnier Paris
- 16th February** - 2016 results

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