INDEPENDENT RESEARCH UPDATE

14th December 2016

TMT

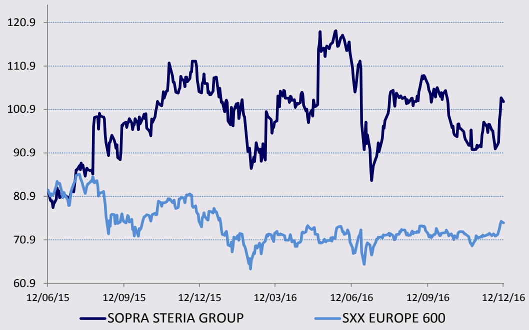
Sopra Steria Group

Don't be afraid of the United Kingdom

Fair Value EUR125 (price EUR101.70) **BUY**

Bloomberg	SOP FP
Reuters	SOPR.PA
12-month High / Low (EUR)	119.0 / 84.5
Market capitalisation (EURm)	2,083
Enterprise Value (BG estimates EURm)	2,663
Avg. 6m daily volume ('000 shares)	28.60
Free Float	66.8%
3y EPS CAGR	15.2%
Gearing (12/15)	43%
Dividend yield (12/16e)	1.87%

YE December	12/15	12/16e	12/17e	12/18e
Revenue (€m)	3,584	3,743	3,861	4,042
EBITA €m)	245.5	288.7	328.5	359.7
Op.Margin (%)	6.8	7.7	8.5	8.9
Diluted EPS (€)	7.39	8.78	10.21	11.29
EV/Sales	0.7x	0.7x	0.7x	0.6x
EV/EBITDA	8.6x	7.9x	6.7x	5.8x
EV/EBITA	10.6x	9.2x	7.8x	6.6x
P/E	13.8x	11.6x	10.0x	9.0x
ROCE	11.0	11.4	12.8	14.0



We reiterate our Buy recommendation and our DCF-derived fair value of EUR125, leaving upside potential of 23%. While the shares have suffered from the company's exposure to the United Kingdom, we expect Sopra Steria to benefit from: 1) an improvement in organic growth; 2) over-estimated 'Brexit' risks; 3) capacity for future acquisitions; and 4) an attractive valuation.

- **Improving trends**. While the cost synergies linked to the acquisition of Steria are mostly behind us, in our view Sopra Steria's investment appeal now resides in its ability to maintain above-market growth. Whereas consulting and systems integration, banking software and the other solutions are driving growth, Germany and infrastructure services in France and the United Kingdom are seeing an improvement.

- **Risks over-estimated in the United Kingdom**. We expect Brexit to have limited impact on Sopra Steria in the United Kingdom since 78% of sales there are recurring and 68% is generated with the government. We expect flat sales given stable government activity, a return to growth in banking and the business reconstruction under way in the rest of the commercial sector. Lastly, rising interest rates point to an eventual stablisation, or even decline, in the pension fund liabilities.

- **Significant capacity to reduce debt to finance acquisitions.** On our numbers, with the achievement of the synergies linked to Steria, free cash flow should reach an annual EUR150m by 2018, enabling Sopra Steria to reduce its gearing to zero by 2020. We have no concerns about the financing of future acquisitions (up to EUR100-150m per year), with EUR1bn of undrawn credit lines.

- **An attractive valuation**. Despite our projected EPS CAGR of 15% for 2015-18e, the shares are trading at EV/EBIT multiples of 9.2x 2016e and 7.8x 2017e, i.e. a 10% discount relative to the IT Services average in Europe.

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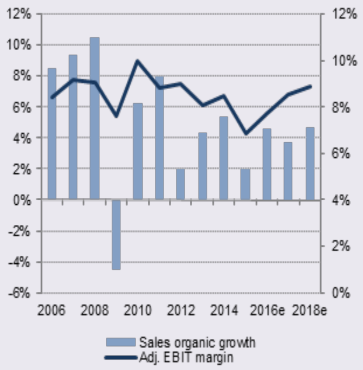
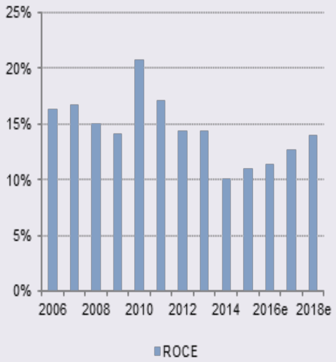




Company description

Founded in 1968, and listed on Euronext Paris since 1990, Sopra Steria is an IT Services group employing more than 38,000 staff. The group generates 57% of its revenues in Consulting & Systems Integration, 15% in Business Process Services, 14% in Infrastructure Management, and 14% in Solutions (Sopra Banking Software 8%, Sopra HR Software 4%, Real Estate Solutions 2%). France accounts for 46% of group sales, followed by the UK (29%), the rest of Europe (23%) and the rest of the World (2%). Government is the largest contributor to Sopra Steria's revenues (25%), followed by Banking (21%), Aerospace/Defence/Homeland Security (16%), Energy/Utilities (8%), Telecom/Media (6%), Insurance (5%), Transport (5%) and Distribution (3%).

Simplified Profit & Loss Account (EURm)	**2013**	**2014**	**2015**	**2016e**	**2017e**	**2018e**	**2019e**
Revenues	1,349	2,280	3,584	3,743	3,861	4,042	4,248
Change (%)	*10.9%*	*69.0%*	*57.2%*	*4.4%*	*3.2%*	*4.7%*	*5.1%*
Ifl change (%)	*4.3%*	*5.4%*	*2.0%*	*4.6%*	*3.7%*	*4.7%*	*5.1%*
Adjusted EBITDA	130	220	304	339	380	411	443
Depreciation & amortisation	(21.3)	(27.0)	(58.4)	(50.1)	(51.1)	(51.1)	(51.1)
Adjusted EBIT	109	193	246	289	328	360	392
EBIT	104	148	153	238	280	310	341
Change (%)	*13.9%*	*42.6%*	*3.0%*	*56.3%*	*17.3%*	*10.9%*	*10.0%*
Financial results	(8.4)	(18.1)	(23.0)	(22.1)	(19.9)	(17.9)	(17.4)
Pre-Tax profits	95.5	130	130	216	260	292	324
Exceptionals	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Tax	(32.5)	(34.4)	(47.2)	(77.9)	(91.7)	(102)	(113)
Profits from associates	8.4	5.8	7.2	9.8	12.1	13.9	16.0
Minority interests	0.01	3.3	5.2	1.3	3.0	5.0	5.0
Net profit	71.4	98.2	84.4	147	177	199	221
Restated net profit	74.9	130	151	180	210	232	255
Change (%)	*10.1%*	*73.7%*	*16.1%*	*19.3%*	*16.4%*	*10.6%*	*10.0%*
Cash Flow Statement (EURm)							
Operating cash flows	56.8	118	174	226	241	261	281
Change in working capital	(1.7)	14.8	(81.9)	(79.8)	(41.1)	(11.3)	(23.7)
Capex, net	(16.9)	(26.2)	(42.3)	(46.9)	(49.0)	(51.0)	(53.0)
Financial investments, net	0.98	(4.3)	1.9	(36.5)	2.2	2.2	2.2
Acquisitions, net	41.1	(134)	(92.3)	(105)	0.0	0.0	0.0
Dividends	(20.2)	(22.5)	(37.5)	(34.8)	(38.9)	(43.0)	(47.1)
Other	(22.8)	(57.0)	120	96.1	22.9	20.3	18.7
Net debt	155	442	531	580	463	301	138
Free Cash flow	38.3	106	49.4	99.7	151	198	205
Balance Sheet (EURm)							
Tangible fixed assets	49.2	110	119	120	122	126	132
Intangibles assets & goodwill	372	1,695	1,801	1,812	1,787	1,762	1,737
Investments	124	230	245	311	321	333	347
Deferred tax assets	25.6	155	143	163	163	163	163
Current assets	506	1,098	1,291	1,357	1,390	1,444	1,517
Cash & equivalents	102	222	223	174	291	453	615
Total assets	1,179	3,510	3,821	3,937	4,074	4,281	4,512
Shareholders' equity	358	1,087	1,233	1,208	1,348	1,506	1,680
Provisions	71.1	528	444	599	605	611	618
Deferred tax liabilities	2.1	8.1	15.8	15.8	15.8	15.8	15.8
L & ST Debt	257	665	754	754	754	754	754
Current liabilities	490	1,222	1,375	1,361	1,352	1,395	1,445
Total Liabilities	1,178	3,510	3,821	3,937	4,074	4,281	4,512
Capital employed	512	1,529	1,764	1,788	1,810	1,806	1,818
Ratios							
Operating margin	8.07	8.46	6.85	7.71	8.51	8.90	9.22
Tax rate	34.07	26.44	36.42	36.00	35.30	35.00	35.00
Net margin	5.29	4.31	2.35	3.93	4.59	4.92	5.21
ROE (after tax)	19.95	9.04	6.84	12.17	13.15	13.21	13.18
ROCE (after tax)	14.37	10.14	10.97	11.43	12.75	13.95	15.01
Gearing	43.19	40.71	43.05	48.00	34.32	19.97	8.23
Pay out ratio	31.65	37.87	41.10	26.49	24.27	23.69	21.27
Number of shares, diluted	11.96	19.65	20.45	20.52	20.53	20.53	20.53
Data per Share (EUR)							
EPS	6.00	5.02	4.14	7.17	8.65	9.71	10.81
Restated EPS	6.26	6.62	7.39	8.78	10.21	11.29	12.41
% change	*9.9%*	*5.7%*	*11.6%*	*18.8%*	*16.3%*	*10.6%*	*10.0%*
EPS bef. GDW	6.26	6.62	7.39	8.78	10.21	11.29	12.41
BVPS	29.92	55.30	60.31	58.87	65.64	73.33	81.82
Operating cash flows	4.75	5.99	8.49	11.03	11.74	12.70	13.71
FCF	3.20	5.41	2.42	4.86	7.35	9.66	9.97
Net dividend	1.90	1.90	1.70	1.90	2.10	2.30	2.30

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

1. Clearly undervalued

1.1. DCF model: EUR125 per share

Our DCF-derived fair value of EUR125 factors in an adjusted EBIT margin of 9% over the medium term.

Fig. 1: DCF assumptions

Risk-free interest rate	1,6%
Equity risk premium	7,0%
Beta	1,58
Return expected on equity	12,6%
Stock price (EUR)	101,7
Number of shares (m)	20,49
Market Capitalisation (EURm)	2 083
Net debt on 31/12/2016e (EURm)	580
Entreprise value (EURm)	2 663
Interest rate on debt	2,0%
Tax rate	35,0%
Sales growth rate to perpetuity	2,5%
WACC	10,3%

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

Fig. 2: Discounted FCF

in EURm (FYE 31/12)	2015	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e	2026e
Sales	3 584	3 743	3 861	4 042	4 244	4 457	4 679	4 913	5 159	5 417	5 688	5 972
% chg	57,2%	4,4%	3,2%	4,7%	5,0%	5,0%	5,0%	5,0%	5,0%	5,0%	5,0%	5,0%
Operating profit	246	289	328	360	382	401	421	442	464	488	512	538
as a % of sales	6,8%	7,7%	8,5%	8,9%	9,0%	9,0%	9,0%	9,0%	9,0%	9,0%	9,0%	9,0%
Theoretical tax rate	36,4%	36,0%	35,3%	35,0%	35,0%	35,0%	35,0%	35,0%	35,0%	35,0%	35,0%	35,0%
Theoretical tax	89	104	116	126	134	140	147	155	163	171	179	188
NOPAT	156	185	213	234	248	261	274	287	302	317	333	349
Depreciation	58	50	51	51	51	53	56	59	62	65	68	72
as a % of sales	1,6%	1,3%	1,3%	1,3%	1,2%	1,2%	1,2%	1,2%	1,2%	1,2%	1,2%	1,2%
Capex	43	47	49	51	51	53	56	59	62	65	68	72
as a % of sales	1,2%	1,3%	1,3%	1,3%	1,2%	1,2%	1,2%	1,2%	1,2%	1,2%	1,2%	1,2%
WCR	-83,4	-3,6	37,5	48,8	-21,2	-22,3	-23,4	-24,6	-25,8	-27,1	-28,4	-29,9
as a % of sales	-2,3%	-0,1%	1,0%	1,2%	-0,5%	-0,5%	-0,5%	-0,5%	-0,5%	-0,5%	-0,5%	-0,5%
Change in WCR	82	80	41	11	-70	-1	-1	-1	-1	-1	-1	-1
Free cash flows	90	108	174	223	318	262	275	289	303	318	334	351
Discounted free cash flows	90	108	157	183	237	177	168	160	152	145	138	131
Sum of discounted FCF	1 626											
Terminal value	1 683											
Enterprise value	3 309											
Fair value of associates	164											
Fair value of financial assets	147											
Provisions	599											
Fair value minority interests	40											
NPV of tax credits	163											
Dilution (s/o, warrants, conv bds)	5											
Net debt on 31/12/2016e	580											
Equity value	2 569											
Diluted nbr of shares (m)	20,53											
Valuation per share (EUR)	125											

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

Our DCF-derived valuation of EUR125, i.e. 23% above the current share price, is based on a risk-free rate of 1.6%, an equity risk premium of 7% and a beta of 1.58.

Fig. 3: Sensitivity analysis - EBIT margin and WACC (EUR)

		EBIT margin				
	122	**7.0%**	**8.0%**	**9.0%**	**10.0%**	**11.0%**
WACC	**9.5%**	110	127	144	162	179
	10.0%	100	116	132	148	164
	10.3%	95	110	**125**	140	156
	11.0%	85	98	112	126	139
	11.5%	78	91	104	116	129

Source: Bryan, Garnier & Co. ests.

1.2. Analysis of the share price performance

An excellent share price performance since mid-2012 but marked underperformance over one year given the concerns linked to Brexit, the decline in long-term bond yields, the US Presidential elections and the slowing momenentum for Indian IT Services companies.

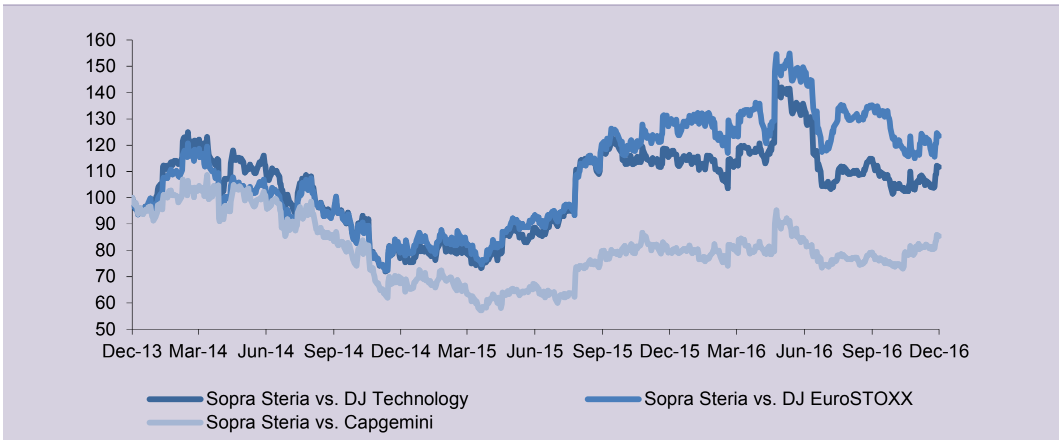
In view of the uncertainties linked to Brexit, the Sopra Steria share price has decreased by 2% over the past year, outperforming relative to Capgemini (-9%) but underperforming relative to Atos (+26%), Accenture (+22% in euros), Tieto (+10%), and Indra (+9%). Over six months, the decline has been 10%, compared with +22% for Atos, +11% in euros for Accenture, +5% for Tieto, +3% for Indra, and -11% for Capgemini. **Sopra Steria's share price performance has effectively been more correlated with that of its Indian peers than its European comparables** (over the last six months TCS, Infosys, Cognizant and Wipro have witnessed respective falls, in euros, of 9%, 13%, 1% and 12% due to their growth deceleration since the Q1 2016). And yet, unlike its Indian peers, Sopra Steria is not exposed to the risk of a restriction in the number of H-1B work visas for the United States, which could negatively impact their margins.

Sopra Steria shares have delivered a very strong performance, albeit volatile, from their low of EUR34.3 on 15/07/2012 (+200%), following a slowdown in organic growth and the spin-off of Axway in early June 2011. From this low point, the share price had rebounded by 87% to reach EUR64 on 01/03/2013 before experiencing a 15% correction to EUR54.1 on 14/06/2013 on the back of a sharp downwards revision to the operating margin guidance following the acquisition of the then-loss-making HR Access. The shares subsequently made steady progress (+47%) through to 26/02/2014 (EUR94.5) with a 2013 operating margin comfortably higher than the guidance (8.1% vs. 7.3%-7.7%) thanks to a spectacular turnaround at HR Access. The shares then collapsed by 41% to EUR56 on 14/11/2014 on investor concerns regarding the Steria integration and the credibility of the targets set for 2017 (sales of EUR3.8bn-EUR4bn and an operating margin of 9%-10% with operating synergies of EUR62m for a EUR65m cost of synergies).

Since mid-November 2014, the shares have rebounded by 100%, reaching EUR112 on 3/12/2015, thanks to 2014 results ahead of expectations (pro forma operating margin with 12 months of Steria at 6.9% vs. the consensus at 6.5%) and an upwards revision in the 2015 operating margin guidance to 6.5% vs. 6% - this despite the reduction on 19/03/2015 of the 2017 operating margin target to 8%-9% (vs. 9%-10%, given salary increases, additional costs in the joint-ventures with the UK government and the acceleration in Sopra Banking Software investment). They then fell back by 21% to EUR89 on 24/02/2016 on the back of a sales warning from Cognizant, marking the beginning of a deceleration in growth momentum for the Indian IT services companies. The shares then recovered by 33% to EUR118.8 as of 5/05/2016 given an above-guidance 2015 operating margin (6.8% vs. 6.5%) thanks to cost synergies with Steria ahead of schedule (EUR45m at end 2015 vs. guidance of

EUR35m), and an upwards revision to the guidance on 2016 organic growth (3%-5% vs. 2%) before declining by 29% to EUR84.5 on 6/07/2016 on the back of concerns linked to Brexit and declining long-term bond yields – with negative repercussions for the pension deficit. After a rally in July 2016, the shares were to gain 29% to EUR108.65 on 5/09/2016 before once more experiencing a correction on uncertainties linked to the US Presidential election which proved particularly negative for the Indian IT Services companies, the election of Donald Trump raising the risk of additional restrictions on the admission of qualified workers to the United States.

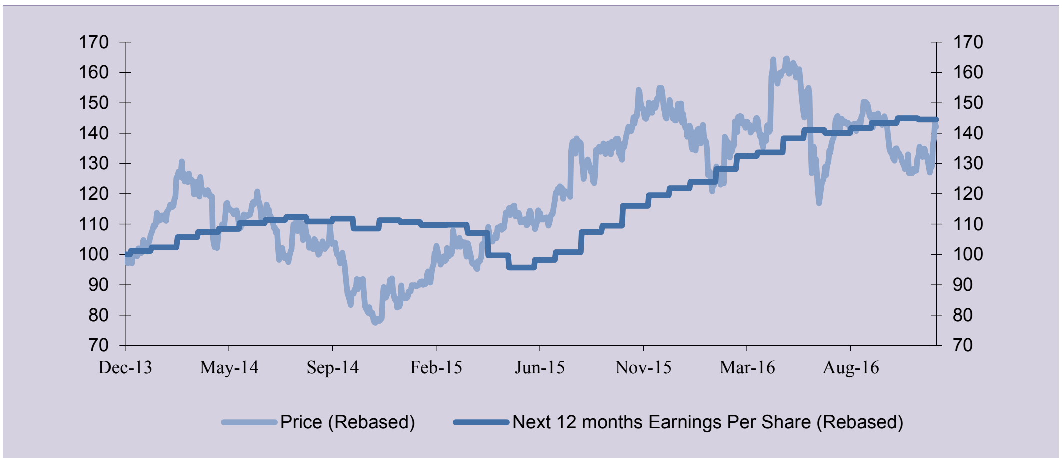
Fig. 4: Sopra Steria vs. DJ Technology, DJ EuroSTOXX and Capgemini



Source: Thomson Reuters.

Furthermore, in our view, Sopra Steria's share price variations have not reflected the growth dynamic in the consensus on EPS. As seen in Fig. 5, over the last three years the share price has increased by 42% whereas the consensus on 12-month forward EPS has moved up by 45% over the period. This positive revision momentum for consensus EPS has been seen since the summer of 2015, underpinned by management's new upwards revision to 2015 guidance in August (sales at c. +2% vs. 'positive', operating margin at c. 6.5% vs. c. 6%).

Fig. 5: EPS momentum and share price performance over 3 years (base 100)



Source: Thomson Reuters.

1.3. Peer group comparison

Based on 2016e and 2017e EV/EBIT multiples, Sopra Steria trades at a discount of 10% relative to the leading European IT Services company average, a 35%-45% discount to the US average, and a 20%-30% discount to the Indian average, as seen below:

Fig. 6: Peer group comparison

IT Services	Currency	Rating	Price	Fair	Market cap	PER			EV/sales			EV/EBIT		
			13-Dec-16	value	(m)	2015	2016e	2017e	2015	2016e	2017e	2015	2016e	2017e
Capgemini	EUR	BUY	76,4	95	13 106	16,5	13,7	12,7	1,2	1,2	1,1	11,8	10,1	8,7
Atos	EUR	BUY	95,7	115	10 026	16,4	13,9	11,6	0,9	0,8	0,6	10,3	8,5	6,1
Sopra Steria Group	**EUR**	**BUY**	**101,7**	**125**	**2 083**	**13,8**	**11,6**	**10,0**	**0,7**	**0,7**	**0,6**	**10,6**	**9,2**	**7,8**
Tieto	EUR	Not rated	25,4	N/A	1 882	16,1	16,0	15,0	1,3	1,3	1,2	12,6	12,3	12,3
Indra Sistemas	EUR	BUY	10,0	12	1 642	N/M	22,7	12,8	0,8	0,9	0,8	50,9	15,1	9,2
European average						**16,2**	**13,9**	**12,7**	**0,9**	**0,9**	**0,8**	**11,8**	**10,1**	**8,7**
Sopra Steria vs. Europe						-15%	-17%	-22%	-17%	-17%	-14%	-10%	-8%	-11%
IBM	USD	Not rated	165,4	N/A	160 019	11,3	12,5	12,0	2,3	2,4	2,4	11,4	13,1	13,0
Accenture	USD	Not rated	121,7	N/A	77 787	26,0	23,5	21,1	2,4	2,2	2,1	16,3	15,2	15,1
CGI Group	CAD	Not rated	62,5	N/A	19 880	20,8	18,8	17,4	1,9	1,8	1,7	13,4	12,2	11,6
Computer Sciences	USD	Not rated	61,9	N/A	8 586	24,2	22,0	18,8	1,4	1,3	1,3	23,7	17,4	17,2
US average						**22,5**	**20,4**	**18,1**	**2,1**	**2,0**	**1,9**	**14,9**	**14,1**	**14,9**
Atos vs. US avg						-39%	-43%	-45%	-66%	-64%	-65%	-28%	-35%	-45%
TCS	INR	Not rated	2195,8	N/A	4 335 530	20,1	17,8	23,1	4,4	3,7	5,2	16,4	14,1	14,9
Infosys	INR	Not rated	984,7	N/A	2 263 251	16,8	15,9	14,4	3,1	2,8	2,4	12,4	11,2	10,8
Cognizant	USD	Not rated	56,2	N/A	34 394	18,5	16,7	15,5	2,5	2,2	1,9	12,5	11,3	10,8
Wipro	INR	Not rated	458,6	N/A	1 145 866	12,8	13,3	12,2	2,2	1,8	1,8	12,1	10,8	10,3
Indian average						**17,6**	**16,3**	**14,9**	**2,8**	**2,5**	**2,2**	**12,5**	**11,2**	**10,8**
Atos vs. Indian avg						-22%	-29%	-33%	-74%	-71%	-70%	-15%	-18%	-28%

Source: Thomson Reuters; Bryan, Garnier & Co ests.

2. Returning to the fundamentals

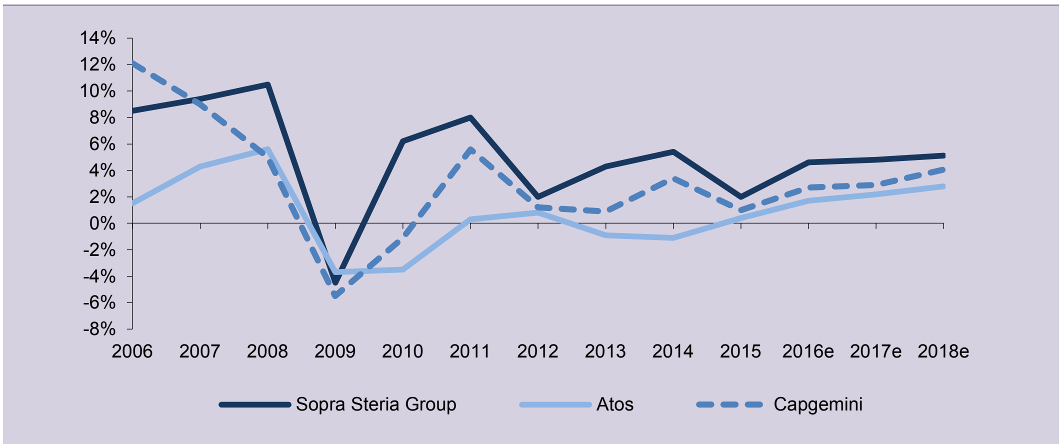
Note that, for 2016, Sopra Steria is expecting like-for-like sales growth of 3%-5% (the management is looking for a figure at the top end of the range), **an operating margin in excess of 7.5% and strong growth in free cash flow** relative to the EUR49m reported for 2015. The consensus on the operating margin is currently 7.8%. Based on the achievement of the EUR62m of cost synergies initially foreseen with Steria (of which EUR45m already realised at the end of 2015), **the management is targeting sales of EUR3.8bn-EUR4bn for 2017 and an operating margin of 8%-9%.**

2.1. Ability to outperform the market growth

Sopra Steria has generated average annual organic growth of 5.2% over the past decade.

In our view, Sopra Steria's investment appeal mainly resides in its ability to deliver sales growth above that of its market. As seen in Fig. 7, Sopra Steria has delivered average annual sales growth (and Sopra prior to 2014) of 5.2% over the past decade, compared with 3.2% for Capgemini and 0.4% for Atos.

Fig. 7: Lfl sales growth for Sopra Steria vs. Capgemini and Atos (2006-2018e)



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

This superior growth relative to the leading competitors is based on five pillars:

1) Historic positioning in applications services (consulting and systems integration, application management), a market that is seeing faster growth than managed services[1] and continues to contribute the bulk of group sales despite the acquisition of Steria (est. 57%, vs. around 80% prior to the Steria acquisition), the latter generating more than 40% of sales in managed services and BPO. We estimate this exposure to applications services at 70%-75% for Capgemini and 27% for Atos.

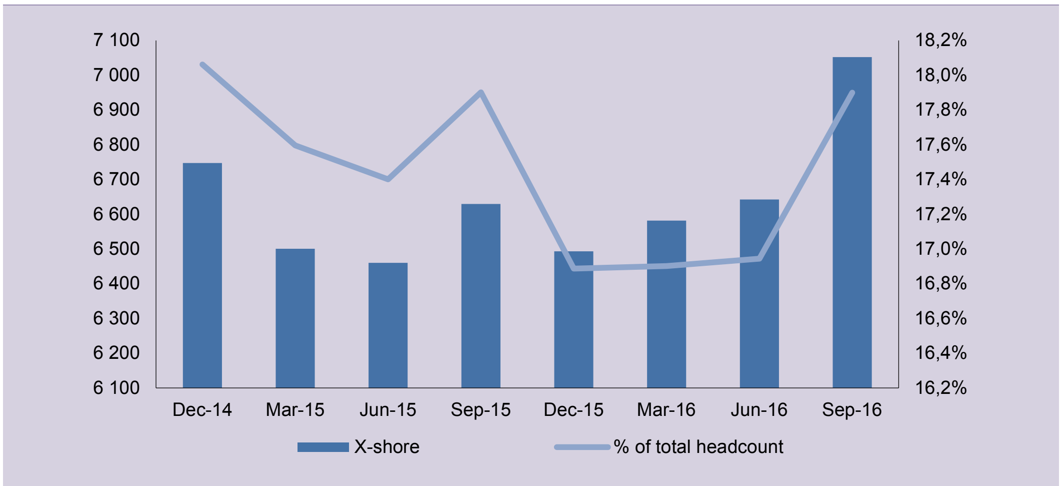
[1] Cross-referencing the data supplied by IDC and Gartner, we estimate that the applications services market (and consulting & systems integration) is currently growing by around 3%-4% per year, whereas managed services (or infrastructure management) is growing by only 0%-1% per year.

This growth is underpinned by historic positioning in applications services, market share gains in systems integration in France, limited exposure to managed services, a competitive model and a value proposition tailored to client needs.

2) Market share gains in consulting and systems integration in France (est. 36% of 2016e sales), thanks to a strategy of focusing on large clients based on a priority vertical market approach (banking, governement, manufacturing, etc.), strong business-specific expertise – for example, a client will work with Sopra Steria given its bank process expertise: payments, loans, etc. - , and a business and technology consulting practice embedded in each vertical. On our estimates, France represents 56% of the group's Consulting & Systems Integration sales. This model, which has hitherto proven its worth in France, is set to be replicated in other countries where Sopra Steria is present – starting with the United Kingdom and Germany.

3) Limited exposure to infrastructure management (14% of sales in 2015, vs. around 50% for Atos and 15%-20% for Capgemini), a market which has been suffering from downwards pressure for several years given the concentration around a few big players (IBM, HPE/CSC, Fujitsu, Atos), the bringing back in-house of some major contracts on their expiry (e.g. Aspire with the HMRC for Capgemini in June 2017), the increasing complexity of calls to tender – often reducing the short list to two bidders prior to the final choice -, and the transition to private and public cloud infrastructures – unfavourable sales mix effect since managed services contracts in cloud mode are generally smaller than those involving traditional infrastructures.

Fig. 8: X-shore (nearshore and offshore) headcount since the end of 2014



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

4) A competitive business model (recourse to nearshore and offshore). Historically, Sopra had prioritised regional operations with services centres and investment in the recruitment and training of young graduates. Sopra had also been a very early adopter of a nearshore model out of Spain and an offshore model as of the acquisition of the UK IT Services company Newell & Budge (2005, 100 people offshore at the time). For its part, Steria had acquired the UK company Xansa in 2007 (the company had more than 5,000 people in India) and invested in nearshore in Poland and Morocco. **At the end of September 2016, more than 7,000 Sopra Steria employees were working in offshore mode, i.e. 18% of the total headcount** (compared with more than 26,000 i.e. 28%, at Atos and nearly 104,000 i.e. 55%, at Capgemini) whereas more than 40% of its sales are generated in France, a country where the offshore lever is progressing but remains low (8% of the market for 2016 according to Syntec Numérique) – whereas France only contributes 20% of sales for Capgemini and 16% for Atos excluding Worldline.

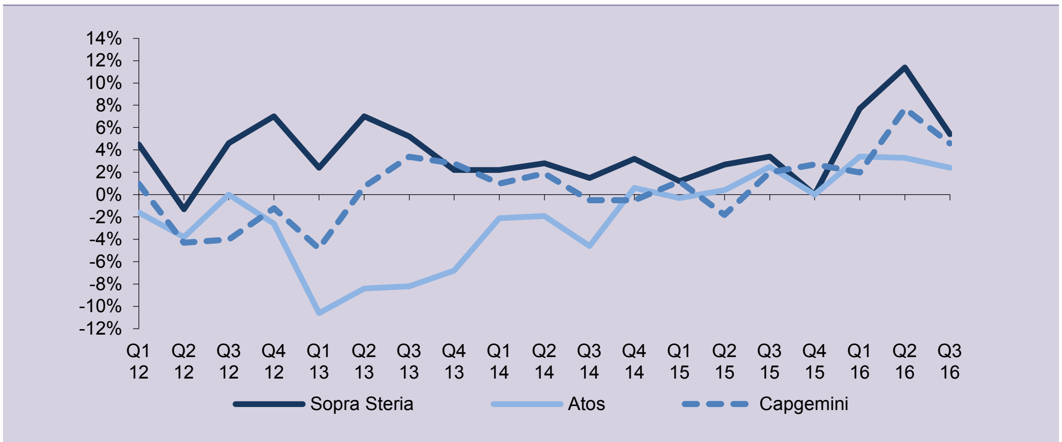
5) A value proposition tailored to client needs. Sopra Steria has long been addressing the digital transformation subject, as evidenced by its client references and technological partnerships. Thus Sopra Steria was recently chosen by Enedis (ex-ERDF) on Big Data to optimise the electricity distribution network in France, by Société Générale to roll out its new security operations centre (SOC) and by the SNCF (French railways) for the digital transformation of its passenger information system for stations and connections – a project including the predictive maintainance of rolling stock via the internet of things. The group also has active partnerships at the technological level enabling the digital transformation with Microsoft Azure, Amazon Web Services, IBM Watson, and the former subsidiary Axway. Lastly, in line with the Accenture and Capgemini model, Sopra Steria has rolled out DigiLabs in its main countries to showcase the group's innovative capability.

2.2. An acceleration in France

A strong acceleration in organic growth in France since the beginning of 2016.

Sopra Steria's organic growth is accelerating in 2016 relative to 2015. In H1 2016, organic growth came in at +9.5% (with two more business days, concentrated in the Q2), and stood at 5.4% in Q3 2016 (with one fewer business day), versus only +1.7% in 2015. The acceleration comes not only from the Consulting & Systems Integration business (87% of sales in France) - +11.5% in H1 2016 and +6.6% in Q3 2016 versus +3.5% in 2015 – but also from a gradual recovery in the I2S business (13% of sales in France, coming from Steria) - -2.1% in H1 2016 and -1.5% in Q3 2016 vs. -7.8% in 2015.

Fig. 9: Organic sales growth in France: Sopra Steria vs. competition



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

Consulting & Systems Integration

Sopra Steria is growing twice as fast as the Consulting & Systems Integration market in France, while maintaining its margins at close to 10%.

In this area, on our numbers, Sopra Steria is growing twice as fast as the market (comparable activities estimated to be up by 3.7%-3.9% for 2016 according to the latest Syntec Numérique/IDC research published in November 2016) **thanks to the double-digit growth in consulting** (+22% in H1 2016, +12% in Q3 2016) **and a good performance on the large strategic accounts** (+13% in H1 2016, +7% in Q3 2016), particularly in defence, aeronautics and transport. The focusing of the commercial strategy on a limited number of large accounts (Airbus, EDF, Société Générale, Orange, Crédit Agricole, SNCF, BNP Paribas, etc.) is continuing to pay off. **We expect Q4 2016 growth to be similar to its Q3 level** given one less business day relative to Q4 2015. The management considers the group's 'normative' growth in France to be around 5%-6% in Consulting & Systems Integration although, for the moment, Sopra Steria is below this level, even after restatement for the number of days billed. **In 2017, the group will have to contend with two fewer billing days** (two days more in Q1, three days less in Q2 and one day less in Q3), **something which should, on our estimates, be reflected in a loss of three percentage points of organic growth relative to 2016 in Consulting & Systems Integration.** While the integration of the Steria terms has been completed – with the inter-contract issue having been resolved as of the Q2 2015 – and the bulk of the cost synergies implemented, **the operating margin continues to increase, by 0.2 points in H1 2016 and we expect +0.8 of a point in 2016 to 9.5%. For 2017 and 2018, we expect the margin to remain stable, at 9.6%.**

A bit of a lag in the I2S division, but in our view an operating margin approaching 5% in 2017 is a credible scenario.

I2S (Infrastructure & Security Services).

The division continues to deliver negative organic growth due to the clean-up of the portfolio of services and contracts under way for more than 18 months in Steria's legacy Infrastructure activities - the latter having been loss-making or low in profitability since they offer little value-added, prices are under pressure and/or lacking critical mass. This clean-up of the portfolio seems to be coming to an end although synergies will need to continue to be realised with key clients in the Consulting & Systems Integration business. The Security business is seeing strong growth (+13% in Q3 2016) and is beginning its development outside France, although still only accounts for 10% of I2S sales. **In early 2016, the management had been confident of I2S's ability to return to positive organic growth during the H2 2016. However, given a Q3 2016 at -1.5%, we now see this return to growth target being pushed out to 2017. Similarly, whereas the early 2016 target had been to achieve an operating margin in excess of 5% in 2017, we now expect I2S to approach but still come in short of the 5% mark in 2017. Our forecasts are for respective operating margins of 4.6% and 5% in 2017 and 2018.**

Fig. 10: Our forecasts - France

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e
France							
Revenues	796.4	828.0	1 009.8	1 364.3	1 539.0	1 619.4	1 721.9
% change	2.5%	4.0%	22.0%	35.1%	12.8%	5.2%	6.3%
% lfl change	3.7%	4.1%	2.8%	1.7%	7.4%	5.0%	6.3%
Operating margin	68.2	68.4	88.8	102.0	131.2	145.6	156.2
% of sales	8.6%	8.3%	8.8%	7.5%	8.5%	9.0%	9.1%
o/w C&SI							
Revenues	*796.4*	*828.0*	*930.3*	*1 161.1*	*1 339.4*	*1 421.6*	*1 521.1*
% change	*2.5%*	*4.0%*	*12.4%*	*24.8%*	*15.4%*	*6.1%*	*7.0%*
% lfl change	*3.7%*	*4.1%*	*2.8%*	*3.5%*	*9.0%*	*5.8%*	*7.0%*
Operating margin	*68,2*	*68,4*	*88,8*	*101,3*	*127,0*	*136,5*	*146,1*
% of sales	*8,6%*	*8,3%*	*9,5%*	*8,7%*	*9,5%*	*9,6%*	*9,6%*
o/w I2S							
Revenues			*79,5*	*203,2*	*199,6*	*197,9*	*200,9*
% change				*155,6%*	*-1,8%*	*-0,9%*	*1,5%*
% lfl change				*-7,8%*	*-1,8%*	*-0,9%*	*1,5%*
Operating margin			*0,0*	*0,7*	*4,1*	*9,1*	*10,0*
% of sales			*0,0%*	*0,3%*	*2,1%*	*4,6%*	*5,0%*

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

2.3. Continental Europe: a turnaround in Germany

Decent growth and a margin progression in the 'Other Europe' zone, driven by a turnaround in Germany, a country we see reaching a 7% margin over the medium term.

The 'Other Europe' zone (regrouping Germany, the Benelux countries, Scandinavia, Italy, Spain and Switzerland) **is now delivering decent organic growth** (+6.3% in 2015, +5.7% in H1 2016, +6.4% in Q3 2016), **mainly driven by Spain, Italy and the Benelux countries** which are posting double-digit increases, even rising to above 20% in some quarters like in Italy and the Benelux. **However, the bulk of the region's operating margin improvement** (4.4% in H1 2016, versus 0.6% in H1 2015) **is coming from Germany**. With the ongoing turnaround in Germany (which the management hopes will end up with an operating margin close to that of France), **we expect an operating margin in the 'Other Europe' zone of 5.4% for 2016, 6.5% for 2017, and 7% for 2018**. Concerning organic growth, we are forecasting +6.1% for 2016, +4.6% for 2017 (including a negative business day effect) and +5% for 2018.

One of the points of concern had been the growth and profitability in Germany. On our numbers, Germany represents 5% of sales. **In 2016, this country has confirmed its return to organic growth that began in Q2 2015** (+2.2% in Q3 2016) **and profitability** (margin of 3.4% in H1 2016, versus -4.5% in H1 2015). At the time of the business combination between Sopra and Steria, Germany had been in negative growth and generating losses on both sides for reasons specific to each company: 1) on the Steria side, since 2013 the subsidiary had been suffering from significant consultant attrition following the departure of part of the management team post the 2004 acquisition of Mummert Consulting, and the business required rebuilding; 2) on the Sopra side, the business was limited to one client (Airbus) sub-contracted from a local service provider, within a context of a reduction in the German share of Airbus IT expenditure.

Fig. 11: Our forecasts – Other Europe

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e
Other Europe							
Revenues	143.8	163.7	388.7	697.4	729.2	762.8	800.9
% change	14.1%	13.8%	137.4%	79.4%	4.6%	4.6%	5.0%
% lfl change	3.0%	9.6%	4.1%	6.3%	6.1%	4.6%	5.0%
Operating margin	7.4	6.4	18.9	18.5	39.7	49.4	56.3
% of sales	5.1%	3.9%	4.9%	2.7%	5.4%	6.5%	7.0%

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

2.4. Sopra Banking Software

Sopra Banking Software is confirming its strong growth momentum, but R&D investment means we see no prospect of a margin recovery before 2017.

Sopra Banking Software sales have returned to the organic growth path since 2014 with the signature of the first licence sales in the vast project to transform the core banking system for La Banque Postale in France which will run through to at least 2017 inclusive. After the acquisitions of Delta-Informatique in 2011 and Callataÿ & Wouters in 2012 - supplemented by COR&FJA Banking Solutions in Germany in 2014 and Cassiopæ in the specialised financing segment in 2016 -, **Sopra Banking Software now has two complementary offers enabling it to respond to the banking digital transformation needs**: 1) Sopra Banking Platform, a core banking platform in the form of software components, adapted to the needs of the large banks; 2) Sopra Banking Amplitude, a core banking integrated solution aimed at small banks and subsidiaries of large banks with 140 clients in 45 countries. **At geographical level, Sopra Banking Software generates the bulk of its sales in France** (38% of 2015 revenues), Belgium and French-speaking Africa.

The Banque Postale dynamic continues.

In 2015, the Sopra Banking Software benefited from the ramp-up of the Platform product at La Banque Postale, and projects at BNP Paribas and Crelan (ex-Crédit Agricole Belgium), while the Amplitude suite signed 28 new clients and completed 26 roll-outs. In H1 2016, concerning the Platform product, the entity delivered the account management module for La Banque Postale and signed an industrial and commercial partnership in payments with Société Générale and La Banque Postale within the framework of their joint subsidiary Transactis[2] (which will be equipped with the Sopra Banking Platform for Payments solution), while Amplitude signed six new clients and completed 11 roll-outs. In total, for Sopra Banking Software, we are forecasting organic growth of 7.2% for 2016 and 8% for 2017 and 2018, driven by a positive overall dynamic in this market[3].

The Sopra Banking Software operating margin is currently being impacted by the R&D investment required to ensure that its products are aligned with the needs of large clients and, in particular La Banque Postale. In our view, this investment is likely to dampen profitability until 2017, with a peak in 2016. The 2015 margin thus fell by one point to 9.1% given the additional R&D expenditure while the H1 2016 margin was down by 2.9 points at 4.3%, on the back of a EUR6bn increase in R&D investment. **The aim remains to manage the margin at around 10% for 2017 taking this investment into account.** In view of these elements, and introducing an element of caution concerning the level of 2017 investment, **we are forecasting a margin of 6.8% for 2016, 8.8% for 2017 and 10.1% for 2018**.

Fig. 12: Our forecasts – Sopra Banking Software

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e
Sopra Banking Software							
Revenues	194.9	217.3	263.3	282.4	345.9	386.9	417.9
% change	118.5%	11.5%	21.2%	7.3%	22.5%	11.8%	8.0%
% lfl change	-3.9%	-0.3%	7.6%	2.5%	7.2%	8.0%	8.0%
Operating margin	28.2	23.6	26.7	25.7	23.6	34.0	42.4
% of sales	14.5%	10.9%	10.1%	9.1%	6.8%	8.8%	10.1%

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

[2] Transactis is a joint-venture responsible for the investment, maintenance and operation of the Société Générale and La Banque Postale electronic banking systems. In June 2016, Transactis announced that, as of 2018, it will expand its operations to the joint processing of the bank transfers and direct debts of the two banking groups (including Crédit du Nord). Transactis handles 22% of payment card and electronic banking transactions in France.

[3] See our research on Temenos published on 13/10/2016 ('Success breeds success').

In our view, the target of doubling sales between 2014 and 2019 looks achievable, subject to the acquisition of EUR100m of additional sales.

On the basis of the 2014 pro forma including a full year of the Steria legacy activities (EUR271m), Sopra Banking Software is aiming to double its sales within the next five years. We make this the equivalent of EUR540m of sales in 2019. Integrating Cassiopæ as of April 2016 and based on our forecast of annual like-for-like growth 8% for 2016-2019, we estimate that the subsidiary will need to acquire come EUR100m of additional sales to achieve this target – penetration of a new geographical zone or adjacent market, or else the addition of new functionalities. Created in 1987, **Cassiopæ is an example of an acquisition realised to penetrate a market adjacent to core banking.** It is a developer of integrated 'front to back' software solutions for specialised finance and real estate management, and for the management of social housing, with sales of EUR50m in 2014 and 300 clients in 40 countries. **The strategic attraction is to become a reference player in the specialised finance companies market,** but also begin to penetrate new geographies (Latin America, Asia, USA). The potential synergies with Sopra Banking Software are at the level of the products, integration services and additional services (managed services, SaaS), knowing that **Cassiopæ's operating margin should be in the double digits**.

2.5. Other Solutions

The other solutions are making progress, driven by Sopra HR Software, with double-digit margins.

The 'Other Solutions' division includes Sopra HR Software (76% of 'Other Solutions' 2015 sales, i.e. around EUR150m, coming from the historic Pléiades human resources management offer and the acquisition of HR Access in 2013 and the IBM services activities dedicated to HR Access in 2014) **and Sopra Steria Solutions Immobilier** (24% of 'Other Solutions' sales, i.e. c.EUR48m). **2015 had seen a slowdown in organic growth** (+3.2%) given an exceptional EUR4m sale of licences in 2014 at the level of HR Software. **The latter continued its slowdown in H1 2016** (+1.7%) **before beginning a catch-up in Q3 2016** (+4.3%) **thanks to a number of significant new business wins at the end of H1 2016.** We expect organic growth of 3.8% for this division in 2016, 4.2% in 2017 and 5% in 2018. **The margin remains in double digits over a full year: after 11.6% in 2015 we are forecasting 12.1% in 2016, 12.6% in 2017 and 12.9% in 2018**.

Fig. 13: Our forecasts – Other Solutions

EURm (FYE 31/12)	2013	2014	2015	2016e	2017e	2018e
Other solutions						
Revenues	56.1	174.7	198.3	206.3	214.9	225.7
% change		211.4%	13.5%	4.0%	4.2%	5.0%
% lfl change	2.4%	10.9%	3.2%	3.8%	4.2%	5.0%
Operating margin	4.3	14.6	23.1	25.0	27.1	29.1
% of sales	7.7%	8.4%	11.6%	12.1%	12.6%	12.9%

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

3. Focus on the United Kingdom

3.1. Risks limited in the United Kingdom

Sopra Steria's business in the United Kingdom is characterised by a very high proportion of recurring sales and very strong exposure to the public sector. The commercial sector business is in the reconstuction process.

The United Kingdom accounted for 29% of 2015 sales and we see this proportion falling to 25% in 2016. In our view, Sopra Steria's risks linked to the United Kingdom have been over-estimated given its specific positioning in this country. The risk is not linked to Brexit – except Sterling fluctuations against the Euro – nor to a very unlikely reversal in the governmental strategy of outsourcing administrative services – a move initiated in the early 2000s to ensure more efficient functioning and reduce costs.

- **Currency effect**. The weakening of Sterling against the Euro has been the only negative impact from Brexit on Sopra Steria's sales. We estimate this effect at -3.3% in 2016 and -0.9% in 2017.

- **A very high proportion of recurring sales**. 78% of UK sales is recurring in nature (BPO, infrastructure and applications management), with multi-year contracts over three to ten years, **meaning that the overwhelming majority of Sopra Steria activity in the United Kingdom is independent of the economic environment** – including the country's planned exit from the European Union.

- **Substantial exposure to the public sector**. 68% of UK sales is generated with the UK government, of which half within the framework of joint-ventures with public-sector entities - NHS SBS with the National Health Service since 2005[4], SSCL with the Cabinet Office since 2013[5] - and the rest directly (ministries, governmental agencies, local authorities). **The post-Brexit discussions between the representatives of the UK government and their IT suppliers have resulted in no reversal in the outsourcing strategy.** Admittedly, the discussions around Brexit have only just started but in our view the **substitution risk is very low** given the recurring nature of the contracts and Steria's long history with the UK administrations (itself inherited from Bull, whose UK services business had been acquired by Steria in 2002).

- **Sopra Steria is rebuilding its commercial sector business**. The commercial sector accounts for 32% of Sopra Steria's sales in the United Kingdom, with around 10% in Financial Services and a little over 20% in other sectors (Telecoms, Utilities, Media). **Financial Services returned to growth in 2016** after a fall of around 10% in 2015 following the appointment of a new MD for this business in April 2015[6] coming from CGI (Logica) and responsible for implementing a

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[4] Sopra Steria holds a 50% + 1 share stake in the joint-venture. The remaining stake is held by the NHS.

[5] Sopra Steria holds a 75% in the joint-venture. The remaining stake (25%) is held by the Cabinet Office.

[6] Melba Foggo, who had been MD, Financial Services & Business Consulting at CGI and Logica (2010-2015) and Director at E&Y (1999-2010).

solutions model aligned with that of France, including synergies with Sopra Banking Software. **The other sectors have continued to see sales declines in 2016** (of around 10%) after a fall of 13% in 2015, and more work will be required – around two years – with the appointment of a new head for this business to be responsible for turning around the situation.

The joint-ventures with the government are in the transition phase after years of strong growth.

For 2016, we are forecasting stable sales on a like-for-like basis in the United Kingdom, with modest growth in the governmental activities and a moderate decline in the private sector. After a period of strong growth (2013-2015) linked to client ramp-ups, **SSCL has seen its sales stagnate due to an inability to absorb new capacity.** For its part, the Metropolitan Police joined SSCL at the end of 2015. **SSCL sales are expected to be down in 2017, unless the joint-venture signs new ministries –** something that seems unlikely before H2 2017. **Concerning NHS SBS, we see a slight decline in 2016 due to an administrative reorganisation at the NHS which has withdrawn from NHS SBS part of the business scope that it had hitherto managed.** With this effect behind us, in our view **NHS SBS has a good chance of returning to modest growth as of 2017.** In the private sector, Banking should see some modest growth in 2016-2017 in our view, thanks to the work carried out on the offers and marketing although the latter could have done better had cost reduction plans (RBS, etc.) not been launched by some clients within a context of low interest rates. Our forecasts have sales falling for the rest of the commercial sector in 2016 and 2017 before returning to low growth in 2018 if the solutions model is successfully replicated. **For the operating margin, we expect stabilisation at 7.5% for 2016, then 8.2% for 2017 and 8.6% for 2018**.

Fig. 14: Our forecasts – United Kingdom

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e
UK							
Revenues	81.7	83.9	443.8	1 042.0	922.5	877.2	875.9
% change	39.7%	2.7%	429.0%	134.8%	-11.5%	-4.9%	-0.1%
% lfl change	-2.9%	1.8%	0.5%	-0.7%	-0.2%	-1.1%	-0.1%
Operating margin	10.3	6.2	36.3	76.2	69.2	72.3	75.8
% of sales	12.6%	7.4%	8.2%	7.3%	7.5%	8.2%	8.6%

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

3.2. SSCL, three years on

SSCL's target was to deliver GBP1bn of savings for the UK government and police by 2020.

SSCL is a vast programme to outsource HR, Finance and Procurement services to a single common operating platform (SOP: Single Operating Platform), set to be around for 10-20 years and which is only just at its inception. This platform was originally that of the DWP[7] created in 2006 (118,000 users including the Cabinet Office, the Department of Education, the Scottish Government, the Social Security Agency in Northern Ireland, the Welsh Government Assembly and two other agencies) and based on the Oracle R12 E-Business Suite. Its aim is to deliver GBP1bn of savings for the UK government and police by 2020.

[7] Department for Work & Pensions.

Three clients at the end of 2013 with a sales volume of EUR1.2bn over ten years…

On its inception in November 2013, in addition to the DWP, SSCL included Defra[8] (15,000 users including the Department of Energy and ten other agencies), **and the Environment Agency** (13,000 users, including two other agencies), both of which were on Oracle's R11 version and regrouped 1,100 civil servants at eight sites in the United Kingdom. **The R12 migration for the Environment Agency had initially been scheduled for January 2015 and in April 2015 for Defra, but these effectively took place in September 2015 and May 2016 respectively.** These migrations included the transfer to SSCL of the technical support and hosting by various suppliers (Fujitsu until 2014 for the DWP, IBM until 2018 for Defra, Capgemini until 2016 for the Environment Agency). Furthermore, we understand that, while the BIS[9] UK Shared Business Services platform (10,000 users) had been expected to transfer around 15% of its transaction volumes to SSCL as of April 2015, the agreement was terminated in September 2015, UK SBS having deemed that the migration was no longer viable – apparently due to a change in BIS's requirements.

…six clients currently with a sales volume of EUR2.5bn over ten years.

In October 2014, the Home Office (29,500 users) **and the Ministry of Justice** (MoJ, 76,000 users) **joined SSCL**. The Home Office had been committed to Oracle on Oracle R11 via a contract running from 2009 to 2016 with an upgrade to R12 planned with Fujitsu for April 2015. In 2011, the MoJ had rolled out an in-house shared services centre on ERP Oracle operated by Steria, only for this to be abandoned in June 2014 to be outsourced to SSCL. Its migration to Oracle R12 should be finalised in December 2016. Lastly, **in July 2015 the Metropolitan Police** (55,000 users) **joined SSCL** (contract value: GBP216m over ten years), in a proprietary entity (Police SSCL) to outsource three of its administrative departments representing 400 public sector employees, aimed at generating GBP100m of savings over the period. **The migration of the Metropolitan Police services to a proprietary platform** (P-SOP) – with the likelihood of other UK police forces coming on board – **should begin in October 2016 and be completed by H2 2017. This platform looks set to recruit other police forces in the United Kingdom,** knowing that the only two other platforms of this type are those operated by Sopra Steria (Cleveland Police), and Capgemini (MFSS or Multi-Force Shared Services, signed up to by Norfolk & Suffolk Constabularies, Cheshire Constabulary and Northamptonshire Police).

Other ministries, government agencies and police forces are likely to join SSCL, but probably not before H2 2017.

In time, numerous other ministries, agencies and police forces are likely to join the programme. Currently, SSCL generates sales of around EUR250m, corresponding to EUR2.5bn over ten years, i.e. a volume twice the level communicated by Steria on the launch of the joint-venture (GBP1bn or EUR1.2bn over ten years), with more than 2,200 people. Once the bulk of the transformation phase to the new Oracle platform is over, the joint-venture will move into a phase of maturity. Savings can be made once clients have completed their migration to the platform. **SSCL is now in a transition phase prior to the coming on board of new clients.** Each negotiation with a new client takes between nine and 18 months depending on the size of the entity.

[8] Department for Environment, Food & Rural Affairs.

[9] Department for Business Innovation & Skills.

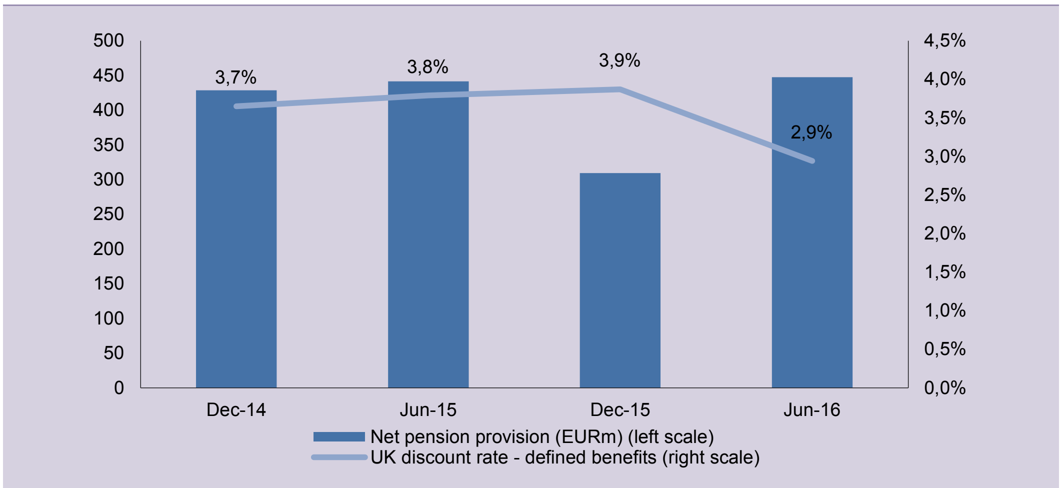
This explains the decline in SSCL's profitability in 2016, especially since there has been some delay in the savings promised by the Cabinet Office.

3.3. Pension provision

The decline in long bond yields was behind a sharp rise in pension liabilities in H1 2016.

As of 30/06/2016, Sopra Steria's pension liabilities stood at EUR430.6m, i.e. 20% of the group's current market capitalisation. This represented a EUR148m increase relative to 31/12/2015 mostly due to the change in actuarial assumptions linked to the decline in long-term bond yields in the United Kingdom. **This country represented 63% of the pension liability at 30/06/2016** – a legacy of the acquisition of Steria, which had itself inherited it with the acquisition of Bull Integris Europe in 2002 and the signature of managed services contracts with the UK government -, followed by France (26%) and Germany (11%). **For its part, 80% of the increase in the net pension liabilities during H1 2016 came from the United Kingdom** (discount rate reduced to 2.94% versus 3.87% at the end of 2015), versus 16% from France and 5% from Germany. **Around 50% of the pension assets are invested in bonds,** versus c.35% in equities and c.15% in real estate assets. The reference rate used for the United Kingdom is the 15 year for AA-rated corporate bonds as defined by Mercer and Markit.

Fig. 15: Pension provision and the UK discount rate



Source: Company Data.

The recent rise in UK bond yields points to a stabilisation or even fall in the pension liabilities, even if price and salary inflation is again picking up.

Between early January and the end of August 2016, UK long-term bond yields virtually halved, with a marked acceleration in the decline the day after the Brexit referendum on 24/06/2016. **They have since returned to their levels of prior to the referendum (June 2016) but remain 20%-25% below their levels of the end of 2015.** In summary, at this stage **we don't expect Sopra Steria to make a material upwards revision to its actuarial assumptions at the 2016 year end, unless long-term bond yields continue to rise.** That said, the decline now seems to be behind us and, in our view, we are unlikely to see a further deterioration in Sopra Steria's pension liabilities on the back of interest rates alone. **On the other hand, were price and salary inflation to pick up, we could see a further degradation.**

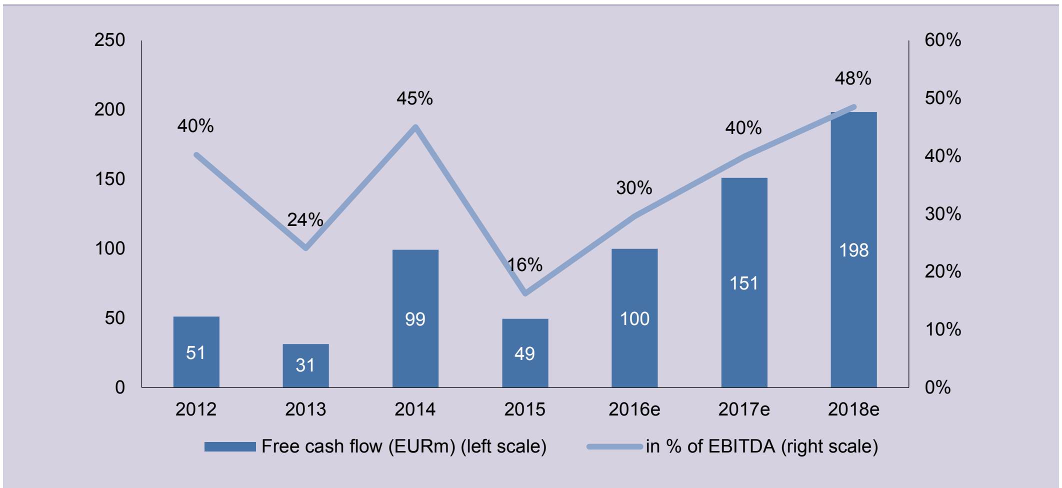
4. Acquisition capability beyond 2016

4.1. An improvement in free cash flow in prospect

Our estimates see Sopra Steria doubling its free cash flow in 2016, thanks to a reduction in restructuring charges and an improved contribution from SSCL.

While 2015 free cash flow had been much higher than expectation (EUR49m vs. guidance of zero – better-than-expected WCR management at the level of average client payment periods), **our estimates see Sopra Steria doubling its free cash flow in 2016 to c.EUR100m, or 30% of EBITDA and reaching EUR151m in 2017, or 40% of EBITDA, and continuing to improve through to 2018, to a level that we forecast at EUR198m or 48% of EBITDA**.

Fig. 16: Our free cash flow forecasts (2012-2018e)



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

- **The 2016 WCR has a good chance of progressing in line with 2015** (around EUR82m), including a EUR30m negative impact linked to the change in social security payment periods (now monthly as opposed to quarterly, 2/3), and new regulations in the United Kingdom concerning supplier payment periods, 1/3). **Beyond 2016, excluding exceptional items, the WCR should progress at a slower rate**.

- **Restructuring: EUR55.8m was disbursed in 2015** (of which EUR25m in H1 and EUR30.8m in H2) **and we expect EUR35m for 2016** (of which EUR14.1m in H1 and an estimated EUR21m in H2), and EUR25m for 2017. **Farther out, the integration of Steria having been realised, we expect Sopra Steria to spend 0.4% of its sales on restructuring**. This figure compares with our estimates of 1% of sales for Atos and 0.6% for Capgemini.

- **SSCL contribution to free cash flow: this will be zero in 2016** whereas it had been a EUR10m negative in 2015 and EUR65m at the level of Steria in 2014. **As of 2017, we expect SSCL to make a positive annual contribution of EUR25m-EUR30m.**

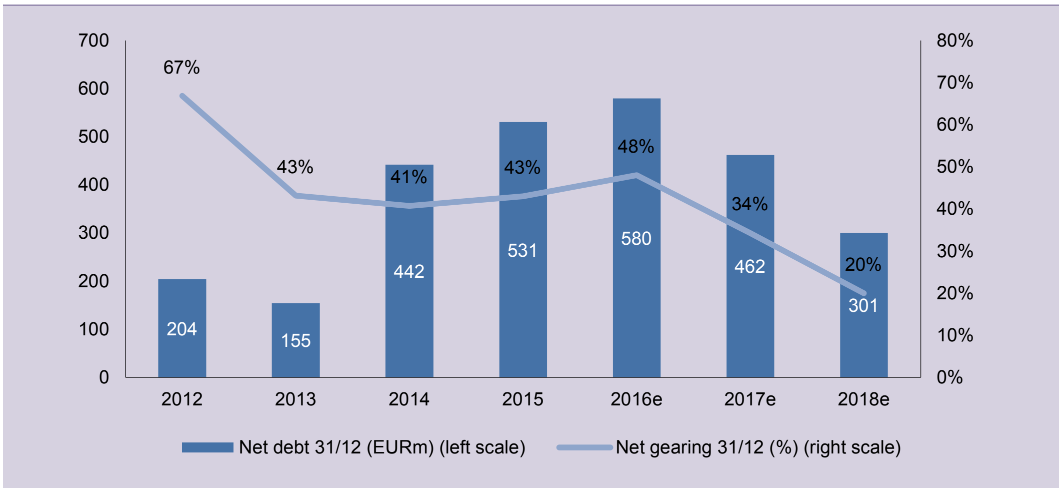
- **Pension provision: Sopra Steria is paying an additional annual contribution of GBP17m** (EUR18.7m in 2014, EUR23.3m in 2015) through to June 2017, the date beyond which a new negotiation will take place with the trustees within the framework of the plan to close the pension deficit over four to 13 years established in 2014. On the basis of an average EUR/GBP exchange rate of 0.82 in 2016 and 0.85 in 2017-18 and assuming that the payments remain at GBP17m per year, we calculate these amounts at EUR20.8m for 2016 and EUR20m beyond that date.

4.2. Theoretical debt reduction by 2020

At end 2018, we expect net financial debt of around EUR300m, excluding any fresh acquisitions and capital increases reserved to employees.

As shown in Fig. 17, excluding future acquisitions and any capital increases reserved to employees, we might expect Sopra Steria to pay down its debt in full by 2020 – although in our view this eventuality is highly improbable in that the group has always fuelled its growth with acquisitions**,** always paid a dividend and has never been in a net cash position since 1998. For 2016, given the Cassiopæ transaction, we expect net debt to rise by EUR49m to EUR580m (gearing: 48%, +5 pts). **For the end of 2017, we are forecasting a EUR117m reduction in this debt to EUR463m,** i.e. gearing of 34%. **For the end of 2018, on the current scope, we are forecasting net debt of EUR301m** and gearing of 20%. Assuming a EUR150m annual reduction in debt, we estimate that gearing could fall to zero by the end of 2020.

Fig. 17: Our net debt forecasts excluding acquisitions (2012-2018e)



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

4.3. Nearly EUR1bn of undrawn credit lines

Additional debt capacity of EUR1bn through to 2019, but no major transactions before 2017.

As of 30/06/2016, net debt stood at EUR719.6m, i.e. 2.2x the EBITDA, while the bank covernants foresee a limit of 3x. Given this level, Sopra Steria will mark a pause in acquisitions until 2017 unless these are very modest in size (three transactions in 2016 of around EUR1m: EchoSystems and Active3D for Real Estate Solutions, and Solid Group for Services in Norway). **Sopra Steria benefits from EUR1,561 million of credit lines** (EUR900m of multi-currency revolving credit facilities, a EUR200m bank overdraft facility, a EUR180m bond loan, EUR267m of syndicated credit in EUR and GBP and EUR14m of finance leases), **of which EUR564 have been drawn. There thus remain EUR1bn of unused credit facilities** – i.e. 47% of the authorisations – on which the group can draw in the future. The bond loan matures in 2019, while the bank lines mature in 2021 with a possible extension to 2023. Excluding Steria (2014, EUR1,042 million in enterprise value, via a share swap), the most expensive acquisitions realised in recent years have been Delta-Informatique (2011, EUR30m, for Banking Software), Callataÿ & Wouters (2012, EUR141m, for Banking Software), Cimpa (2015, EUR92m, for Consulting & Systems Integration France), and Cassiopæ (2016, EUR51m for 75%, for Banking Software).

5. Financial statements

5.1. Income statement

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e	CAGR 15-18e
Net revenue	**1 216,7**	**1 349,0**	**2 280,4**	**3 584,4**	**3 742,9**	**3 861,2**	**4 042,2**	**4,1%**
% change	15,9%	10,9%	69,0%	57,2%	4,4%	3,2%	4,7%	
Gross Margin	**1 078,7**	**1 198,3**	**1 964,7**	**2 996,7**	**3 144,0**	**3 228,0**	**3 387,4**	
% of revenue	**88,7%**	**88,8%**	**86,2%**	**83,6%**	**84,0%**	**83,6%**	**83,8%**	
Other third-party expenses	(133,8)	(155,6)	(289,9)	(500,2)	(520,3)	(529,0)	(553,8)	
% of revenue	11,0%	11,5%	12,7%	14,0%	13,9%	13,7%	13,7%	
Taxes	(15,4)	(17,6)	(23,4)	(32,4)	(29,9)	(30,9)	(32,3)	
Personnel costs	(811,8)	(911,9)	(1 437,7)	(2 185,6)	(2 271,9)	(2 309,0)	(2 409,2)	
% of revenue	66,7%	67,6%	63,0%	61,0%	60,7%	59,8%	59,6%	
Other expenses	8,8	17,0	6,3	25,4	16,9	20,5	18,7	
Amortisation	(17,0)	(21,3)	(27,0)	(58,4)	(48,5)	(49,5)	(49,5)	
Net operating provisions	0,0	0,0	0,0	0,0	(1,6)	(1,6)	(1,6)	
Adjusted EBIT	**109,6**	**108,9**	**193,0**	**245,5**	**288,7**	**328,5**	**359,7**	**13,6%**
% of revenue	**9,0%**	**8,1%**	**8,5%**	**6,8%**	**7,7%**	**8,5%**	**8,9%**	
Net restructuring charge	(6,6)	(25,3)	(25,1)	(67,2)	(15,0)	(15,4)	(16,2)	
Capital gains or losses	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
Goodwill amortisation	(4,2)	(4,9)	(10,6)	(19,4)	(21,5)	(22,3)	(22,3)	
Stock-based compensation	(2,2)	(3,0)	(2,0)	(1,2)	(11,0)	(11,0)	(11,0)	
Other exceptional gains (losses)	(5,3)	28,2	(7,1)	(5,1)	(2,8)	0,0	0,0	
EBIT	**91,3**	**103,9**	**148,2**	**152,6**	**238,5**	**279,7**	**310,2**	**26,7%**
% of revenue	**7,5%**	**7,7%**	**6,5%**	**4,3%**	**6,4%**	**7,2%**	**7,7%**	
Cost of net debt	(7,2)	(7,0)	(7,4)	(8,1)	(7,1)	(4,9)	(2,9)	
Other financial gains (losses)	(1,0)	(1,4)	(10,7)	(14,9)	(15,0)	(15,0)	(15,0)	
Profit before tax	**83,1**	**95,5**	**130,1**	**129,6**	**216,3**	**259,8**	**292,3**	**31,1%**
Income taxes	(33,5)	(32,5)	(34,4)	(47,2)	(77,9)	(91,7)	(102,3)	
Tax rate	40,4%	34,1%	26,4%	36,4%	36,0%	35,3%	35,0%	
Consolidated net profit	**49,5**	**63,0**	**95,7**	**82,4**	**138,4**	**168,1**	**190,0**	**32,1%**
% of revenue	**4,1%**	**4,7%**	**4,2%**	**2,3%**	**3,7%**	**4,4%**	**4,7%**	
Profit from associates	6,1	8,4	5,8	7,2	9,8	12,1	13,9	
Minority interests	0,0	0,0	3,3	5,2	1,3	3,0	5,0	
Attributable net profit	**55,6**	**71,4**	**98,2**	**84,4**	**146,9**	**177,2**	**198,9**	**33,1%**
Average nb of shares - basic (m)	11,9	11,9	19,6	20,4	20,5	20,5	20,5	
Average nb of shares - diluted (m)	11,9	12,0	19,7	20,4	20,5	20,5	20,5	
Basic EPS (EUR)	**4,67**	**6,00**	**5,02**	**4,14**	**7,17**	**8,65**	**9,71**	**32,9%**
% change	**-11,8%**	**28,4%**	**-16,4%**	**-17,6%**	**73,4%**	**20,6%**	**12,2%**	
Adjusted EPS (EUR)	**5,70**	**6,26**	**6,62**	**7,39**	**8,78**	**10,21**	**11,29**	**15,2%**
% change	**-8,5%**	**9,9%**	**5,7%**	**11,6%**	**18,8%**	**16,3%**	**10,6%**	

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

5.2. Balance sheet

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e
Goodwill	314,6	317,5	1 475,2	1 586,9	1 620,1	1 597,8	1 575,5
Intangible fixed assets	59,2	54,0	219,5	214,0	191,6	189,1	186,6
Tangible fixed assets	39,2	49,2	109,9	118,5	120,3	122,3	126,2
Fixed assets and goodwill	**413,0**	**420,7**	**1 804,7**	**1 919,4**	**1 932,0**	**1 909,2**	**1 888,4**
Investments	**117,8**	**123,7**	**229,7**	**245,1**	**311,4**	**321,4**	**333,1**
Deferred tax assets	**34,5**	**25,6**	**154,7**	**142,7**	**162,7**	**162,7**	**162,7**
Inventories	0,5	0,2	0,3	0,4	0,4	0,4	0,5
Accounts receivables	387,8	446,1	988,9	1 154,1	1 199,8	1 227,1	1 273,6
Other short term assets	30,2	59,9	109,3	136,9	157,2	162,2	169,8
Current assets	**418,5**	**506,3**	**1 098,4**	**1 291,4**	**1 357,4**	**1 389,8**	**1 443,9**
Cash & cash equivalents	**47,4**	**102,2**	**222,4**	**222,7**	**173,7**	**290,9**	**452,7**
TOTAL ASSETS	**1 031,1**	**1 178,5**	**3 510,0**	**3 821,3**	**3 937,3**	**4 073,9**	**4 280,8**
Shareholders' equity	305,3	357,9	1 057,1	1 194,4	1 167,8	1 306,1	1 462,0
Minority interests	0,0	0,0	29,7	38,7	40,0	41,7	43,7
Consolidated equity	**305,3**	**357,9**	**1 086,8**	**1 233,1**	**1 207,8**	**1 347,8**	**1 505,7**
Long-term provisions	**55,3**	**71,1**	**527,9**	**444,1**	**599,1**	**604,5**	**610,7**
Deferred tax liabilities	**18,0**	**2,1**	**8,1**	**15,8**	**15,8**	**15,8**	**15,8**
Convertible bonds	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Long-term debt	73,0	135,5	594,9	437,8	437,8	437,8	437,8
Short-term debt	178,4	121,3	69,9	315,7	315,7	315,7	315,7
Debt	**251,4**	**256,8**	**664,8**	**753,5**	**753,5**	**753,5**	**753,5**
Accounts payable and accrued	56,1	68,9	260,3	259,4	257,3	252,2	258,7
Deferred revenues	76,4	100,1	191,4	249,3	252,5	260,5	272,7
Salary and income tax payable	257,7	312,0	689,9	760,8	746,8	731,9	750,9
Other liabilities	11,0	9,4	80,7	105,3	104,5	107,8	112,8
Current liabilities	**401,1**	**490,5**	**1 222,3**	**1 374,8**	**1 361,1**	**1 352,3**	**1 395,1**
TOTAL LIABILITIES	**1 031,1**	**1 178,5**	**3 510,0**	**3 821,3**	**3 937,3**	**4 073,9**	**4 280,8**

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

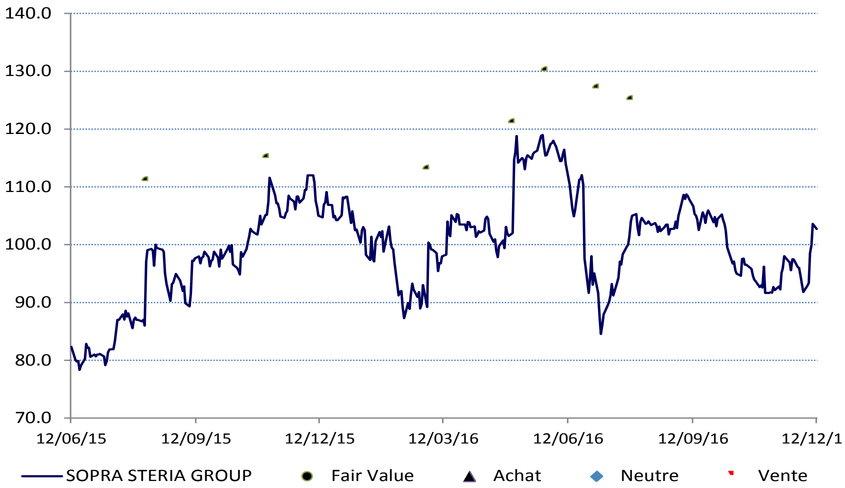
5.3. Cash flow statement

EURm (FYE 31/12)	2012	2013	2014	2015	2016e	2017e	2018e
Operating cash flow	**70,4**	**56,8**	**117,8**	**173,6**	**226,4**	**241,1**	**260,7**
Change in WCR	(8,6)	(1,7)	14,8	(81,9)	(79,8)	(41,1)	(11,3)
Capital expenditure	(6,8)	(17,1)	(26,3)	(42,5)	(47,0)	(49,0)	(51,0)
Disposals in fixed assets	3,1	0,2	0,1	0,2	0,1	0,0	0,0
Net capex	(3,7)	(16,9)	(26,2)	(42,3)	(46,9)	(49,0)	(51,0)
Free cash flow	**58,1**	**38,3**	**106,4**	**49,4**	**99,7**	**151,0**	**198,4**
Investments	(0,8)	(1,2)	(9,1)	(0,3)	(38,7)	0,0	0,0
Disposals in investments	2,0	2,1	4,8	2,2	2,2	2,2	2,2
Acquisitions (goodwill)	(175,5)	41,1	(134,2)	(92,3)	(104,7)	0,0	0,0
Cash flow after investing activity	**(116,1)**	**80,3**	**(32,1)**	**(41,0)**	**(41,5)**	**153,2**	**200,6**
Dividends paid	(22,6)	(20,2)	(22,5)	(37,5)	(34,8)	(38,9)	(43,0)
Issuance of shares	0,7	1,4	0,9	(22,5)	11,3	0,0	0,0
Cap. Incr. for minority interests	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Incr. cash bef. loan repayments	(138,0)	61,5	(53,7)	(101,0)	(65,1)	114,2	157,6
Repayment of loans	123,8	(22,8)	(57,0)	119,7	96,1	22,9	20,3
Net increase in cash	**(14,2)**	**38,7**	**(110,8)**	**18,7**	**31,0**	**137,1**	**177,9**

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

Price Chart and Rating History

Sopra Steria Group



Ratings Date	Ratings	Price
26/11/2008	BUY	EUR21,7658

Target Price Date	Target price
29/07/2016	EUR125
04/07/2016	EUR127
27/05/2016	EUR130
03/05/2016	EUR121
01/03/2016	EUR113
04/11/2015	EUR115
07/08/2015	EUR111
20/03/2015	EUR90
19/03/2015	Under review
13/01/2015	EUR91
31/10/2014	EUR97
06/08/2014	EUR118
25/04/2014	EUR105
20/02/2014	EUR101
10/01/2014	EUR85
15/11/2013	EUR76
24/09/2013	EUR75
14/06/2013	EUR70

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 55,6% NEUTRAL ratings 34% SELL ratings 10,5%

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15	Other disclosures	Other specific disclosures: Report sent to Issuer to verify factual accuracy (with the recommendation/rating, price target/spread and summary of conclusions removed).	No

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