

LafargeHolcim

Price CHF52.80

Updated forecasts, Indian mess, new FV... Back to Neutral for now.

Fair Value CHF58 (+10%)

NEUTRAL vs. BUY

President Modi's decision deteriorates the visibility on Indian macro at least for the short term. This is a clear disappointment as a very good monsoon season gave hopes previously. LHN is strongly diversified but India remains a key country (>10% of sales, #1 in cement capacity). Besides, we have wisely downgraded our estimates to land closer to the company's guidance, which is translated by a new FV at CHF58 (-EUR2). Following the good share price performance since our upgrade, we downgrade to Neutral.

On 8th November 2016, President Modi announced the demonetisation of INR500 and INR1000 notes, which represented more than 85% of cash in circulation. The initial aim was not to limit the use of cash, but to force people to exchange (within a 50-day period, i.e. until the end of 2016) their old notes for new ones (INR500 and INR2000) and therefore justify the origin of their cash. It was presented as a way of fighting corruption and the black market. The exemptions in place since the demonetisation announcement (for paying utility bills or buying medicine) will not be extended beyond today. It remains to see what the impact on day to day business could be. This is difficult to predict but press comments suggest it is not headed in the right direction (uncertainty on printing capacities, impact on Indian GDP...).

ANALYSIS

- President Modi decision to demonetise was unexpected. The short-term impact of this decision is likely to be disturbing at the very least, as a large part of transactions are paid in cash. We suspect infrastructure construction should be less perturbed but the impact on private residential is certainly a question mark. This segment represents 60-65% of the cement market while one third of transactions are paid in cash or partly in cash, which means c20% of the cement market could be impacted. Hence business at the end of 2016 and part of 2017 is likely to be affected at LHN, even if the group is not resting on its laurels and plan to offer non-cash solutions to its clients. Note that India Cement, which is mostly exposed to the south, said on 22nd November that demonetisation had had no impact so far. In any case, assuming LHN cement in India is down -20% in November and December and down again -10% in 2017, then the negative impact would be CHF5-6 on our FV.
- Earlier, we were optimistic on the Q4 performance for LHN, especially thanks to better trends in Nigeria (Dangote has increased prices by c40% in September) and in India (positive impact from the monsoon in 2017 but also a bit in Q4 2016). Admittedly, visibility on India in Q4 has strongly deteriorated with the Modi decision and cannot be seen as a proper short term catalyst anymore. From a long term point of view however, the Indian cement market is still promising though.
- Admittedly, LHN will benefit from Donald Trump's infrastructure plan and our view on US Construction has recently improved too. We were worried about the steady deterioration in construction spending (as disclosed by the Census bureau) but the last release was better (+3.4% y/y SAAR in October), after a steady slowdown in growth over the past six months. But the Trump plan has started to be priced in by the market, and there are others players better placed to play US Construction like CRH for instance. Plus, there are some risks which might emerge in 2017: impact of the Trump policy on EM macro (c60% of 2015 EBITDA), Brexit (UK is the #1 EBITDA contributor in Europe) and uncertainties regarding energy costs inflation (c15% of the cost base).
- Finally, we have updated our forecasts with more conservative assumptions and taking into account the latest guidance (e.g. new scope impact, share-buy-back programme). We are overall a bit more cautious on margin performance (22.8% EBITDA margin in 2018e vs 24.4% previously).

VALUATION

- Our new FV of CHF58 is derived from the application of historical multiples to our 2018 estimates, discounted back at 9.3% (cost of equity). CHF58 is close to the peak price in the last 12 month.

NEXT CATALYSTS

- FY 2016 results to be released on 2nd March

Bloomberg	LHN VX
Reuters	LHN.VX
12-month High / Low (CHF)	57.0 / 34.1
Market Cap (CHF)	32,045
Ev (BG Estimates) (CHF)	47,090
Avg. 6m daily volume (000)	1 799
3y EPS CAGR	47.6%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-5.8%	6.0%	34.4%	5.0%
Cons & Mat	2.4%	4.2%	14.2%	7.1%
DJ Stoxx 600	5.2%	5.1%	11.0%	-2.8%

YEnd Dec. (CHFm)	2015	2016e	2017e	2018e
Sales	29,483	27,052	27,092	29,562
% change		-8.2%	0.1%	9.1%
EBITDA	5,751	5,651	6,216	7,025
EBIT	3,416	3,216	3,781	4,590
% change		-5.8%	17.6%	21.4%
Net income	833.0	1,519	2,045	2,604
% change		82.4%	34.6%	27.3%

	2015	2016e	2017e	2018e
Operating margin	11.6	11.9	14.0	15.5
Net margin	-6.7	7.2	8.4	9.9
ROE	2.7	4.7	6.3	7.9
ROCE	4.4	4.3	5.4	6.6
Gearing	48.7	36.5	28.5	25.8

(CHF)	2015	2016e	2017e	2018e
EPS	1.38	2.51	3.41	4.42
% change	-	82.4%	35.7%	29.8%
P/E	38.4x	21.0x	15.5x	11.9x
FCF yield (%)	NM	6.4%	10.0%	10.2%
Dividends (CHF)	1.50	2.00	2.15	2.30
Div yield (%)	2.8%	3.8%	4.1%	4.4%
EV/Sales	1.7x	1.7x	1.6x	1.5x
EV/EBITDA	8.9x	8.3x	7.2x	6.2x
EV/EBIT	14.9x	14.6x	11.8x	9.5x



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