

## COMPANY NOTE

Company Update

Belgium | Consumer | Food Retailers

13 December 2017

# Jefferies

## Colruyt (COLR BB) Uncool COLR

### Key Takeaway

**Fiscal 17/18 started in a challenging manner for the group, with H1 EBIT -7% YoY, reflecting a tough Belgian retail market. This is despite the help from ongoing sub-optimal execution at Delhaize integrated stores and an Easter calendar boost. Valuation remains disconnected from the lack of earnings growth potential and the risk of increasing competitive attrition.**

**A tough H1 update...** with group sales/EBIT/net income growth (adjusted for disposals) of +4%/-7%/-2%, with EBIT coming in at €232m vs JEFe/cons at €236m/€238.m. Pressures in the retail division reflect the ongoing challenges of driving market share gains in a profitable manner in Belgium (note that H1 benefitted from the inclusion of Easter in 2017, compared with no festive trading in April 2016; this will unwind in H2). COLR confirmed guidance for fiscal year 17/18 net income as close as possible to the €348m of 16/17. It is unclear whether this includes the €8m hike in one-off benefit enjoyed in H1 from the equity investment in Parkwind. We trimmed FY net income by 2% (to €349m vs cons €352m) to reflect worse than feared progress YTD, but EPS cuts are prevented by stepped up buybacks.

**...as competitive tension deteriorated in Belgium.** Peers had already highlighted a toughening Belgian competitive backdrop, and this looks borne out by Colruyt's own H1 retail challenges. Retail sales growth of c.3% becomes 1.9% when looking at the eponymous chain (the disproportionate contributor to group profits). H1 retail margin of -75bps YoY confirms the heavy lifting that COLR has had to do in order to grow share by a modest 8bps in H1.

**We see more risks than opportunities from here...** In our mind the biggest structural risk to current industry dynamics is the added pressure that normalised trading in integrated Delhaize stores would imply, as these currently are a soft source of share. There seems to be a clear desire by AD to reinvest in value here, and the Dutch learnings should help develop a more compelling multichannel offering. This is not an immediate, incremental risk, but rather one that should continue to weigh on the investment debate for some time to come.

**...and a disconnected valuation context** as COLR trades on a cal 2018E P/E of 18x and EV/EBITDA of >8x. Yield attractions also remain modest with prospective div yield of 2.5% and FCY of 3.7%.

### Valuation/Risks

**Valuation:** €37 PT = 14.8x cal 2018E P/E, at the low end of history to reflect ongoing margin slippage. **Risks:** Improving Belgian consumer/competition.

| EUR         | Prev. | 2017A   | Prev. | 2018E   | Prev. | 2019E   | Prev. | 2020E   |
|-------------|-------|---------|-------|---------|-------|---------|-------|---------|
| Rev. (MM)   | --    | 9,493.0 | --    | 9,011.0 | --    | 9,296.0 | --    | 9,403.0 |
| EV/Rev      |       | 0.7x    |       | 0.7x    |       | 0.7x    |       | 0.7x    |
| EBITDA (MM) | --    | 722.0   | 708.6 | 701.0   | 731.9 | 707.0   | 747.8 | 716.0   |
| EV/EBITDA   |       | 9.1x    |       | 9.4x    |       | 9.3x    |       | 9.2x    |
| <b>EPS</b>  |       |         |       |         |       |         |       |         |
| FY Mar      | --    | 2.48    | --    | 2.43    | --    | 2.53    | --    | 2.60    |
| FY P/E      |       | 18.1x   |       | 18.4x   |       | 17.7x   |       | 17.2x   |

## UNDERPERFORM

Price target €37.00

Price €44.77^

### Financial Summary

|                 |          |
|-----------------|----------|
| Net Debt (MM):  | (€419.0) |
| Dividend Yield: | 2.5%     |

### Market Data

|                           |                 |
|---------------------------|-----------------|
| 52 Week Range:            | €50.17 - €42.63 |
| Total Entprs. Value (MM): | €6,586.7        |
| Market Cap. (MM):         | €7,005.7        |
| Institutional Ownership:  | 42.3%           |
| Shares Out. (MM):         | 156.5           |
| Float (MM):               | 60.0            |
| Avg. Daily Vol.:          | 309,252         |

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### Price Performance



^Prior trading day's closing price unless otherwise noted.

## Scenarios

### Base Case

- We forecast retail sales growth of 3%, 3.1% and 2.8% in each of the next three years.
- We assume retail margin at 6.0% for 2017/18, falling to 5.8% and 5.7% in the following two years
- We assume annual capex of between €350m and €360m in the next three years, and buybacks of €350m over the next two years.
- Calendarised 2018 EPS: €2.50; Target Multiple: 14.8x; Target Price €37.

### Upside Scenario

- A re-acceleration in the rate of market share gains in Belgium and resumption in margin gains in retail.
- Softer-than-anticipated competitive dynamics in Belgium.
- An incremental €0.5bn share buyback programme.
- Calendarised 2018 EPS: €2.90; Target Multiple: 17x; Target Price: €49.

### Downside Scenario

- Colruyt sees a major slippage in its retail mkt share dynamics.
- Ahold steps up Belgian expansion sharply in the mid-term and uses Delhaize's scale to step up price action.
- Accelerated French retail expansion depresses group margins beyond our current estimates.
- Calendarised 2018 EPS: €2.00; Target Multiple: 12x Target Price: €24.

## Investment Thesis / Where We Differ

- Whilst recognising the superior returns profile of the COLR retail business, we believe a more capable competitor set has made it more challenging for the group to continue to add market share in Belgium.
- We are of the view that these challenges could worsen further as Ahold Delhaize stabilizes pressures at the eponymous Delhaize integrated stores and, in time, pushes a compelling multi-channel offering (in line with the success of Albert Heijn in the Netherlands).
- We believe that the current valuation context largely overlooks the margin risks implicit in the above scenario.

## Catalysts

- FY 17/18 – 19<sup>th</sup> Jun 2018
- 2018 AGM – 26<sup>th</sup> Sep 2018
- H1 18/19 – 11<sup>th</sup> Dec 2018 (est)

## Long Term Analysis

### Long Term Financial Model Drivers

|                         |                   |
|-------------------------|-------------------|
| <b>LT Earnings CAGR</b> | <b>-1% to +5%</b> |
| Sales growth            | <b>1% to 3%</b>   |
| Margin leverage         | <b>-3% to 0%</b>  |
| Financial deleverage    | <b>1 to 2%</b>    |

Table 1: Colruyt H1 17/18 Results

| €m                            | H1<br>15/16  | H2<br>15/16  | FY<br>15/16  | H1<br>16/17  | H1 16/17<br>Pro-forma* | H2<br>16/17A | FY<br>16/17A | H1<br>17/18E | H1<br>2017/18A |
|-------------------------------|--------------|--------------|--------------|--------------|------------------------|--------------|--------------|--------------|----------------|
| <b>Group sales</b>            | <b>4,547</b> | <b>4,631</b> | <b>9,177</b> | <b>4,740</b> | <b>4,300</b>           | <b>4,754</b> | <b>9,494</b> | <b>4,515</b> | <b>4,458</b>   |
| growth %                      | 2.9          | 2.9          | 2.9          | 4.2          | n/a                    | 2.4          | 3.4          | -4.7         | 3.7            |
| <b>Retail</b>                 | <b>3,427</b> | <b>3,722</b> | <b>7,148</b> | <b>3,547</b> | <b>3,555</b>           | <b>3,722</b> | <b>7,319</b> | <b>3,635</b> | <b>3,683</b>   |
| growth %                      | 4.3          | 6.8          | 5.6          | 3.0          | n/a                    | 2.7          | 2.4          | 2.5          | 3.2            |
| <b>Foodservice</b>            | <b>788</b>   | <b>801</b>   | <b>1,589</b> | <b>811</b>   | <b>456</b>             | <b>877</b>   | <b>1,688</b> | <b>479</b>   | <b>463</b>     |
| growth %                      | 2.2          | 4.0          | 3.1          | 9.0          | n/a                    | 2.9          | 6.2          | -41.0        | 1.6            |
| <b>Group EBIT</b>             | <b>259</b>   | <b>249</b>   | <b>507</b>   | <b>262</b>   | <b>248</b>             | <b>221</b>   | <b>483</b>   | <b>236</b>   | <b>232</b>     |
| growth %                      | 6.3          | -1.4         | 2.4          | 1.3          | n/a                    | -0.4         | -2.8         | -9.7         | -6.5           |
| margin %                      | 5.7          | 5.4          | 5.5          | 5.5          | 5.8                    | 4.6          | 5.2          | 5.2          | 5.2            |
| <b>Retail</b>                 | <b>239</b>   | <b>228</b>   | <b>467</b>   | <b>241</b>   | <b>238</b>             | <b>198</b>   | <b>439</b>   | <b>225</b>   | <b>219</b>     |
| margin %                      | 7.0          | 6.1          | 6.5          | 6.8          | 6.7                    | 5.3          | 6.2          | 6.2          | 5.9            |
| <b>Total foodservice EBIT</b> | <b>18</b>    | <b>14</b>    | <b>31</b>    | <b>19</b>    | <b>23</b>              | <b>24</b>    | <b>43</b>    | <b>9</b>     | <b>14</b>      |
| Foodservice margin %          | 2.3          | 1.7          | 2.0          | 2.4          | 5.0                    | 2.7          | 2.5          | 1.9          | 3.0            |
| <b>PBT</b>                    | <b>259</b>   | <b>260</b>   | <b>518</b>   | <b>267</b>   | <b>258</b>             | <b>233</b>   | <b>500</b>   | <b>241</b>   | <b>251</b>     |
| <b>Net income</b>             | <b>182</b>   | <b>182</b>   | <b>365</b>   | <b>195</b>   | <b>183</b>             | <b>169</b>   | <b>364</b>   | <b>179</b>   | <b>179</b>     |
| EPS (€)                       | 1.24         | 1.25         | 2.49         | 1.35         | 1.24                   | 1.13         | 2.48         | 1.22         | 1.23           |

\*Note pro-forma excludes impact of Pro a Pro operations on historic group profits

Source: Jefferies

**Table 2: Colruyt Summary P&L**

| €m                | 2015/16     | 2016/17     | 2017/18E    | 2018/19E    | 2019/20E    |
|-------------------|-------------|-------------|-------------|-------------|-------------|
| Group sales       | 9,177       | 9,493       | 9,011       | 9,296       | 9,403       |
| growth %          | 2.9         | 3.4         | -5.1        | 3.2         | 1.2         |
| <b>EBITDA</b>     | <b>720</b>  | <b>734</b>  | <b>701</b>  | <b>707</b>  | <b>716</b>  |
| <b>margin %</b>   | <b>7.8</b>  | <b>7.7</b>  | <b>7.8</b>  | <b>7.6</b>  | <b>7.6</b>  |
| growth %          | 2.9         | 1.9         | -2.9        | 0.9         | 1.2         |
| EBIT              | 507         | 483         | 474         | 473         | 477         |
| margin %          | 5.5         | 5.1         | 5.3         | 5.1         | 5.1         |
| growth %          | 2.4         | -4.7        | -1.8        | -0.3        | 0.9         |
| PBT               | 518         | 500         | 494         | 495         | 501         |
| <b>Net income</b> | <b>365</b>  | <b>363</b>  | <b>349</b>  | <b>355</b>  | <b>364</b>  |
| <b>EPS</b>        | <b>2.49</b> | <b>2.48</b> | <b>2.43</b> | <b>2.53</b> | <b>2.60</b> |
| growth %          | 1.6         | -0.3        | -1.9        | 4.1         | 3.1         |

Source: Company data, Jefferies

**Table 3: Colruyt Summary Cash Flow**

| €m                           | 2015/16    | 2016/17    | 2017/18E    | 2018/19E   | 2019/20E   |
|------------------------------|------------|------------|-------------|------------|------------|
| <b>Operating cashflow</b>    | <b>641</b> | <b>537</b> | <b>575</b>  | <b>588</b> | <b>603</b> |
| Capex                        | -381       | -376       | -360        | -350       | -350       |
| Acquisitions                 | -3         | -7         | 0           | 0          | 0          |
| Disposals                    | 6          | 198        | 10          | 10         | 10         |
| New shares                   | 17         | 14         | 10          | 10         | 10         |
| Buybacks                     | 0          | -100       | -180        | -170       | -70        |
| Dividend                     | -150       | -169       | -160        | -166       | -170       |
| <b>Net retained cashflow</b> | <b>129</b> | <b>97</b>  | <b>-105</b> | <b>-77</b> | <b>34</b>  |
| Closing net cash             | 433        | 524        | 419         | 341        | 375        |

Source: Company data, Jefferies

## Company Description

Colruyt is a top three Belgian food retailer. The company operates through its eponymous chain a soft discount format which occupies value leadership in the country. In addition, the company also runs a small (but rapidly growing) chain of convenience stores in Belgium as well as supermarkets in France. Whilst retail operations account for 80% of the group, Colruyt also trades in the food service industry (supplying both wholesale retail clients and institutional clients) through major activities in Belgium and France.

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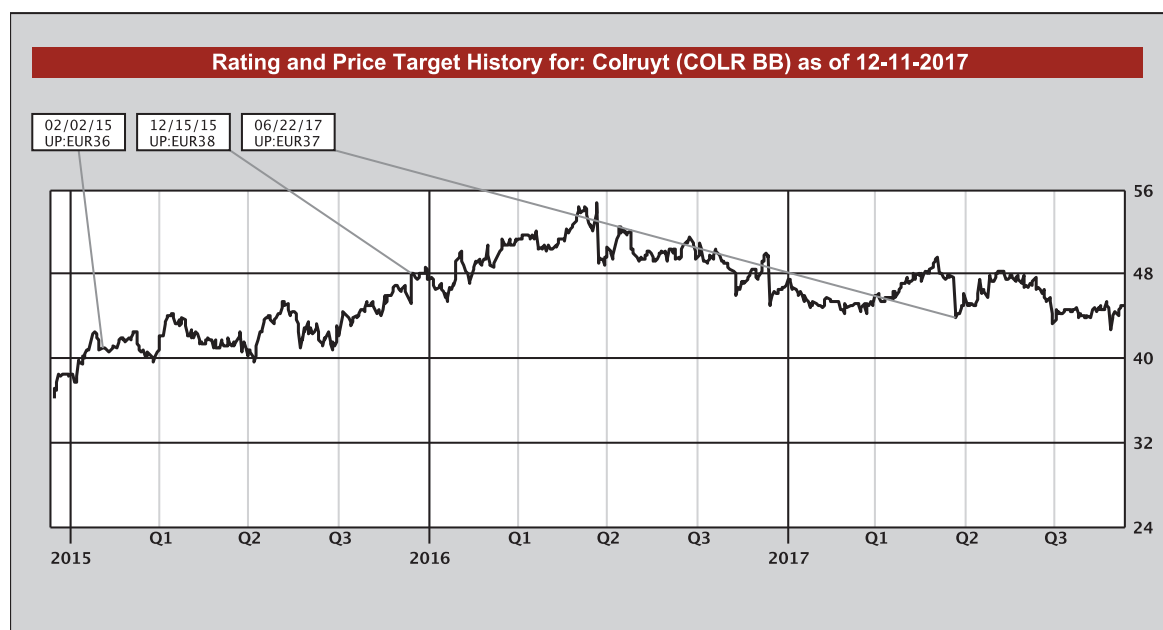
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|--------------|-------|---------|-----------------------|---------|----------------------------|---------|
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| HOLD         | 831   | 40.16%  | 162                   | 19.49%  | 21                         | 2.53%   |
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