

| Sainsbury | |
|------------------------|------|
| Ticker Site BiG | SBRY |
| Ticker BiGlobal Trade | SBRY |
| Ticker BT24 | SBRY |
| Ticker BiG Power Trade | SBRY |
| P/E Ratio 2019E | 9,3 |
| P/BV Ratio | 0,53 |
| EV/EBITDA | 5,33 |

Source: Big Research;

| Price and Performance (Values in GBP) | |
|---------------------------------------|-----------|
| Price | 190,65 |
| 52 week high | 341,80 |
| 52 week low | 185,30 |
| YTD | -28,1% |
| Average daily volume (un) | 9.446.174 |
| Market Capitalization (mn) | 4.217 |
| Beta | 0,73 |
| Dividend | 0,10 |
| EPS | 0,09 |

Source: BiG Research;

| Analysts Consensus (last 3 months) | |
|------------------------------------|----|
| Buy | 5 |
| Hold | 10 |
| Sell | 5 |

Source: BiG Research;

| Financial Data | |
|---------------------|---------|
| Sales (GBP mn) | 29.007 |
| EBITDA (GBP mn) | 1.104 |
| Number of Employees | 116.400 |
| ROA | 1,0% |
| ROE | 2,9% |
| D/E | 0,21 |
| Dividend Yield | 5,77% |

Source: BiG Research;

Notes:

All quotes were updated in Bloomberg at 10h25 of July 12st, 2019.

Relevant Information:

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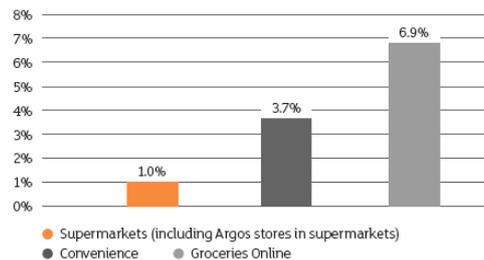
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Sainsbury (Ticker: SBRY)

Description

Sainsbury is a UK based retail company being the third biggest player in the UK. The company operates only in the UK and in the Ireland Republic in the retail segment with the supermarkets and convenience stores, the financial services segment with the Sainsbury Bank, and property investments segment with the joint ventures with the British Land Company and land Securities Group. Sainsbury has approximately 770 convenience stores and offers over 15,000 own brand products. The Sainsbury bank offers products including insurances, credit cards, savings and loans. Sainsbury has 116,400 employees and a market capitalization of GBP 4.2 bn.

Sainsbury's channel performance year-on-year % growth FY2018/19



Source: Company's data

Investment Thesis

Sainsbury is a company that appears to be quite attractive in terms of comparable with a P/E of 9.3x vs 13.7x, a net debt/EBITDA of 0.4x, and a dividend yield of 5.77%. Nevertheless, its revenues suffered a slowdown in 2019 growing only 2% and its EBIT and net income have been decreasing in the last year, -51% and -42% respectively since 2016. This implies a reduction in its margins that are low when compared with its peers, 3.8% vs 6%. YTD the stock fell 28%. Furthermore, although the company is well established in the UK market, which is its main market (it is only present in Ireland Republic besides the UK), this weight in the UK leaves the company really exposed to the Brexit resolution that by now is very uncertain and may have some repercussion especially with the relations with its suppliers. So, for now we see the company to be a good investment.

Investment Case

Cash flows: The company has faced in past years a decline momentum in cash flows. Since 2017, the operating cash flow has decreased 46% to GBP 618 mn in 2019. These weakened cash flows then pressure the company to face the GBP 500 mn of capex that is used in average each year and still pay dividends of GBP 200 mn and still the buybacks.

Optimistic guidance: The company expects to decrease net debt levels GBP 600 mn in the next three years (GBP 200 mn each year). In order to keep the expected capital expenditure of GBP 550 mn and the average GBP 200 mn in dividend payments and some other extraordinary items the company would have to generate a level of cash flow that in the past few years have been struggling to reach it.

Stock Price depressed: Despite appearing to be quite attractive in terms of its peers with a P/E of 9.3x vs. 13.7x the stock fell 28.1% YTD being trading at its lowest values since 1990.

Sainsbury-Asda merger: Asda, an UK discounter owned by Walmart, and Sainsbury were planning on a merger between them in a deal of GBP 7 bn. However, the deal was blocked by the regulator that stated that this merger would push prices for consumers up and reduce the choice of different products on sale stores. This operation may be blocked by the regulator by 10 years.

▲ Environmental, Social, and Governance (ESG)

Sainsbury affirms that they are a company that is concerned about environmental problems and for that is struggling to develop a sustainable business. Some key performances are the zero-waste landfill since 2013, 7,992 tonnes of CO2 saved through their “Greenest Grocer”, and less 1 bn litres of water used when compared with 2005/2006. Also, regarding plastic and packaging, Sainsbury is a member of the UK Plastics Pact and by 2025 the company is committed to eliminate problematic or unnecessary single-use plastic packaging, have 100% of plastic packaging to be reusable, recyclable or compostable, 70% of plastic packaging effectively recycled or composted, and 30% average recycled content across all plastic packaging. For now, it has already reached a reduction of 35% since 2005 in their own brand packaging and about 40% of their packaging uses recycled content. In 2018, Sainsbury was involved in a controversy in which was found pork meat in a vegetarian meat free meatballs food that the company was selling.



Source: Company's data

▲ Management

Mike Coupe served the Sainsbury Group since the 1st of August 2007 as Executive director and since the 9th of July 2014 as the CEO of the group. Moreover, he already was member of the operating board since October 2004. Before joining Sainsbury, Mike Coupe worked as board member in Big Food Group and as Managing director of Iceland Food Stores, as well as several senior management roles at Asda and Tesco. With all these Mr. Coupe was able to develop a wide variety of experience in retail industry in trading, strategy, marketing, digital, online, and multi-site store experience. In 2018 Mr. Mike Coupe made GBP 3.9 mn in total compensation of which GBP 1.3 mn in fixed pay, GBP 0.6 mn in annual bonus, GBP 0.6 mn in share award, and GBP 1.4 in LTIP/Future Builder.

▲ Relative Valuation

| Name | Country | Market Cap (mn) | Currency | P/E 2019 | P/E 2020E | EV/EBITDA | EV/Sales | YTD | Div. Yield | NetDebt/EBITDA | Margin EBITDA |
|------------------------------|-------------|-----------------|----------|----------|-----------|-----------|----------|--------|------------|----------------|---------------|
| SONAE | PORTUGAL | 1.613 | EUR | 10,3 | 9,5 | 13,4 | 1,0 | -0,4% | 5,5% | 6,7 | 7,1% |
| JERONIMO MARTINS | PORTUGAL | 9.106 | EUR | 21,2 | 19,6 | 10,0 | 0,7 | 39,9% | 2,2% | 2,1 | 6,6% |
| TESCO PLC | BRITAIN | 21.330 | GBP | 12,7 | 11,7 | 7,3 | 0,4 | 14,6% | 2,6% | 1,1 | 5,5% |
| CARREFOUR SA | FRANCE | 12.698 | EUR | 13,6 | 11,7 | 11,1 | 0,4 | 5,5% | 2,9% | 5,7 | 3,7% |
| CASINO GUICHARD PERRACHON | FRANCE | 3.741 | EUR | 12,5 | 10,2 | 12,5 | 0,5 | -5,1% | 9,0% | 6,8 | 4,4% |
| KONINKLIJKE AHOLD DELHAIZE N | NETHERLANDS | 24.302 | EUR | 12,7 | 11,9 | 5,4 | 0,4 | -7,0% | 2,9% | 0,8 | 7,4% |
| MARKS & SPENCER GROUP PLC | BRITAIN | 3.668 | GBP | 9,5 | 9,5 | 8,3 | 0,6 | -20,4% | 7,2% | 1,9 | 6,8% |
| DISTRIBUIDORA INTERNACIONAL | SPAIN | 303 | EUR | - | 8,5 | 13,3 | 0,3 | 5,6% | - | 11,2 | 1,9% |
| SAINSBURY (J) PLC | BRITAIN | 4.217 | GBP | 9,3 | 9,3 | 5,3 | 0,2 | -28,1% | 5,8% | 0,4 | 3,8% |
| Average exc. Sainsbury | | | | 13,9 | 12,4 | 9,9 | 0,6 | 7,92% | 4,21% | 3,9 | 6% |

Source: BiG Research

In terms of relative valuation, Sainsbury is quite attractive, with a P/E of 9.3x vs. 13.9x and an EV/EBITDA of 5.3x vs. 9.9x of its peers, and a 5.8% dividend yield vs 4.2% of peers. Although its margins are lower than its peers, 3.8% vs. 6%, its net debt/EBITDA is significantly lower than the average, 0.4x vs. 3.9x. Despite that, the stock was penalized with -28.1% YTD compared to the 7.92% of peers average.

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| Income Statement (GBP mn.) | 2017 | 2018 | 2019 |
|----------------------------|---------------|---------------|---------------|
| Retail | 25824 | 27944 | 28466 |
| Financial Services | 407 | 515 | 541 |
| Property Investments | 0 | 0 | 0 |
| Net Revenues | 26224 | 28456 | 29007 |
| COGS | 24.590 | 26.574 | 27.000 |
| Administrative expenses | 1.207 | 1.415 | 1.733 |
| other income | 215 | 51 | 38 |
| Operating Expenses | 26.012 | 28.040 | 28.771 |
| EBIT | 642 | 518 | 312 |
| Finance income | 34 | 19 | 22 |
| Finance costs | 136 | 140 | 99 |
| Other income/(expense) | (37) | 12 | 4 |
| EBT | 503 | 409 | 239 |
| Income tax | 126 | 100 | 20 |
| Net Income | 377 | 309 | 219 |
| Earnings per share | 0,18 | 0,13 | 0,09 |

Source: Company's data

| Free Cash Flow (GBP mn) | 2017 | 2018 | 2019 |
|------------------------------------|--------------|--------------|--------------|
| Operational Cash Flow | 1.153 | 1.365 | 618 |
| Operating Profit | 642 | 518 | 312 |
| Depreciation and amortization | 628 | 731 | 792 |
| Change Working Capital | 395 | 339 | (555) |
| Taxes | (170) | (161) | (131) |
| Others | (342) | (62) | 200 |
| Investment Cash Flow | (750) | (470) | (474) |
| Capex net | (579) | (507) | (414) |
| Acquisitions | 101 | 135 | 0 |
| Purchase of intangible assets | (110) | (140) | (116) |
| Others | (162) | 42 | 56 |
| Financial Cash Flow | (466) | (244) | (752) |
| Debt change net | (174) | 26 | (458) |
| Dividends payment | (253) | (235) | (247) |
| Buy backs | 0 | (14) | (30) |
| issuance of stock | 6 | 12 | 22 |
| Others | (45) | (33) | (39) |
| Change in free cash flow | (63) | 651 | (608) |
| Cash and equivalents at end | 1.077 | 1.728 | 1.120 |

Source: Company's data

| Balance Sheet (GBP mn.) | 2017 | 2018 | 2019 |
|-------------------------------------|---------------|---------------|---------------|
| Assets | 19.798 | 22.001 | 23.541 |
| Cash & Equivalents | 1.083 | 1.730 | 1.121 |
| intangible assets | 803 | 1.072 | 1.044 |
| Financial services customers | 4.602 | 5.692 | 6.987 |
| Receivables | 643 | 788 | 694 |
| Inventories | 1.775 | 1.810 | 1.929 |
| Property Plant & Equipment | 10.006 | 9.898 | 9.708 |
| Other Assets | 886 | 1.011 | 2.058 |
| Liabilities | 12.926 | 14.590 | 15.085 |
| Short term Debt | 172 | 638 | 832 |
| Long term Debt | 2.039 | 1.602 | 950 |
| Payables | 4.045 | 4.635 | 4.784 |
| Provisions | 186 | 166 | 160 |
| Financial services customers | 4.921 | 6.524 | 7.601 |
| Net retirement benefit obligations | 974 | 257 | 0 |
| Other liabilities | 589 | 768 | 758 |
| Total Shareowner's Equity | 6.872 | 7.411 | 8.456 |
| Total Equity and Liabilities | 19.798 | 22.001 | 23.541 |

Source: Company's data

Income Statement

Net revenues grew 11% since 2017 but only 2% from 2018 to 2019, from GBP 28.5 bn to GBP 29 bn, of which grocery retail sales only grew 0.4%. As for the operating income, EBIT has been decreasing since 2017, having declined 51% from 2017 to 2019. The biggest impact in this slide was from 2018 to 2019 decreasing 40% from GBP 518 mn to GBP 312 mn implying an EBIT margin of 1%. Moreover, net income also decreased significantly, -42% since 2017 and -29% from 2018 to 2019 reaching GBP 219 mn in 2019.

Free Cash Flow

As for the cash flow, the company saw its operations decrease since 2017 by 46% accounting GBP 618 mn in 2019 mainly because of changes in networking capital originated by an increasing in its inventories and the need of the financial services customers and other deposit. Capex was slightly less than previous years, GBP 414 mn. Finally, the financial outflow increased significantly to GBP 752 mn mainly due to repayment of debt of GBP 458 mn and dividends payment of GBP 247 mn. The company also did GBP 30 mn in buy backs and issued stocks in an amount of GBP 22 mn.

Balance Sheet

Regarding the balance sheet, levels of debt decreased 20% reaching GBP 1.78 bn and total net debt accounted GBP 661 mn. The company has a quite low net debt/EBITDA ratio of 0.4x which is way below the peers average of 3.8x.

Earnings

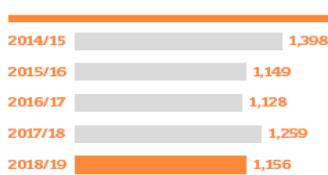
The company release a trading statement for the 1Q of 2020 in which reported an outlook for sales to decrease 1.2% with a decrease in lfl of 1.6%. Regarding the segments, the outlook is to grocery sales be down by 0.5% while merchandising sales to decline by 3.1% and clothing sales by -4.5%.

Guidance

For the FY 2020 the company's guidance for the retail segment is to open 2 new Sainsbury supermarket stores, around 10 convenience stores, and about 10 Argos stores in supermarkets reaching that way 290 Argos stores. As for the financial services, the guidance of the company is to reach an underlying operating profit of GBP 45 mn of which GBP 10 mn are benefits from a change in transfer pricing between Argos and Argos Financial services, transition costs are expected to be around GBP 30 mn and finally, the company expects to do a capital injection into the bank of GBP 80 mn. The Capex is expected to be around GBP 550 mn per annum over the medium term. Moreover, the company expects to reduce net debt by GBP 200 mn each year for three years.

Retail operating cash flow (£m)

Definition: Retail cash generated from operations after changes in working capital and pension contributions, and before exceptional pension contributions



Source: Company's data

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▲ Main segments

Sainsbury operations can be distinguished by four segments: Retail - food, Retail - General Merchandise and Clothing, Financial Services, and Property Investment.

Retail: GBP 28 bn in revenues (+2% growth); GBP 692 mn underlying operating profit; 2% margin. In the retail segment the company divide its operations by categories such as groceries/food and general merchandising and clothing. These categories can be described as follows:

Retail – Food: Sainsbury is the brand of the supermarket stores that are now 605 supermarkets opened, 807 convenience stores, and an online store that has 250,000 orders online each week. The brand has more than 15 thousand own brand products.

Retail – General Merchandise and Clothing: This segment is present through Argo stores which sell a wide variety of products from electronics to toys products in more than 800 stores and online store that reached 1 bn visitors. Another brand is Tu which are clothing stores that are about 400 stores opened with more than 2500 items of clothing that are sold in stores and in online stores. Finally, there is Sainsbury Home and Habitat, that are brands focused in house products. The first one is a brand that sells home and garden products in about 400 stores with 80% of in-house design categories. The second, is focused in home design with 1 London Habitat design studio and 16 stores in the UK.

Financial Services: GBP 515 mn in revenues (+6% growth); GBP 51 mn underlying operating profit; 6% underlying profit margin. In this segment the company operates with Sainsbury Bank and Argos Financial Services entities. Sainsbury Bank has more than 1700 ATMs, more than 230 travel money bureau, and more than 8 financial products.

Property Investment: In this segment the company operates with joint ventures with The British Land Company and Land Securities Group.

Source: Company's data



Source: Company's data

▲ Supply Chain & Logistics

Sainsbury has sources products from over 70 countries and in some part has its own source of supplying, having invested in British farming and is involved in 12 research programs to improve agricultural productivity and reduce the environmental impact of British farming. As for the logistics Sainsbury has 33 distribution centres that supply stores and online stores and Argos has a hub and Spoke logistics (centralized, integrated logistics system that is designed to control and keep costs down) network to fulfill fast track orders.

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▲ M&A

Nectar: Before Nectar, the last acquisition was in 2016 and only in 2018 the company returned to a acquisition strategy with Nectar, a loyalty program card that allows its customers to earn nectar points by shopping in the Sainsbury stores and then spend it in travel, family, or online products. Sainsbury acquired all the Nectar business and assets for GBP 60 mn.

▲ Risks

Brexit: All the major operations of Sainsbury are concentrated in the UK so, the uncertainty about Brexit and how will be the relationship with EU in case of a no-deal Brexit can difficult the supply management with European suppliers, originate delays at boarders reducing product availability, cost impact associated with tariffs, loss of trade and currency, and create barriers if the company decides to follow an international expansion.

Political & Regulation: Even more there is an increasing in regulation and control in the business segments in which Sainsbury is present, resulting in an additional cost, which may reduce its margins.

Competition: Sainsbury has a well-diversified portfolio with the different types of business, from banking to grocery, to electronics, to clothing and home products, so it faces several competitors that most times are only specialized in that type of business.

▲ Graph

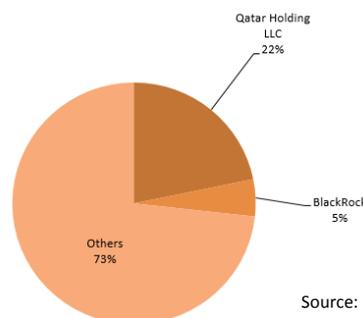


Source: BiG Global Trade

▲ Calendar

7th of November 2019: Interim results announcement

▲ Shareholders



Source: BiG Research

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