

Diageo plc

CORE HOLDING*

Recommended since 03.07.18

14.08.2023



Country GB	Market capitalization (bn) GBP 75,6	Perf. since reco. (%)
Sector Food & Beverage	Free float 97,1%	Diageo plc 23,0
Factset DGE-GB	Closing price GBP 33,56	Sector 14,3
ISIN GB0002374006	ESG Risk score* 19,3 Low risk	

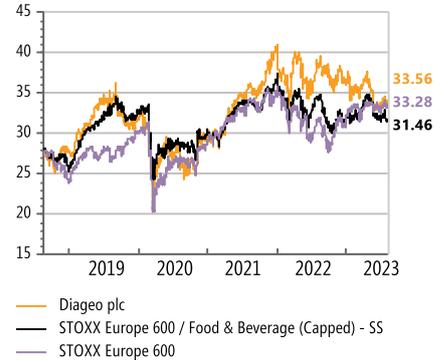
*From 2015, B&Cie separates its investment recommendations into Core Holdings (higher organic growth potential, high free cash flow, ROCE in excess of the cost of capital and balance sheet efficiency throughout the cycle) and Satellite Recommendations, which do not meet the above criteria but are likely to outperform in the short-to-medium term.

Profile

Global leader in spirits by volume, sales and EBIT, with a market share of 26% (vs. 17% for Pernod Ricard and 9% for Bacardi). Sales are evenly distributed: one quarter in Europe, one third in North America and 40% in emerging markets. Brands include whiskies (Lagavulin, J.Walker, Bushmills, J&B, etc.), vodka (Smirnoff), gin (Tanqueray), Tequila (José Cuervo), rum (Captain Morgan), liqueur (Baileys) and beer (Guinness). Owns 34% of Hennessy (cognac).

Market - competition - positions - barriers to entry

Diageo's leading position is built on its comprehensive portfolio of brands, a retail network spanning all markets, and strong positions in the premium segment, emerging markets and the US. A global presence and a healthy balance sheet make it the most defensive player in a resilient sector. Targeted acquisitions (emerging markets) and refocusing on its core business (sale of wine business) have helped speed up profitable growth!



Source: Factset

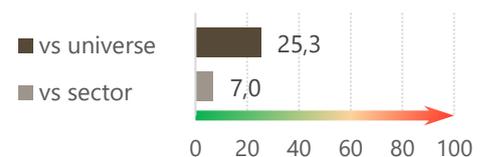
Investment case

- The global spirits market has returned to a steady pace between 2017 and 2019. Europe and the US benefited from solid demand for scotch, gin and tequila. The tequila boom in the USA (José Cuervo & Don Julio brands), the revival of gin (Tanqueray) in the USA and Europe combined with better dynamics in cognac and whisky in emerging markets where premiumization is playing a full role (new middle classes). In addition, the good health of travel retail (air traffic +3/4% per year) has helped. In this context, Diageo's sales growth accelerated and its positioning on the most buoyant categories (price mix), its innovations and a cost reduction plan boosted its operating profitability.
- Post fiscal year 2020 (ending June 30) and the impact of Covid, Diageo recorded a rebound in its sales and operating performance. The momentum remains solid in 2023 with organic growth of +6% reflecting the recovery of the on-trade in the US and Europe, the resilience of the off-trade, the return of travel retail and market share gains (growing share of spirits in total alcoholic beverages). EBIT reached a record £4.60bn / margin at 30.7% thanks to an improved channel mix and operating leverage which compensated well for MP/freight cost inflation.
- In this context, Diageo exceeded its medium-term guidance 2023-25 of +5/7% organic sales growth per year and +6/9% EBIT. Management confirms a more demanding comparison base for H1 FY2024 and therefore a normalization of the commercial dynamics in the US market (modest growth) as well as continued, albeit more moderate, growth in Europe, while Latin America is rebounding and Asia could hold some positive surprises (fewer restrictions in China). Its operating margin should hold up thanks to higher volumes, a more favorable distribution mix, continued premiumization and a less penalizing currency effect. The quality of the H2 results (resilience of volume to price increases) and a rather favorable outlook allow Diageo to offer some visibility in a context of global economic slowdown and inflationary pressures.

ESG - risks and key points

- Thanks to its average exposure and serious approach to managing the relevant issues, Diageo is at low risk of suffering significant financial impacts as a result of ESG factors.
- Diageo is exposed to risks associated with the social costs of excessive alcohol consumption and government efforts to reduce those costs through taxation.
- Legislation on alcohol and dominant position -> risks linked to business ethics. Water is a necessary ingredient in preparing beverages.

ESG risk vs. universe & sector (percentile)*



Source: Sustainalytics

Valuation** in GBP

Current price	Value Bordier Scenario
33,6	38,6

Our scenario assumes UK 10-year yields of 3%, a further rebound in sales in 2023, targeting 10% growth in 2026, and a margin reaching 32.5% over this timeframe as a normative long-term level.

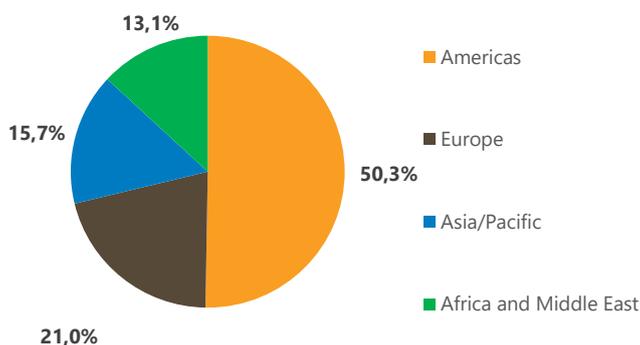
**) The theoretical value reflects the company's business model, our baseline growth and profit scenario and market data, exogenous to the company (risk-free rate and equity risk premium). It does not in itself constitute a target price.

"Bordier Core Holding" indicators

In millions of GBP	2021	2022	2023e	2024e	2025e
Sales revenue	12 733	15 452	17 113	17 489	18 539
Sales growth %	8,3%	21,4%	10,7%	2,2%	6,0%
<i>o/w organic</i>	16,0%	21,4%	6,0%	5,0%	6,0%
<i>o/w perimeter</i>	0,0%	0,2%	0,0%	0,0%	0,0%
<i>o/w forex</i>	-7,7%	-0,2%	6,2%	-2,8%	0,0%
EBITDA	4 193	5 289	5 850	6 066	6 504
% of sales	32,9%	34,2%	34,2%	34,7%	35,1%
EBIT	3 746	4 797	5 305	5 509	5 914
% of sales	29,4%	31,0%	31,0%	31,5%	31,9%
Adjusted EPS	1,16	1,40	1,70	1,77	1,90
Adjusted EPS growth	91,0%	20,7%	21,1%	4,1%	7,8%
FCF/Sales	19,9%	26,7%	19,9%	20,8%	21,4%
Dividend yield	2,2%	2,3%	2,5%	2,7%	2,9%
ROCE - WACC	0,0%	0,0%	0,0%	0,0%	0,0%
ROE (%)	38,4%	41,7%	39,5%	33,7%	30,5%
Gearing	142,0%	144,4%	102,7%	73,9%	51,6%

Source: Factset, Bordier estimates

Sales breakdown - 06/2023



Ratios

	Stoxx Europe 600		
	Diageo plc	Sector	Market
PE (x)***		Food & Beverage	Stoxx 600
2022	23,3	20,5	13,1
2023e	19,8	19,6	13,2
2024e	19,0	17,8	12,4
P/B (x)***			
2022	10,5	3,4	2,0
2023e	7,6	3,0	1,8
2024e	6,2	2,9	1,7
Beta (2Y, daily) vs market:			0,77

***) The valuation ratios set out are provided for information only. They do not constitute the criteria based upon which Core Holdings are selected, and may present significant premi-ums representing the quality of the company's business model.

Governance and ownership structure

Since 2012 CEO Ivan Menezes, CFO K. Mikells.

Key shareholders (if any):

Capital Research 5.1%; MFS 3.1%.

Agenda

H1-FY 2024 results on 25/01/2024.

Any special characteristics of ownership (multiple voting rights, controlling holding company, shareholders' agreements, etc.):

None.

Glossary

ESG Risk Score

At B&Cie, we take particular care to ensure that the companies in which we recommend investing are sustainable. Accordingly, our selection process takes account of risks relating to environmental, social and governance (ESG) issues. This approach is underpinned by research from Sustainalytics, the global leader in ESG and corporate governance analysis, whose methodology aims to identify major controversies and risks and assess a company's ESG risks relative to both its sector and the investment universe as a whole. The corresponding score is expressed as a percentile: the lower the overall risk score, the lower the risk within the investment universe.

b-Digital, b-Transition & b-Well

Over and above the conventional geographical and sectoral approaches to asset management, at B&Cie we believe the world of tomorrow is being shaped by structural trends. We have identified three main megatrends: ongoing digital globalisation of the economy; economic transition, particularly in the energy sector; and the quest for wellness. We believe selecting and investing in companies that play an active role in these transformations should lead to more resilient portfolios that generate higher long-term returns. Our investment recommendations in the digital globalisation space are labelled "b-Digital", those in the economic transition space "b-Transition" and those in the wellness space "b-Well". A given recommendation may fall under more than one theme, in which case it will carry the relevant matching labels.

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