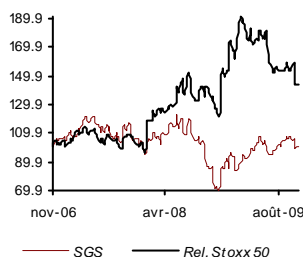


26/11/2009



Source: Natixis Securities

## Support services

# SGS

SGS.N / SGS@VX

Switzerland

**Add**

## A mitigated reflection of the global economic climate

Price	11/25/2009	CHF1,298.00
Target		CHF1,463.00
Upside		12.7%

Performance	1m	12m	1 Jan
Absolute	-5.3%	35.1%	18.0%
Sector	0.6%	39.2%	33.4%
Stoxx 50	1.9%	20.9%	22.1%

12-month high/low	CHF1,400.00 / CHF908.50
SMI	6422.2
Stoxx 50	2521.3

Market capitalisation	CHF10.2bn
Free float	55.1%
Von Finck Family	15.1%
Daily volume	CHF23m

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- **Swiss group SGS is the world's leading certification and inspection company** thanks to its vast geographic networks, its positions on most sectors of the economy and its global brand.
- The strategy implemented by chairman Sergio Marchionne has made the trade-related activities less prominent and **refocused the group more on upstream activities involving consulting, testing and analysis services**. This refocusing drive has boosted organic revenue growth substantially and kept the operating margin growing steadily.
- **SGS' growth has lost a lot of momentum for the first time in 5 years**, even though the crisis is having a relatively mitigated impact on the group. Business has slowed down in the Oil-Gas-Chemicals, Industrial and Automotive divisions. The Minerals division saw its revenues plummet in H1 09 as demand for commodities collapsed.
- **2009 is set to show modest revenue growth**, undermined by another unfavourable currency effect (strong Swiss franc), **and a slight dip in operating margin and earnings**.
- Although it is not a cyclical company as such, **SGS will probably benefit in 2010 and 2011 as the climate improves for a certain number of global sectors**: refining, construction, mining, automotive. The group's other divisions, meanwhile, are far more recurring in nature: Certification, Agriculture, Consumer Testing, Environment, Governments & Institutions.
- **The group's long-term growth will be driven by two factors (09/11e EPS CAGR of 7%): 1/ the extension and increasing complexity of regulations**, resulting in a growing number of regulated activities and thus of fields that need to be controlled; **2/ a continued shift towards consulting and analysis services**.
- Although it is trading at a premium over the sector's other listed players, we believe SGS harbours upside potential (impact of the recovery, resumption in external growth). **We are initiating coverage of the stock with an Add rating and a DCF-based target price of CHF1,463.**

Close on 31/12	Turnover (CHFm)	Reported net profit (CHFm)	Adjusted EPS (CHF)	Chg. EPS (%)	PE (x)	EV/EBIT (x)	P/CF (x)	Net yield (%)
2008	4,818	692	77.98	16.5	-	-	-	-
2009e	4,831	571	77.86	-0.2	16.7	12.8	12.0	3.2
2010e	5,058	620	82.99	6.6	15.6	11.9	11.1	3.4
2011e	5,365	670	89.68	8.1	14.5	10.8	10.1	3.6

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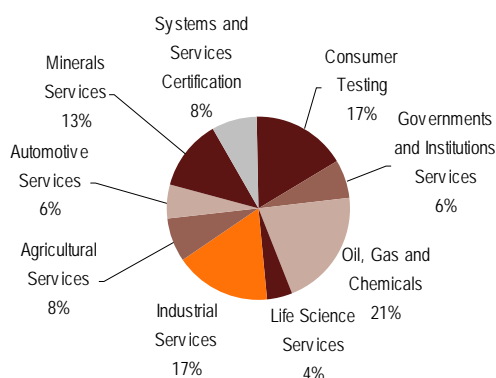
## Company profile

SGS is the world's leading certification and inspection company. Its business is split into about ten divisions. The biggest contributors to operating profit are the Oil&Gas, Consumer Testing and Industrial divisions. The previously predominant international trade activities are being scaled back as the group expands its value-added services: upstream operations, testing, analysis and consulting. This shift has boosted the group's sales growth and resulted in the highest operating margin in the sector. The group boasts a very healthy financial situation. Its net cash position should enable it to make large-scale acquisitions as soon as the climate begins to improve.

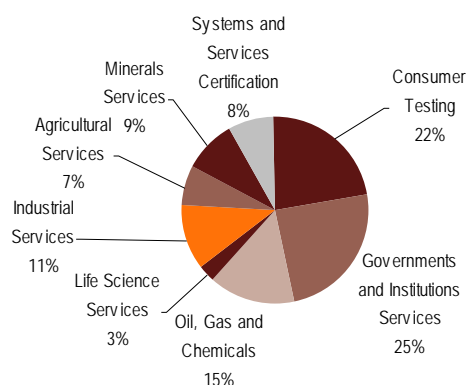
## Recent events

Earnings per share rose by 1.5% in H1 09 to CHF35.23 before exceptionals. Revenues remained almost flat at CHF2.327bn after negative currency effects (organic growth reached +4.1%). The operating margin improved a little to 16.2% from 16.1%. Net profit before exceptionals was flat at CHF264m.

## Sales 09e



## Operating profit 09e



## Opportunities / Strengths

- SGS boasts a very vast geographic network and a global brand.
- Its status as the world's leading player gives it access to a client base of multinational companies keen on having the same provider worldwide.
- Its market is being buoyed up by the extension and increasing complexity of regulations.
- Fluctuations in the climate have a mitigated impact on the company.

## Weaknesses / Threats

- Some of its activities are nonetheless sensitive to the climate: minerals, automotive, energy, construction.
- SGS's operating margin seems to have reached a plateau.
- There are some political and group liability risks.
- External growth, a pillar of the group's strategy, can pose an integration risk.

## Share ownership

	Shares	Votes
Von Finck Family	15.1%	15.1%
EXOR	15.0%	15.0%
Allianz SE	7.4%	7.4%
Own shares	4.5%	4.5%
Bank of NY Mellon Corp.	3.0%	3.0%
Free float	55.1%	55.1%

## Diary dates

01/15/2010 Earnings 2009

## Investment summary

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**SGS'S leadership status is well-established in the inspection and certification sector.**

Its dominant position is attributable to its size and geographic network but also to the range of activities in which it operates, its profitability and its excellent financial situation. With its 10 divisions, it applies its expertise in most sectors of the economy with the exception of the marine and construction sectors. It has a more evenly-balanced portfolio than Intertek, the no.3 listed player in the sector, even though the Oil-Gas-Chemicals division generates over 20% of its earnings. But it seems to have a more cyclical profile than Bureau Veritas (Reduce, target price €34), the sector's no.2, as it provides services to the minerals, industrial, automotive, oil, gas and chemicals sector.

**The strategy implemented by chairman of the board Sergio Marchionne has refocused the group more on value-added upstream consulting and analysis services and has thus made SGS less sensitive to international trade.** Organic revenue growth has been rising steadily and the operating margin improved up until 2008. The von Finck shareholding family recently reduced its 25% stake in SGS to 15% on 11 November 2009. It is now on a par with Exor (former Ifil).

**The group operates in a sector that will remain buoyant for the long term thanks to the trend towards increasingly widespread and complex regulations.** This trend is enhanced further by the outsourcing of control measures by public and semi-public bodies, by the liberalisation of the market and by an almost-permanent external growth drive as the global market is extremely fragmented. **Moreover, there is little competition** as there are only three truly international players. Last of all, **business is highly recurrent** for two reasons: 1/ a considerable proportion of contracts are long-term, 2/ the economic climate has only a mitigated impact on business operations, and some of them are hardly sensitive to the climate at all.

Nonetheless, 2009 will probably be the first in ten years to show a slight dip in margins and earnings on account of a sharp slowdown in 5 of the group's 10 divisions. **We see organic revenue growth returning in 2010 and then picking up in 2011.** Although the group's operating margins are the highest in the sector, we believe they will continue improving in 2010 and 2011 thanks to cost-savings generated in 2009. **We see EPS growth reaching +7% in the medium term.**

**Our valuation works out at CHF1,463 per share.** This is based on a discounted cash-flows model and implies attractive upside potential on the stock (13%). It also reflects a bigger premium over Intertek and Bureau Veritas, easily justified by SGS'S leadership qualities. **We therefore initiate coverage of the stock with an Add rating.**

## 1. Attractive upside potential

We are initiating coverage of SGS with an Add rating and CHF1,463 target price calculated using a discounted cash-flows model. Our rating is based on the group's potential to beat the GDP growth rate over the long term and its justified premium over the sector.

### A justified premium over the sector

SGS is the leader of a very fragmented certification, verification and inspection market, with an estimated global market share of around 6%. There are five players in the world with revenues of over a billion euros and a dozen with over €500m.

The sector's three listed groups are the UK's Intertek (not covered), France's Bureau Veritas (Reduce, target price of €34) and SGS (Add, target price of CHF1,463). SGS is the most liquid of the three thanks to its size. It is also the only one to boast a solid balance sheet with a free net cash position (€217m estimated at end-2009). But it appears to be more sensitive to business cycles as it is exposed to the minerals segment (14% of 2008 revenues). Intertek, the smallest of the listed players, is probably the least cyclical with almost half of its EBITA generated from the consumer goods segment. Bureau Veritas, meanwhile, like Intertek, has a high level of debt (gearing of 130.6% in 2009) and its EBITA margin is also the lowest of the three (less involved in minerals and consumer goods).

SGS's multiples reflect a premium of about 12% over the other stocks in the sector. This seems justified given the group's global leadership status and its excellent financial situation.

Table 1: Financial ratios of listed inspection-certification groups (at 25/11/09)

2008	BV	SGS	Intertek
Market capitalisation	€3.7bn	CHF9.7bn	£2.0bn
Revenues	€2.549bn	CHF4.818bn	£1.003bn
EBITA margin as % of revenues	15.20	16.81	15.52
Gearing as % of shareholders' equity	289	-13	164

Source: Companies

Table 2: Valuation multiples of listed inspection-certification groups (at 25/11/09)

x	Cap. (bn)	Rev. 08 (m)	EBITA margin 08 (%)	PE 11e	EV/EBITA 11e	EV/EBITDA 11e
SGS (CHF)	9.7	4 818	16.81	14.5	10.8	8.3
Bureau Veritas (€)	3.7	2 549	15.20	11.9	8.4	7.2
Intertek (£)	2.0	1 003	15.52	13.0	9.0	7.2
Sector average			15.84	13.1	9.4	7.6

Sources: Natixis Securities estimates, Thomson One/First Call

## DCF valuation

Table 3: DCF assumptions

Discount rate %	
Risk-free rate	3.28
Market premium	6.01
Beta	1.00
Cost of capital	9.29
Net cash position 2008 (CHFm)	239
WACC	9.29

Source: Natixis Securities estimates

We have used a beta of 1x owing to the recurring nature of the group's activities and its low-risk profile. Our WACC is equal to the cost of capital since the group is in a net cash position.

Table 4: Discounted cash-flows

CHFm	2008	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e	2018e
Revenues	4,818	4,831	5,058	5,365	5,642	5,783	5,927	6,075	6,227	6,383	6,543
<i>Change (%)</i>		0.3	4.7	6.1	5.2	2.5	2.5	2.5	2.5	2.5	2.5
<b>EBITA</b>	<b>810.0</b>	<b>810</b>	<b>857</b>	<b>924</b>	<b>986</b>	<b>1,010</b>	<b>1,036</b>	<b>1,062</b>	<b>1,088</b>	<b>1,115</b>	<b>1,143</b>
<i>Change (%)</i>		0.0	5.9	7.7	6.7	2.5	2.5	2.5	2.5	2.5	2.5
<i>Operating margin (%)</i>	16.8	16.8	17.0	17.2	17.5	17.5	17.5	17.5	17.5	17.5	17.5
Taxes	-190	-202	-214	-231	-246	-253	-259	-265	-272	-279	-286
<i>Tax rate (%)</i>	-23.5	-25.0	-25.0	-25.0	-25.0	-25.0	-25.0	-25.0	-25.0	-25.0	-25.0
<b>EBITA after tax</b>	<b>620</b>	<b>607</b>	<b>643</b>	<b>693</b>	<b>739</b>	<b>758</b>	<b>777</b>	<b>796</b>	<b>816</b>	<b>837</b>	<b>857</b>
Amortisation & impairment	180	217	228	268	282	289	296	304	311	319	327
Change in WCR	-22	-24	25	27	28	29	30	30	31	32	33
Investments	-290	-290	-303	-295	-282	-289	-296	-304	-311	-319	-327
Operating cash-flow	<b>488</b>	<b>511</b>	<b>592</b>	<b>693</b>	<b>768</b>	<b>787</b>	<b>806</b>	<b>827</b>	<b>847</b>	<b>868</b>	<b>890</b>
<i>Change (%)</i>		4.7	16.0	16.9	10.8	2.5	2.5	2.5	2.5	2.5	2.5
<b>Discounted cash-flows</b>		<b>506</b>	<b>537</b>	<b>575</b>	<b>583</b>	<b>547</b>	<b>513</b>	<b>481</b>	<b>451</b>	<b>423</b>	<b>397</b>

Source: Natixis Securities estimates

We have estimated infinite growth at 2.5%, i.e. a price effect of +1% and a volume effect of +1.5%. This 2.5% growth rate is justified by the highly favourable trend towards increasingly widespread and complex regulations, which should enable the group's revenue growth to slightly beat the GDP growth rate over the long term.

Capex is already at a high level for the sector and should remain relatively stable in the short term on account of a rather sluggish economic climate. Moreover, we believe the group will continue efforts to reduce its WCR.

**Table 5: Target price calculation**

CHFm	
Sum of discounted CF	5,012
Residual value	5,988
Infinite growth rate (%)	2.5
<b>Total</b>	<b>11,000</b>
2008 net cash position	239
Minorities	-308
Valuation	10,931
Number of shares	7,473,436
Valuation per share (CHF)	1,463

Source: Natixis Securities estimates

Our discounted cash-flows model yields a valuation of CHF1,463, which we have adopted as our target price, harbouring 13% upside. We are initiating coverage of SGS with an Add rating.

## 2. A buoyant market for the long term

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The global certification, inspection and testing market can be estimated at €45bn. It is a structural growing and relatively protected market. It is also only moderately affected by changes in the economic climate.

### A favourable climate

A number of favourable factors should boost growth in SGS's activities.

*Increasing regulations* governing most economic activities are forcing companies to comply with rules and ever more frequent controls, offering new outlets for inspection and verification groups. One recent example is the US regulation concerning toys and other consumer goods (Consumer Product Safety Improvement Act, voted in August 2008). Protectionism in disguise can also result in a surge in standards.

*Outsourcing:* inspection and verification measures are traditionally carried out by public authorities or insurance groups. These traditional players are increasingly passing the work on to specialist groups. This is the case especially for certification and for government services.

*The liberalisation of the market* also has a positive impact in that it enables private players to take on work that was previously carried out by the public authorities. In the automotive sector, SGS is now in charge of driving tests in certain countries (Ireland) as well as the examinations taken by London's taxi drivers. In the field of urban development, the sector responsible for controlling the compliance of building permits in the UK was privatised in 2007.

*The high degree of fragmentation in the market* (SGS has a market share of only 6%), especially in inspection, certification and environment, allows for a steady stream of external growth operations which add a few growth points each year.

### Limited competition

There is little competition between players operating in the certification, inspection and testing sector for a number of reasons.

*Barriers to entry are high* and make it difficult for new players to move in. First of all, these are technical operations so companies need to hire renowned specialists. Moreover, where control operations are concerned, a reputation for integrity and a long track record in the business (i.e. a brand) are particularly important. Last of all, the network must be dense enough, at least on a regional level, to be accessible to a sufficiently large number of clients and must offer them a diversified range of services allowing for scale economies. The sector's main players operate through hundreds of geographic sites (offices and laboratories).

*The recurring nature of SGS's operations* also ensures a minimum threshold for the group's activities. Without officially binding the clients, they do encourage them to keep the same provider from one year to the next. This recurrence is particularly prominent in inspection (control of technical facilities), certification (compliance of systems with ISO standards) and

government services (inspection of goods involved in international trade operations), where contracts last several years.

*A small number of international players:* there are 10 companies generating more than €700m revenues, of which only 3 are listed and truly international players.

**Table 6: Main characteristics of the sector's three listed players**

	SGS	BV	Intertek
Number of offices or laboratories	1,000	900	270 labs
Number of staff	55,000	40,000	11,900
Number of divisions	10	8	6
Business lines:			
Marine	No	X	No
Industry	X	X	X
Automotive	X	No	No
Construction	No	X	No
Consumer goods	X	X	X
Mining	X	X	X
Energy, chemicals	X	X	X
Systems & Certification	X	X	X
Inspection	No	X	X
Agriculture	X	No	X
Environment-Security	X	X	No
Government Services	X	X	X
Life Sciences	X	No	No

Sources: Companies

The other operators have a more regional profile and are generally subsidiaries of non-profit associations or organisations.

**Table 7: Main characteristics of the sector's other unlisted players**

	Dekra	TÜV Süd	Det Norske Veritas	TÜV Rheinland	Lloyd's Register	TÜV Nord
Nationality	German	German	Norwegian	German	British	German
Shareholder	Dekra e.V (association)	TÜV Süd e. V. (association)	Private foundation	TÜV Rheinland Berlin Brandenburg Pfalz e.V (association)	Non-profit organisation (charity)	TÜV Nord e.V (association)
Revenues	€1.400bn	€1.300bn	€1.100bn	€1.000bn	€800m	€700m
Specialities	- Automotive - Industry - Personnel	- Automotive - Industry - Products - Chemicals - Personnel	- Marine - Industry - Energy - IT technology	- Automotive - Industry - Certification	- Marine - Energy - Transport - Certification	- Mobility - Energy - Certification

Sources: Companies

## A less cyclical profile

Operations carried out by inspection and certification companies are not cyclical as such, since recurring activities account for a significant share of their revenue bases. This is particularly true for inspection proper, as this involves checking that technical facilities (lifts, electricity, pressure equipment, fire safety) comply with regulatory standards on a regular basis. Contracts are therefore multi-year or annual but are renewed automatically.

Certification consists of certifying that management systems (quality, security, environment, etc.) used in companies comply with international, national or industry standards, especially ISO standards, and is a recurring activity by nature. Some 90% of contracts are multi-year since the certification process generally follows a three-year cycle.

Similarly, government services (inspection of import operations) are provided on the basis of long-term contracts.

Depending on the economic sector in question, the other services provided by inspection and certification companies are more or less sensitive to economic cycles.

The most sensitive is the metals sector. Testing operations are not very sensitive to changes in volume but, on the other hand, the sector is penalised by the discontinuation of mining operations.

Agricultural services feel the effects of trends in global trade but this is mitigated as they are paid for on a per-service basis. But the degree of sensitivity diminishes as groups provide increasingly upstream services (precision agriculture).

In consumer goods, services are provided along the entire production and supply chain. They are not very sensitive to changes in sales volumes. However, the number of items does have an impact, as do changes in regulations.

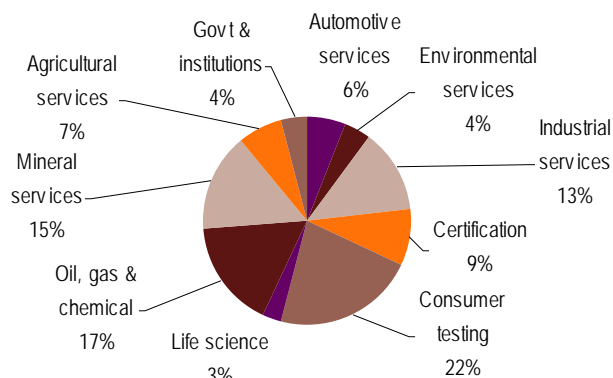
In the marine segment, contracts are long-term when it comes to classifying and certifying active vessels (at least 5 years). The impact of the economic climate is therefore felt on new vessels but it is a deferred impact since the construction of a vessel is spread out over several years.

In the other sectors (automotive, construction, energy), there is the same dichotomy between the stock of goods or facilities that need to be controlled (regulatory inspection of automobiles, compliance of building works,) and flows of new goods or facilities (commercial vehicle inspections, follow-up of real estate assets, services carried out during the investment phase) generated depending on the economic climate.

### 3. A global offer

SGS has segmented its activity into 10 divisions, which broadly equate to economic sectors. However, two thirds of operating profit stems from four of the divisions: Minerals, Oil, Gas and Chemicals, Consumer testing and Industrial services. Aside from comfortable operating margins, they also enjoyed growth levels of +10% to +20% till 2008. That said, they were hit by the economic crisis more sharply than the other divisions at the start of 2009.

Chart 1: Operating profit by division



Source: Company

### Agriculture: upstream to downstream

Table 8: Operating performances for the Agricultural services division

CHFm	2006	2007	2008	H1 09
Sales	316.9	356.5	358.3	176.3
Organic growth for sales (%)	+5.8	+4.3	+8.3	+9.2
Operating margin (%)	12.4	13.4	15.6	15.7
Recent acquisitions	n/a	Mid Iowa Grain (USA) Mid West Seed Services (USA)	Central Analytical Laboratories (S. Afr.) Alvey Group (USA)	n/a

Source: Company

Much of the division (80% of sales) still consists of trading, undertaken in Europe, Africa and Asia. Grain trading is still substantial (42% of sales) in this division. The group intervenes at the level of the supply chain, in order to improve its efficiency and to help its clients conform to regulatory demands in terms of traceability. It has laboratories to respond to food requirements in terms of security and offers temporary storage services to reduce sales volatility between harvests. Variations in raw materials prices do not impact sales, as the group is billed at the service provision. We note a concentration of trading around large groups, owing to the financing difficulties in this sector.

However, the product mix plays positively on the operating margin. This applies in particular to upstream (which represents 20% of sales). The group intervenes there at the production level. This involves soil analysis, seeds, assessment of needs in fertiliser, irrigation, all that can be understood in terms of 'precision' agriculture (mapping to allow GPS management). The group works to preserve quality and to manage the state of the soil and harvests, and to develop new types of seeds. It aids farmers to adopt precision techniques to maximise land utilisation. It is also active in assessment of the next generation raw materials aimed at hydrocarbons. This business is mainly American.

This division is the 6<sup>th</sup> in the group in terms of its contribution to earnings. Despite the steady rise in its operating margin, its profitability is below the group's.

In 2009, organic growth remained strong in H1 despite the limitation on loans by banks, notably thanks to sound market conditions for raw materials and the development of packages of services in land, which has also underpinned the operating margin.

## Minerals: sensitive to raw material demand

Table 9: Operating performances for the Minerals division

CHFm	2006	2007	2008	H1 09
Sales	467.0	559.8	662.9	261.5
<i>Organic growth for sales (%)</i>	<i>+16.1</i>	<i>+17.3</i>	<i>+21.4</i>	<i>-8.4</i>
<i>Operating margin (%)</i>	<i>17.2</i>	<i>17.5</i>	<i>18.9</i>	<i>14.1</i>
			Wamtech (Austr.)	n/a
	n/a	n/a	Holman Wilfey (UK)	
			Geostat Syst. (Can.)	
			CEM (Can.)	
Recent acquisitions				

Source: Company

This division makes most of business in three almost equal zones: Australia, North America; Africa-Latin America. It can provides services at all stages of the mining business: exploration, exploitation, transformation and trading. Its range of services covers: 1/ energy minerals (30% of sales), mainly coal and uranium, 2/ geochemicals (30%), i.e. exploration and gold, 3/ the balance comprising metallurgy, fertilisers, steel and oil sands.

The group has over 150 laboratories in the world. Via pilot factories, it manages to simulate the future performance of its clients' processing plants by duplicating the conditions in which their plants have to operate.

It is paid on provision of the service, and is thus little exposed to the shift in production volumes. However, it suffers from the interruption to exploration, notably in iron and gold. This situation explains the decline in volumes and operating margin in H1 09. Moreover, an exceptional cost was booked with regard to the suppression of 1,000 jobs in Canada and in Australia.

In H1 09, the decline in raw material demand led to a fall in geochemical analysis volumes for exploration companies and deterioration in the operating margin.

## Oil, Gas and Chemicals: less and less tied to trade

Table 10: Operating performances for the Oil, Gas and Chemicals division

CHFm	2006	2007	2008	H1 09
Sales	783.4	891.3	953.5	468.6
<i>Organic growth for sales (%)</i>	<i>+13.4</i>	<i>+12.5</i>	<i>+10.8</i>	<i>+1.8</i>
<i>Operating margin (%)</i>	<i>14.4</i>	<i>15.0</i>	<i>14.7</i>	<i>14.3</i>
Recent acquisitions	nd	nd		

Source: Company

This division offers services in the gas, oil and chemical areas (fuels, heating fuels, plastics, fertiliser and drugs).

About half of sales is tied to trade, this mainly consisting of inspections involving the taking of sample on tankers in order to determine the value of cargos. It has shifted its services aimed at liquid fuels to broaden its bio fuel offer. Its expertise and technology in fuel analysis allows it both to issue a report twice a year on the fuels available in the world. It thus provides the sector with the information needed to make motors more efficient and to reduce their consumption.

15% of the division's business consists in the management of terminals (tankers). These services ex inspection also include the processing of cargos, the subcontracting of lab analyses and the marking of fuel. The product portfolio has been enriched in the domain of mobile solutions in the maintenance of well heads. In the area of hazardous substance transport, it offers its clients an emergency communication/liaison network, which smoothes intervention in case of accidents.

10% covers services linked to upstream (site exploration). Amongst others, it ensures the surveillance of well drilling conditions and supplies well engineering services.

SGS has diversified its services to adapt them to growth in alternative fuel sources (natural gas, biofuels).

In H1 09, the decline in the chemicals business was offset by the growth in upstream services. Margin erosion is linked to the end of attestation contracts on the integrity of fuels.

## Life sciences: ramp-up in Asia

Table 11: Operating performances for the Life sciences division

CHFm	2006	2007	2008	H1 09
Sales	193.4	200.4	204.4	101.0
<i>Organic growth for sales (%)</i>	<i>+9.1</i>	<i>+4.3</i>	<i>+8.6</i>	<i>+7.0</i>
<i>Operating margin (%)</i>	<i>12.7</i>	<i>12.0</i>	<i>13.5</i>	<i>10.7</i>
Recent acquisitions	Aster Cephac (Fr.) Northern Biosciences (USA)	nd	nd	nd

Source: Company

In this division, which makes 70% of its sales in France and in Belgium, the customer base mainly comprises pharma groups. The business is divided between quality control (40%, notably in the US, Asia and Europe) and clinical trials (60%, notably in France and Belgium).

Its main business consists of research operations. It undertakes clinical trials (European leader in phase 1 trials and bio analysis and biometry services) in outsourcing (15,000 volunteers in Paris). It runs early clinical phase installations in Europe and is present in advanced phase trials in Europe and the US. It helps its clients to pilot through procedures and regulations applicable to drug trials on humans.

It also exercises quality control on medical products and equipment, in order to guarantee the constancy of quality standards for the entirety of a portfolio of suppliers. In particular, the development of generic drugs, by pushing pharma groups to extend their sources of supply towards emerging countries, has forced the sector to tighten supplier control. It also aids its clients to evolve within national regulations governing the pharma supply chain.

in H1 09, growth remained strong thanks to Asia, despite a negative climate in clinical research. The margin improved owing to the arrival of profitability at the Asian labs.

## Consumer testing: quite a diverse portfolio

Table 12: Operating performances for Consumer testing division

CHFm	2006	2007	2008	H1
Sales	592.7	654.7	733.9	391.2
<i>Organic growth for sales (%)</i>	<i>+22.0</i>	<i>+10.3</i>	<i>+15.8</i>	<i>+12.1</i>
<i>Operating margin (%)</i>	<i>23.1</i>	<i>23.2</i>	<i>23.2</i>	<i>25.4</i>
Recent acquisitions	7 Layers (UK) Wireless Test Systems (USA)	Lab Merten (Ger.)	Blue sign Tech. (CH) Nokia Siemens Networks (Ger.)	n/a Tesco Eng. (Korea)

Source: Company

The controls undertaken throughout the supply chain help avoid contamination that risks impacting consumer health and brand image. SGS clients thus use its services to minimise security and quality risks throughout the logistics chains from raw materials to the end of the product life cycle: working conditions, commercial practice, regulatory conformity, reduction in carbon emissions.

The group has labs on all continents, in order to accompany its clients for whom suppliers change according to the comparative advantages of each region.

It is the market leader in CDMA (Code Division Multiple Access) services in North America in the mobile phone sector.

The group undertakes tests in four sectors: soft lines (textile) 25% of division sales, hard lines (furniture, toys) 25%, electrical and electronic products 30%, food products 20%. The toys do not exceed 8% of sales for the division, which exposes SGS less to the CPSIA legislation than its rival BV. The sensitivity of this business to the macro climate emerges via the number of references, but there is not necessarily any correlation to the extent that the number of references tends to increase, even in a period of slowdown, under the impact of innovation, as well as protectionism. Its services include the inspection of factories, the control of product

performance and analysis of limited usage products. This results from the pressure exercised by the market on importers and distributors to control their suppliers (product conformity, social and environmental standards).

In H1 09, the business was buoyed by the entry into force of the new CPSIA regulation on products for children, hence a rise in the margin by leverage impact on volumes and improvement in the product mix.

## Systems and Certification: some recurrence

Table 13: Operating performances for the System & Certification division

CHFm	2006	2007	2008	2009
Sales	318.7	353.5	365.6	175.7
<i>Organic growth for sales (%)</i>	<i>+14.9</i>	<i>+9.2</i>	<i>+9.2</i>	<i>+5.0</i>
<i>Operating margin (%)</i>	<i>18.5</i>	<i>18.4</i>	<i>19.1</i>	<i>19.1</i>
Recent acquisitions	nd	nd	nd	

Source: Company

This sector includes the traditional certification of processes and systems (ISO 9001, ISA 14001) for 80% of the activity, plus certification specific to some industries (ISO 22000, IECQ HSPM 080000) founded on conformity directives valid worldwide and personalised audit solutions (focused on performance in relation to the Key Performance Indicator index). This division also includes training services. Hygiene-Security-Environment is fully integrated and represents some 10% of sales.

The markets concerned by this sector are mainly: food, finance, pharma and energy.

Multinational companies are increasingly interested in a one-stop shop able to provide solutions applicable worldwide, which favours the selection of world players like SGS. But small players exercise pressure on the prices of services.

In H1 09, despite a clear slowdown in production capacity and pressure on prices, partly offset by rise in market share and the specialisation on HSE certification systems, margins have improved substantially thanks to the product mix and the reduction in costs.

## Industrial services: cyclicity diminished thanks to energy

Table 14: Operating performances for Industrial division

CHFm	2006	2007	2008	H1 09
Sales	510.4	624.7	738.5	371.3
<i>Organic growth for sales (%)</i>	<i>13.1</i>	<i>+15.7</i>	<i>+16.7</i>	<i>+4.8</i>
<i>Operating margin (%)</i>	<i>14.6</i>	<i>16.1</i>	<i>14.3</i>	<i>13.3</i>
Recent acquisitions	SRS Tech Co (Korea)	FTS (US)	nd	PID

Source: Company

This activity includes the regulatory inspection of buildings and building standards, non-destructive tests and the inspection of building maintenance. The Building portion per se represents €200m of sales, mainly chalked up in Spain.

It also covers equipment surveillance and inspection services of great value (notably in the energy sector) plus surveillance of large infrastructure projects and analysis of materials in situ.

The group thus helps its clients cut risk on the operation of industrial installations thanks to equipment ensuring a deep and predictive maintenance programme. This involves the verification of installations, equipment, infrastructure and tests whether the projects meet all the regulatory quality and performance equipments, whether voluntary or imposed by the client.

SGS acquired the PID group in Brazil in 2009.

In H1 09, the diminution in infrastructure projects and the decline in construction in Europe and the US impacted division sales and margins. But energy markets (oil refineries, electrical power stations) showed greater resilience.

## Environment: the relay in emerging countries

Table 15: Operating performances for the Environmental division

CHFm	2006	2007	2008	H1 09
Sales	249.2	281.1	296.4	140.2
<i>Organic growth for sales (%)</i>	<i>+6.0</i>	<i>+14.1</i>	<i>+9.8</i>	<i>+4.3</i>
<i>Operating margin (%)</i>	<i>9.7</i>	<i>9.8</i>	<i>10.6</i>	<i>9.6</i>
Recent acquisitions	nd	EcoServPty (SA)	nd	nd

Source: Company

Environmental analyses relate to large worksites and industrial projects (mines, K lliken dump in Switzerland for example), notably with regard to their impact on the contamination of soils, water and air. The group helps its clients confirm to regulatory standards in this respect. It is also present in the control of waters (Paris-Rive gauche). In particular, it focuses on lab samples and trials relating to compliance.

It is a purely local speciality, where the group's world network plays no role owing to the broad diversity of specific regulations for each zone. Economies of scale are thus difficult to obtain.

In H1 09, sales growth resisted thanks to the group's involvement in emerging countries, which has also helped boost the margin via leverage on volumes. The group has also pressed on with its investment in projects linked to climate change and air quality.

## Automotive: linked in part to automobile cycles

Table 16: Operating performances for the Automotive services division

CHFm	2006	2007	2008	H1 09
Sales	220.3	249.2	292.6	144.5
<i>Organic growth for sales (%)</i>	<i>+4.0</i>	<i>+10.3</i>	<i>+22.3</i>	<i>0.0</i>
<i>Operating margin (%)</i>	<i>13.5</i>	<i>13.6</i>	<i>16.3</i>	<i>14.4</i>
Recent acquisitions	n/a	COTA (Alger.) Adria Control (Slov.)	n/a	n/a

Source: Company

This division includes regulatory inspection services for cars (technical controls and CO2 emissions as well as the passing of building permit examinations and the granting of taxi licences), which represent 75% of sales. In this area, SGS has 40% of the French market and strong positions in French-speaking states.

The group also undertakes commercial inspections and quality control services at the production level (audit and inspection of spare parts). Above all, it consists of a business based in the US in relation with the rental companies, concessionaires and producers. This second business is thus much more cyclical than the first.

In H1 09, though obligatory technical controls showed their recurrence, the services provided to car parts suppliers declined with vehicle production. The margin thus fell by 240bp.

## Governments and Institutions: less dependant on international trade

Table 17: Operating performances for the Governments & Institutions division

CHFm	2006	2007	2008	H1 09
Sales	nd	200.4	211.9	103.1
<i>Organic growth for sales (%)</i>		<i>+19.8</i>	<i>+10.5</i>	<i>+9.5</i>
<i>Operating margin (%)</i>		<i>14.4</i>	<i>16.9</i>	<i>17.9</i>
Recent acquisitions	n/a	n/a	n/a	n/a

Source: Company

This division comprises: 1/ the control of imports (55% of sales), which is undertaken by scanners at the point of arrival. SGS' solution enables verification of the value of goods, hence to give a levy to taxation, to ensure commercial efficacy and to validate the meeting of national regulations in terms of exchange at the point of delivery; 2/ control at the point of departure (45%), which is purely visual. This inspection before embarkation, which uses 14 units across the world, is diminishing compared with the first activity.

Moreover, this division includes services controlling the efficacy of aid programmes. This comprises evaluation services and verification of public administrations and non-profit organisations receiving subsidies and loans accorded by international development aid programmes. They help improve the performance of the audited institutions and guarantee sound governance practice.

Other services deal with the management of forests (environmental conformity solutions), the monitoring of cargos, the surveillance of forex transactions, the fight against forgery.

In H1 09, inspection before embarkation sales stagnated but inspection solutions by scanners and product conformity programmes increased. The operating margin improved thanks to new projects and productivity gains.

## 4. A temporary slowdown

SGS has seen growth acceleration and improvement in its margin recently. Even if its business is not risk-free, the macro situation only impacts it in marginal fashion. This does not mean that growth will not pick up again once the economic picture improves.

### A strategy focused on value-added services

Under the impulse of its CEO, Sergio Marchionne, SGS changed strategy in 2002 by focusing on value-added advisory services, tests and analysis services (obligatory regulatory inspections, services provided on production sites) – businesses less tied to international trade than its traditional missions (commercial inspections). The latter still represent over a third of group sales and now mainly concern agriculture, mining and oil.

Group sales grew much faster than the market till 2009, at some 3/4% per year.

Table 18: Sales trend for SGS of 2003 to 2008

CHFm	2002	2003	2004	2005	2006	2007	2008	H1 09
Sales	2,392	2,454	2,885	3,308	3,821	4,372	4,818	2,327
<i>Reported change (%)</i>	+2.6	+2.6	+17.5	+14.6	+15.5	+14.4	+10.2	+1.3
<i>Like-for-like change(%)</i>	n/a	+7.0	+10.7	+11.4	+10.3	+12.0	+15.3	+4.1
Operating profit	216	300	393	502	605	711	810	376
<i>Operating margin (%)</i>	9.0	12.2	13.6	15.2	15.8	16.3	16.8	16.2

Source: Company

Over the last three years, the 10 divisions have posted strong growth, notably minerals, consumer goods and industrial. The services to agriculture and to automotive, plus life sciences, have shown greater volatility, but we can see that the growth dynamic is quite well spread between the various businesses.

Table 19: Organic sales trend for SGS' divisions

%	2005	2006	2007	2008
Agriculture	+11.8	+5.7	+4.3	+9.3
Minerals	+17.1	+15.9	+17.0	+27.6
Oil, Gas and Chemicals	+9.4	+13.2	+12.4	+11.6
Life sciences	+15.5	+9.2	+4.3	+9.2
Consumer testing	+27.2	+21.7	+12.4	+16.9
Systems and certification	+15.1	+14.7	+9.0	+9.7
Industrial services	+12.5	+13.1	+15.7	+16.7
Environment	+8.8	+6.5	+13.8	+10.4
Automotive	-0.7	+4.0	+10.2	+23.8
Governments and institutions	-10.5	-28.1	+19.8	+11.1

Source: Company

## Low risk

Though the group is only impacted by macro fluctuations to a limited degree, it does face some risks.

- The poor integration or reorganisation of companies acquired is an ongoing risk for a company active in a highly fragmented market and for which external growth is part of its strategies. That said, this risk is diminished by the fact that most acquisitions concern companies of a modest size.
- The decline in world trade was historically one of the risks that group faced. At present, for Agriculture, the group division most impacted by international trade, even though its weight has not changed much (7% of group operating profit versus 8.5% in 2001), the impact of world trade is weaker, as a growing slice of sales in the division is generated by upstream services, such as those linked to 'precision' agriculture (soil analysis, fertiliser requirements, etc.).
- Currencies have quite a large impact on SGS' accounts, as they are denominated in Swiss francs. Of the group's four key currencies, the euro has the greatest weight and the US dollar, the Chinese yuan and Australian dollar, together weigh less than the euro, and each in quite different proportions.

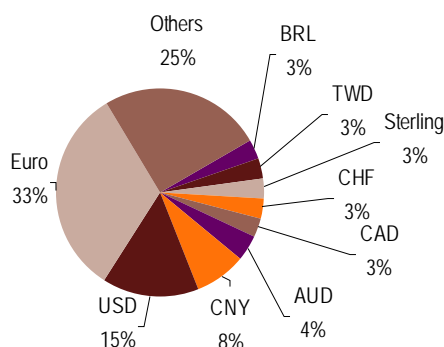
Table 20: Impact of currencies on sales and operating profit at SGS

%	2005	2006	2007	2008	H1 09
Organic sales growth	+11.4	+10.3	+12.0	+15.3	+4.1
Impact of currencies on sales	+1.4	+1.6	+1.5	-7.5	-4.7
Organic operating profit growth	+23.2	+15.2	+14.4	+20.4	+6.1
Impact of currencies on operating profit	+1.8	+1.7	+1.7	-9.0	-5.3

Source: Company

Currency impacts were fairly moderate in the last few years, with the exception of 2008, with variations in the euro being offset by those of other currencies. The scale of the variation in 2008 was due to the simultaneous fall of the US dollar, the euro, the Australian dollar and sterling.

Chart 2: Breakdown of SGS' sales by currency



Source: Company

The impact of currencies is above all marked at the level of the euro versus the Swiss franc. The effect stemming from trends in the US dollar is more limited, except when it is combined with a trend in the same direction for the Australian dollar and the Chinese yuan.

Table 21: Estimated impact of currency variations on sales and net profit

€/CHF exchange rate (chg. in %)	1.45 (-4%)	1.51	1.60 (+6%)
Sales (CHFm / chg. in %.)	(62) (-1.5%)	0	92 (+2.0%)
Net profit (CHFm / chg. in %.)	(5) (-0.9%)	0	7 (+1.3%)
\$/CHF exchange rate (chg. in %)	1.05 (-7%)	1.13	1.20 (+6%)
Sales (CHFm / chg. in %)	(51) (-1%)	0	43 (+0.9%)
Net profit (CHFm / chg. in %)	(2) (-1%)	0	5 (+0.9%)

Source: Company

- A risk specific to SGS' activity is that of the loss or non-renewal of accreditations. Indeed, a good part of the group's operations can only be carried out if they are authorised by the public authorities or professional bodies at the local, national or international level. The group is not immune to the risk of unilateral suspension or non-renewal of these accreditations. We can include with this risk that relating to contracts entered into as part of services to governments (import controls), which can generally be terminated unilaterally. A termination of this sort can have a substantial impact on the company, insofar as there are not many of these contracts.
- Insurance coverage of the group's activities gives rise to a particular risk. SGS has to cover the financial consequences of the engagement of its professional civil liability. And it may be that it cannot cover all of the risks taken or that the policies are inadequate or that the cost of insurance is so high that it is forced to give up an activity.

## Healthy financial situation

The group boasts an excellent financial situation with net cash of €239m at the end of 2008. Debt is mainly short term and three-quarters denominated in Swiss francs, with the balance in euros. The group's cash comprises liquidities and short-term deposits.

In H1 09, liquidities amounted to CHF251m.

Outside of periods of large-scale acquisitions or share buybacks, cash flow generation is abundant (5% of sales over the last two years), despite a high level of capex (6% of sales relative to 2.5% for Bureau Veritas), which is due to the weight of the testing business, and despite a payout rate of over 50%. This situation is due to the group's operating margin and its lower level of WCR.

Table 22: Capex, payout rate and WCR of listed sector groups

%	BV	SGS	Intertek
Capex as % of sales	2.5	6	5
Distribution (payout)	33	54	30
WCR as % of sales	8	5	10
Change in WCR as % of sales	0.5	1.0	0.7
Cash flow generation	7	5	3

Sources: Companies

Capex is concentrated in minerals, consumer goods and energy, which account for two-thirds of the amounts (CHF290m in 2008), being big consumers of testing machines.

In 2009, the financial situation will remain largely in surplus, due to the stability of capex (levels of capex maintained or lowered in times of crisis) and in the absence of large-scale acquisitions.

At constant scope, by our estimates net cash should exceed CHF500m in 2011e, since we anticipate growing cash flow generation, exceeding €200m in 2011e.

Table 23: Simplified provisional cash flow statement

CHFm	2007	2008	2009e	2010e	2011e
Cash flow from operations	694.0	860.0	774.0	847.8	938.4
Capex	-271.0	-278.0	-289.8	-303.5	-295.1
Decrease (Increase) in the WCR	12.0	-22.0	-24.2	25.3	26.8
<b>Free cash flow</b>	<b>435.0</b>	<b>560.0</b>	<b>460.0</b>	<b>569.6</b>	<b>670.2</b>
Acquisitions	-71.0	-184.0	-100.0	-100.0	-100.0
Payout	-153.0	-267.0	-377.0	-320.0	-341.1
Capital increase	-8.0	-201.0	0.0	0.0	0.0
Income from disposals	0.0	0.0	0.0	0.0	0.0
Miscellaneous	-40.0	-38.0	-5.0	-5.0	-5.0
Increase (Decrease) in cash	163.0	130.0	-22.0	144.6	224.1
<b>Net debt</b>	<b>-369.0</b>	<b>-239.0</b>	<b>-217.0</b>	<b>-361.6</b>	<b>-585.7</b>

Sources: Natixis Securities estimates

## Return to growth in 2010

### 2009: earnings resilience

The group's guidance for 2009 is fairly conservative, limited to forecasting (single-digit) organic growth in sales and a maintenance of operating margins at the level in 2008.

Unlike in 2008, organic growth in sales is no longer likely to come from the Minerals, Oil, Gas and Chemicals, Industrial Services and Automotive divisions, which have been affected by the crisis. Conversely, Consumer Testing should maintain a strong rate of growth, even though a slowdown is foreseeable in H2 09 as a result of weaker economic growth. Agricultural Services will probably remain dynamic, thanks to the growing weight of packages of services, like Governments and Institutions Services, which are driven by the installation of new scanners in a growing number of countries. The other divisions are more recurring: Life Science Services thanks to quality control volumes, Systems and Services Certification despite some capacity closures, Environmental Services thanks to the potential of emerging countries. Overall, the group's sales are likely to show virtually zero growth, given an exchange-rate effect that will probably be negative (-3/-4%e) and a fairly limited impact from acquisitions (+1/-2%e).

Operating margins are likely to see contrasting trends. It is fairly certain that the most cyclical divisions will show declines in operating margin relative to 2008 (Minerals, Oil, Gas and Chemicals, Industrial Services, Automotive). Conversely, the other divisions where activity is more recurring will probably show margin increases reflecting improvements in the product mix and cost reductions. We expect a margin slightly below the 2008 level of 16.8% (decrease of 5 basis points to 16.76%).

Table 24: Estimates for sales and EBITA by division

CHFm	2007	2008	2009e
<b>Sales</b>	<b>4,372</b>	<b>4,818</b>	<b>4,831</b>
<i>Change (%)</i>	<i>+14.4</i>	<i>+10.2</i>	<i>+0.3</i>
Agricultural Services	357	358	366
Minerals Services	560	663	601
Oil, Gas and Chemicals	891	954	935
Life Science Services	200	204	206
Consumer Testing	655	734	788
Systems and Services Certification	354	366	372
Industrial Services	625	738	765
Environmental Services	281	296	299
Automotive Services	249	293	281
Governments and Institutions Services	200	212	219
<b>EBITA</b>	<b>711</b>	<b>810</b>	<b>810</b>
Agricultural Services	47	56	65
Minerals Services	98	125	86
Oil, Gas and Chemicals	133	140	137
Life Science Services	24	28	27
Consumer Testing	152	170	206
Systems and Services Certification	65	70	75
Industrial Services	101	106	102
Environmental Services	28	31	30
Automotive Services	34	48	40
Governments and Institutions Services	29	36	41
<b>Operating margin (%)</b>	<b>16.26</b>	<b>16.81</b>	<b>16.76</b>
Agricultural Services	13.17	15.64	17.64
Minerals Services	17.50	18.85	14.35
Oil, Gas and Chemicals	14.93	14.68	14.68
Life Science Services	12.00	13.73	13.23
Consumer Testing	23.21	23.16	26.16
Systems and Services Certification	18.36	19.13	20.13
Industrial Services	16.16	14.36	13.36
Environmental Services	9.96	10.47	10.17
Automotive Services	13.65	16.38	14.38
Governments and Institutions Services	14.50	16.98	18.48

Sources: Natixis Securities estimates

The other items in the P&L account are not likely to contain any particular surprise: stable interest expense, non-recurring items limited to low restructuring costs, tax rate of 25% up slightly relative to 2008. Net profit (excluding non-recurring items) should come to €582m, by our estimates, slightly below that in 2008 (-2%).

### 2010 and 2011: Recovery in growth possible

The end of 2010 could see a return to growth in SGS' main businesses, which are also the most cyclical. The cost reductions achieved in 2008 should normally enable a continuation of operating margin gains. SGS should therefore return to a progression in recurring net profit in 2010 and 2011.

Table 25: GDP growth forecasts for the main world economies

%	2009e	2010e	2011e
USA	-2.5	1.4	2.1
Japan	-6.3	0.5	1.2
Euro zone	-3.9	0.2	0.7
UK	-4.0	1.0	1.8
China	8.1	9.3	9.3

Source: Natixis estimates

At current dollar and euro rates, the currency effect is likely to remain negative in 2010, given the strength of the Swiss franc vis-à-vis other currencies.

At constant currencies, we expect to see an acceleration in organic growth in sales (+5%e in 2010, +6%e in 2011), under the impetus of the group's four businesses.

First, Minerals Services should take advantage of a relative increase in the production of iron ore and steel, which could result in the reopening of operating sites and an increase in analysis volumes. Upstream, the resumption of exploration projects should also lead to increased revenues for the division.

Table 26: Forecasts for growth in the supply of iron ore by producer

Mt	2009e	2010e	2011e
Vale	252.2	292.2	305.0
Brio	273.7	288.6	314.5
Rio Tinto	152.0	158.1	168.9
BHP Billiton	121.8	130.4	145.7
Arcelor Mittal	42.0	47.7	47.7
World production	2,032.9	2,081.4	2,167.8
<i>Change (%)</i>	<i>-8</i>	<i>+3</i>	<i>+4</i>

Source: AME Mineral Economics

In automotive, the most cyclical activity, commercial inspections, will be the main growth driver in 2010/11, due to the expected rebound in worldwide production. For passenger cars (excluding light commercial vehicles), the estimates of forecasters are as follows.

Table 27: Forecasts for growth in the production of passenger cars in the world

(000 units)	2009e	2010e	2011e
North America	3,917	4,845	5,937
Mercosur	2,722	2,771	2,886
Western Europe	10,929	10,539	11,191
Eastern Europe	4,293	4,811	5,444
Japan	7,414	8,029	8,851
Asia Pacific	13,803	14,049	15,379
World	44,945	47,056	53,767
<i>Change (%)</i>	<i>-13.4</i>	<i>+4.7</i>	<i>+14.3</i>

Sources: J.D. Power, Automotive forecasting

The Industrial Services division could see a favourable impact from a recovery in construction, given that a large share of revenues is generated in building (around one-third). However, this should be qualified since 2010/11 will mainly benefit from the recovery in residential construction and public works. Conversely, non-residential construction, which includes industrial installations, is much more a late cyclical activity. It probably will not recover until 2012.

Table 28: Estimates for growth in worldwide construction spending: Western Europe

€bn 2008	2006	2007	2008	2009e	2010e	2011e
Residential construction	700.7	706.0	651.3	549.3	573.7	616.6
<i>Change (%)</i>	<i>4.5</i>	<i>0.7</i>	<i>-7.7</i>	<i>-15.7</i>	<i>4.4</i>	<i>7.5</i>
Non-residential construction	429.9	450.1	453.3	419.1	395.4	406.1
<i>Change (%)</i>	<i>2.9</i>	<i>4.7</i>	<i>0.7</i>	<i>-7.5</i>	<i>-5.7</i>	<i>2.7</i>
Public works	290.7	298.5	298.2	291.9	296.9	303.1
<i>Change (%)</i>	<i>3.2</i>	<i>2.7</i>	<i>-0.1</i>	<i>-2.1</i>	<i>1.7</i>	<i>2.1</i>
<b>Total</b>	<b>1,421.2</b>	<b>1,454.5</b>	<b>1,402.9</b>	<b>1,260.3</b>	<b>1,266.0</b>	<b>1,325.8</b>
<i>Change (%)</i>	<i>3.8</i>	<i>2.3</i>	<i>-3.6</i>	<i>-10.2</i>	<i>0.5</i>	<i>4.7</i>

Sources: Euroconstruct, Natixis Securities estimates

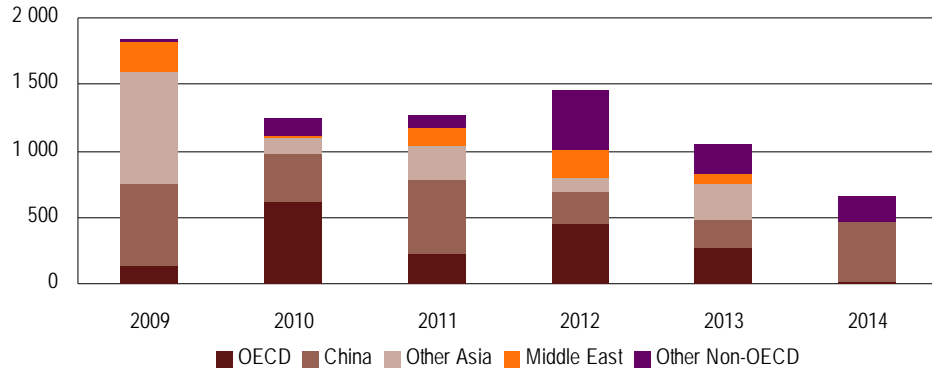
Table 29: Estimates for growth in worldwide construction spending: USA

\$bn 1996	2006	2007	2008	2009e	2010e	2011e
Residential construction	403.8	307.7	230.6	163.6	189.4	259.9
<i>Change (%)</i>	<i>-4.0%</i>	<i>-23.8%</i>	<i>-25.1%</i>	<i>-29.1%</i>	<i>15.8%</i>	<i>37.2%</i>
Non-residential construction	145.1	163.2	176.1	143.4	114.6	114.2
<i>Change (%)</i>	<i>8.0%</i>	<i>12.5%</i>	<i>7.9%</i>	<i>-18.6%</i>	<i>-20.1%</i>	<i>-0.3%</i>
Public works	172.4	180.7	184.3	175.3	186.8	192.2
<i>Change (%)</i>	<i>2.5%</i>	<i>4.8%</i>	<i>2.0%</i>	<i>-4.9%</i>	<i>6.6%</i>	<i>2.9%</i>
Other	45.8	57.3	63.3	63.4	59.3	60.1
<i>Change (%)</i>	<i>5.3%</i>	<i>25.1%</i>	<i>10.5%</i>	<i>0.2%</i>	<i>-6.5%</i>	<i>1.3%</i>
<b>Total</b>	<b>767.1</b>	<b>708.9</b>	<b>654.3</b>	<b>545.7</b>	<b>550.1</b>	<b>626.4</b>
<i>Change (%)</i>	<i>0.1%</i>	<i>-7.6%</i>	<i>-7.7%</i>	<i>-16.6%</i>	<i>0.8%</i>	<i>13.9%</i>

Sources: PCA, Natixis Securities estimates

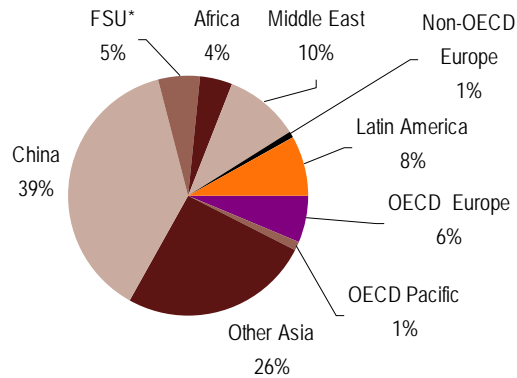
In the Oil, Gas and Chemicals division, the outlook for trading activities (tanker inspections) and terminal management in the next two years looks promising in view of the growth in additional refining capacities.

Chart 3: Estimates for the increase in refining capacities worldwide



Sources: IEA Medium-Term Oil Market Report, June 2009

Chart 4: Geographic breakdown of the new refining capacities



\* Former Soviet Union

Sources: IEA Medium-Term Oil Market Report, June 2009

7.6m b/d in additional capacity is expected until 2014. The Asia and Middle East zones will be the main contributors (70%). The increase in capacities will logically have repercussions for all means of transport and port facilities, which should be a source of new contracts for SGS.

In 2010 and 2011, volume effects should normally result in an improvement in margins (estimated at +/-20bp), but we do not expect anything extraordinary in this respect, as the level reached (more than 17%) already makes SGS the leader in the sector and the room for improvement looks fairly limited.

Table 30: Estimates for sales and EBITA by division

CHFm	2009e	2010e	2011e
<b>Sales</b>	<b>4,831</b>	<b>5,058</b>	<b>5,365</b>
<i>Change (%)</i>	<i>+0.3</i>	<i>+4.7</i>	<i>+6.1</i>
Agricultural Services	366	384	403
Minerals Services	601	607	667
Oil, Gas and Chemicals	935	982	1,031
Life Science Services	206	210	214
Consumer Testing	788	860	920
Systems and Services Certification	372	380	391
Industrial Services	765	813	878
Environmental Services	299	311	327
Automotive Services	281	279	285
Governments and Institutions Services	219	233	249
<b>EBITA</b>	<b>810</b>	<b>857</b>	<b>924</b>
Agricultural Services	65	69	73
Minerals Services	86	87	96
Oil, Gas and Chemicals	137	145	155
Life Science Services	27	28	29
Consumer Testing	206	225	243
Systems and Services Certification	75	77	80
Industrial Services	102	109	121
Environmental Services	30	33	35
Automotive Services	40	40	42
Governments and Institutions Services	41	44	49
<b>Operating margin (%)</b>	<b>16.76</b>	<b>16.95</b>	<b>17.22</b>
Agricultural Services	17.64	17.84	18.14
Minerals Services	14.35	14.35	14.45
Oil, Gas and Chemicals	14.68	14.78	15.08
Life Science Services	13.23	13.33	13.43
Consumer Testing	26.16	26.16	26.46
Systems and Services Certification	20.13	20.33	20.53
Industrial Services	13.36	13.46	13.76
Environmental Services	10.17	10.47	10.77
Automotive Services	14.38	14.48	14.68
Governments and Institutions Services	18.48	18.98	19.48

Sources: Natixis Securities estimates

Net profit growth will therefore come from the increase in sales and the rise in financial income, as, in the absence of acquisitions, SGS' net cash will by our estimates largely exceed €350m est. at the end of 2010 (vs. €217m est. at the end of 2009). Even invested short term in euros or Swiss francs, it will generate a few million Swiss francs in financial income per year.

However, it is highly probable that 2010 and 2011 will see a resumption in acquisitions, as purchase prices will be more reasonable than before the crisis, the main sector players will start to buy up rivals and economic prospects will improve.

We look for an increase in net profit of 6.6% in 2010e and 8.1% in 2011e.

Table 31: Provisional P&L account

CHFm	2007	2008	2009e	2010e	2011e
Sales	4,372	4,818	4,831	5,058	5,365
<i>Change (%)</i>	14.4	10.2	0.3	4.7	6.1
<i>Organic growth (%)</i>	12.0	15.3	0.3	4.7	6.1
Gross operating profit	908	1,024	1,027	1,085	1,192
<i>Change (%)</i>	16.9	12.8	0.3	5.6	9.9
Reported operating profit	690	937	795	857	924
<i>Change (%)</i>	10.6	35.8	-15.2	7.9	7.7
Operating profit, adjusted	711	810	810	857	924
<i>Change (%)</i>	17.5	13.9	0.0	5.9	7.7
<b><i>Operating margin (%)</i></b>	<b>16.26</b>	<b>16.81</b>	<b>16.76</b>	<b>16.95</b>	<b>17.22</b>
Net financial result	2	-4	-3	2	4
Underlying profit before tax	692	933	792	859	928
Exceptional result	0	0	0	0	0
Corporate tax	-172	-219	-198	-215	-232
Goodwill amortisation	0	0	0	0	0
Earnings of equity affiliates	0	0	0	0	0
Minority interests	-20	-22	-23	-24	-25
Net profit of activities divested	0	0	0	0	0
Net attributable profit	500	692	571	620	670
<i>Change (%)</i>	12.9	38.4	-17.5	8.7	8.1
Net profit, adjusted	516	595	582	620	670
<i>Change (%)</i>	20.3	15.3	-2.2	6.6	8.1

Sources: Natixis Securities estimates

## Financial Data on 31/12

**SGS**

Breakdown by activities (CHFm)	2007	2008	2009e	2010e	2011e	CAGR 08/11
<b>Turnover</b>	<b>4,372</b>	<b>4,818</b>	<b>4,831</b>	<b>5,058</b>	<b>5,365</b>	<b>3.6%</b>
Agricultural Services	357	358	366	384	403	4.0%
Minerals Services	560	663	601	607	667	0.2%
Oil, Gas and Chemicals	891	954	935	982	1,031	2.6%
Life Science Services	200	204	206	210	214	1.6%
Consumer Testing	655	734	788	860	920	7.8%
Systems and Services Certification	354	366	372	380	391	2.2%
Industrial Services	625	738	765	813	878	6.0%
Environmental Services	281	296	299	311	327	3.4%
Automotive Services	249	293	281	279	285	-0.9%
Governments and Institutions Services	200	212	219	233	249	5.5%
<b>Adjusted operating profit</b>	<b>711</b>	<b>810</b>	<b>810</b>	<b>857</b>	<b>924</b>	<b>4.5%</b>
Agricultural Services	47	56	65	69	73	9.3%
Minerals Services	98	125	86	87	96	-8.3%
Oil, Gas and Chemicals	133	140	137	145	155	3.5%
Life Science Services	24	28	27	28	29	0.9%
Consumer Testing	152	170	206	225	243	12.7%
Systems and Services Certification	65	70	75	77	80	4.7%
Industrial Services	101	106	102	109	121	4.5%
Environmental Services	28	31	30	33	35	4.3%
Automotive Services	34	48	40	40	42	-4.5%
Governments and Institutions Services	29	36	41	44	49	10.5%
<b>Adjusted operating margin</b>	<b>16.3%</b>	<b>16.8%</b>	<b>16.8%</b>	<b>17.0%</b>	<b>17.2%</b>	
Agricultural Services	13.2%	15.6%	17.6%	17.8%	18.1%	
Minerals Services	17.5%	18.9%	14.4%	14.4%	14.5%	
Oil, Gas and Chemicals	14.9%	14.7%	14.7%	14.8%	15.1%	
Life Science Services	12.0%	13.7%	13.2%	13.3%	13.4%	
Consumer Testing	23.2%	23.2%	26.2%	26.2%	26.5%	
Systems and Services Certification	18.4%	19.1%	20.1%	20.3%	20.5%	
Industrial Services	16.2%	14.4%	13.4%	13.5%	13.8%	
Environmental Services	10.0%	10.5%	10.2%	10.5%	10.8%	
Automotive Services	13.7%	16.4%	14.4%	14.5%	14.7%	
Governments and Institutions Services	14.5%	17.0%	18.5%	19.0%	19.5%	

Profit & loss statement (CHFm)	2007	2008	2009e	2010e	2011e	CAGR 08/11
<b>Turnover</b>	<b>4,372</b>	<b>4,818</b>	<b>4,831</b>	<b>5,058</b>	<b>5,365</b>	<b>3.6%</b>
<i>Change</i>	<i>14.4%</i>	<i>10.2%</i>	<i>0.3%</i>	<i>4.7%</i>	<i>6.1%</i>	
Organic growth	12.0%	15.3%	0.3%	4.7%	6.1%	
<b>EBITDA</b>	<b>908</b>	<b>1,024</b>	<b>1,027</b>	<b>1,085</b>	<b>1,192</b>	<b>5.2%</b>
<i>Change</i>	<i>16.9%</i>	<i>12.8%</i>	<i>0.3%</i>	<i>5.6%</i>	<i>9.9%</i>	
<b>EBIT</b>	<b>690</b>	<b>937</b>	<b>795</b>	<b>857</b>	<b>924</b>	<b>-0.5%</b>
<i>Change</i>	<i>10.6%</i>	<i>35.8%</i>	<i>-15.2%</i>	<i>7.9%</i>	<i>7.7%</i>	
Adjusted EBIT	711	810	810	857	924	4.5%
<i>Change</i>	<i>17.5%</i>	<i>13.9%</i>	<i>0.0%</i>	<i>5.9%</i>	<i>7.7%</i>	
Operating margin	16.3%	16.8%	16.8%	17.0%	17.2%	
Financial items	2	-4	-3	2	4	
Pre-tax profit on ordinary activities	692	933	792	859	928	-0.2%
Exceptional items	0	0	0	0	0	
Corporate tax	-172	-219	-198	-215	-232	
Goodwill amortisation/ impairment	0	0	0	0	0	
Equity associates	0	0	0	0	0	
Minority interests	-20	-22	-23	-24	-25	
Net profit on divested activities	0	0	0	0	0	
<b>Reported net profit</b>	<b>500</b>	<b>692</b>	<b>571</b>	<b>620</b>	<b>670</b>	<b>-1.1%</b>
<i>Change</i>	<i>12.9%</i>	<i>38.4%</i>	<i>-17.5%</i>	<i>8.7%</i>	<i>8.1%</i>	
Adjusted net profit	516	595	582	620	670	4.1%
<i>Change</i>	<i>20.3%</i>	<i>15.3%</i>	<i>-2.2%</i>	<i>6.6%</i>	<i>8.1%</i>	

Cash flow statement (CHFm)	2007	2008	2009e	2010e	2011e	CAGR 08/11
Cash flow from operations	694	860	774	848	938	3.0%
Nets Investments	-271	-278	-290	-303	-295	2.0%
Decrease (Increase) in WCR	12	-22	-24	25	27	
Free cash flow	435	560	460	570	670	6.2%
Acquisitions	-71	-184	-100	-100	-100	
Dividend	-153	-267	-377	-320	-341	8.5%
Capital increase	-8	-201	0	0	0	
Divestments	0	0	0	0	0	
Miscellaneous	-40	-38	-5	-5	-5	
Increase (Decrease) in cash	163	-130	-22	145	224	
Net debt	-369	-239	-217	-362	-586	
Gearing	-18.4%	-12.8%	-10.2%	-15.1%	-21.6%	

Balance sheet (CHFm)	2007	2008	2009e	2010e	2011e	CAGR 08/11
Net fixed assets	1,636	1,699	1,734	1,810	1,837	2.6%
o/w net goodwill	563	594	594	594	594	
o/w gross goodwill	563	594	594	594	594	
Financial fixed assets	2	2	2	2	2	
WCR	202	247	238	239	243	
Net assets on divested activities	0	0	0	0	0	na
Total equity	2,007	1,862	2,118	2,402	2,710	13.3%
o/w shareholders' equity	1,971	1,825	2,076	2,355	2,656	
Provisions	123	134	134	141	149	
Net debt	-369	-239	-217	-362	-586	

Per share data (CHF)	2007	2008	2009e	2010e	2011e	CAGR 08/11
Shares outstanding (millions)	-	-	7.8	7.8	7.8	-
Diluted shares (millions)	7.6	7.5	7.5	7.5	7.5	0.0%
Reported EPS	64.87	90.72	76.35	82.99	89.68	-0.4%
Adjusted EPS	66.91	77.98	77.86	82.99	89.68	4.8%
Goodwill	0.00	0.00	0.00	0.00	0.00	na
Cash flow	93.98	124.17	108.53	116.68	128.98	1.3%
Net dividend	35.00	50.00	40.91	43.61	47.12	-2.0%
Payout ratio	54.0%	55.1%	53.6%	52.5%	52.5%	
Book value	258.36	244.20	277.73	315.07	355.43	13.3%

Financial ratios	2007	2008	2009e	2010e	2011e	CAGR 08/11
Personnel expenses (€m)	2,076	2,243	2,249	2,355	2,498	3.6%
Personnel expenses (% of sales)	47.5%	46.6%	46.6%	46.6%	46.6%	
Operating margin	15.8%	19.4%	16.4%	17.0%	17.2%	
Adjusted operating margin	16.3%	16.8%	16.8%	17.0%	17.2%	
Effective rate of tax	-24.9%	-23.5%	-25.0%	-25.0%	-25.0%	
Net margin	11.9%	14.8%	12.3%	12.7%	13.0%	
ROE	25.4%	37.9%	27.5%	26.3%	25.2%	
ROCE	29.1%	31.9%	30.8%	31.4%	33.3%	
Capital employed (€m)	1,838	1,946	1,972	2,049	2,080	2.2%
Interest cover (x)	na	na	na	na	na	
Debt/EBITDA (x)	-0.4	-0.2	-0.2	-0.3	-0.5	
Gearing	-18.4%	-12.8%	-10.2%	-15.1%	-21.6%	
WCR (% of sales)	4.6%	5.1%	4.9%	4.7%	4.5%	
Goodwill (% of book value)	28.1%	31.9%	28.0%	24.7%	21.9%	
Net investments (% of sales)	-6.2%	-5.8%	-6.0%	-6.0%	-5.5%	

Investment ratios	2009e	2010e	2011e
EV/Turnover (x)	2.1	2.0	1.9
EV/EBITDA (x)	10.1	9.4	8.3
EV/Adjusted EBIT (x)	12.8	11.9	10.8
P/BV (x)	4.7	4.1	3.7
P/CF (x)	12.0	11.1	10.1
Adjusted P/E	16.7	15.6	14.5
Reported P/E	17.0	15.6	14.5
Net yield	3.2%	3.4%	3.6%
Free cash flow yield (%)	4.5%	5.6%	6.6%

This document may mention valuation methods, which are defined as follows:

- 1/ Peer comparison method: valuation multiples for the company in question are compared with those of a sample of companies in the same sector, or with a similar financial profile. The sample average acts as a valuation benchmark, to which the analyst can, where necessary, apply discounts or premiums resulting from his/her perception of the company's specific features (legal status, growth outlook, profitability, etc.).
- 2/ NAV method: Net asset value is an assessment of the market value of the assets on a company's balance sheet using the method that the analyst deems most relevant.
- 3/ Sum of the parts method: this method involves valuing each of the company's businesses separately using the most appropriate valuation methods for each, and then adding them together.
- 4/ DCF method: the discounted cash flow method involves assessing the current value of cash that a company will generate in the future. The analyst draws up cash flow projections based on his/her assumptions and models. The discount rate used is the average weighted cost of capital, which equates to the company's cost of debt and the theoretical cost of equity as estimated by the analyst, and weighted by the proportion of each of these two components in the company's financing.
- 5/ Method based on transaction multiples: with this valuation method, the company's multiples are compared with those seen in transactions involving groups with a similar business profile.
- 6/ Dividend discount method: with this method, the analyst establishes the present value of dividends to be paid to shareholders by the company, using a projection of dividend payments and an appropriate discount rate (generally the economic cost of equity).
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Add	upside of 0-15% and/or high risk.
Reduce	downside of 0-15%.
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