

## Downgrade on valuation

### ■ Mixed 2009 results

FY09 results disappointed on organic revenue growth (+1.3% vs UBSe +2.4%) but surprised positively on margins (up 50bp to 17.3% vs UBSe 16.8%). Top-line pressures increased in 2H09 with 7/10 divisions reporting negative organic revenue growth. SGS also declared a special dividend of 30 SFr per share.

### ■ Conservative outlook

SGS sees "top line and earnings increasing over 2009 levels" but would not be more specific and would not commit to organic revenue growth in 2010 (conservative in our view). There is much more confidence in margins, with management seeing record 2009 levels as sustainable as cost management initiatives continue to benefit. We make no material changes to our forecasts, which already incorporate stable margins and revenue recovery through 2010.

### ■ Key issues remain

We learned nothing incrementally new at the results on the key strategic issues, namely the intentions of the Von Finck family over its remaining 15% holding, and acquisitions or balance sheet strategy (the company would only say it saw limited opportunities to create value via bolt-on deals).

### ■ Valuation

We maintain our PT of 1300 SFr (based on 16.5x 2010e EPS), but move our rating to Sell. SGS is a good business with long-term growth prospects but we see earnings momentum headwinds, a premium valuation and share overhang driving a period of short/medium-term underperformance.

Highlights (CHFm)	12/08	12/09	12/10E	12/11E	12/12E
Revenues	4,818	4,712	4,817	5,112	5,510
EBIT (UBS)	810	814	833	886	960
Net Income (UBS)	579	579	593	632	686
EPS (UBS, CHF)	76.19	77.23	79.05	84.31	91.53
Net DPS (UBS, CHF)	50.00	60.00	35.00	37.33	40.52

Profitability & Valuation	5-yr hist av.	12/09	12/10E	12/11E	12/12E
EBIT margin %	15.5	17.3	17.3	17.3	17.4
ROIC (EBIT) %	50.9	49.9	49.4	49.9	51.0
EV/EBITDA (core) x	11.1	9.2	9.8	9.1	8.1
PE (UBS) x	19.6	16.6	17.6	16.5	15.2
Net dividend yield %	2.5	4.7	2.5	2.7	2.9

Source: Company accounts, Thomson Reuters, UBS estimates. (UBS) valuations are stated before goodwill, exceptional and other special items. Valuations: based on an average share price that year, (E): based on a share price of CHF1,389.00 on 18 Jan 2010 19:07 EST

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## Global Equity Research

Switzerland

Industrial Services

12-month rating **Sell**  
Prior: *Neutral*

12m price target CHF1,300.00/US\$12.66  
*Unchanged*

Price CHF1,389.00/US\$13.57 (ADR)

RIC: SGSN.VX BBG: SGSN VX

19 January 2010

### Trading data (local/US\$)

52-wk range	CHF1,405.00-1,036.00/US\$13.84-8.81
Market cap.	CHF10.6bn/US\$10.3bn
Shares o/s	7.60m (REG )/760m (ADR)
ADR ratio	100 ADR:1 REG
Free float	64%
Avg. daily volume ('000)	27/45
Avg. daily value (m)	CHF36.5/US\$0.6

### Balance sheet data 12/10E

Shareholders' equity	CHF2.26bn
P/BV (UBS)	4.6x
Net Cash (debt)	CHF0.57bn

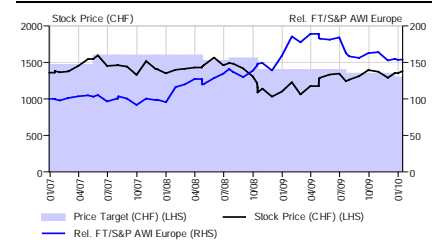
### Forecast returns

Forecast price appreciation	-6.4%
Forecast dividend yield	2.6%
Forecast stock return	-3.8%
Market return assumption	5.6%
Forecast excess return	-9.4%

### EPS (UBS, CHF)

	12/10E		Cons.	12/09 Actual
	From	To		
H1E	38.92	38.84	-	35.45
H2E	-	-	-	41.93
12/10E	78.21	79.05	81.30	
12/11E	83.50	84.31	89.02	

### Performance (CHF)



Source: UBS

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**ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 10.**

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## Results summary and key issues

SGS reported FY09 results that were largely in-line with our expectations at the bottom line. However, the company underperformed on revenue (with weaker than anticipated organic revenue growth in 2H09), but significantly outperformed on margins through strong cost and capacity management initiatives.

- **Outlook** – this was high level only with SGS expecting to grow top line and earnings in 2010. The company would not confirm this growth would be organic. While the lack of confidence is of some concern, this caution is likely conservatism driven by the 2009 experience when commentary on growth deteriorated though the year. We note that management are much more confident at the prospect of maintaining margins at record 2009 levels.
- **Special dividend** – SGS announced a special dividend of 30 SFr per share to reflect the exceptional cash generation in the group. We do not view this as particularly significant – the cost (c.200-250m SFr) is not great in the context of the strong SGS balance sheet, while the company had also done very little under the authorised buyback programme in 2009.
- **Acquisitions** – SGS announced one small acquisition (Intron) in European Industrial Services. Management were cautious about the prospects for bolt-on deals in 2010 as they saw limited “opportunities to create value”.
- **Share placing prospects** – the company gave no meaningful comments (unsurprisingly) on the situation surrounding the Von Finck shareholding.

Table 1: 2009 FY results summary

YE 31 Dec; SFrM	1H2008A	2H2009A	2008A	1H2009A	2H2009A	FY2009A	FY2009E	Diff
Revenue	2,298	2,520	4,818	2,327	2,385	4,712	4,807	-2.0%
Growth	10.0%	10.4%	10.2%	1.3%	-5.4%	-2.2%	-0.2%	
- organic	14.1%	14.4%	14.3%	3.9%	-1.1%	1.3%	2.4%	
- acquisitions	1.9%	2.7%	2.3%	1.8%	0.5%	1.1%	0.9%	
- fx	-6.0%	-6.8%	-6.4%	-4.4%	-4.8%	-4.6%	-3.5%	
Total EBIT Pre Exceptionals	370	440	810	376	438	814	807	0.9%
Margin	16.1%	17.4%	16.8%	16.2%	18.4%	17.3%	16.8%	
Other	127	0	127	-15	-5	-20	-15	
Total EBIT	497	440	937	361	433	794	792	0.3%
Financial (expense)/income	-1	- 3	-4	-3	0	-3	-6	
Profit Before Tax	496	437	933	358	433	791	786	0.6%
Taxation	-108	- 111	-219	-91	- 109	-200	-200	
Reported rate	21.8%	25.4%	23.5%	25.4%	25.2%	25.3%	25.4%	
Profit After Tax	388	326	714	267	324	591	585	1.0%
Adjusted Basic EPS (SFr)	34.7	41.5	76.2	35.3	41.9	77.2	76.3	1.2%
Adjusted Diluted EPS (SFr)	34.4	41.5	75.9	35.2	41.7	76.9	76.1	
DPS (SFr)			50			60	28	114%

Source: Company data; UBS estimates

## Changes to numbers

We have made no material changes to our forecasts at the EPS level following in-line results and only broad company guidance/targets. We still assume organic revenue growth starts to stabilise in 1H10 and then starts to recover in 2H10. We note that the company would not commit to organic revenue growth in FY10 and has no specific financial targets for the year. Our expectation of flat margins in 2010 is in-line with our prior forecasts (and company belief that there is “no reason not to protect” margins in 2010), albeit from the new, higher 2009 base. We continue to forecast only the underlying normal dividend.

**Table 2: Key forecasts and assumptions**

YE 31 Dec; SFrm	2005A	2006A	2007A	2008A	2009A	2010e	2011e	2012e	2013e	2014e
Revenue - previous forecasts	3,308	3,821	4,372	4,818	4,807	4,925	5,226	5,633	6,112	6,490
Revenue - current forecasts	3,308	3,821	4,372	4,818	4,712	4,817	5,112	5,510	5,979	6,490
Upgrade / (downgrade)	0%	0%	0%	0%	-2.0%	-2.2%	-2.2%	-2.2%	-2.2%	0.0%
Organic revenue growth - previous forecasts	11.5%	10.4%	12.1%	14.3%	2.4%	3.6%	6.1%	7.8%	8.5%	8.5%
Organic revenue growth - current forecasts	11.5%	10.4%	12.1%	14.3%	1.3%	3.5%	6.1%	7.8%	8.5%	8.5%
EBITA - previous forecasts	502	605	711	810	807	823	876	950	1031	1132
EBITA - current forecasts	502	605	711	810	814	833	886	960	1042	1132
Upgrade / (downgrade)	0.0%	0.0%	0.0%	0.0%	0.9%	1.3%	1.2%	1.1%	1.1%	0.0%
EBITA margin - previous forecasts	15.2%	15.8%	16.3%	16.8%	16.8%	16.7%	16.8%	16.9%	16.9%	17.4%
EBITA margin - current forecasts	15.2%	15.8%	16.3%	16.8%	17.3%	17.3%	17.3%	17.4%	17.4%	17.4%
EPS - previous forecasts	49.5	56.8	67.4	76.2	76.3	78.2	83.5	90.7	98.6	108.1
EPS - current forecasts	49.5	56.8	67.4	76.2	77.2	79.1	84.3	91.5	99.5	108.1
Upgrade / (downgrade)	0%	0%	0%	0%	1.1%	0.9%	0.8%	0.8%	0.8%	0.0%
DPS - previous forecasts	30	20	35	50	28	35	37	41	44	48
DPS - current forecasts	30	20	35	50	60	35	37	41	44	48
Upgrade / (downgrade)	0%	0%	0%	0%	114.3%	0.0%	-0.1%	-0.2%	-0.1%	0.0%

Source: Company data; UBS estimates

**Table 3: Divisional organic revenue growth forecasts**

YE 31 Dec	2005A	2006A	2007A	2008A	2009A	2010e	2011e	2012e	2013e	2014e
Agricultural	12.2%	5.8%	4.3%	8.3%	4.0%	2.5%	5.0%	5.0%	5.0%	5.0%
Minerals	17.5%	16.1%	17.3%	25.3%	-10.3%	3.8%	5.0%	10.0%	10.0%	10.0%
Oil, Gas & Chemicals	9.5%	13.4%	12.5%	10.8%	0.1%	2.5%	5.0%	6.0%	9.0%	9.0%
Life Science	15.6%	9.1%	4.3%	8.6%	3.1%	2.5%	7.0%	7.0%	7.0%	7.0%
Consumer Testing	27.5%	22.0%	10.3%	15.8%	9.1%	7.5%	10.0%	10.0%	10.0%	10.0%
Systems & Services	15.3%	14.9%	9.2%	9.2%	4.6%	3.0%	5.0%	10.0%	5.0%	5.0%
Industrial	12.6%	13.1%	16.0%	15.7%	2.1%	2.0%	6.0%	7.5%	10.0%	10.0%
Environmental	9.0%	6.3%	13.8%	9.8%	1.1%	2.0%	5.0%	7.0%	9.0%	9.0%
Automotive	-0.5%	4.0%	10.3%	22.3%	-4.3%	2.5%	5.0%	7.5%	7.5%	7.5%
Trade Assurance	-10.5%	-26.1%	19.8%	10.5%	6.9%	5.0%	5.0%	5.0%	5.0%	5.0%
<b>Group</b>	<b>11.5%</b>	<b>10.4%</b>	<b>12.1%</b>	<b>14.3%</b>	<b>1.3%</b>	<b>3.5%</b>	<b>6.1%</b>	<b>7.8%</b>	<b>8.5%</b>	<b>8.5%</b>

Source: Company data; UBS estimates

Table 4: Divisional margin forecasts

YE 31 Dec	2005A	2006A	2007A	2008A	2009A	2010e	2011e	2012e	2013e	2014e
Agricultural	11.4%	11.7%	13.4%	15.6%	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%
Minerals	15.9%	17.2%	17.5%	19.8%	16.1%	18.0%	18.0%	18.0%	18.0%	18.0%
Oil, Gas & Chemicals	12.6%	14.4%	15.0%	14.2%	15.4%	16.0%	16.0%	16.0%	16.0%	16.0%
Life Science	15.2%	13.2%	12.0%	13.5%	13.9%	16.0%	16.0%	16.0%	16.0%	16.0%
Consumer Testing	21.4%	23.6%	23.2%	23.2%	25.3%	23.3%	23.3%	23.3%	23.3%	23.3%
Systems & Services	17.0%	18.5%	18.4%	19.1%	21.1%	19.0%	19.0%	19.0%	19.0%	19.0%
Industrial	13.2%	14.6%	16.1%	14.3%	13.9%	14.0%	14.0%	14.0%	14.0%	14.0%
Environmental	11.1%	9.7%	9.8%	10.6%	11.7%	12.0%	12.0%	12.0%	12.0%	12.0%
Automotive	12.6%	13.5%	13.6%	16.3%	15.9%	16.0%	16.0%	17.0%	17.0%	17.0%
Trade Assurance	21.2%	13.7%	14.4%	16.9%	18.4%	18.4%	18.4%	18.4%	18.4%	18.4%
<b>Group</b>	<b>15.2%</b>	<b>15.8%</b>	<b>16.3%</b>	<b>16.8%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.4%</b>	<b>17.4%</b>	<b>17.4%</b>

Source: Company data; UBS estimates

## Divisional highlights

Within the divisions, we note that pressure on growth was broad-based and intensified through the year. 7/10 divisions saw negative organic growth in 2H10, although we note November and December did seem some stabilisation/improvement in revenue growth run rates.

- **Agricultural** - In what is still a relatively volatile business, there was pressure from tough conditions in the trade inspection business. Increasingly this is seen as a business that can move “in-land” and up the supply chain to offer more value-added services. This, and flexibility in the cost structure, saw margins increase through the year.
- **Minerals** - This remains the weakest performing division due to what was a “precipitous” deterioration in conditions in the wider industry. Limited capex expenditure from clients and reductions in research and development budgets meant volumes were significantly down. While conditions started to ease towards the end of H2 and the company is hopeful of a sustained recovery in end markets, this is not likely to be rapid. Reduced volumes hit utilisation rates and therefore margins, although these did improve in the second half of the year. Cost reduction initiatives mean that a revenue pick-up has the potential to further benefit margins in 2010.
- **Oil, Gas and Chemicals** - As expected, conditions in the trade-related inspection and testing businesses were difficult, especially in the chemicals segment. Refined products and fuels clients saw pressure on profitability in 2H10 which meant a reduction in capacity. Offsetting this, the continued increase into production-focused testing is bearing fruit. Of further interest was the announcement of a joint cooperation agreement with Halliburton the day before the results (14 January 2010) for analysis of oil and fluid samples. Essentially this agreement with a major oil services company moves SGS further up the value stream and satisfies an industry need for independent testing of samples as well as faster turnaround times in the testing process.

- **Life Science Services** - Conditions here remain difficult but SGS is seeing improving trends. Underlying performance reflects tough trading in the CRO (Contract Research Organisation) market. Within the detail, late phase is weak but offset by better performance in early phase services. Laboratory-focused businesses like quality control and bio-analysis are also performing better. Margins improved slightly and good capacity utilisation and potential for further laboratory consolidation mean there is potential margin upside.
- **Consumer Testing Services** - This business saw a considerable boost from the impact of the US CPSIA legislation. However this only accounted for the strong performance of the division “in part”. The company believes it has taken market share in textiles, hard goods and food. The weakest area remains E&E (Electrical & Electronics) although improved conditions here are anticipated. Q110 will have a tough comparative from the US CPSIA benefit in 2009 and we believe this will also make it difficult for SGS to sustain margins at the 25% level and see some modest pressure in 2010.
- **Systems & Services Certification** - This is a business that has performed well through the year. While there has been some benefit, we believe from 2009 being an ISO recertification year, there has also been a boost from increasing demand for industry and company-specific standards. Again, we believe that the boost to margin may have been due to some one-off factors (eg strong performance in France and Asia Pac; the ISO recertification boost) and the company believes it will be hard to maintain margins at the 2009 level in 2010.
- **Industrial Services** - This division suffered as the result of capex constraints at clients and severe weakness in the public and infrastructure markets in Europe. SGS remains optimistic about the prospects for renewable energy related testing, especially in wind where it has made investments during the year. Going forward, any pick-up in capex (especially on the oil and gas side) in 2010 will be helpful, but difficult conditions in European infrastructure are expected to continue to drag.
- **Environmental Services** - Weakness here was fairly broad-based as economic conditions impacted. The modest growth that was seen was mainly driven by new services and emerging markets. The company expects some pick-up in later 2010 post the traditional winter slowdown and if emerging markets can continue to offset weaker conditions in Europe.
- **Automotive** - Poor performance in this division was mainly due to the continued bad environment in commercial vehicle inspection. In general the statutory inspection side (which covers both vehicles themselves and emission) did much better. However SGS was impacted by the decision of the Irish Government to “in-source” driver testing as a result of economic conditions (rather than any poor performance within the contract).
- **Government and Institutions Services** - The core PSI business (now <50% of this division) was pressurised by weak underlying economic conditions in contracting countries. Yet non-traditional areas like scanning and product conformity are still showing good growth. Margin performance was also solid due to operational gearing and the benefits of prior IT investment.

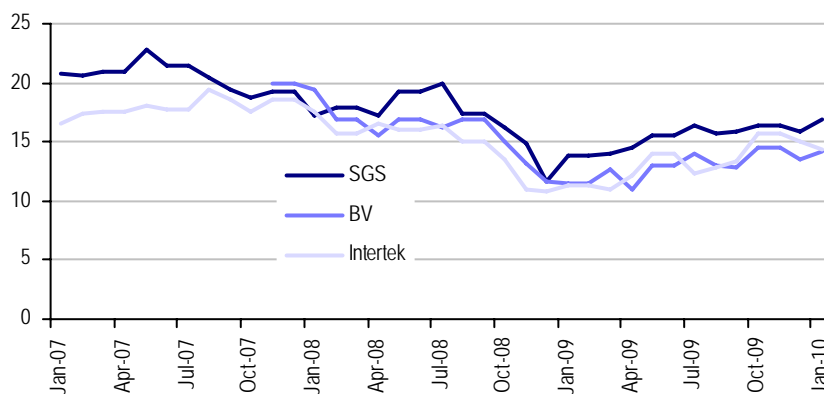
## Valuation

We downgrade SGS to Sell from Neutral, mainly on valuation grounds. Our 1300 SFr PT is unchanged and based on 16.5x 2010e EPS. While we like the business model and its longer-term prospects we do see predominant downside risks in the valuation:

- While the current PE of 17.5x PER is well within a range where SGS has traded in the past, this was in a very different growth and market environment (a bull market in equities and at a time when SGS was targeting 15% top-line growth and showing strong double digit earnings growth);
- We see overhang risk from a potential further placing of the remaining Von Finck share holding (the family placed 10% out of a total 25% shareholding on 11 November 2009; the six month lock-up period therefore expires in early May 2010);
- While the market leadership position, balance sheet and growth track-record means some premium to testing peers is merited in our view, we note this is again approaching relatively high levels;
- SGS remains, in our view the most likely consolidator in the testing and inspection industry, given its strong balance sheet. Market speculation intensified in 2009 (as reported on Reuters 23 April 2009) that a bid for Intertek was possible. A large acquisition presents operational and valuation risks in our view.

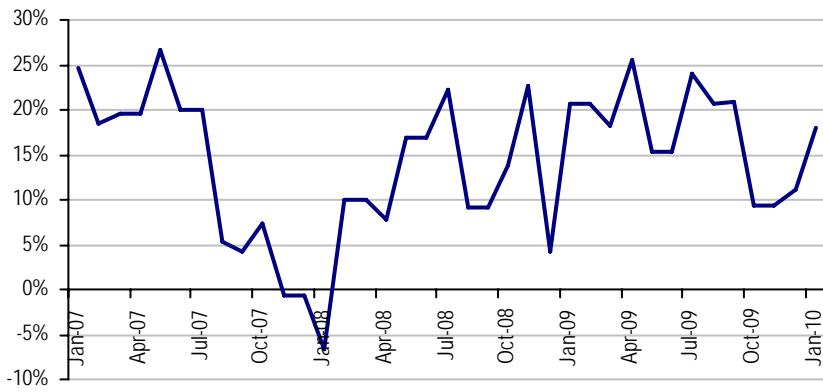
We do see this downside risk as limited by a long-term market willingness to pay a premium multiple for SGS. Furthermore, we accept that our 2011 forecasts are 2% and 5% below consensus for 2010e and 2011e respectively. In addition, we acknowledge that revenue pressures are expected to trough at some point in 2010 (which is incorporated in our forecasts) providing a floor to numbers. Finally the company retains the balance sheet strength to make acquisitions or buy back shares (it has permission for up to 250m SFr) which could also boost earnings. However, we remain cautious in the short-term and wait for a better opportunity to be more positive.

Chart 1: 1 Yr forward PE multiple trends



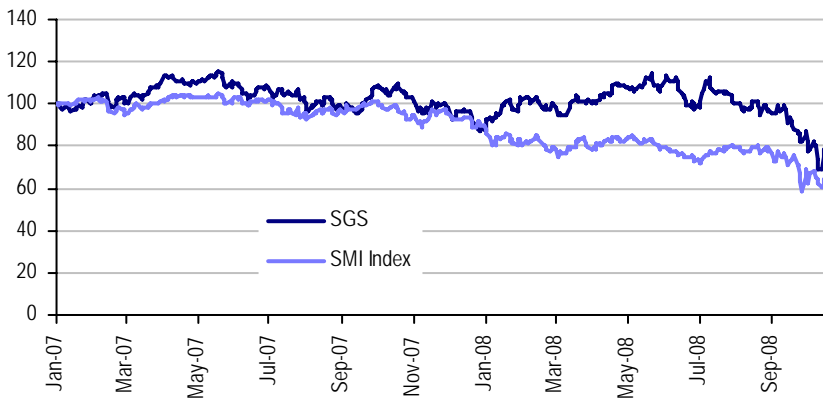
Source: Thomson Financial

Chart 2: SGS premium to BV/Intertek (average)



Source: Thomson Financial

Chart 3: SGS performance vs Swiss market



Source: Thomson Financial

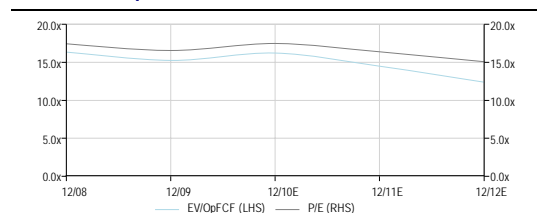
Income statement (CHFm)	12/05	12/06	12/07	12/08	12/09	12/10E	% ch	12/11E	% ch	12/12E	% ch
Revenues	3,308	3,821	4,372	4,818	4,712	4,817	2.2	5,112	6.1	5,510	7.8
Operating expenses (ex depn)	(2,666)	(3,044)	(3,464)	(3,794)	(3,670)	(3,774)	2.8	(4,007)	6.2	(4,313)	7.7
EBITDA (UBS)	642	777	908	1,024	1,042	1,044	0.2	1,105	5.9	1,196	8.2
Depreciation	(140)	(172)	(197)	(214)	(228)	(211)	-7.6	(219)	3.9	(236)	7.8
Operating income (EBIT, UBS)	502	605	711	810	814	833	2.3	886	6.4	960	8.3
Other income & associates	0	0	0	0	0	0	-	0	-	0	-
Net interest	5	(1)	2	(4)	(3)	(4)	45.7	(2)	-43.5	(1)	-70.5
Abnormal items (pre-tax)	0	19	(21)	127	(20)	0	-	0	-	0	-
Profit before tax	507	623	692	933	791	829	4.8	884	6.6	960	8.6
Tax	(119)	(155)	(172)	(219)	(200)	(211)	5.7	(225)	6.6	(245)	8.6
Profit after tax	388	468	520	714	591	617	4.5	658	6.6	715	8.6
Abnormal items (post-tax)	0	0	0	0	0	0	-	0	-	0	-
Minorities / pref dividends	(17)	(25)	(20)	(22)	(25)	(25)	-1.2	(26)	6.6	(29)	8.6
Net income (local GAAP)	371	443	500	692	566	593	4.7	632	6.6	686	8.6
Net Income (UBS)	371	424	515	579	579	593	2.4	632	6.6	686	8.6
Tax rate (%)	23	25	25	23	25	26	0.9	26	0.0	26	0.0
Pre-abnormal tax rate (%)	23	26	25	25	26	26	-0.1	26	0.0	26	0.0
Per share (CHF)	12/05	12/06	12/07	12/08	12/09	12/10E	% ch	12/11E	% ch	12/12E	% ch
EPS (local GAAP)	49.46	58.28	65.47	91.06	75.50	79.05	4.7	84.31	6.6	91.53	8.6
EPS (UBS)	49.46	55.77	67.43	76.19	77.23	79.05	2.4	84.31	6.6	91.53	8.6
Net DPS	30.30	19.69	35.00	50.00	60.00	35.00	-41.7	37.33	6.6	40.52	8.6
Cash EPS	68.12	78.42	93.23	104.35	107.64	107.16	-0.4	113.53	5.9	123.02	8.4
BVPS	183.97	199.69	248.15	240.23	279.80	302.00	7.9	355.04	17.6	413.30	16.4
Balance sheet (CHFm)	12/05	12/06	12/07	12/08	12/09	12/10E	% ch	12/11E	% ch	12/12E	% ch
Net tangible fixed assets	586	656	738	721	751	832	10.8	920	10.5	1,014	10.3
Net intangible fixed assets	429	644	716	759	785	785	0.0	785	0.0	785	0.0
Net working capital (incl. other assets)	446	407	418	464	439	435	-0.9	447	2.7	465	4.1
Other liabilities	(418)	(332)	(275)	(332)	(326)	(326)	0.0	(326)	0.0	(326)	0.0
Operating invested capital	1,043	1,375	1,597	1,612	1,649	1,726	4.7	1,826	5.8	1,939	6.2
Investments	2	2	2	2	2	2	0.0	2	0.0	2	0.0
Total capital employed	1,045	1,377	1,599	1,614	1,651	1,728	4.7	1,828	5.7	1,941	6.2
Shareholders' equity	1,439	1,562	1,941	1,825	2,090	2,259	8.1	2,655	17.6	3,091	16.4
Minority interests	36	30	36	37	37	37	0.0	37	0.0	37	0.0
Total equity	1,475	1,592	1,977	1,862	2,127	2,296	7.9	2,692	17.3	3,128	16.2
Net debt / (cash)	(430)	(215)	(378)	(248)	(476)	(567)	19.2	(865)	52.4	(1,187)	37.3
Debt deemed provisions	0	0	0	0	0	0	-	0	-	0	-
Total capital employed	1,045	1,377	1,599	1,614	1,651	1,728	4.7	1,828	5.7	1,941	6.2
Cash flow (CHFm)	12/05	12/06	12/07	12/08	12/09	12/10E	% ch	12/11E	% ch	12/12E	% ch
Operating income (EBIT, UBS)	502	605	711	810	814	833	2.3	886	6.4	960	8.3
Depreciation	140	172	197	214	228	211	-7.6	219	3.9	236	7.8
Net change in working capital	(60)	(38)	16	(21)	13	4	-71.2	(12)	-	(19)	58.4
Other (operating)	(20)	(103)	(76)	28	0	-	-	-	-	-	-
Operating cash flow	562	746	920	1,002	1,055	1,048	-0.7	1,094	4.4	1,178	7.7
Net interest received / (paid)	5	(1)	2	2	(6)	-	-	-	-	-	-
Dividends paid	(97)	(248)	(178)	(281)	(391)	(449)	14.8	(262)	-41.7	(279)	6.6
Tax paid	(107)	(144)	(177)	(195)	(217)	(211)	-2.6	(225)	6.6	(245)	8.6
Capital expenditure	(205)	(248)	(285)	(290)	(209)	(253)	21.0	(307)	21.3	(331)	7.8
Net (acquisitions) / disposals	(80)	(154)	(57)	(172)	8	(39)	-	0	-	0	-
Other	(39)	(15)	(36)	75	(28)	(25)	-11.8	(26)	6.6	(29)	8.6
Share issues	(1)	(102)	(8)	(201)	15	0	-	0	-	0	-
Cash flow (inc)/dec in net debt	38	(166)	181	(66)	230	67	-71.1	271	307.0	294	8.5
FX / non cash items	(46)	(49)	(18)	(64)	(2)	25	-	26	6.6	29	8.6
Balance sheet (inc)/dec in net debt	(8)	(215)	163	(130)	228	91	-60.0	297	225.8	323	8.5
Core EBITDA	642	777	908	1,024	1,042	1,044	0.2	1,105	5.9	1,196	8.2
Maintenance capital expenditure	(221)	(221)	(221)	(221)	(221)	(221)	0.0	(221)	0.0	(221)	0.0
Maintenance net working capital	(195)	(195)	(195)	(195)	(195)	(195)	0.0	(195)	0.0	(195)	0.0
Operating free cash flow, pre-tax	226	360	492	608	626	628	0.3	689	9.8	780	13.2

Source: Company accounts, UBS estimates. (UBS) valuations are stated before goodwill, exceptionals and other special items. Note: For some companies, the data represents an extract of the full company accounts.

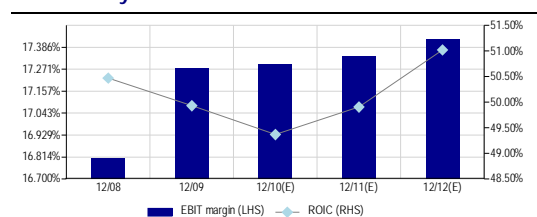
## Company profile

SGS is the largest inspection, testing and certification organisation in the world. The core services offered by SGS (split between 10 divisions) can be divided into three categories: (1) inspection services - SGS inspects and verifies the quantity, weight and quality of traded goods; (2) testing services - SGS tests product quality and performance against various health, safety and regulatory standards; and (3) certification services - SGS certifies that systems or services meet the requirements of standards set by governments, standardisation bodies or by SGS customers.

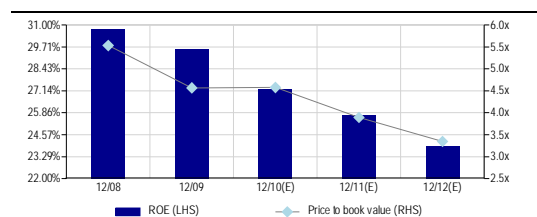
## Value (EV/OpFCF & P/E)



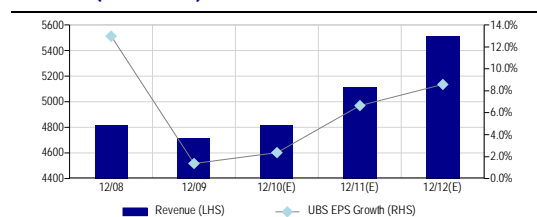
## Profitability



## ROE v Price to book value



## Growth (UBS EPS)



Valuation (x)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
P/E (local GAAP)	19.3	14.7	17.0	17.6	16.5	15.2
P/E (UBS)	19.6	17.4	16.6	17.6	16.5	15.2
P/CEPS	14.1	12.7	11.9	13.0	12.2	11.3
Net dividend yield (%)	2.5	3.8	4.7	2.5	2.7	2.9
P/BV	5.4	5.5	4.6	4.6	3.9	3.4
EV/revenue (core)	2.2	2.1	2.0	2.1	2.0	1.8
EV/EBITDA (core)	11.1	9.7	9.2	9.8	9.1	8.1
EV/EBIT (core)	14.1	12.3	11.7	12.3	11.3	10.1
EV/OpFCF (core)	24.0	16.4	15.3	16.3	14.6	12.5
EV/op. invested capital	7.2	6.2	5.9	6.1	5.7	5.2

Enterprise value (CHFm)	12/08	12/09	12/10E	12/11E	12/12E
Average market cap	10,098	9,711	10,552	10,552	10,552
+ minority interests	37	37	37	37	37
+ average net debt (cash)	(313)	(362)	(522)	(716)	(1,026)
+ pension obligations and other	120	162	162	162	162
- non-core asset value	0	0	0	0	0
Core enterprise value	9,941	9,548	10,230	10,035	9,725

Growth (%)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
Revenue	13.7	10.2	-2.2	2.2	6.1	7.8
EBITDA (UBS)	19.2	12.8	1.8	0.2	5.9	8.2
EBIT (UBS)	19.9	13.9	0.5	2.3	6.4	8.3
EPS (UBS)	18.8	13.0	1.4	2.4	6.6	8.6
Cash EPS	18.3	11.9	3.2	-0.4	5.9	8.4
Net DPS	43.6	42.9	20.0	-41.7	6.6	8.6
BVPS	11.2	-3.2	16.5	7.9	17.6	16.4

Margins (%)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
EBITDA / revenue	19.9	21.2	22.1	21.7	21.6	21.7
EBIT / revenue	15.5	16.8	17.3	17.3	17.3	17.4
Net profit (UBS) / revenue	11.2	12.0	12.3	12.3	12.4	12.5

Return on capital (%)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
EBIT ROIC (UBS)	50.9	50.5	49.9	49.4	49.9	51.0
ROIC post tax	-	37.6	37.2	36.8	37.2	38.0
Net ROE	28.3	30.7	29.6	27.3	25.7	23.9

Coverage ratios (x)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
EBIT / net interest	-	NM	NM	NM	NM	NM
Dividend cover (UBS EPS)	2.2	1.5	1.3	2.3	2.3	2.3
Div. payout ratio (% UBS EPS)	49.0	65.6	77.7	44.3	44.3	44.3
Net debt / EBITDA	NM	NM	NM	NM	NM	NM

Efficiency ratios (x)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
Revenue / op. invested capital	3.2	3.0	2.9	2.9	2.9	2.9
Revenue / fixed assets	3.4	3.3	3.1	3.1	3.1	3.1
Revenue / net working capital	18.6	20.2	20.3	22.1	23.0	23.2

Investment ratios (x)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
OpFCF / EBIT	0.6	0.8	0.8	0.8	0.8	0.8
Capex / revenue (%)	6.4	6.0	4.4	5.2	6.0	6.0
Capex / depreciation	1.5	1.4	0.9	1.2	1.4	1.4

Capital structure (%)	5Yr Avg	12/08	12/09	12/10E	12/11E	12/12E
Net debt / total equity	(21.4)	(13.6)	(22.8)	(25.1)	(32.6)	(38.4)
Net debt / (net debt + equity)	(27.2)	(15.7)	(29.5)	(33.5)	(48.3)	(62.4)
Net debt (core) / EV	(4.3)	(3.1)	(3.8)	(5.1)	(7.1)	(10.6)

Source: Company accounts, UBS estimates. (UBS) valuations are stated before goodwill, exceptionals and other special items. Valuations: based on an average share price that year, (E): based on a share price of CHF1,389.00 on 18 Jan 2010 19:07 EST Market cap(E) may include forecast share issues/buybacks.

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## ■ **SGS**

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Risks for SGS include a weakening US dollar, loss of reputation, and a lack of or unfavourable regulation.

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UBS 12-Month Rating	Rating Category	Coverage <sup>1</sup>	IB Services <sup>2</sup>
Buy	Buy	48%	40%
Neutral	Hold/Neutral	40%	35%
Sell	Sell	13%	26%
UBS Short-Term Rating	Rating Category	Coverage <sup>3</sup>	IB Services <sup>4</sup>
Buy	Buy	less than 1%	17%
Sell	Sell	less than 1%	67%

1:Percentage of companies under coverage globally within the 12-month rating category.

2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

3:Percentage of companies under coverage globally within the Short-Term rating category.

4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS. Rating allocations are as of 31 December 2009.

### UBS Investment Research: Global Equity Rating Definitions

UBS 12-Month Rating	Definition
Buy	FSR is > 6% above the MRA.
Neutral	FSR is between -6% and 6% of the MRA.
Sell	FSR is > 6% below the MRA.
UBS Short-Term Rating	Definition
Buy	Buy: Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.
Sell	Sell: Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.

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**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

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**UBS Limited:** William Vanderpump; Mark Shepperd; Jaime Brandwood, CFA.

**Company Disclosures**

Company Name	Reuters	12-mo rating	Short-term rating	Price	Price date
SGS <sup>4, 5, 13, 15, 18a, 18b</sup>	SGSN.VX	Sell	N/A	CHF1,389.00	18 Jan 2010

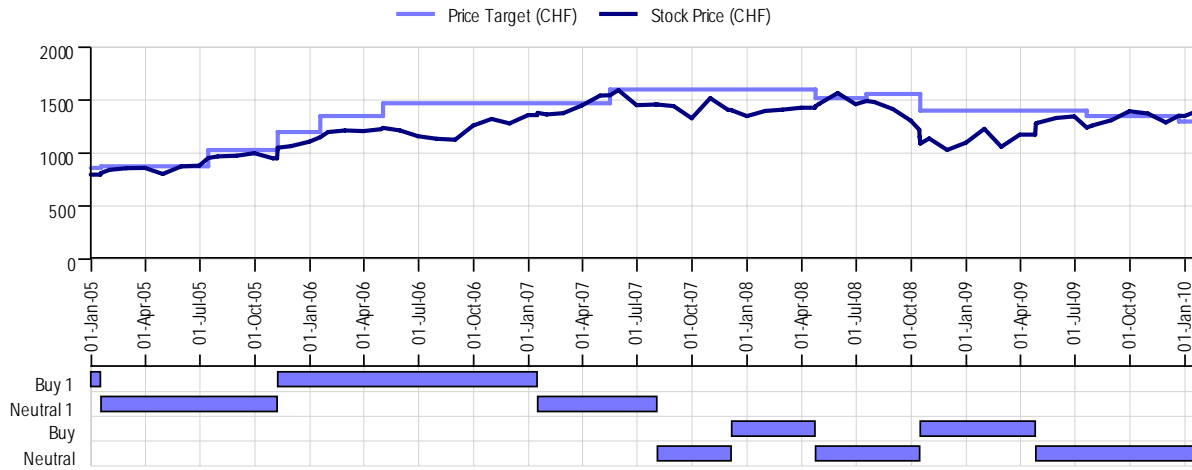
Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

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SGS (CHF)



Source: UBS; as of 18 Jan 2010

Note: On August 4, 2007 UBS revised its rating system. (See 'UBS Investment Research: Global Equity Rating Definitions' table for details). From September 9, 2006 through August 3, 2007 the UBS ratings and their definitions were: Buy 1 = FSR is > 6% above the MRA, higher degree of predictability; Buy 2 = FSR is > 6% above the MRA, lower degree of predictability; Neutral 1 = FSR is between -6% and 6% of the MRA, higher degree of predictability; Neutral 2 = FSR is between -6% and 6% of the MRA, lower degree of predictability; Reduce 1 = FSR is > 6% below the MRA, higher degree of predictability; Reduce 2 = FSR is > 6% below the MRA, lower degree of predictability. The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities. From October 13, 2003 through September 8, 2006 the percentage band criteria used in the rating system was 10%.

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