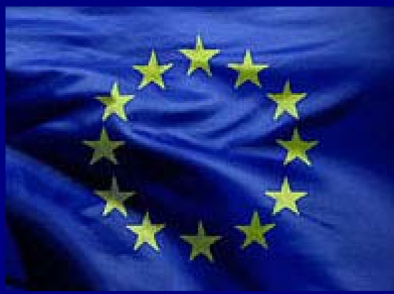
# Dolmen Stockbrokers

# European Front Five



13 Feb 2006

# ADIDAS

## BUY

| | |
|---|---|
| **Current Price** | **€169** |
| **Target Price** | **€184** |
| **Market Cap** | **€8.6bln** |

**Stock Codes**

| | |
|---|---|
| **ADSG.DE** | **Reuters** |
| **ADS GY** | **Bloomberg** |

**Sales by region**

| | |
|---|---|
| **US & LatAm** | **36%** |
| **Europe** | **46%** |
| **Asia** | **16%** |
| **RoW** | **2%** |

**Profits by division**

| | |
|---|---|
| **Adidas Brand** | **88%** |
| **Taylormade** | **12%** |

**Company Profile:**
Adidas is a global leader in the sporting goods industry and offers a broad portfolio of products. The group's principal brands are Adidas (Footwear, apparel, and hardware such as bags and balls), TaylorMade-Adidas Golf (Golf equipment, golf apparel, golf shoes) and Maxfli (Golf balls, irons and accessories). In 1997 adidas AG acquired the Salomon Group with the brands Salomon, TaylorMade, Mavic and Bonfire, forming a new company named adidas-Salomon AG. In October 2005 the Salomon Group was sold to Amer Sports. The legal name of the company will change to "Adidas AG" in May/ June 2006.

**Buoyant outlook:** Things are looking good for Adidas in 2006. Through the completion of its takeover of Reebok, Adidas can close the gap on its closest rival and world leader, Nike, while sales are to receive a boost in the run-up to the 2006 football World Cup in June.

Merger synergies : In August 2005, Adidas announced plans to buy  Reebok in a €3.1bn deal through a combination of debt and equity. In November 2005, Adidas raised €648m through a placing of c.4.5m new shares at €143 per share. The placing accounted for 20% of the projected takeover price, leaving the balance to be financed by debt. The deal is expected to be completed in the first half of 2006, once it is approved by Reebok's shareholders as well as by the regulatory authorities. Adidas is now filing for European anti-trust approval for the takeover after US authorities had voiced no objections.

**Positive earnings impact:** The complementary nature of the two businesses in various geographical regions, products and customer segments provides a significant opportunity for increased value creation. The deal will give rise to substantial cost savings (in the region of €125m) as well as incremental revenue and profits from more complete coverage of all consumer segments. Taking over Reebok will more than double the German group's North American sales. The deal will create a company with combined worldwide sales of €8.9 bn, closing the gap with Nike, which has annual sales of c.€10 bn. The deal will boost earnings by at least 10% in the first full year, rising to c.20% over 3 years.

**Recent results:** A day before the share placing, Adidas reported forecast beating Q3 sales numbers and lifted its earnings forecast for 2005. The company said it expected robust growth in North America, order backlogs and positive trading conditions to boost sales growth, while European Q4 sales will be boosted by products launched ahead of the 2006 World Cup. The group predicted it would increase earnings by "double digit rates" in 2006 and currency-neutral sales by "high-single digit rates".

**Peer discount:** Following the Reebok deal, Adidas appears to be on course to generate a 2006 eps of €11.50, leaving the shares currently trading at 14.0x 2006 eps, an 8% discount to Nike, which is trading at 15.1x 2006 eps. Given Adidas' stronger earnings growth, our view is that this valuation gap should close over the course of 2006, and our 12 month price target of €184.

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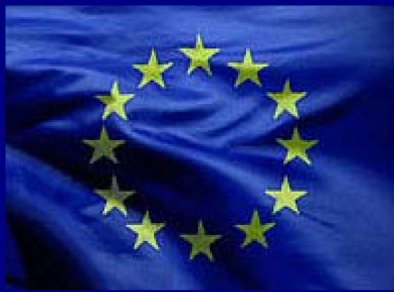

13 Feb 2006

# INDITEX

## BUY

| | |
|---|---|
| **Current Price** | **€28.60** |
| **Target Price** | **€31.50** |
| | |
| **Market Cap** | **€17bln** |

**Stock Codes**

| | |
|---|---|
| **ITX.MC** | **Reuters** |
| **ITX** | **Bloomberg** |

**Sales by Region**

| | |
|---|---|
| **Spain** | **45.5%** |
| **Rest of EU** | **37.3%** |
| **America** | **10.5%** |
| **RoW** | **6.7%** |

**Profits by Division**

| | |
|---|---|
| **Zara** | **67.4%** |
| **Pull and Bear** | **6.7%** |
| **MassimoDutti** | **8.5%** |
| **Bershka** | **9.1%** |
| **Kiddys Class** | **2.1%** |
| **Strad & Oysho** | **5.6%** |

**Company Profile:**
Inditex Group is engaged in clothing and textile design, manufacturing and distribution. The Company roots are in Spain and Inditex's activities are primarily based around eight sales formats: Zara, Pull and Bear, Massimo Dutti, Bershka, Stradivarius, Oysho, Zara Home and Kiddy's Class. These retail outlets predominantly sell women's fashion clothing, but also offer lingerie, cosmetics, shoewear, children's clothing and menswear. As of January 31, 2004 (fiscal year-end 2003), Inditex's subsidiaries operated through 2,035 stores across 50 countries in Europe, the Americas, Asia and Africa. In 2003, Zara Home was established, which is a specialty home furnishings chain. Its focus is on textiles such as bed, table and bathroom linens, complemented by tableware, cutlery, glassware and decorative items.

**Q3 results:** Aggressive expansion coupled with cost controls helped Inditex post a 28 per cent increase in net profits for the nine months to the end of October, ahead of expectations. The company said net profit for the February 1 to October 31 period was €520.5m, up from €407.4m a year earlier. Total sales rose 20 percent to €4.65bn. Growth was buoyed by the opening of 323 stores during the first nine months of the year, compared with 241 store openings a year earlier.

**Improving margins:** Inditex also said that on the back of good product management it had reduced its cost of sales by 1.4 percentage points, to give a gross margin of 57 per cent. This represented the company's third consecutive quarter of decreasing costs. Its cost control is particularly impressive given the company's aggressive expansion strategy.

**Special dividend:** Speaking after the results in December, management at Inditex said that they are 'comfortable with a no cash, no debt position.'. This is in line with the view that that the company will distribute a proportion of the company's cash to shareholders by way of a generous dividend policy, which could see the payout ratio increase from 30 per cent to 60 per cent. This could double the company's dividend yield to 3.5% - 4%. The exact details of the company's dividend policy should accompany the FY results release, due on March 29th.

**Valuation:** Inditex shares now trade on a 21x 2005/06 P/E falling to 18.8x in 2006/07. This compares to Swedish company, H&M, Inditex closest peer, which trades on 2005e and 2006e P/Es of 24x and 21x. The 15% discount that Inditex trades at compared to H&M would appear unjustified given the superior earnings growth of Inditex. Our price target of €31.5 is based on 21.8x 06/07 consensus eps of €1.44. **BUY**

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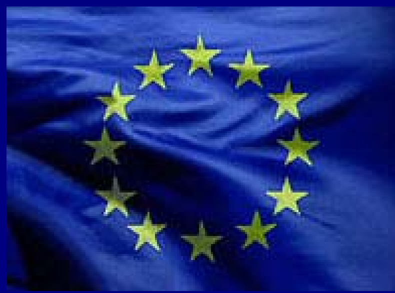

13 Feb 2006

# SAP

## BUY

| | |
|---|---|
| **Current Price** | **€167** |
| **Target Price** | **€190** |
| | |
| **Market Cap** | **€45bln** |

**Stock Codes**
**SAPG.DE Reuters**
**SAP GY Bloomberg**

| **Sales by Region** | |
|---|---|
| **Europe** | **50%** |
| **US** | **36%** |
| **Asia** | **14%** |

| **Sales by Division** | |
|---|---|
| **License Revs** | **33%** |
| **Maintenance Revs** | **38%** |
| **Consulting Revs** | **25%** |
| **Training Revs** | **4%** |

**Company Profile:**
Company profile: SAP AG (SAP) is a provider of business software solutions. Its principal activities are the development, marketing, sales and support of a variety of software solutions, primarily enterprise application software products for organizations, including corporations, governmental agencies and educational institutions.

**Recent results:** In late January SAP released an impressive set of full year numbers for 2005. The business software-maker reported a 14% rise in fourth-quarter net profit to €619m, with revenue up 15% to €2.75bn, led by 30% growth in the Americas. License sales rose 18% in the period. It raised its worldwide market share to 62%, up two percentage points from the third quarter, and increased its U.S. market share to 47%, up three percentage points from the third quarter.

**Raised guidance:** The results had been well flagged from a previous update in early January, so it was the company's guidance for 2006 that was under the spotlight. The company's outlook for 2006 was stronger than expected and indicates that the company is comfortable to build on the momentum from 2005. SAP said 2006 license sales should rise 15% to 17% (versus market expectations of 14%), and predicted that earnings per share this year would rise 16% to 20%, or €5.58-€6.00 (versus market expectations of €5.75).

**Improving margins:** SAP also said that operating margins should rise 50bp-100bp in 2006. With expected 2006 margins in the range of 28.8%-29.3%, it would appear that management is on track to achieving its 2007 margin target of 30%.

**Increased share buyback:** SAP also confirmed that it intends to increase its buyback activities in 2006 after buying 3.21m shares (€417m total value) in 2005.

**Conclusion:** The strength of SAP's guidance is impressive and will go a long way in dispelling any concerns that some bears have had regarding the company's margin expansion and revenue growth. The company's accelerating revenue profile, highlighted by the strength of its license revenue growth, and evidence of further market share gains will ensure another strong performance from SAP in 2006. Based on 06 eps forecast SAP currently trades in line with the peer average of 24x. However given the quality of SAP's earnings growth forecast for 06-07 a multiple of 27x would appear more applicable. Our price target of €190 is based on 27x 07 eps of €7.00. **BUY**

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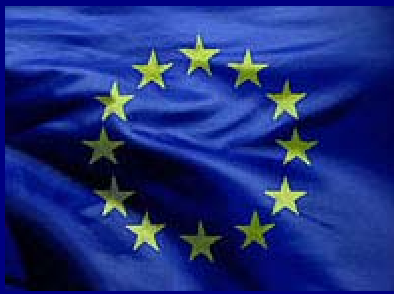

13 Feb 2006

# BMW

## BUY

**Current Price** €39.50
**Target Price** €48.00

**Market Cap** €25bln

**Stock Codes**

| | |
|---|---|
| BMWG.DE | Reuters |
| BMW GY | Bloomberg |

**Sales by Region**

| | |
|---|---|
| Germany | 27% |
| North America | 23% |
| Rest of Europe | 24% |
| UK | 12% |
| Asia | 11% |
| Other | 3% |

**Sales by Units**

| | |
|---|---|
| 1 Series | 13% |
| 3 Series | 38% |
| Z3/Z4 | 3% |
| 5 Series | 20% |
| 6 Series | 2% |
| 7 Series | 4% |
| X3 | 10% |
| X5 | 9% |

**Company Profile**

With the three brands, BMW, MINI and Rolls-Royce Motor Cars, the BMW Group has its sights set firmly on the premium sector of the international automobile market.

**Recent Results**

Stronger FY2005 sales highlight how strong Q4 2005 revenues were, albeit no doubt helped by the stronger yoy US$ rate. Gross auto revenues grew 12% to EUR12.3bn, despite just 5.5% unit sales growth against tough Q4 2005 comps. Revenue per unit grew 6.1% in Q4 to . 36.2k, the only positive quarter in 2005. New 3-series sales are improving the sales mix, and should help BMW maintain margins. Group revenues in Q4 rose 15.6% to EUR12.4bn, the best quarter of 2005. The company left its profit guidance of flat earnings in 2005 unchanged. The full set of numbers will be released in early March, about one week ahead of the publication of the annual report on 15 March.

**Cashflow**

Cash flow remains a BMW strength, with industrial Free Cash Flow of EUR547m in Q3 2005, albeit helped by strong inflows from working capital, against industrial FCF of EUR456m in Q3 2004. Operating cash flow has remained very strong, at EUR2.5bn, due to strong working capital inflows which calculates to over 10% of the group market capitalisation. BMW has gone through a significant capital expenditure programme over the past three years as the group brought a number of new flagship models to the market. Capex has slowed since H1 2005 and the group has committed to buying back up to 10% of its market capitalisation.

**Buy Back Programme**

To reflect the cash accumulation, BMW in May announced that it would seek authorisation to buy back up to 10% of its share capital for up to €2.5bn. BMW announced a 3% buy-back in September, and has purchased around 19m shares already since then. We expect a further 3% buy-back to be announced in March 2006. We have reflected this in our 2005E and 2006E forecasts. The point is, however, that the share buy-back underpins the shares at current levels, and should limit downside risk. With limited downside risk, and with over 30% upside to our TP of €48, we believe the shares remain very attractive.

**Valuation**

BMW's 2006E P/E is at a 12-year low versus annual averages at 10.2 times. 6bn industrial cash and . 2bn annual free cash flow continue to support our buy recommendation. Underpinned by the expected EUR2.5bn share buy-back programme, this sets the scene for an inevitable rerating of BMW shares from current levels. The stock under-performed the German market by 8% in 2005 but has started 2006 in a better position rising 9% and out-performing the DAX by 3.2%. We are expecting this trend to continue for 2006 and have a 12 month target of €48 on BMW representing 20% upside.

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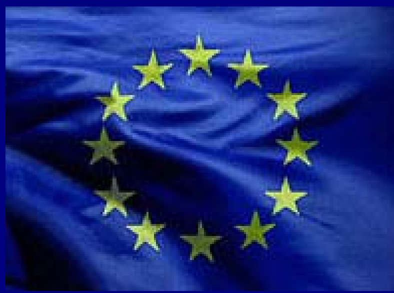

13 Feb 2006

# TOTAL

## BUY

**Current Price €214**
**Target Price €235**

**Market Cap €130bln**

**Stock Codes**

| | |
|---|---|
| **TOTP.PA** | **Reuters** |
| **BMW FP** | **Bloomberg** |

**Production by Region**

| | |
|---|---|
| **EU** | **37%** |
| **Africa** | **34%** |
| **US** | **3%** |
| **Asia** | **11%** |
| **Middle East** | **5%** |
| **South America** | **10%** |

**Sales by Division**

| | |
|---|---|
| **Exploration/Prod** | **74%** |
| **Refining** | **19%** |

**Company Profile:**
Total, is our preferred European stock in this sector. Total's businesses cover the entire oil and gas chain, from crude oil and natural gas exploration and production to the gas downstream, transportation, refining, petroleum product marketing, and international crude oil and product trading. Total is also a world-class chemicals manufacturer. Total's global businesses are divided into three segments: Upstream (Exploration & Production), Downstream (Trading & Shipping, and Refining), and Chemicals.

**Oil stocks to out-perform:** In 2005 the oil sector has enjoyed a year of substantial out-performance as crude oil prices surged for a vast array of reasons ranging from supply/demand imbalances, weather related production delays, a lack of refining capacity and an increase in the level of speculative activity via hedge funds. With the price of oil at $67 the sector still holds attractions for investors. The 'stress test' level for the main producers is typically between US$25-US$30, so at current prices the oil majors are generating enormous levels of cash, which will continue to support dividend increases and continued share buy-back programmes.

Cash returns: Total's continued return of excess capital to shareholders through a combination of dividends and share buybacks offer investors a compelling attraction to its shares. Since 2000, Total has repurchased over €20bln of its outstanding shares and paid almost €17bln in dividends.

We expect Total to continue to pursue this strategy over the coming years. The expected sale of Total's 12.5% stake in Sanofi-Aventis (within next 18 months) could result in further cash returns, while the imminent spin-off of its Arkema base chemicals business (expected in May) has the potential to return an additional €3bn to shareholders.

**Increased dividend:** In Q3, Total confirmed its shareholder return policy with a 25% increase in the interim dividend to €3 per share. Total is currently on course to pay a FY dividend of €6.50 (a yield of c.3%), which would represent a 20% year on year increase.

**Q3 results:** In November 2005 Total revealed a sharp jump in third-quarter profits as it benefited from rising crude oil prices in the wake of hurricanes Katrina and Rita. The group said net profits increased 32 per cent to €3.13bn in the three months to September 30. Sales rose 19 per cent to €38.4bn. The third quarter was marked by a 48 per cent increase in Brent Crude oil prices and a 35 per cent rise in refining margins in Europe, where Total is the leading refiner. Total suffered less than its larger European rivals BP and Shell because of its reduced exposure to the hurricane-hit region.

Total is due to report results on Wednesday and we are expecting a strong set of numbers from the Group. Q4 net income is expected to rise 25% to circa €3lbn. We remain bullish on the Oil sector for 2006 and Total is our top European pick in the sector given its strong production base, attractive valuation and good business mix.

# Dolmen Stockbrokers

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