

27 August 2013 | 20 pages

Department Stores (GICS) | Retailing - Broadlines (Citi)  
Western Europe | United Kingdom

# Marks and Spencer Group PLC (MKS.L)

## There Is A Light

- **M&S upgraded to Buy (from Neutral), target price 535p (from 470p)** — The combination of recent, material upgrades to UK economic growth forecasts, and M&S management initiatives have markedly improved the credibility of double-digit FY15 and FY16 M&S EPS growth forecasts. We argue that this should underpin the group's current undemanding valuation metrics. Holding the group's 11.5x FY15E EV/EBIT multiple out to FY16 drives a new 535p price target (raised from 470p) and our move to a Buy rating.
- **2014 and 2015 UK non-food sector LFL sales forecast raised c.+2%pts to +2.5% and +3.5%** — In combination, the recent +80bp upgrade to Citi's 2014 GDP growth forecast (the largest upgrade across our global economic coverage), recent reductions in UK savings ratio expectations, and upgrades to 2015 UK employment growth/wage growth forecasts, have driven a +150bp and +250bp increase in our 2014 and 2015 UK non-food LFL sales forecasts to +2.5% and +3.5%.
- **M&S management initiatives support better LFL gross profit trends post FY14** — Primarily as a consequence of significant IT, logistics and supply chain investment programmes over the last 3-4 years, M&S General Merchandise should begin to see both revenue (availability +9%pts) and gross margin improvements (reduced mark-down activity) from FY14.
- **Credible double-digit M&S EPS growth in FY15 and FY16 despite dull 2QFY14** — While we have trimmed our FY14 EPS by -2.2% to reflect a dull 2Q LFL and GM% forecast (see below), as a consequence of the above analysis, we are more confident that following eight quarters of LFL sales declines, the M&S General Merchandise division can deliver positive LFL gross profit trends beyond this year. This drives a +13% and +11% FY15 and FY16 EPS growth forecast, representing an unchanged and +3.2% EPS forecast increase respectively (see below).
- **Future uses of cash** — Management's statement that material improvement in free cashflow from FY15 will drive an assessment of cash uses with a view to delivering improved shareholder returns, offers further medium term share price support.

- Rating Change
- Target Price Change
- Estimate Change

Buy	1
from Neutral	
Price (23 Aug 13)	£4.64
Target price	£5.35
from £4.70	
Expected share price return	15.4%
Expected dividend yield	3.9%
Expected total return	19.3%
Market Cap	£7,489M
	US\$11,674M

Price Performance  
(RIC: MKS.L, BB: MKS LN)



Figure 1. Marks & Spencer – Statistical Abstract

Yr to Mar	EBIT (£m)	PBT (£m)	Tax Rate (%)	EPS (p)	EPS Old (p)	P/E	Net Div (p)	Div Yld (%)	EV/ Sales	EV/ EBIT	EV/ EBITDA
2011A	825	714	25.1%	32.7	32.7	14.0	17.0	3.7	0.95	11.2	7.2
2012A	810	706	24.5%	32.0	32.0	14.3	17.0	3.7	0.93	11.4	7.1
2013A	782	665	22.7%	31.3	31.3	14.7	17.0	3.7	0.99	12.7	8.0
2014E	814	670	21.5%	32.0	32.8	14.3	18.0	3.9	0.98	12.5	7.6
2015E	884	745	20.5%	36.2	36.2	12.7	19.0	4.1	0.93	11.3	6.9
2016E	956	825	20.5%	40.1	38.9	11.4	20.0	4.4	0.87	10.2	6.5
							Price	YTD	1M	3M	12M
							Abs%	19.5	(5.6)	(2.3)	25.3
							Rel %	8.6	(2.6)	2.9	12.1
	Gearing = 66.6%			Shares = 1,599.7							
	FV = 10,143			MV = 7,342.6							

Richard Edwards  
+44-20-7986-4006  
richard.edwards@citi.com

Assad M Malic  
+44-20-7986-8139  
assad1.malic@citi.com

Dan F Homan  
+44-20-7986-4112  
dan.homan@citi.com

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

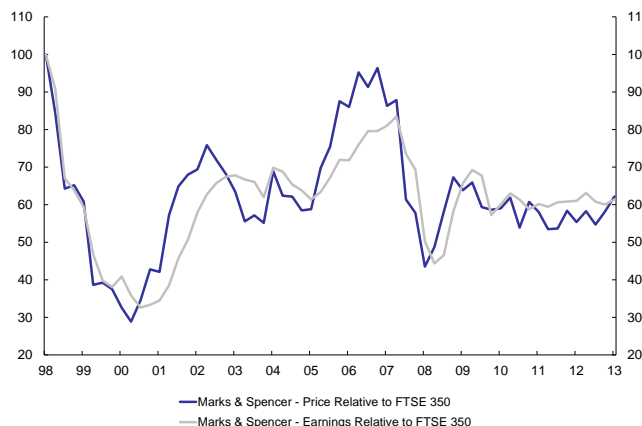
Citi Research is a division of Citigroup Global Markets Inc. (the "Firm"), which does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the Firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.

MKS.L: Fiscal year end 31-Mar						Price: £4.64; TP: £5.35; Market Cap: £7,497m; Recomm: Buy					
Profit & Loss (£m)	2012	2013	2014E	2015E	2016E	Valuation ratios	2012	2013	2014E	2015E	2016E
Sales revenue	9,934	10,027	10,308	10,752	11,194	PE (x)	14.5	14.8	14.5	12.8	11.6
Cost of sales	-5,884	-5,927	-6,073	-6,303	-6,522	PB (x)	2.6	3.0	2.7	2.4	2.2
Gross profit	4,050	4,100	4,236	4,449	4,672	EV/EBITDA (x)	7.2	7.7	7.6	7.1	6.6
Gross Margin (%)	40.8	40.9	41.1	41.4	41.7	FCF yield (%)	4.2	1.6	2.5	7.6	8.4
<b>EBITDA (Adj)</b>	<b>1,290</b>	<b>1,249</b>	<b>1,331</b>	<b>1,434</b>	<b>1,506</b>	Dividend yield (%)	3.7	3.7	3.9	4.1	4.3
EBITDA Margin (Adj) (%)	13.0	12.5	12.9	13.3	13.5	Payout ratio (%)	53	54	56	53	50
Depreciation	-480	-467	-517	-550	-550	ROE (%)	18.6	19.0	19.6	20.1	20.1
{001763}	0	0	0	0	0	Cashflow (£m)					
<b>EBIT (Adj)</b>	<b>810</b>	<b>782</b>	<b>814</b>	<b>884</b>	<b>956</b>	EBITDA	1,290	1,249	1,331	1,434	1,506
EBIT Margin (Adj) (%)	8.2	7.8	7.9	8.2	8.5	Working capital	86	-5	0	-20	-20
Net interest	-130	-143	-150	-145	-137	Other	-301	-298	-369	-298	-306
Associates	0	0	0	0	0	<b>Operating cashflow</b>	<b>1,075</b>	<b>946</b>	<b>962</b>	<b>1,116</b>	<b>1,180</b>
Non-op/Except	26	27	6	6	6	Capex	-766	-830	-775	-550	-550
<b>Pre-tax profit</b>	<b>706</b>	<b>665</b>	<b>670</b>	<b>745</b>	<b>825</b>	Net acq/disposals	-102	-644	-100	-100	-100
Tax	-173	-151	-144	-153	-169	Other	0	0	0	0	0
Extraord./Min.Int./Pref.div.	-24	-10	-10	-10	-10	<b>Investing cashflow</b>	<b>-868</b>	<b>-1,474</b>	<b>-875</b>	<b>-650</b>	<b>-650</b>
<b>Reported net profit</b>	<b>509</b>	<b>504</b>	<b>516</b>	<b>582</b>	<b>646</b>	Dividends paid	-268	-272	-274	-287	-303
Net Margin (%)	5.1	5.0	5.0	5.4	5.8	<b>Financing cashflow</b>	<b>-481</b>	<b>524</b>	<b>-87</b>	<b>-466</b>	<b>2,284</b>
Core NPAT	509	504	516	582	646	<b>Net change in cash</b>	<b>-274</b>	<b>-3</b>	<b>0</b>	<b>0</b>	<b>2,814</b>
Per share data						Free cashflow to s/holders					
Reported EPS (p)	32.0	31.3	32.0	36.2	40.1		309	117	187	566	630
Core EPS (p)	32.0	31.3	32.0	36.2	40.1						
DPS (p)	17.0	17.0	18.0	19.0	20.0						
CFPS (p)	67.5	58.8	59.8	69.3	73.3						
FCFPS (p)	19.4	7.2	11.6	35.2	39.1						
BVPS (p)	176.7	156.6	171.9	190.3	211.6						
Wtd avg ord shares (m)	1,592	1,610	1,610	1,610	1,610						
Wtd avg diluted shares (m)	1,592	1,610	1,610	1,610	1,610						
Growth rates											
Sales revenue (%)	2.0	0.9	2.8	4.3	4.1						
EBIT (Adj) (%)	-1.8	-3.5	4.1	8.6	8.1						
Core NPAT (%)	-2.3	-1.0	2.3	12.9	10.9						
Core EPS (%)	-2.3	-2.1	2.3	12.9	10.9						
Balance Sheet (£m)											
Cash & cash equiv.	196	193	193	193	193						
Accounts receivables	116	112	115	120	125						
Inventory	682	767	789	823	857						
Net fixed & other tangibles	4,790	5,034	5,291	5,291	5,291						
Goodwill & intangibles	584	695	695	695	695						
Financial & other assets	75	97	97	97	97						
<b>Total assets</b>	<b>6,443</b>	<b>6,898</b>	<b>7,180</b>	<b>7,219</b>	<b>7,258</b>						
Accounts payable	989	1,026	1,026	1,026	1,026						
Short-term debt	0	0	0	0	0						
Long-term debt	2,053	2,807	2,994	2,814	2,587						
Provisions & other liab	622	578	430	354	278						
<b>Total liabilities</b>	<b>3,664</b>	<b>4,412</b>	<b>4,450</b>	<b>4,194</b>	<b>3,891</b>						
Shareholders' equity	2,790	2,505	2,750	3,044	3,386						
Minority interests	-11	-19	-19	-19	-19						
<b>Total equity</b>	<b>2,779</b>	<b>2,486</b>	<b>2,731</b>	<b>3,025</b>	<b>3,367</b>						
<b>Net debt</b>	<b>1,857</b>	<b>2,614</b>	<b>2,801</b>	<b>2,621</b>	<b>2,394</b>						
Net debt to equity (%)	66.8	105.1	102.6	86.7	71.1						

For further data queries on Citi's full coverage universe please contact Citi Research Data Services at CitiRsch.DataServices.Global@citi.com  
For definitions of the items in this table, please click [here](#).

## Share Price and Earnings Trends

Figure 2. Marks and Spencer – 15 Yr Price & Earnings Relative



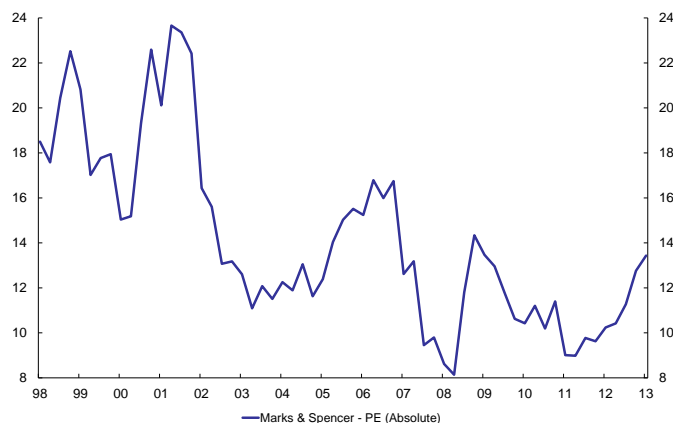
Source: DataStream

Figure 3. Marks and Spencer – 15 Yr Price & Earnings Absolute



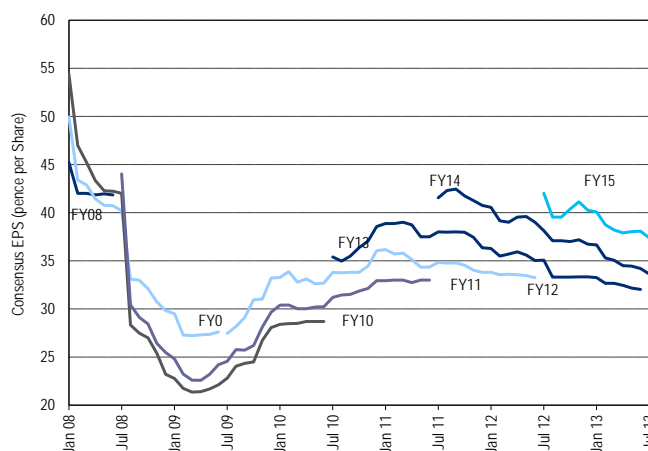
Source: DataStream

Figure 4. Marks and Spencer – Long Run PE Valuation



Source: DataStream

Figure 5. Marks and Spencer – Consensus EPS



Source: DataStream

**Changes:** FY14, FY15 and FY16 EPS -2.2%, unchanged, and +3.2% to 32p, 36.2p and 40.1p respectively

**Next results:** Interims on 5 November 2013

**The market view?** 9 Buys, 10 Holds, 10 Sells

Source: Reuters

## UK HAC Analysis

**UK GDP growth forecasts have been significantly raised in the last month for 2014 and 2015**

On the back of recent UK macro-economic data and economists' UK forecast revisions, we have reviewed our UK Household Available Cashflow forecast agenda. Here we make three observations.

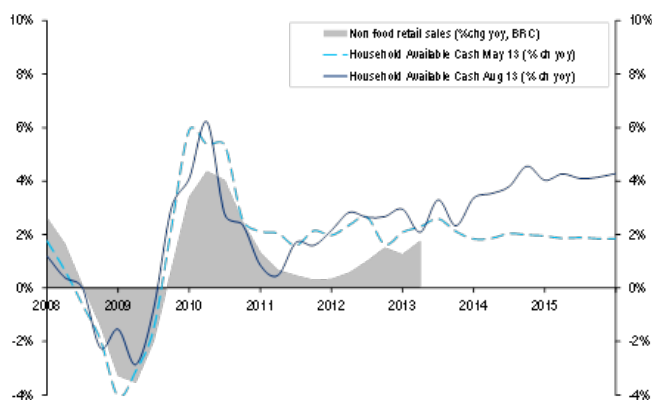
- Firstly, UK GDP growth forecasts have been significantly raised in the last month for 2014 and 2015, so for example, Citi has raised its 2013, 2014 and 2015 UK GDP growth forecasts from +0.9%, +1.3% and +1.8% to +1.1%, +2.1% and +2.7% respectively (cf: [Global Economic Outlook and Strategy - August 2013](#), 21 August).
- Secondly, and more specifically in relation to UK Household Available Cashflow growth trends, UK savings ratio forecasts have reduced from a steady 7% to sub-6% for 2013-2015.
- Finally looking out to 2015, wage inflation and/or employment growth forecasts have significantly improved, driving UK consumer gross earnings growth forecasts of c.+4% from c.+2.5%.

**We raise our 2014 and 2015 UK non-food retail LFL sales forecast to +2.5% and +3.5% in 2014 and 2015 (from a c.+1% forecast in both years)**

Taking these themes together, we have raised our previous steady c.+2% p.a. HAC growth forecast (2012-2015) to +2.8%, +3.5% and +4.3% in 2013, 2014 and 2015 respectively. Stripping the c.+1% annual UK retail space increase (albeit this is a fading metric), we derive a +1.6% 2013 UK non-food retail LFL sales forecast (broadly in line with the BRC non-food LFL sales trend so far this year), rising to +2.5% and +3.5% in 2014 and 2015 (from our previous c.+1% forecast in both years).

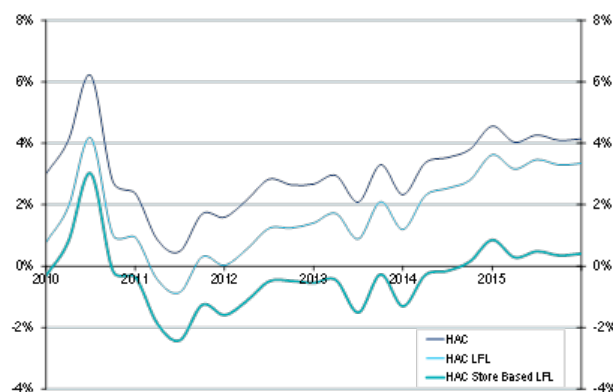
The analysis behind this forecast and the recent trends of the primary drivers are set out below. Notably, as a consequence of this improved UK non-food retail demand forecast, the current declining store-based LFL sales (ex-online sales) trends are expected to stabilise in 2014 and 2015, easing some of the pressure on store-based operating profit margins (albeit opex reduction programmes are still likely to be needed to hold store-based EBIT margins).

Figure 6. Household Available Cash (short run, 2008-15)



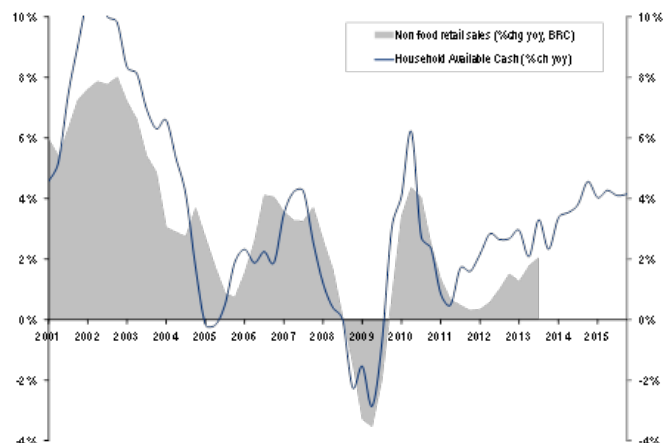
Source: ONS, DataStream, BoE and BRC and Citi Research Estimates

Figure 7. Household Available Cash with Implied Store LFL



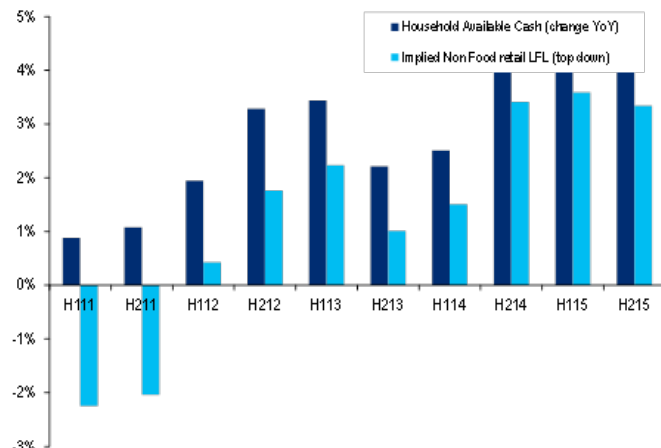
Source: ONS, DataStream, BoE and BRC and Citi Research Estimates

Figure 8. Household Available Cash vs. Non-Food Retail Sales



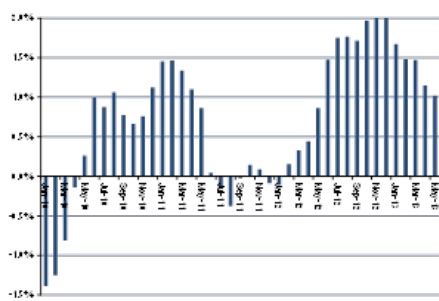
Source: ONS, DataStream, BoE and BRC and Citi Research Estimates

Figure 9. Household Available Cash – Half-Yearly LFL



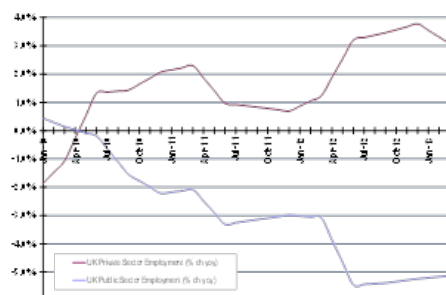
Source: ONS, DataStream, BoE and BRC and Citi Research Estimates

Figure 10. UK Employment (3m ave % ch yoy)



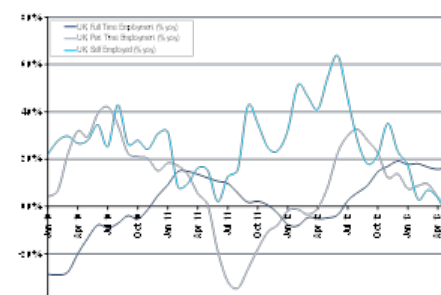
Source: LFS and Citi Research

Figure 11. UK Employment – Private vs Public Sector (% ch yoy)



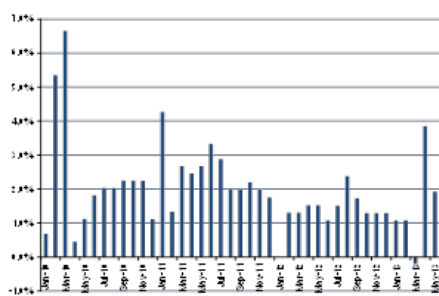
Source: LFS and Citi Research

Figure 12. UK Employment by Category (yoy %chg)



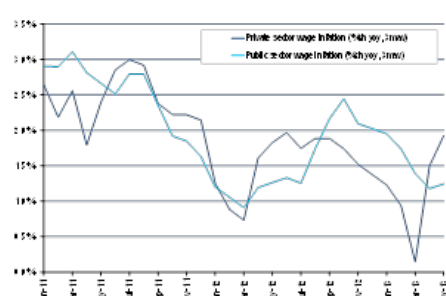
Source: LFS and Citi Research

Figure 13. UK Weekly Earnings (%ch yoy)



Source: LFS and Citi Research

Figure 14. Public vs Private sector Wage Inflation (3m average)



Source: LFS and Citi Research

Figure 15. UK Household Savings ratio



Source: ONS, DataStream

Figure 16. UK Household Available Cashflow (2005-2015E)

£m	2005	2006	2007	2008	2009	2010	2011	2012	2013e	2014e	2015e
Gross earnings	726,928	766,517	811,806	827,429	808,438	839,358	864,940	890,057	906,182	928,516	960,378
- % ch yoy	4.2%	5.4%	5.9%	1.9%	(2.3%)	3.8%	3.0%	2.9%	1.8%	2.5%	3.4%
State benefits	211,542	225,986	226,921	251,187	276,584	287,531	295,554	312,568	328,221	343,388	358,840
- % ch yoy	6.8%	6.8%	0.4%	10.7%	10.1%	4.0%	2.8%	5.8%	5.0%	4.6%	4.5%
Income tax & NIC	(117,764)	(169,046)	(182,534)	(187,533)	(179,448)	(181,450)	(189,038)	(187,043)	(187,891)	(191,581)	(197,197)
- % ch yoy	(19.6%)	43.5%	8.0%	2.7%	(4.3%)	1.1%	4.2%	(1.1%)	0.5%	2.0%	2.9%
- as % gross earnings	(0.0%)	0.0%	0.0%	0.0%	(0.0%)	0.0%	0.0%	(0.0%)	0.0%	0.0%	0.0%
Other	10,300	48,315	53,420	39,001	53,862	66,250	62,708	49,882	33,689	26,752	23,824
- as % gross earnings	1.4%	6.3%	6.6%	4.7%	6.7%	7.9%	7.3%	5.6%	3.7%	2.9%	2.5%
<b>After Tax Earnings</b>	<b>831,006</b>	<b>871,772</b>	<b>909,613</b>	<b>930,084</b>	<b>959,436</b>	<b>1,011,689</b>	<b>1,034,164</b>	<b>1,065,464</b>	<b>1,080,201</b>	<b>1,107,074</b>	<b>1,145,844</b>
- % ch yoy	4.3%	4.9%	4.3%	2.3%	3.2%	5.4%	2.2%	3.0%	1.4%	2.5%	3.5%
Food	(59,599)	(61,593)	(64,422)	(69,087)	(70,526)	(73,229)	(76,036)	(79,685)	(82,436)	(84,599)	(86,291)
Beverages	(22,087)	(22,585)	(23,018)	(23,064)	(23,485)	(24,077)	(26,094)	(27,281)	(28,103)	(28,842)	(29,418)
Tobacco	(15,309)	(15,556)	(15,781)	(15,902)	(15,869)	(17,182)	(18,286)	(18,718)	(19,273)	(19,851)	(20,446)
Rent	(32,034)	(34,777)	(38,359)	(40,750)	(43,300)	(47,463)	(50,922)	(54,880)	(57,515)	(60,391)	(62,806)
Household Maintenance	(2,524)	(2,423)	(2,371)	(2,044)	(1,942)	(2,101)	(2,251)	(1,901)	(2,151)	(2,222)	(2,295)
Power	(18,302)	(22,570)	(23,982)	(28,855)	(29,361)	(30,591)	(29,068)	(32,252)	(35,745)	(38,021)	(40,492)
Water	(6,385)	(6,929)	(7,617)	(8,040)	(8,231)	(8,636)	(9,044)	(9,303)	(9,601)	(9,841)	(10,185)
Medical	(9,731)	(10,852)	(11,796)	(11,314)	(11,606)	(11,888)	(12,900)	(12,777)	(12,807)	(13,012)	(13,220)
Transport	(29,163)	(31,266)	(34,315)	(34,168)	(32,733)	(33,377)	(36,597)	(39,677)	(41,193)	(42,141)	(43,110)
Vehicle fuel	(23,248)	(24,855)	(26,624)	(29,522)	(25,379)	(28,665)	(31,319)	(30,827)	(30,184)	(30,872)	(31,798)
Communication	(16,557)	(16,591)	(17,301)	(17,284)	(16,796)	(18,064)	(18,662)	(18,955)	(19,539)	(20,126)	(20,629)
Insurance	(35,001)	(32,742)	(35,923)	(31,807)	(33,412)	(33,265)	(34,713)	(32,011)	(30,609)	(30,447)	(30,752)
Financial & misc services	(32,695)	(35,984)	(37,947)	(37,776)	(32,665)	(35,177)	(35,570)	(36,510)	(37,862)	(39,253)	(40,849)
Non-discretionary costs	(302,635)	(318,723)	(339,456)	(349,613)	(345,305)	(363,715)	(381,462)	(394,777)	(407,017)	(419,616)	(432,292)
- % ch yoy	7.2%	5.3%	6.5%	3.0%	(1.2%)	5.3%	4.9%	3.5%	3.1%	3.1%	3.0%
Mortgage Interest	(48,617)	(56,600)	(61,137)	(62,388)	(61,783)	(46,678)	(44,953)	(43,485)	(42,824)	(42,790)	(43,008)
Consumer credit cost	(16,983)	(16,713)	(16,350)	(17,690)	(15,084)	(12,487)	(12,354)	(12,163)	(12,282)	(12,840)	(13,456)
Interest payments	(65,599)	(73,314)	(77,487)	(80,079)	(76,867)	(59,165)	(57,307)	(55,648)	(55,106)	(55,630)	(56,464)
- % ch yoy	13.7%	11.8%	5.7%	3.3%	(4.0%)	(23.0%)	(3.1%)	(2.9%)	(1.0%)	1.0%	1.5%
Net Inc/(Dec) in Household Debt	23,079	17,123	19,933	14,491	(31,914)	(59,806)	(61,216)	(66,885)	(54,454)	(48,710)	(49,102)
Savings ratio	3.0%	3.4%	2.2%	2.2%	7.1%	7.5%	6.9%	7.0%	5.9%	5.7%	5.7%
Non discretionary costs and debt delta	(345,155)	(374,914)	(397,010)	(415,201)	(454,086)	(482,686)	(499,985)	(517,310)	(516,577)	(523,956)	(537,859)
Total Discretionary Income	485,851	496,859	512,603	514,883	505,350	529,003	534,179	548,154	563,625	583,118	607,986
- % ch yoy	0.7%	2.3%	3.2%	0.4%	(1.9%)	4.7%	1.0%	2.6%	2.8%	3.5%	4.3%
Less Space contribution	(3.7%)	(2.6%)	(2.1%)	(2.4%)	(2.1%)	(1.9%)	(1.3%)	(1.5%)	(1.2%)	(1.0%)	(0.8%)
VAT					1.8%	(1.8%)	(1.8%)				
Implied Non Food Retail LFL	(3.0%)	(0.3%)	1.1%	(2.0%)	(2.2%)	1.0%	(2.1%)	1.1%	1.6%	2.5%	3.5%
Online Contribution							1.6%	1.7%	2.4%	2.7%	3.0%
Store based LFL							(3.7%)	(0.6%)	(0.8%)	(0.2%)	0.5%

Source: Company Reports and Citi Research Estimates

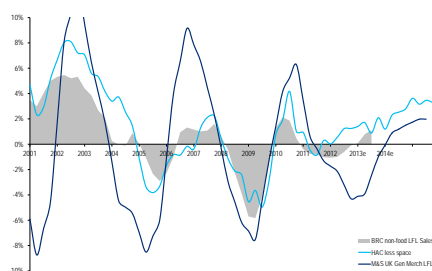
## Positive General Merch LFLs in FY14/FY15

### M&S General Merchandise more cyclical than the sector

**Gen Merchandise LFL has been more cyclical than both the non-food BRC and our HAC LFL**

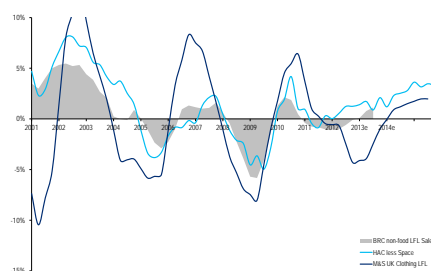
To put the impact of an improving UK macro environment in an M&S context, we have reviewed the M&S General Merchandise LFL sales performance over time against both the UK BRC non-food LFL sales trend, our UK HAC LFL, as well as a selection of clothing and home retail peers (Next, Debenhams, Dunelm). While this analysis makes no adjustment for periodic company specific events, over a meaningful time period (since 2001) this analysis demonstrates that the M&S Gen Merchandise LFL has generally been more cyclical than the non-food BRC, our HAC LFL, as well as its peers. Consequently, as our HAC LFL forecast improves from here, there is a reasonable prospect of the M&S Gen Merchandise division experiencing a significant LFL sales growth uplift (following the recent eight quarters of LFL sales declines).

Figure 17. M&S Gen Merch LFL vs BRC non-food LFL sales vs HAC less space



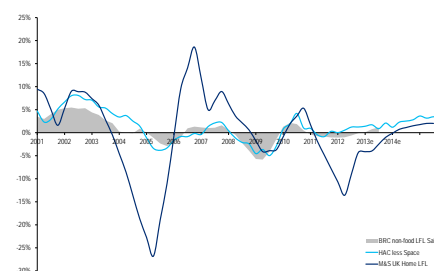
Source: Company Reports and Citi Research estimates

Figure 18. M&S Clothing LFL vs BRC non-food LFL sales vs HAC less space



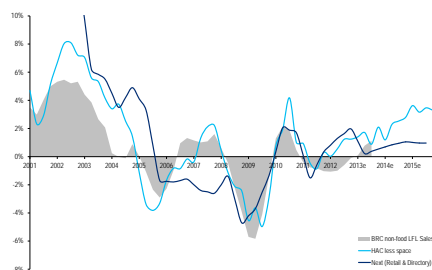
Source: Company Reports and Citi Research estimates

Figure 19. M&S Home LFL vs BRC non-food LFL sales vs HAC less space



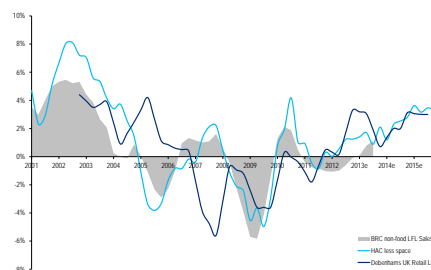
Source: Company Reports and Citi Research estimates

Figure 20. Next LFL vs BRC non-food LFL sales vs HAC less space



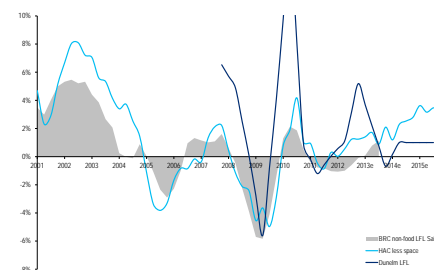
Source: Company Reports and Citi Research estimates

Figure 21. Debenhams LFL vs BRC non-food LFL sales vs HAC less space



Source: Company Reports and Citi Research estimates

Figure 22. Dunelm LFL vs BRC non-food LFL sales vs HAC less space



Source: Company Reports and Citi Research estimates

## M&S initiatives support improving LFL gross profit trends

**Management initiatives are expected to deliver a c.+9%pt improvement in General Merchandise product availability by 2015**

Primarily as a consequence of significant IT, logistics and supply chain investment programmes over the last 3-4 years, M&S should begin to see both revenue and gross margin improvements from FY14. These programmes include a dramatic rationalisation of UK distribution facilities to three regional distribution centres (from 110 DCs), new stock systems, new POS software, SAP implementation, and a move to a supply base comprising 65% Direct and 35% Full Service Vendors (from the reverse). Amongst other benefits, M&S targets these management initiatives to deliver a c.+9%pt improvement in General Merchandise product availability by 2015.



**Management's recent reference to a >1:1 relationship between product availability and LFL sales trends suggests that underlying LFL sales trends could improve beyond FY14**

To date, very little of this 9%pt improvement has been achieved, given the phasing of these investments, albeit this quantum of availability improvement is still expected by FY16. With this in mind, management's recent reference to a >1:1 relationship between Gen Merchandise product availability and LFL sales trends supports the view that underlying LFL sales trends could improve beyond FY14. In addition, the group's notable investment in e-commerce should also improve group revenue growth trends once the e-commerce distribution centre at Castle Donnington goes 'fully live' by the end of FY14.

**Gen Merchandise gross margins should also improve, primarily through reduced mark-down**

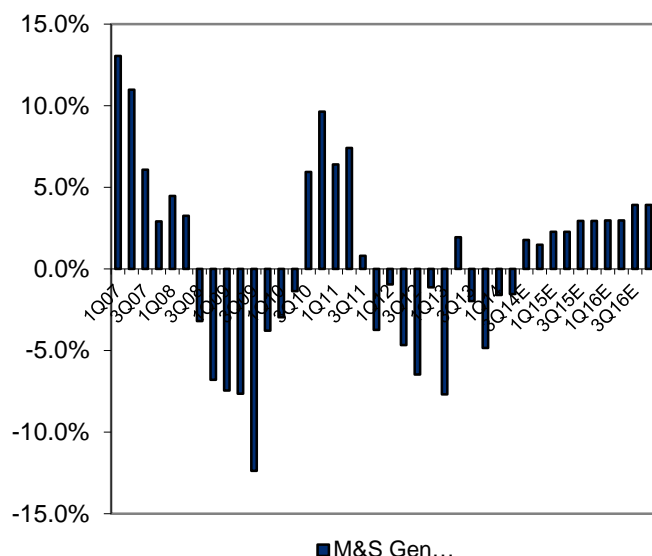
These investment programmes should also improve the Gen Merchandise gross margin beyond FY14, primarily through reduced mark-down activity. This drives management's recent view that the annual Gen Merchandise gross margin delta should increase beyond FY14 (FY14 guidance +30-50bp).

**Gen Merch LFL gross profit forecast to increase +2.5% and +3.5% in FY15 and FY16**

Taken together, these revenue and gross margin dynamics drive an improvement in our expected M&S General Merchandise LFL gross profit trend from the recent -3% and -1.5% across FY13 and 1H FY14, to +2.5% and +3.5% in FY15 and FY16. This forecast assumes the Gen Merchandise LFL sales growth trend remains below the UK non-food retail average.

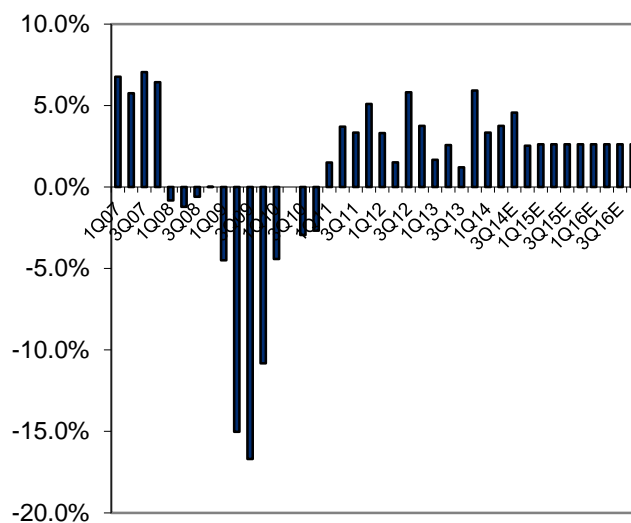
## LFL Gross Profit Analysis

Figure 23. M&S – Gen Merchandise LFL Gross Profit



Source: Company reports, Citi Research

Figure 24. M&S – Food LFL Gross Profit



Source: Company reports, Citi Research



Figure 25. M&S – LFL Gross Profit Analysis

2013-2014E		1QA	2QE	H1E	3QE	4QE	2HE	FYE
Gen Merchandise	LFL %	-1.6%	-0.4%	-1.0%	1.0%	0.8%	0.9%	0.0%
	GM (bp)	0	-60	-30	40	37	39	6
	LFL GP%	-1.6%	-1.5%	-1.6%	1.8%	1.5%	1.6%	0.1%
Food	LFL %	1.8%	2.2%	2.0%	3.0%	1.0%	2.0%	2.0%
	GM (bp)	50	50	50	50	50	50	50
	LFL GP%	3.3%	3.7%	3.5%	4.6%	2.5%	3.5%	3.5%
2012-2013A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	-6.8%	-1.8%	-4.3%	-3.8%	-4.0%	-3.9%	-4.1%
	GM (bp)	-50	200	75	100	-44	28	50
	LFL GP%	-7.7%	1.9%	-2.9%	-2.0%	-4.8%	-3.4%	-3.2%
Food	LFL %	0.6%	1.5%	1.1%	0.3%	4.3%	2.3%	1.7%
	GM (bp)	35	35	35	30	52	41	38
	LFL GP%	1.7%	2.6%	2.1%	1.2%	5.9%	3.6%	2.9%
2011-2012A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	0.0%	-2.6%	-1.3%	-1.8%	-2.8%	-2.1%	-1.8%
	GM (bp)	-50	-110	-80	-250	90	-80	-80
	LFL GP%	-1.0%	-4.7%	-2.8%	-6.5%	-1.1%	-3.6%	-3.3%
Food	LFL %	3.0%	1.2%	2.1%	3.0%	1.0%	2.0%	2.1%
	GM (bp)	10	10	10	90	90	90	52
	LFL GP%	3.3%	1.5%	2.4%	5.8%	3.8%	4.8%	3.7%
2010-2011A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	6.0%	7.0%	6.3%	0.8%	0.7%	0.6%	3.2%
	GM (bp)	20	20	20	0	-231	-116	-51
	LFL GP%	6.4%	7.4%	6.7%	0.8%	-3.7%	-1.6%	2.2%
Food	LFL %	1.5%	3.7%	2.6%	1.8%	3.4%	2.6%	2.6%
	GM (bp)	0	0	0	50	54	52	28
	LFL GP%	1.5%	3.7%	2.6%	3.3%	5.1%	4.2%	3.5%
2009-2010A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	-2.4%	-0.8%	-1.3%	3.0%	6.2%	4.2%	1.6%
	GM (bp)	-30	-30	-30	150	170	160	71
	LFL GP%	-3.0%	-1.4%	-1.8%	5.9%	9.6%	7.3%	3.0%
Food	LFL %	-0.5%	0.0%	-0.3%	0.4%	1.8%	0.8%	0.3%
	GM (bp)	-130	0	-65	-110	-145	-128	-98
	LFL GP%	-4.4%	0.0%	-2.3%	-2.9%	-2.7%	-3.1%	-2.7%
2008-2009A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	-6.2%	-6.4%	-6.3%	-8.9%	-4.8%	-7.5%	-6.9%
	GM (bp)	-70	-70	-70	-200	56	-72	-70
	LFL GP%	-7.5%	-7.6%	-7.5%	-12.4%	-3.8%	-8.8%	-8.1%
Food	LFL %	-4.5%	-5.9%	-5.2%	-5.2%	-3.7%	-4.7%	-5.0%
	GM (bp)	0	-320	-160	-400	-244	-322	-244
	LFL GP%	-4.5%	-15.0%	-9.8%	-16.7%	-10.8%	-14.0%	-12.0%
2007-2008A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	2.9%	1.7%	2.3%	-3.2%	-3.1%	-3.2%	-0.6%
	GM (bp)	80	80	80	0	-200	-100	-20
	LFL GP%	4.5%	3.2%	3.9%	-3.2%	-6.8%	-5.0%	-1.0%
Food	LFL %	0.7%	0.3%	0.5%	-1.5%	-0.9%	-1.2%	-0.4%
	GM (bp)	-50	-50	-50	30	30	30	-10
	LFL GP%	-0.8%	-1.2%	-1.0%	-0.6%	0.0%	-0.3%	-0.7%
2006-2007A		1QA	2QA	H1A	3QA	4QA	2HA	FYA
Gen Merchandise	LFL %	9.5%	7.5%	8.3%	7.3%	4.1%	5.7%	-7.2%
	GM (bp)	170	170	170	-60	-60	-60	40
	LFL GP%	13.0%	11.0%	11.8%	6.1%	2.9%	4.5%	-6.5%
Food	LFL %	5.8%	4.8%	5.3%	3.6%	3.0%	3.3%	4.2%
	GM (bp)	30	30	30	110	110	110	70
	LFL GP%	6.8%	5.8%	6.3%	7.1%	6.4%	6.7%	6.4%

Source: Company Reports and Citi Research Estimates

## Credible +13%/+11% FY15E/16E EPS growth

**FY14, FY15 and FY16 M&S EPS forecasts -2.2%, unchanged, and +3.2% to 32p, 36.2p and 40.1p (+2.3%, +12.9% and +10.9% yoy)**

In updating our M&S earnings forecast agenda, we have looked at both the above support for General Merchandise revenue and gross margin trends in FY15 and FY16, as well as our shorter term expectations for current trading in 2Q-4Q FY14. In summary, this has driven a -2.2%, unchanged, and +3.2% movement in our FY14, FY15 and FY16 M&S EPS forecasts to 32p, 36.2p and 40.1p (+2.3%, +12.9% and +10.9% yoy respectively).

### **FY14 EPS trimmed -2.2%**

**2Q14 Gen Merch: LFL -0.5% and gross margin -60bp, driving LFL gross profit in line with 1Q (-1.5%)**

For FY14, we do not expect any material improvement in 2Q General Merchandise LFL gross profit sales trends from 1Q. Specifically, we forecast 2Q Gen Merch LFL sales -0.5% and gross margin -60bp, driving a -1.5% 2Q LFL gross profit trend (in line with 1Q). Food is also forecast to continue the +2% and c.+20bp 1Q LFL and gross margin trends into 2Q.

**2H14 Gen Merch: LFL +1% and gross margin +40bp (from +2.3% and +60bp)**

Across 2H, we assume some modest Gen Merch LFL sales progress (+1%) and a +40bp gross margin increase, reflecting a modestly better trading environment and management's FY14 gross margin guidance (from +2.3% and +60bp previously). Net of c.+3% FY14 opex growth (better than the c.+3.5% guidance), we derive a £670million FY14 PBT forecast (EPS 32p, +2.3% yoy – see below). This forecast is struck excluding c.£30m of Castle Donnington double running costs, and represents a £15million reduction from our previous estimate. We believe that the market consensus FY14 PBT forecast is c.£700m on the same basis, leaving our forecast -4% below the street.

### **FY15 and FY16 EPS unchanged and raised +3.2%**

**FY15 Gen Merch: LFL +1.8% (from +1%), gross margin +40bp (from +30bp)**

Looking out to FY15 and FY16, for the General Merchandise division we have raised our LFL sales forecast by c. +80bp and c.+150bp to +1.8% and +2.5% respectively, alongside +40bp and +50bp FY15 and FY16 gross margin progress (previously both +30bp). This shape change reflects the macro-economic and self-help initiatives discussed above, albeit this revised Gen Merch LFL sales forecast agenda is still c.-100bp below our HAC view that the calendar 2014 and 2015 UK non-food LFL could be c.+3% and +3.5% respectively. Hence, we argue that these forecast assumptions remain credible, and could be conservative. As set out in the Financials section below, from this revenue and gross margin base we forecast a £745million and £825million FY15 and FY16 PBT forecast (EPS 36.2p and 40.1p, +12.9% and +10.9% respectively).

**We forecast £745million and £825million FY15 and FY16 PBT (EPS 36.2p and 40.1p, +12.9% and +10.9% respectively)**

While this updated M&S earnings forecast agenda is not materially changed from our previous view, we argue that this return to double-digit EPS growth beyond FY14 is now more credible, particularly in the light of the recently upgraded UK demand environment referred to above. As a consequence, we review the group's FY15 and FY16 valuation metrics below.

## Sustainable valuation multiples

**M&S cal 2014 EV/EBIT in line with Next, and a -12% PE discount to the sector should be sustainable valuation metrics**

**535p target price references 11.5x FY16 EV/EBIT and equates to 13.3x PE**

**Rating raised to Buy (from Neutral)**

**Buyback/special dividend possibility**

In thinking about the M&S valuation metrics in absolute terms and vs its UK peers, we continue to focus on the EV/EBIT multiple to capture balance sheet/cash generation differences. As set out below, at 11.3x calendar 2014 EV/EBIT, M&S is trading in line with Next and a modest 5% premium to the broader sector. Alongside a c.4% dividend yield, and a -12% cal 2014 PE discount to peers, we argue that M&S valuation metrics are undemanding, and can be sustained over time. Taking this approach we derive a new 535p M&S target price (raised from 470p). This targets an 11.5x FY16 EV/EBIT multiple (rolled forward to FY16 given greater forecast agenda confidence), equating to 13.3x PE and 3.7% dividend yield for the same forecast year.

Management's statement that material improvement in free cashflow from FY15 will drive an assessment of cash uses with a view to delivering improved shareholder returns, offers further medium term share price support.

Source: Powered by dataCentral; prices as of 22 August 2013

1 = Buy    2 = Neutral    3 = Sell

## Financials

Figure 27. Marks & Spencer – P&L (Pounds in Millions)

Year end March (£m)	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
<b>General merchandise</b>														
Sales	3,877.8	3,846.1	3,643.4	3,644.4	4,002.8	4,059.3	3,918.3	4,077.3	4,233.6	4,195.1	4,093.9	4,151.4	4,290.2	4,441.9
% change	9.7%	-2.4%	-5.3%	0.0%	9.8%	1.4%	-3.5%	4.1%	3.8%	-0.9%	-2.4%	1.4%	3.3%	3.5%
Like-for-like sales	9.1%	-1.7%	-7.0%	-0.9%	7.8%	-0.6%	-6.9%	1.6%	3.2%	-1.8%	-4.1%	0.0%	1.8%	2.5%
Gross margin (%) (E)	47.4%	46.7%	45.6%	52.3%	52.8%	52.6%	51.9%	52.6%	52.1%	51.3%	51.8%	51.9%	52.3%	52.8%
Gross profit (£)	1837	1796	1663	1907	2112	2135	2034	2145	2206	2152	2121	2153	2244	2346
<b>Food</b>														
Sales	3,188.2	3,313.7	3,391.3	3,665.5	3,974.7	4,249.8	4,246.0	4,322.4	4,499.4	4,673.1	4,857.5	5,027.7	5,219.6	5,385.7
% change	4.8%	3.9%	2.3%	8.1%	8.4%	6.9%	-0.1%	1.8%	4.1%	3.9%	3.9%	3.5%	3.8%	3.2%
Like-for-like sales	3.7%	1.6%	-2.6%	3.7%	4.2%	-0.4%	-5.0%	0.3%	2.6%	2.1%	1.7%	2.0%	2.0%	2.0%
Gross margin (%) (E)	29.2%	32.5%	32.5%	33.3%	34.0%	33.9%	31.5%	30.5%	30.8%	31.3%	31.7%	32.2%	32.4%	32.6%
Gross profit (£)	932	1077	1102	1222	1353	1442	1337	1319	1386	1463	1540	1619	1691	1756
<b>UK retail sales</b>	<b>7,027.1</b>	<b>7,159.8</b>	<b>7,034.7</b>	<b>7,309.9</b>	<b>7,977.5</b>	<b>8,309.1</b>	<b>8,164.3</b>	<b>8,399.7</b>	<b>8,733.0</b>	<b>8,868.2</b>	<b>8,951.4</b>	<b>9,179.1</b>	<b>9,509.8</b>	<b>9,827.6</b>
% change	6.9%	1.9%	-1.7%	3.9%	9.1%	4.2%	-1.7%	2.9%	4.0%	1.5%	0.9%	2.5%	3.6%	3.3%
Like-for-like sales	6.6%	-0.3%	-5.0%	1.3%	5.9%	-0.5%	-5.9%	0.9%	2.9%	0.2%	-1.0%	1.1%	1.9%	2.2%
Gross margin (%) (E)	39.4%	40.1%	39.3%	42.8%	43.4%	43.0%	41.3%	41.2%	41.1%	40.8%	40.9%	41.1%	41.4%	41.7%
Gross profit (£)	2,768.7	2,869.7	2,765.0	3,129.1	3,464.6	3,575.4	3,371.1	3,464.3	3,591.3	3,615.6	3,660.5	3,771.8	3,935.2	4,101.5
Less costs (£)	2,124.9	2,147.6	2,176.7	2,339.0	2,508.1	2,602.5	2,718.3	2,820.3	2,913.6	2,939.0	2,999.1	3,085.8	3,191.3	3,302.5
% change	4.9%	1.1%	1.4%	7.5%	7.2%	3.8%	4.4%	3.8%	3.3%	0.9%	2.0%	2.9%	3.4%	3.5%
<b>UK retail profit</b>	<b>643.8</b>	<b>722.1</b>	<b>588.3</b>	<b>790.1</b>	<b>956.5</b>	<b>972.9</b>	<b>652.8</b>	<b>644.0</b>	<b>677.6</b>	<b>676.6</b>	<b>661.4</b>	<b>686.0</b>	<b>744.0</b>	<b>799.0</b>
% change	27.4%	12.2%	-18.5%	34.3%	21.1%	1.7%	-32.9%	-1.3%	5.2%	-0.2%	-2.2%	3.7%	8.5%	7.4%
<b>UK EBIT %</b>	<b>9.2%</b>	<b>10.1%</b>	<b>8.4%</b>	<b>10.8%</b>	<b>12.0%</b>	<b>11.7%</b>	<b>8.0%</b>	<b>7.7%</b>	<b>7.8%</b>	<b>7.6%</b>	<b>7.4%</b>	<b>7.5%</b>	<b>7.8%</b>	<b>8.1%</b>
<b>International sales</b>	<b>391.2</b>	<b>426.2</b>	<b>455.8</b>	<b>522.7</b>	<b>610.6</b>	<b>712.9</b>	<b>897.8</b>	<b>949.4</b>	<b>1,007.3</b>	<b>1,066.1</b>	<b>1,075.4</b>	<b>1,129.2</b>	<b>1,242.1</b>	<b>1,366.3</b>
International EBIT	34.9	41.8	60.4	65.7	87.5	116.4	116.1	135.3	147.0	133.4	120.2	128.0	140.0	157.0
International EBIT %	8.9%	9.8%	13.3%	12.6%	14.3%	16.3%	12.9%	14.3%	14.6%	12.5%	11.2%	11.3%	11.3%	11.5%
Financial Services	86.4	56.6	31.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Kings	7.9	2.4	4.5	5.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Group Revenue</b>	<b>7,748.2</b>	<b>7,916.0</b>	<b>7,942.3</b>	<b>8,054.6</b>	<b>8,588.1</b>	<b>9,022.0</b>	<b>9,062.1</b>	<b>9,349.1</b>	<b>9,740.3</b>	<b>9,934.3</b>	<b>10,026.8</b>	<b>10,308.3</b>	<b>10,751.9</b>	<b>11,193.9</b>
<b>Group EBIT</b>	<b>773.0</b>	<b>822.9</b>	<b>653.2</b>	<b>861.1</b>	<b>1,044.0</b>	<b>1,089.3</b>	<b>768.9</b>	<b>779.3</b>	<b>824.6</b>	<b>810.0</b>	<b>781.6</b>	<b>814.0</b>	<b>884.0</b>	<b>956.0</b>
Net interest	(40.5)	(44.5)	(121.3)	(121.9)	(99.6)	(141.1)	(199.9)	(157.6)	(148.2)	(129.7)	(142.9)	(150.0)	(145.0)	(137.0)
FRS 17 (charge)/Credit		(15.2)	28.1	17.5	20.8	58.9	35.4	10.8	37.6	25.6	26.5	6.0	6.0	6.0
<b>Clean pre-tax</b>	<b>759.5</b>	<b>763.2</b>	<b>560.0</b>	<b>756.7</b>	<b>965.2</b>	<b>1,007.1</b>	<b>604.4</b>	<b>632.5</b>	<b>714.0</b>	<b>705.9</b>	<b>665.2</b>	<b>670.0</b>	<b>745.0</b>	<b>825.0</b>
% change	15.2%	0.5%	-26.6%	35.1%	27.6%	4.3%	-40.0%	4.6%	12.9%	-1.1%	-5.8%	0.7%	11.2%	10.7%
Tax rate %	28.8	30.0	28.5	31.0	29.4	28.5	27.0	25.6	25.1	24.5	22.7	21.5	20.5	20.5
Minorities	6.4	3.0	29.2	0.0	0.0	0.0	1.2	0.0	13.4	23.5	10.0	10.0	10.0	10.0
<b>Earnings</b>	<b>534.7</b>	<b>531.2</b>	<b>371.2</b>	<b>522.1</b>	<b>681.4</b>	<b>720.1</b>	<b>440.0</b>	<b>470.6</b>	<b>521.4</b>	<b>509.5</b>	<b>504.2</b>	<b>516.0</b>	<b>582.3</b>	<b>645.8</b>
Average Fully diluted Shares (million)	2,322.9	2,282.1	2,018.5	1,681.5	1,714.9	1,687.3	1,574.0	1,586.5	1,592.7	1,592.2	1,610.3	1,610.3	1,610.3	1,610.3
<b>EPS p</b>	<b>23.0</b>	<b>23.3</b>	<b>18.4</b>	<b>31.1</b>	<b>39.7</b>	<b>42.7</b>	<b>28.0</b>	<b>29.7</b>	<b>32.7</b>	<b>32.0</b>	<b>31.3</b>	<b>32.0</b>	<b>36.2</b>	<b>40.1</b>
% change	43.7%	1.1%	-21.0%	68.8%	28.0%	7.4%	-34.5%	6.1%	10.4%	-2.3%	-2.1%	2.3%	12.9%	10.9%
<b>DPS p</b>	<b>10.5</b>	<b>11.5</b>	<b>12.1</b>	<b>14.0</b>	<b>18.3</b>	<b>22.5</b>	<b>17.8</b>	<b>15.0</b>	<b>17.0</b>	<b>17.0</b>	<b>17.0</b>	<b>18.0</b>	<b>19.0</b>	<b>20.0</b>
% change	10.5%	9.5%	5.2%	15.7%	30.7%	23.0%	-20.9%	-15.7%	13.3%	0.0%	0.0%	5.9%	5.6%	5.3%

Source: Company Reports and Citi Research Estimates

Figure 28. Marks & Spencer - Cashflow (Pounds in Millions)

Year end March (£m)	2003A	2004A	2005A	2006A	2007A	2008A	2009A	2010A	2011A	2012A	2013A	2014E	2015E	2016E
Trading Profit	800.0	822.9	653.2	861.1	1,044.0	1,089.3	768.9	779.3	824.6	810.0	781.6	814.0	884.0	956.0
Depreciation	234.9	241.9	250.4	274.0	282.7	317.6	409.0	427.9	467.5	479.7	467.4	517.4	550.0	550.0
Working capital	191.3	6.8	717.9	43.7	106.3	(158.3)	212.2	83.5	106.0	86.2	(4.7)	0.0	(20.0)	(20.0)
Other	(19.3)	(405.0)	(82.4)	18.7	(6.1)	(12.6)	(18.2)	59.0	(13.2)	(23.8)	0.0	(75.0)	0.0	0.0
<b>Generated from operations</b>	<b>1,206.9</b>	<b>666.6</b>	<b>1,539.1</b>	<b>1,197.5</b>	<b>1,426.9</b>	<b>1,236.0</b>	<b>1,371.9</b>	<b>1,349.7</b>	<b>1,384.9</b>	<b>1,352.1</b>	<b>1,244.3</b>	<b>1,256.4</b>	<b>1,414.0</b>	<b>1,486.0</b>
Net interest received	(38.2)	(49.8)	(101.6)	(129.9)	(131.8)	(84.1)	(184.4)	(130.0)	(142.3)	(128.2)	(191.7)	(150.0)	(145.0)	(137.0)
Dividends paid	(225.4)	(247.1)	(236.9)	(204.1)	(260.6)	(343.6)	(354.6)	(223.6)	(247.5)	(267.8)	(271.8)	(273.8)	(286.6)	(302.7)
Tax paid	(216.9)	(220.4)	(166.7)	(101.5)	(150.8)	(166.2)	(81.3)	(120.7)	(185.3)	(149.1)	(106.3)	(144.1)	(152.7)	(169.1)
<b>Tax &amp; returns on investment</b>	<b>(480.5)</b>	<b>(517.3)</b>	<b>(505.2)</b>	<b>(435.5)</b>	<b>(543.2)</b>	<b>(593.9)</b>	<b>(620.3)</b>	<b>(474.3)</b>	<b>(575.1)</b>	<b>(545.1)</b>	<b>(569.8)</b>	<b>(567.8)</b>	<b>(584.4)</b>	<b>(608.9)</b>
Capital spend on fixed assets	(324.5)	(428.8)	(232.2)	(309.4)	(712.8)	(1,019.0)	(662.4)	(408.6)	(450.3)	(765.5)	(829.7)	(775.0)	(550.0)	(550.0)
Disposal of fixed assets														
Acquisitions and disposals	(9.5)	186.2	363.8	0.0	35.3	(46.4)	0.0	0.0	(139.8)	(102.0)	(644.0)	(100.0)	(100.0)	(100.0)
<b>Investing activities</b>	<b>(334.0)</b>	<b>(242.6)</b>	<b>131.6</b>	<b>(309.4)</b>	<b>(677.5)</b>	<b>(1,065.4)</b>	<b>(662.4)</b>	<b>(408.6)</b>	<b>(590.1)</b>	<b>(867.5)</b>	<b>(1,473.7)</b>	<b>(875.0)</b>	<b>(650.0)</b>	<b>(650.0)</b>
Share issues	(280.1)	(66.6)	(2,265.1)	55.8	36.5	(555.9)	(40.9)	0.0	8.4	44.3	0.0	0.0	0.0	0.0
Net cash flow	112.3	(159.9)	(1,099.6)	508.4	242.7	(979.2)	48.3	466.8	228.1	(16.2)	(799.2)	(186.4)	179.6	227.1
Exchange movements/Other	(36.7)	(3.4)	828.0	(135.1)	(462.9)	(243.4)	480.3	(44.4)	(60.9)	60.3	42.0	0.0	0.0	0.0
<b>Reduction in net debt (inc)</b>	<b>75.6</b>	<b>(163.3)</b>	<b>(271.6)</b>	<b>373.3</b>	<b>(220.2)</b>	<b>(1,222.6)</b>	<b>528.6</b>	<b>422.4</b>	<b>167.2</b>	<b>44.1</b>	<b>(757.2)</b>	<b>(186.4)</b>	<b>179.6</b>	<b>227.1</b>
Year end net cash (debt)	(1,831)	(1,994)	(2,147)	(1,729)	(1,949)	(3,077)	(2,490)	(2,068)	(1,901)	(1,857)	(2,614)	(2,800)	(2,621)	(2,393)
Shareholders' equity	3,378.1	2,454.0	521.4	808.1	1,648.2	1,956.7	2,081.7	2,168.6	2,673.5	2,790.2	2,505.4	2,749.5	3,043.9	3,385.8
<b>Net cash % (gearing %)</b>	<b>54.2%</b>	<b>81.3%</b>	<b>411.9%</b>	<b>214.0%</b>	<b>118.3%</b>	<b>157.3%</b>	<b>119.7%</b>	<b>95.4%</b>	<b>71.1%</b>	<b>66.6%</b>	<b>104.3%</b>	<b>101.9%</b>	<b>86.1%</b>	<b>70.7%</b>

Source: Company Reports and Citi Research Estimates

Figure 29. Marks & Spencer – Balance Sheet (Pounds in Millions)

Year end March	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E
<b>Retail assets:</b>														
Land & Buildings (if/Long hold if available)	2,120.8	2,129.5	2,329.3	2,310.0	2,372.9	2,421.4	2,458.0	2,457.7	2,486.0	2,486.0	2,486.0	2,486.0	2,486.0	2,486.0
Short leasehold	27.6	22.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fixtures & fittings	1,286.7	1,345.7	1,256.9	1,265.8	1,564.1	2,096.3	2,376.0	2,264.3	2,176.2	2,303.9	2,547.7	2,805.3	2,805.3	2,805.3
Intangible assets	0.0	0.0	165.4	163.5	194.1	305.5	400.3	452.8	527.7	584.3	695.0	695.0	695.0	695.0
<b>Tot Fixed &amp; Intangible assets</b>	<b>3,435</b>	<b>3,498</b>	<b>3,752</b>	<b>3,739</b>	<b>4,131</b>	<b>4,823</b>	<b>5,234</b>	<b>5,175</b>	<b>5,190</b>	<b>5,374</b>	<b>5,729</b>	<b>5,986</b>	<b>5,986</b>	<b>5,986</b>
Stock	362	398	339	374	416	489	536	613	685	682	767	789	823	857
Net debtors/(Creditors)	1,195	1,062	-293	-415	-600	-259	-1,216	-1,283	-1,134	-1,384	-1,264	-1,112	-1,032	-951
Other - Investments	29.7	10.0	0.0	0.0	0.0	0.0	38.6	33.9	29.0	30.3	31.3	31.3	31.3	31.3
Other - pension, financial instruments							254.0	132.9	21.8	44.2	65.3	65.3	65.3	65.3
<b>Capital employed</b>	<b>5,022</b>	<b>4,968</b>	<b>3,798</b>	<b>3,699</b>	<b>3,947</b>	<b>5,053</b>	<b>4,847</b>	<b>4,672</b>	<b>4,792</b>	<b>4,746</b>	<b>5,329</b>	<b>5,759</b>	<b>5,874</b>	<b>5,989</b>
<b>Financed by:</b>														
Share capital and reserves	2,108.3	2,454.0	909.2	1,155.3	1,648.2	1,964.0	2,081.7	2,168.6	2,673.5	2,790.2	2,505.4	2,749.5	3,043.9	3,385.8
Add back of FRS 17 deficit	895.8	469.5	654.2	775.1	283.3	(483.5)	152.2	366.5	168.5	78.0	193.0	193.0	193.0	193.0
Minorities	0.0	0.0	0.0	0.0	0.0	0.0	18.9	17.3	3.9	(11.4)	(19.0)	(19.0)	(19.0)	(19.0)
Provisions etc	186.1	49.3	44.9	28.3	22.5	25.7	103.8	51.1	44.7	32.4	35.2	35.2	35.2	35.2
Cash (-ve)	(471.9)	(720.6)	(212.6)	(362.6)	(180.1)	(318.0)	(422.9)	(405.8)	(470.2)	(196.1)	(193.1)	(193.1)	(193.1)	(193.1)
Debt (+ve) Long term	2,303.3	2,715.3	2,360.3	2,091.9	2,129.6	3,395.7	2,913.7	2,474.2	2,371.4	2,053.2	2,807.4	2,993.8	2,814.2	2,587.0
<b>Net Debt (cash)</b>	<b>1,831.4</b>	<b>1,994.7</b>	<b>2,147.7</b>	<b>1,729.3</b>	<b>1,949.5</b>	<b>3,077.7</b>	<b>2,490.8</b>	<b>2,068.4</b>	<b>1,901.2</b>	<b>1,857.1</b>	<b>2,614.3</b>	<b>2,800.7</b>	<b>2,621.1</b>	<b>2,393.9</b>
Other			41.6	11.1	43.7	469.1								
<b>Capital employed</b>	<b>5,022</b>	<b>4,968</b>	<b>3,798</b>	<b>3,699</b>	<b>3,947</b>	<b>5,053</b>	<b>4,847</b>	<b>4,672</b>	<b>4,792</b>	<b>4,746</b>	<b>5,329</b>	<b>5,759</b>	<b>5,874</b>	<b>5,989</b>
<b>Shareholders Equity</b>	<b>2,108.3</b>	<b>2,454.0</b>	<b>909.2</b>	<b>1,155.3</b>	<b>1,648.2</b>	<b>1,964.0</b>	<b>2,081.7</b>	<b>2,168.6</b>	<b>2,673.5</b>	<b>2,790.2</b>	<b>2,505.4</b>	<b>2,749.5</b>	<b>3,043.9</b>	<b>3,385.8</b>
<b>Net debt/(cash)</b>	<b>1,831.4</b>	<b>1,994.7</b>	<b>2,147.7</b>	<b>1,729.3</b>	<b>1,949.5</b>	<b>3,077.7</b>	<b>2,490.8</b>	<b>2,068.4</b>	<b>1,901.2</b>	<b>1,857.1</b>	<b>2,614.3</b>	<b>2,800.7</b>	<b>2,621.1</b>	<b>2,393.9</b>
<b>Gearing/(net cash)</b>	<b>86.9%</b>	<b>81.3%</b>	<b>236.2%</b>	<b>149.7%</b>	<b>118.3%</b>	<b>156.7%</b>	<b>119.7%</b>	<b>95.4%</b>	<b>71.1%</b>	<b>66.6%</b>	<b>104.3%</b>	<b>101.9%</b>	<b>86.1%</b>	<b>70.7%</b>
<b>Basic ROCE</b>														
Operating profit	773.0	822.9	653.2	861.1	1,044.0	1,089.3	768.9	779.3	824.6	810.0	781.6	814.0	884.0	956.0
Av Capital Employed	5,106.9	4,994.6	4,382.6	3,748.4	3,823.2	4,500.1	4,950.2	4,759.7	4,731.8	4,769.0	5,037.6	5,544.2	5,816.8	5,931.5
<b>ROCE</b>	<b>15.1%</b>	<b>16.5%</b>	<b>14.9%</b>	<b>23.0%</b>	<b>27.3%</b>	<b>24.2%</b>	<b>15.5%</b>	<b>16.4%</b>	<b>17.4%</b>	<b>17.0%</b>	<b>15.5%</b>	<b>14.7%</b>	<b>15.2%</b>	<b>16.1%</b>
<b>Adjusted ROCE</b>														
Adjusted return	831.5	869.1	712.4	915.0	1,104.8	1,160.3	853.9	872.9	929.6	928.2	906.3	944.9	1,021.8	1,100.0
Adjusted Capital (yr av)	6,100.5	5,778.6	5,387.7	4,663.5	4,855.6	5,706.1	6,393.8	6,348.7	6,514.5	6,775.7	7,155.2	7,767.8	8,157.6	8,377.2
<b>Adjusted ROCE</b>	<b>13.6%</b>	<b>15.0%</b>	<b>13.2%</b>	<b>19.6%</b>	<b>22.8%</b>	<b>20.3%</b>	<b>13.4%</b>	<b>13.7%</b>	<b>14.3%</b>	<b>13.7%</b>	<b>12.7%</b>	<b>12.2%</b>	<b>12.5%</b>	<b>13.1%</b>

Source: Company Reports and Citi Research Estimates

## Marks and Spencer Group PLC

### Company description

M&S is the market leader in the UK clothing market with around 11% market share. Clothing accounts for just under half of chain sales, with food having a 46% participation rate. In the food sector, M&S is a niche player focused on premium-quality convenience foods. The chain is now almost entirely UK based, save for a small European franchise business, and has a significant (circa £3bn) freehold property portfolio.

### Investment strategy

The combination of recent, material upgrades to UK economic growth forecasts, and M&S management initiatives have markedly improved the credibility of double digit FY15 and FY16 M&S EPS growth forecasts. We argue that this should underpin the group's current undemanding valuation metrics. Holding the group's 11.5x FY15 EV/EBIT multiple out to FY16 drives our 535p price target and Buy rating on the shares.

### Valuation

Our 535p target is based on a 11.5x FY16e EV/EBIT multiple, in line with the recent average for the large-cap sector peers, and equates to a c.13x PE and a 4% dividend yield for the same forecast year.

### Risks

We would highlight in particular the following risks that could cause the shares to rise above our target price:

M&S has been a long-run market share winner. If the company continues to win market share, there may be upside risk to our estimates.

Consumer spending growth has slowed recently, raising risks to estimates. However, recent weak trading patterns could reverse in the face of UK interest base rate cuts.

Weak LFL sales comparatives across 2H of last year could stimulate a better LFL sales performance later this year.

Clothing market capacity withdrawal could drive a recovery in M&S sales trends.

If the company is subject to a bid, the share price could rise above our target.

If the impact on the company from any of these factors proves to be more negative than we anticipate, the stock will likely have difficulty achieving our financial and price targets.



## Appendix A-1

### Analyst Certification

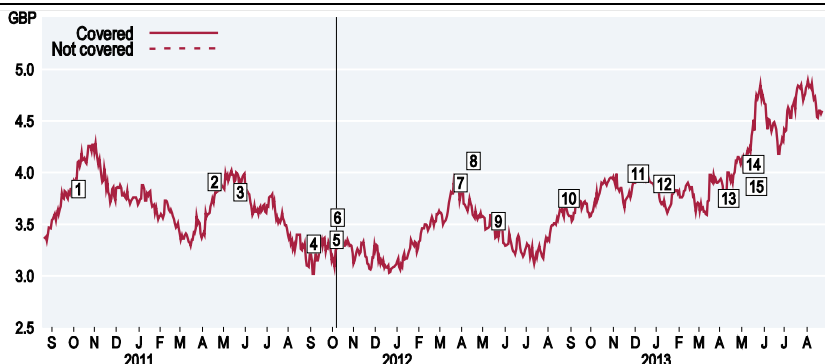
The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

### IMPORTANT DISCLOSURES

#### Marks and Spencer Group PLC (MKS.L)

##### Ratings and Target Price History Fundamental Research

Analyst: Richard Edwards



	Date	Rating	Target Price	Closing Price
1	8-Oct-10	2M	*4.00	4.11
2	19-Apr-11	*1M	*4.25	3.77
3	25-May-11	1M	*4.50	3.93
4	6-Sep-11	*2M	*3.20	3.02
5	7-Oct-11	Stock rating system changed		

\* Indicates change

	Date	Rating	Target Price	Closing Price
6	8-Oct-11	*2	3.20	3.26
7	30-Mar-12	2	*3.65	3.79
8	18-Apr-12	2	*3.55	3.58
9	23-May-12	2	*3.30	3.38
10	30-Aug-12	2	*3.50	3.58

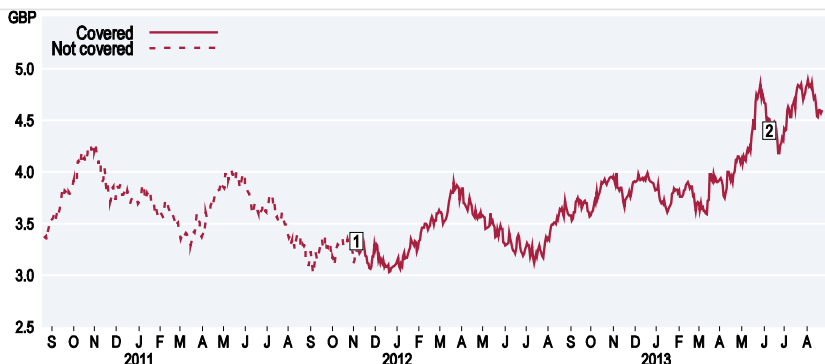
	Date	Rating	Target Price	Closing Price
11	6-Dec-12	2	*3.90	3.98
12	11-Jan-13	2	*3.60	3.73
13	12-Apr-13	2	*4.00	4.00
14	17-May-13	2	*4.40	4.51
15	22-May-13	2	*4.70	4.75

Rating/target price changes above reflect Eastern Standard Time

#### Marks and Spencer Group PLC (MKS.L)

##### Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Richard Edwards



	Date	Rating	Target Price	Closing Price
1	4-Nov-11	*ADD LP	-	3.24

\* Indicates change

	Date	Rating	Target Price	Closing Price
2	10-Jun-13	*REM LP	-	4.51

Rating/target price changes above reflect Eastern Standard Time

An employee of Citigroup Global Markets or its affiliates is a Sales Consultant of Next Retail Ltd.

Citigroup is acting as Bookrunner in relation to Dixons Retail plc's announced offering of sterling - denominated fixed rate guaranteed notes with expected maturity 2017. Citigroup is also acting as Dealer Manager in the announced Tender Offer for existing notes.

Within the past 12 months, Citigroup Global Markets Inc. or its affiliates has acted as manager or co-manager of an offering of securities of Dixons Retail PLC.

Citigroup Global Markets Inc. or its affiliates has received compensation for investment banking services provided within the past 12 months from Debenhams Plc, Steinhoff International Holdings Ltd, adidas Group, Dixons Retail PLC, Marks and Spencer Group PLC.

Citigroup Global Markets Inc. or an affiliate received compensation for products and services other than investment banking services from Inditex, Hennes & Mauritz AB, Halfords Group Plc, Debenhams Plc, ASOS Plc, Steinhoff International Holdings Ltd, Inchcape PLC, adidas Group, Next Group PLC, Dixons Retail PLC, Home Retail Group, Marks and Spencer Group PLC in the past 12 months.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as investment banking client(s): Debenhams Plc, Marks and Spencer Group PLC, Dixons Retail PLC, Steinhoff International Holdings Ltd, adidas Group.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as clients, and the services provided were non-investment-banking, securities-related: Inditex, Hennes & Mauritz AB, Halfords Group Plc, Debenhams Plc, ASOS Plc, Steinhoff International Holdings Ltd, Inchcape PLC, adidas Group, Darty Plc, Dixons Retail PLC, Home Retail Group, Marks and Spencer Group PLC.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as clients, and the services provided were non-investment-banking, non-securities-related: Inditex, Hennes & Mauritz AB, Halfords Group Plc, Debenhams Plc, ASOS Plc, Steinhoff International Holdings Ltd, Inchcape PLC, adidas Group, Next Group PLC, Dixons Retail PLC, Home Retail Group, Marks and Spencer Group PLC.

Analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Citigroup Global Markets Inc. and its affiliates ("the Firm"). Like all Firm employees, analysts receive compensation that is impacted by overall firm profitability which includes investment banking revenues.

The Firm is a market maker in the publicly traded equity securities of Hennes & Mauritz AB, Debenhams Plc, Kingfisher PLC, adidas Group, Dixons Retail PLC, Marks and Spencer Group PLC.

For important disclosures (including copies of historical disclosures) regarding the companies that are the subject of this Citi Research product ("the Product"), please contact Citi Research, 388 Greenwich Street, 28th Floor, New York, NY, 10013, Attention: Legal/Compliance [E6WYB6412478]. In addition, the same important disclosures, with the exception of the Valuation and Risk assessments and historical disclosures, are contained on the Firm's disclosure website at [https://www.citivelocity.com/cvr/eppublic/citi\\_research\\_disclosures](https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures). Valuation and Risk assessments can be found in the text of the most recent research note/report regarding the subject company. Historical disclosures (for up to the past three years) will be provided upon request.

#### Citi Research Equity Ratings Distribution

Data current as of 30 Jun 2013

	12 Month Rating			Relative Rating		
	Buy	Hold	Sell	Buy	Hold	Sell
Citi Research Global Fundamental Coverage	48%	40%	12%	6%	88%	6%
% of companies in each rating category that are investment banking clients	53%	50%	45%	58%	51%	49%

#### Guide to Citi Research Fundamental Research Investment Ratings:

Citi Research stock recommendations include an investment rating and an optional risk rating to highlight high risk stocks.

**Risk rating** takes into account both price volatility and fundamental criteria. Stocks will either have no risk rating or a High risk rating assigned.

**Investment Ratings:** Citi Research investment ratings are Buy, Neutral and Sell. Our ratings are a function of analyst expectations of expected total return ("ETR") and risk. ETR is the sum of the forecast price appreciation (or depreciation) plus the dividend yield for a stock within the next 12 months. The Investment rating definitions are: Buy (1) ETR of 15% or more or 25% or more for High risk stocks; and Sell (3) for negative ETR. Any covered stock not assigned a Buy or a Sell is a Neutral (2). For stocks rated Neutral (2), if an analyst believes that there are insufficient valuation drivers and/or investment catalysts to derive a positive or negative investment view, they may elect with the approval of Citi Research management not to assign a target price and, thus, not derive an ETR. Analysts may place covered stocks "Under Review" in response to exceptional circumstances (e.g. lack of information critical to the analyst's thesis) affecting the company and / or trading in the company's securities (e.g. trading suspension). As soon as practically possible, the analyst will publish a note re-establishing a rating and investment thesis. To satisfy regulatory requirements, we correspond Under Review and Neutral to Hold in our ratings distribution table for our 12-month fundamental rating system. However, we reiterate that we do not consider Under Review to be a recommendation.

**Relative three-month ratings:** Citi Research may also assign a three-month relative call (or rating) to a stock to highlight expected out-performance (most preferred) or under-performance (least preferred) versus the geographic and industry sector over a 3 month period. The relative call may highlight a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Absent any specific catalyst the analyst(s) will indicate the most and least preferred stocks in the universe of stocks under consideration, explaining the basis for this short-term view. This three-month view may be different from and does not affect a stock's fundamental equity rating, which reflects a longer-term total absolute return expectation. For purposes of NASD/NYSE ratings-distribution-disclosure rules, most preferred calls correspond to a buy recommendation and least preferred calls correspond to a sell recommendation. Any stock not assigned to a most preferred or least preferred call is considered non-relative-rated (NRR). For purposes of NASD/NYSE ratings-distribution-disclosure rules we correspond NRR to Hold in our ratings distribution table for our 3-month relative rating system. However, we reiterate that we do not consider NRR to be a recommendation.

Prior to October 8, 2011, the firm's stock recommendation system included a risk rating and an investment rating. **Risk ratings**, which took into account both price volatility and fundamental criteria, were: Low (L), Medium (M), High (H), and Speculative (S). **Investment Ratings** of Buy, Hold and Sell were a function of the Citi Research expectation of total return (forecast price appreciation and dividend yield within the next 12 months) and risk rating. Additionally, analysts could have placed covered stocks "Under Review" in response to exceptional circumstances (e.g. lack of information critical to the analyst's thesis) affecting the company and/or trading in the company's securities (e.g. trading suspension). Stocks placed "Under Review" were monitored daily by management and as practically possible, the analyst published a note re-establishing a rating and investment thesis. For securities in developed markets (US, UK, Europe, Japan, and Australia/New Zealand), investment ratings were: Buy (1) (expected total return of 10% or more for Low-Risk stocks, 15% or more for Medium-Risk stocks, 20% or more for High-Risk stocks, and 35% or more for Speculative stocks); Hold (2) (0%-10% for Low-Risk stocks, 0%-15% for Medium-Risk stocks, 0%-20% for High-Risk stocks, and 0%-35% for Speculative stocks); and Sell (3) (negative total return). For securities in emerging markets (Asia Pacific, Emerging Europe/Middle East/Africa, and Latin America), investment ratings were: Buy (1) (expected total return of 15% or more for Low-Risk stocks, 20% or more for Medium-Risk stocks, 30% or more for High-Risk stocks, and 40% or more for Speculative stocks); Hold (2) (5%-15% for Low-Risk stocks, 10%-20% for Medium-Risk stocks, 15%-30% for High-Risk stocks, and 20%-40% for Speculative stocks); and Sell (3) (5% or less for Low-Risk stocks, 10% or less for Medium-Risk stocks, 15% or less for High-Risk stocks, and 20% or less for Speculative stocks).

Investment ratings are determined by the ranges described above at the time of initiation of coverage, a change in investment and/or risk rating, or a change in target price (subject to limited management discretion). At other times, the expected total returns may fall outside of these ranges because of market price movements and/or other short-term volatility or trading patterns. Such interim deviations from specified ranges will be permitted but will become subject to

review by Research Management. Your decision to buy or sell a security should be based upon your personal investment objectives and should be made only after evaluating the stock's expected performance and risk.

---

#### NON-US RESEARCH ANALYST DISCLOSURES

Non-US research analysts who have prepared this report (i.e., all research analysts listed below other than those identified as employed by Citigroup Global Markets Inc.) are not registered/qualified as research analysts with FINRA. Such research analysts may not be associated persons of the member organization and therefore may not be subject to the NYSE Rule 472 and NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account. The legal entities employing the authors of this report are listed below:

Citigroup Global Markets Ltd

Richard Edwards; Assad M Malic; Dan F Homan

---

#### OTHER DISCLOSURES

The subject company's share price set out on the front page of this Product is quoted as at 21 August 2013 04:40 PM on the issuer's primary market.

Citigroup Global Markets Inc. and/or its affiliates has a significant financial interest in relation to Inditex, Steinhoff International Holdings Ltd, adidas Group, Dixons Retail PLC. (For an explanation of the determination of significant financial interest, please refer to the policy for managing conflicts of interest which can be found at [www.citiVelocity.com](http://www.citiVelocity.com).)

For securities recommended in the Product in which the Firm is not a market maker, the Firm is a liquidity provider in the issuers' financial instruments and may act as principal in connection with such transactions. The Firm is a regular issuer of traded financial instruments linked to securities that may have been recommended in the Product. The Firm regularly trades in the securities of the issuer(s) discussed in the Product. The Firm may engage in securities transactions in a manner inconsistent with the Product and, with respect to securities covered by the Product, will buy or sell from customers on a principal basis.

Citigroup Global Markets Inc. or its affiliates acts as a corporate broker to Debenhams Plc, Dixons Retail PLC, Marks and Spencer Group PLC.

Securities recommended, offered, or sold by the Firm: (i) are not insured by the Federal Deposit Insurance Corporation; (ii) are not deposits or other obligations of any insured depository institution (including Citibank); and (iii) are subject to investment risks, including the possible loss of the principal amount invested. Although information has been obtained from and is based upon sources that the Firm believes to be reliable, we do not guarantee its accuracy and it may be incomplete and condensed. Note, however, that the Firm has taken all reasonable steps to determine the accuracy and completeness of the disclosures made in the Important Disclosures section of the Product. The Firm's research department has received assistance from the subject company(ies) referred to in this Product including, but not limited to, discussions with management of the subject company(ies). Firm policy prohibits research analysts from sending draft research to subject companies. However, it should be presumed that the author of the Product has had discussions with the subject company to ensure factual accuracy prior to publication. All opinions, projections and estimates constitute the judgment of the author as of the date of the Product and these, plus any other information contained in the Product, are subject to change without notice. Prices and availability of financial instruments also are subject to change without notice. Notwithstanding other departments within the Firm advising the companies discussed in this Product, information obtained in such role is not used in the preparation of the Product. Although Citi Research does not set a predetermined frequency for publication, if the Product is a fundamental research report, it is the intention of Citi Research to provide research coverage of the/those issuer(s) mentioned therein, including in response to news affecting this issuer, subject to applicable quiet periods and capacity constraints. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in the Product must take into account existing public information on such security or any registered prospectus.

Investing in non-U.S. securities, including ADRs, may entail certain risks. The securities of non-U.S. issuers may not be registered with, nor be subject to the reporting requirements of the U.S. Securities and Exchange Commission. There may be limited information available on foreign securities. Foreign companies are generally not subject to uniform audit and reporting standards, practices and requirements comparable to those in the U.S. Securities of some foreign companies may be less liquid and their prices more volatile than securities of comparable U.S. companies. In addition, exchange rate movements may have an adverse effect on the value of an investment in a foreign stock and its corresponding dividend payment for U.S. investors. Net dividends to ADR investors are estimated, using withholding tax rates conventions, deemed accurate, but investors are urged to consult their tax advisor for exact dividend computations. Investors who have received the Product from the Firm may be prohibited in certain states or other jurisdictions from purchasing securities mentioned in the Product from the Firm. Please ask your Financial Consultant for additional details. Citigroup Global Markets Inc. takes responsibility for the Product in the United States. Any orders by US investors resulting from the information contained in the Product may be placed only through Citigroup Global Markets Inc.

**The Citigroup legal entity that takes responsibility for the production of the Product is the legal entity which the first named author is employed by.** The Product is made available in **Australia** through Citi Global Markets Australia Pty Ltd. (ABN 64 003 114 832 and AFSL No. 240992), participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in Australia to Private Banking wholesale clients through Citigroup Pty Limited (ABN 88 004 325 080 and AFSL 238098). Citigroup Pty Limited provides all financial product advice to Australian Private Banking wholesale clients through bankers and relationship managers. If there is any doubt about the suitability of investments held in Citigroup Private Bank accounts, investors should contact the Citigroup Private Bank in Australia. Citigroup companies may compensate affiliates and their representatives for providing products and services to clients. The Product is made available in **Brazil** by Citigroup Global Markets Brasil - CCTVM SA, which is regulated by CVM - Comissão de Valores Mobiliários, BACEN - Brazilian Central Bank, APIMEC - Associação dos Analistas e Profissionais de Investimento do Mercado de Capitais and ANBID - Associação Nacional dos Bancos de Investimento. Av. Paulista, 1111 - 11º andar - CEP. 01311920 - São Paulo - SP. If the Product is being made available in certain provinces of **Canada** by Citigroup Global Markets (Canada) Inc. ("CGM Canada"), CGM Canada has approved the Product. Citigroup Place, 123 Front Street West, Suite 1100, Toronto, Ontario M5J 2M3. This product is available in **Chile** through Banchile Corredores de Bolsa S.A., an indirect subsidiary of Citigroup Inc., which is regulated by the Superintendencia de Valores y Seguros. Agustinas 975, piso 2, Santiago, Chile. The Product is made available in **France** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 1-5 Rue Paul Cézanne, 8ème, Paris, France. The Product is distributed in **Germany** by Citigroup Global Markets Deutschland AG ("CGMD"), which is regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin). CGMD, Reuterweg 16, 60323 Frankfurt am Main. Research which relates to "securities" (as defined in the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong)) is issued in **Hong Kong** by, or on behalf of, Citigroup Global Markets Asia Limited which takes full responsibility for its content. Citigroup

Global Markets Asia Ltd. is regulated by Hong Kong Securities and Futures Commission. If the Research is made available through Citibank, N.A., Hong Kong Branch, for its clients in Citi Private Bank, it is made available by Citibank N.A., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong. Citibank N.A. is regulated by the Hong Kong Monetary Authority. Please contact your Private Banker in Citibank N.A., Hong Kong, Branch if you have any queries on or any matters arising from or in connection with this document. The Product is made available in **India** by Citigroup Global Markets India Private Limited, which is regulated by Securities and Exchange Board of India. Bakhtawar, Nariman Point, Mumbai 400-021. The Product is made available in **Indonesia** through PT Citigroup Securities Indonesia. 5/F, Citibank Tower, Bapindo Plaza, Jl. Jend. Sudirman Kav. 54-55, Jakarta 12190. Neither this Product nor any copy hereof may be distributed in Indonesia or to any Indonesian citizens wherever they are domiciled or to Indonesian residents except in compliance with applicable capital market laws and regulations. This Product is not an offer of securities in Indonesia. The securities referred to in this Product have not been registered with the Capital Market and Financial Institutions Supervisory Agency (BAPEPAM-LK) pursuant to relevant capital market laws and regulations, and may not be offered or sold within the territory of the Republic of Indonesia or to Indonesian citizens through a public offering or in circumstances which constitute an offer within the meaning of the Indonesian capital market laws and regulations. The Product is made available in **Israel** through Citibank NA, regulated by the Bank of Israel and the Israeli Securities Authority. Citibank, N.A. Platinum Building, 21 Ha'arba'ah St, Tel Aviv, Israel. The Product is made available in **Italy** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. Via dei Mercanti, 12, Milan, 20121, Italy. The Product is made available in **Japan** by Citigroup Global Markets Japan Inc. ("CGMJ"), which is regulated by Financial Services Agency, Securities and Exchange Surveillance Commission, Japan Securities Dealers Association, Tokyo Stock Exchange and Osaka Securities Exchange. Shin-Marunouchi Building, 1-5-1 Marunouchi, Chiyoda-ku, Tokyo 100-6520 Japan. If the Product was distributed by SMBC Nikko Securities Inc. it is being so distributed under license. In the event that an error is found in an CGMJ research report, a revised version will be posted on the Firm's Citi Velocity website. If you have questions regarding Citi Velocity, please call (81 3) 6270-3019 for help. The Product is made available in **Korea** by Citigroup Global Markets Korea Securities Ltd., which is regulated by the Financial Services Commission, the Financial Supervisory Service and the Korea Financial Investment Association (KOFIA). Citibank Building, 39 Da-dong, Jung-gu, Seoul 100-180, Korea. KOFIA makes available registration information of research analysts on its website. Please visit the following website if you wish to find KOFIA registration information on research analysts of Citigroup Global Markets Korea Securities Ltd. <http://dis.kofia.or.kr/frs/dis2/fundMgr/DISFundMgrAnalystPop.jsp?companyCd2=A03030&pageDiv=02>. The Product is made available in Korea by Citibank Korea Inc., which is regulated by the Financial Services Commission and the Financial Supervisory Service. Address is Citibank Building, 39 Da-dong, Jung-gu, Seoul 100-180, Korea. The Product is made available in **Malaysia** by Citigroup Global Markets Malaysia Sdn Bhd (Company No. 460819-D) ("CGMM") to its clients and CGMM takes responsibility for its contents. CGMM is regulated by the Securities Commission of Malaysia. Please contact CGMM at Level 43 Menara Citibank, 165 Jalan Ampang, 50450 Kuala Lumpur, Malaysia in respect of any matters arising from, or in connection with, the Product. The Product is made available in **Mexico** by Acciones y Valores Banamex, S.A. De C. V., Casa de Bolsa, Integrante del Grupo Financiero Banamex ("Accival") which is a wholly owned subsidiary of Citigroup Inc. and is regulated by Comision Nacional Bancaria y de Valores. Reforma 398, Col. Juarez, 06600 Mexico, D.F. In **New Zealand** the Product is made available to 'wholesale clients' only as defined by s5C(1) of the Financial Advisers Act 2008 ("FAA") through Citigroup Global Markets Australia Pty Ltd (ABN 64 003 114 832 and AFSL No. 240992), an overseas financial adviser as defined by the FAA, participant of the ASX Group and regulated by the Australian Securities & Investments Commission. Citigroup Centre, 2 Park Street, Sydney, NSW 2000. The Product is made available in **Pakistan** by Citibank N.A. Pakistan branch, which is regulated by the State Bank of Pakistan and Securities Exchange Commission, Pakistan. AWT Plaza, 1.1. Chundrigar Road, P.O. Box 4889, Karachi-74200. The Product is made available in the **Philippines** through Citicorp Financial Services and Insurance Brokerage Philippines, Inc., which is regulated by the Philippines Securities and Exchange Commission. 20th Floor Citibank Square Bldg. The Product is made available in the Philippines through Citibank NA Philippines branch, Citibank Tower, 8741 Paseo De Roxas, Makati City, Manila. Citibank NA Philippines NA is regulated by The Bangko Sentral ng Pilipinas. The Product is made available in **Poland** by Dom Maklerski Banku Handlowego SA an indirect subsidiary of Citigroup Inc., which is regulated by Komisja Nadzoru Finansowego. Dom Maklerski Banku Handlowego S.A. ul.Senatorska 16, 00-923 Warszawa. The Product is made available in the **Russian Federation** through ZAO Citibank, which is licensed to carry out banking activities in the Russian Federation in accordance with the general banking license issued by the Central Bank of the Russian Federation and brokerage activities in accordance with the license issued by the Federal Service for Financial Markets. Neither the Product nor any information contained in the Product shall be considered as advertising the securities mentioned in this report within the territory of the Russian Federation or outside the Russian Federation. The Product does not constitute an appraisal within the meaning of the Federal Law of the Russian Federation of 29 July 1998 No. 135-FZ (as amended) On Appraisal Activities in the Russian Federation. 8-10 Gasheka Street, 125047 Moscow. The Product is made available in **Singapore** through Citigroup Global Markets Singapore Pte. Ltd. ("CGMSPL"), a capital markets services license holder, and regulated by Monetary Authority of Singapore. Please contact CGMSPL at 8 Marina View, 21st Floor Asia Square Tower 1, Singapore 018960, in respect of any matters arising from, or in connection with, the analysis of this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). The Product is made available by The Citigroup Private Bank in Singapore through Citibank, N.A., Singapore Branch, a licensed bank in Singapore that is regulated by Monetary Authority of Singapore. Please contact your Private Banker in Citibank N.A., Singapore Branch if you have any queries on or any matters arising from or in connection with this document. This report is intended for recipients who are accredited, expert and institutional investors as defined under the Securities and Futures Act (Cap. 289). This report is distributed in Singapore by Citibank Singapore Ltd ("CSL") to selected Citigold/Citigold Private Clients. CSL provides no independent research or analysis of the substance or in preparation of this report. Please contact your Citigold/Citigold Private Client Relationship Manager in CSL if you have any queries on or any matters arising from or in connection with this report. This report is intended for recipients who are accredited investors as defined under the Securities and Futures Act (Cap. 289). Citigroup Global Markets (Pty) Ltd. is incorporated in the **Republic of South Africa** (company registration number 2000/025866/07) and its registered office is at 145 West Street, Sandton, 2196, Saxonwold. Citigroup Global Markets (Pty) Ltd. is regulated by JSE Securities Exchange South Africa, South African Reserve Bank and the Financial Services Board. The investments and services contained herein are not available to private customers in South Africa. The Product is made available in **Spain** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. 29 Jose Ortega Y Gasset, 4th Floor, Madrid, 28006, Spain. The Product is made available in the **Republic of China** through Citigroup Global Markets Taiwan Securities Company Ltd. ("CGMTS"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan and/or through Citibank Securities (Taiwan) Company Limited ("CSTL"), 14 and 15F, No. 1, Songzhi Road, Taipei 110, Taiwan, subject to the respective license scope of each entity and the applicable laws and regulations in the Republic of China. CGMTS and CSTL are both regulated by the Securities and Futures Bureau of the Financial Supervisory Commission of Taiwan, the Republic of China. No portion of the Product may be reproduced or quoted in the Republic of China by the press or any third parties [without the written authorization of CGMTS and CSTL]. If the Product covers securities which are not allowed to be offered or traded in the Republic of China, neither the Product nor any information contained in the Product shall be considered as advertising the securities or making recommendation of



the securities in the Republic of China. The Product is for informational purposes only and is not intended as an offer or solicitation for the purchase or sale of a security or financial products. Any decision to purchase securities or financial products mentioned in the Product must take into account existing public information on such security or the financial products or any registered prospectus. The Product is made available in **Thailand** through Citicorp Securities (Thailand) Ltd., which is regulated by the Securities and Exchange Commission of Thailand. 18/F, 22/F and 29/F, 82 North Sathorn Road, Silom, Bangrak, Bangkok 10500, Thailand. The Product is made available in **Turkey** through Citibank AS which is regulated by Capital Markets Board. Tekfen Tower, Eski Buyukdere Caddesi # 209 Kat 2B, 23294 Levent, Istanbul, Turkey. In the **U.A.E.**, these materials (the "Materials") are communicated by Citigroup Global Markets Limited, DIFC branch ("CGML"), an entity registered in the Dubai International Financial Center ("DIFC") and licensed and regulated by the Dubai Financial Services Authority ("DFSA") to Professional Clients and Market Counterparties only and should not be relied upon or distributed to Retail Clients. A distribution of the different Citi Research ratings distribution, in percentage terms for Investments in each sector covered is made available on request. Financial products and/or services to which the Materials relate will only be made available to Professional Clients and Market Counterparties. The Product is made available in **United Kingdom** by Citigroup Global Markets Limited, which is authorised and regulated by Financial Services Authority. This material may relate to investments or services of a person outside of the UK or to other matters which are not regulated by the FSA and further details as to where this may be the case are available upon request in respect of this material. Citigroup Centre, Canada Square, Canary Wharf, London, E14 5LB. The Product is made available in **United States** by Citigroup Global Markets Inc, which is a member of FINRA and registered with the US Securities and Exchange Commission. 388 Greenwich Street, New York, NY 10013. Unless specified to the contrary, within EU Member States, the Product is made available by Citigroup Global Markets Limited, which is regulated by Financial Services Authority. Pursuant to Comissão de Valores Mobiliários Rule 483, Citi is required to disclose whether a Citi related company or business has a commercial relationship with the subject company. Considering that Citi operates multiple businesses in more than 100 countries around the world, it is likely that Citi has a commercial relationship with the subject company.

Many European regulators require that a firm must establish, implement and make available a policy for managing conflicts of interest arising as a result of publication or distribution of investment research. The policy applicable to Citi Research's Products can be found at [https://www.citivelocity.com/cvr/eppublic/citi\\_research\\_disclosures](https://www.citivelocity.com/cvr/eppublic/citi_research_disclosures).

Compensation of equity research analysts is determined by equity research management and Citigroup's senior management and is not linked to specific transactions or recommendations.

The Product may have been distributed simultaneously, in multiple formats, to the Firm's worldwide institutional and retail customers. The Product is not to be construed as providing investment services in any jurisdiction where the provision of such services would not be permitted.

Subject to the nature and contents of the Product, the investments described therein are subject to fluctuations in price and/or value and investors may get back less than originally invested. Certain high-volatility investments can be subject to sudden and large falls in value that could equal or exceed the amount invested. Certain investments contained in the Product may have tax implications for private customers whereby levels and basis of taxation may be subject to change. If in doubt, investors should seek advice from a tax adviser. The Product does not purport to identify the nature of the specific market or other risks associated with a particular transaction. Advice in the Product is general and should not be construed as personal advice given it has been prepared without taking account of the objectives, financial situation or needs of any particular investor. Accordingly, investors should, before acting on the advice, consider the appropriateness of the advice, having regard to their objectives, financial situation and needs. Prior to acquiring any financial product, it is the client's responsibility to obtain the relevant offer document for the product and consider it before making a decision as to whether to purchase the product. With the exception of our product that is made available only to Qualified Institutional Buyers (QIBs) and other product that is made available through other distribution channels only to certain categories of clients to satisfy legal or regulatory requirements, Citi Research concurrently disseminates its research via proprietary and non-proprietary electronic distribution platforms. Periodically, individual Citi Research analysts may also opt to circulate research posted on such platforms to one or more clients by email. Such email distribution is discretionary and is done only after the research has been disseminated via the aforementioned distribution channels. Citi Research simultaneously distributes product that is limited to QIBs only through email distribution.

The level and types of services provided by Citi Research analysts to clients may vary depending on various factors such as the client's individual preferences as to the frequency and manner of receiving communications from analysts, the client's risk profile and investment focus and perspective (e.g. market-wide, sector specific, long term, short-term etc.), the size and scope of the overall client relationship with Citi and legal and regulatory constraints. Citi Research product may source data from dataCentral. dataCentral is a Citi Research proprietary database, which includes Citi estimates, data from company reports and feeds from Reuters and Datastream.

© 2013 Citigroup Global Markets Inc. Citi Research is a division of Citigroup Global Markets Inc. Citi and Citi with Arc Design are trademarks and service marks of Citigroup Inc. and its affiliates and are used and registered throughout the world. All rights reserved. Any unauthorized use, duplication, redistribution or disclosure of this report (the "Product"), including, but not limited to, redistribution of the Product by electronic mail, posting of the Product on a website or page, and/or providing to a third party a link to the Product, is prohibited by law and will result in prosecution. The information contained in the Product is intended solely for the recipient and may not be further distributed by the recipient to any third party. Where included in this report, MSCI sourced information is the exclusive property of Morgan Stanley Capital International Inc. (MSCI). Without prior written permission of MSCI, this information and any other MSCI intellectual property may not be reproduced, redissemated or used to create any financial products, including any indices. This information is provided on an "as is" basis. The user assumes the entire risk of any use made of this information. MSCI, its affiliates and any third party involved in, or related to, computing or compiling the information hereby expressly disclaim all warranties of originality, accuracy, completeness, merchantability or fitness for a particular purpose with respect to any of this information. Without limiting any of the foregoing, in no event shall MSCI, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind. MSCI, Morgan Stanley Capital International and the MSCI indexes are services marks of MSCI and its affiliates. The Firm accepts no liability whatsoever for the actions of third parties. The Product may provide the addresses of, or contain hyperlinks to, websites. Except to the extent to which the Product refers to website material of the Firm, the Firm has not reviewed the linked site. Equally, except to the extent to which the Product refers to website material of the Firm, the Firm takes no responsibility for, and makes no representations or warranties whatsoever as to, the data and information contained therein. Such address or hyperlink (including addresses or hyperlinks to website material of the Firm) is provided solely for your convenience and information and the content of the linked site does not in anyway form part of this document. Accessing such website or following such link through the Product or the website of the Firm shall be at your own risk and the Firm shall have no liability arising out of, or in connection with, any such referenced website.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST