

EADS (EAD.PA)

Fundamentals Still Attractive Despite Near-Term Stock Overhang

- **Summary** — From a fundamental perspective, we see EADS' investment case as unchanged and retain our Buy rating with an updated 12-month Target Price of €48.5 (from €45). We still believe that EADS could be worth up to €75/share on a 3-year view and would view any short-term weakness resulting from the overhang of strategic shareholdings as a buying opportunity for the medium to long-term investor.
- **Buyback Details Expected 2 April** — Following the EGM on 27 Mar, we expect the timing, size and form of the buyback to be announced after Easter. EADS has approval to buy back up to 15% of shares. Our base-case assumption, which is now reflected in our EPS forecasts and valuation, is a 12% buyback (€4bn), which is in line with recent company commentary, of which 6% will be from public shareholders and 6% from strategic shareholders (mostly Lagadere). See overleaf for sensitivities.
- **Near Term Stock Overhang** — This will depend on the size and form of the buyback. Per the revised shareholder agreement, Lagadere will sell 7.4% (which will be partially fulfilled by the buyback), Daimler to also sell 7.4% (at an undetermined time) and SEPI will sell 1.15% (into the market by 9 April). In total, this represents 16% of the company / 130m shares (vs. average daily volume of 4.7m YTD). Assuming a €4bn buyback (12%/100m shares), the net overhang is c30m shares. See overleaf for details.
- **FX Continues to be a Benefit** — We raise our DCF-based Target Price to €48.5 (from €45) to reflect an FX rate of \$1.28/€ (from \$1.31). Our EPS forecasts are broadly unchanged, reflecting the benefits of a weaker € (albeit mitigated by hedging) vs. a smaller buyback assumption than previously (12% vs. 15%). For the early part of the year, EADS shares rallied against a strengthening € and improving fundamentals. Now EADS shares have weakened despite € weakness on unchanged fundamentals.
- **Catalysts** — Following the buyback announcement, the next major catalyst will be the 1Q13 results on 14 May, where we expect EADS to maintain its FY13 guidance. The Paris Air Show, traditionally a period of heightened interest in Aerospace stocks, starts 17 June. Progress on the A350 appears to be on track, with 1st flight this summer.

- Company Update
- Target Price Change
- Estimate Change

Buy	1
Price (28 Mar 13)	€39.70
Target price	€48.50
	from €45.00
Expected share price return	22.2%
Expected dividend yield	2.7%
Expected total return	24.9%
Market Cap	€32,910M
	US\$42,061M

Price Performance (RIC: EAD.PA, BB: EAD FP)



EADS (EUR)

Year to 31 Dec	2011A	2012A	2013E	2014E	2015E
Sales (€M)	49,128.0	56,480.0	57,760.0	61,300.0	63,720.0
Net Income (€M)	1,132.0	1,838.0	2,178.7	2,796.4	3,570.3
Basic EPS (€)	1.39	2.24	2.73	3.87	4.94
Basic EPS (Old) (€)	1.39	2.24	2.72	3.90	4.94
PE (x)	28.5	17.7	14.5	10.3	8.0
EV/EBITDA (x)	12.4	9.1	8.6	7.3	6.0
DPS (€)	0.45	0.60	1.09	1.55	1.97
Net Div Yield (%)	1.1	1.5	2.7	3.9	5.0

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

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EAD.PA: Fiscal year end 31-Dec						Price: €39.70; TP: €48.50; Market Cap: €32,910m; Recomm: Buy					
Profit & Loss (€m)	2011	2012	2013E	2014E	2015E	Valuation ratios	2011	2012	2013E	2014E	2015E
Sales revenue	49,128	56,480	57,760	61,300	63,720	PE (x)	28.5	17.7	14.5	10.3	8.1
Cost of sales	-44,472	-51,399	-51,224	-53,820	-55,151	PB (x)	3.6	3.1	4.1	3.0	2.4
Gross profit	4,656	5,081	6,536	7,480	8,569	EV/EBITDA (x)	12.4	9.1	8.6	7.3	6.0
Gross Margin (%)	9.5	9.0	11.3	12.2	13.4	FCF yield (%)	7.7	4.4	-0.1	3.3	7.3
EBITDA (Adj)	3,426	4,812	5,547	6,522	7,691	Dividend yield (%)	1.1	1.5	2.7	3.9	5.0
EBITDA Margin (Adj) (%)	7.0	8.5	9.6	10.6	12.1	Payout ratio (%)	32	27	40	40	40
Depreciation	-1,643	-1,812	-1,859	-1,989	-2,079	ROE (%)	11.7	12.8	23.3	32.3	32.9
Amortisation	-181	-241	-241	-241	-241	Cashflow (€m)	2011	2012	2013E	2014E	2015E
EBIT (Adj)	1,602	2,759	3,447	4,292	5,371	EBITDA	3,328	3,992	5,447	6,522	7,691
EBIT Margin (Adj) (%)	3.3	4.9	6.0	7.0	8.4	Working capital	1,251	70	0	0	0
Net interest	13	-285	-450	-440	-440	Other	111	657	-2,214	-2,483	-2,797
Associates	192	247	253	268	279	Operating cashflow	4,690	4,719	3,233	4,039	4,895
Non-op/Except	-316	-223	-180	-180	-180	Capex	-2,197	-3,270	-3,270	-3,100	-2,800
Pre-tax profit	1,393	1,678	2,970	3,940	5,030	Net acq/disposals	-1,535	-201	0	0	0
Tax	-356	-449	-861	-1,143	-1,459	Other	-489	-856	-500	-500	-500
Extraord./Min.Int./Pref.div.	-4	-1	-1	-1	-1	Investing cashflow	-4,221	-4,327	-3,770	-3,600	-3,300
Reported net profit	1,033	1,228	2,108	2,796	3,570	Dividends paid	-183	-379	-492	-869	-1,121
Net Margin (%)	2.1	2.2	3.6	4.6	5.6	Financing cashflow	-12	-851	-2,662	-869	-1,121
Core NPAT	1,132	1,838	2,179	2,796	3,570	Net change in cash	0	0	-3,198	-430	473
Per share data	2011	2012	2013E	2014E	2015E	Free cashflow to s/holders	2,493	1,449	-37	939	2,095
Reported EPS (€)	1.27	1.50	2.64	3.86	4.93	Segment Sales (€m)	2011	2012	2013E	2014E	2015E
Core EPS (€)	1.39	2.24	2.73	3.86	4.93	Airbus Commercial	31,159	36,943	38,100	41,500	43,600
DPS (€)	0.45	0.60	1.09	1.55	1.97	Airbus Military	2,504	2,131	2,130	2,130	2,130
CFPS (€)	5.76	5.75	4.05	5.58	6.76	Eurocopter	5,415	6,264	6,450	6,640	6,840
FCFPS (€)	3.06	1.77	-0.05	1.30	2.89	EADS Astrium	4,964	5,817	5,930	6,050	6,170
BVPS (€)	10.89	12.70	9.64	13.29	16.68	Cassidian	5,803	5,740	5,570	5,400	5,400
Wtd avg ord shares (m)	813	819	797	723	723	Other Businesses	1,252	1,524	1,520	1,520	1,520
Wtd avg diluted shares (m)	814	821	798	724	724	Headquarters/Consolidation	-1,969	-1,939	-1,940	-1,940	-1,940
Growth rates	2011	2012	2013E	2014E	2015E	Sales - total segments	49,128	56,480	57,760	61,300	63,720
Sales revenue (%)	7.4	15.0	2.3	6.1	3.9	Segment EBIT (€m)	2011	2012	2013E	2014E	2015E
EBIT (Adj) (%)	33.6	72.2	25.0	24.5	25.1	Airbus Commercial	485	1,647	2,320	3,100	4,070
Core NPAT (%)	75.0	62.4	18.5	28.4	27.7	Airbus Military	49.0	93.0	90.0	90.0	90.0
Core EPS (%)	74.4	61.0	21.8	41.5	27.7	Eurocopter	374.0	411.0	460.0	510.0	560.0
Balance Sheet (€m)	2011	2012	2013E	2014E	2015E	EADS Astrium	290.0	312.0	350.0	390.0	430.0
Cash & cash equiv.	16,785	17,071	13,873	13,443	13,916	Cassidian	403.0	340.0	330.0	320.0	350.0
Accounts receivables	6,394	6,790	5,860	6,210	6,460	Other Businesses	49.0	49.0	50.0	50.0	50.0
Inventory	22,563	23,216	25,160	26,700	27,760	Headquarters/Consolidation	144.0	154.0	100.0	100.0	100.0
Net fixed & other tangibles	20,422	22,587	23,757	24,627	25,107	EBIT - total segments	1,794	3,006	3,700	4,560	5,650
Goodwill & intangibles	12,786	13,422	13,422	13,422	13,422	Segment Margin (%)	2011	2012	2013E	2014E	2015E
Financial & other assets	9,532	9,016	10,293	10,841	11,287	Airbus Commercial	1.6	4.5	6.1	7.5	9.3
Total assets	88,482	92,102	92,364	95,243	97,953	Airbus Military	2.0	4.4	4.2	4.2	4.2
Accounts payable	9,630	9,917	9,030	9,480	9,700	Eurocopter	6.9	6.6	7.1	7.7	8.2
Short-term debt	1,476	1,273	1,273	1,273	1,273	EADS Astrium	5.8	5.4	5.9	6.4	7.0
Long-term debt	3,173	3,161	5,331	5,331	5,331	Cassidian	6.9	5.9	5.9	5.9	6.5
Provisions & other liab	65,338	67,317	69,019	69,519	69,559	Margin - total segments	3.7	5.3	6.4	7.4	8.9
Total liabilities	79,617	81,668	84,653	85,603	85,863	Leverage & valuation	2011	2012	2013E	2014E	2015E
Shareholders' equity	8,850	10,409	7,685	9,613	12,062	Adj. net debt (cash)(€m)	-12,136	-12,637	-7,269	-6,839	-7,312
Minority interests	15	25	26	27	28	Pension deficit (surplus)(€m)	5,821	6,433	6,433	6,433	6,433
Total equity	8,865	10,434	7,711	9,640	12,090	Adj. ND to EBITDA (x)	-3.45	-2.98	-1.28	-1.01	-0.92
Net debt	-12,136	-12,637	-7,269	-6,839	-7,312	Adj. EV/EBITDA (x)	7.7	7.9	8.1	6.4	5.3
Net debt to equity (%)	-136.9	-121.1	-94.3	-70.9	-60.5	Adj. EV/EBIT (x)	15.9	15.3	12.9	9.5	7.4
						FCF Yield	14.3	6.4	-0.1	3.3	7.3

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For definitions of the items in this table, please click [here](#).

Our EPS and Target Price are based on a €4bn / 12% buyback. We expect an announcement on the timing, form and size of the buyback early next week.

Buyback Details Expected on 2 April

The EGM on 27 March saw EADS approve changes to the shareholding structure and the executive board, and a buyback of *up to* 15% of share capital. We expect a firm decision on the timing, size and form of the buyback on 2 April or soon after.

The intention to buy back up to 15% of share capital was [first announced in late December](#) alongside major changes to the shareholder structure. At that point EADS' share price was €27 vs. €39 today. Due to the significant price appreciation YTD, EADS has indicated that a buyback is likely to be €3-4bn (9-12% of shares).

Our EPS forecasts and DCF-based Target Price now assume that EADS buys back 12% of shares (€4bn) vs. our previous assumption of 15%. We estimate a 12% buyback to be 10-11% EPS accretive in 2014E and 2015E vs. no buyback at all. If EADS were to announce a €3bn buyback next week (9% of shares) rather than our assumption of 12%, our EPS forecasts could prove to be 3-4% too high.

Figure 1. EADS' DCF is relatively insensitive to the exact size of the buyback

€ 48.50	9.0%	10.0%	11.0%	12.0%	13.0%	14.0%	15.0%
€ 34.00	€ 48.20	€ 48.60	€ 48.90	€ 49.20	€ 49.60	€ 50.00	€ 50.40
€ 36.00	€ 48.00	€ 48.30	€ 48.70	€ 49.00	€ 49.30	€ 49.70	€ 50.00
€ 38.00	€ 47.90	€ 48.10	€ 48.40	€ 48.70	€ 49.10	€ 49.40	€ 49.70
€ 40.00	€ 47.70	€ 47.90	€ 48.20	€ 48.50	€ 48.80	€ 49.10	€ 49.40
€ 42.00	€ 47.50	€ 47.70	€ 48.00	€ 48.20	€ 48.50	€ 48.80	€ 49.10
€ 44.00	€ 47.30	€ 47.50	€ 47.80	€ 48.00	€ 48.20	€ 48.50	€ 48.80
€ 46.00	€ 47.10	€ 47.30	€ 47.50	€ 47.70	€ 48.00	€ 48.20	€ 48.50
€ 48.00	€ 46.90	€ 47.10	€ 47.30	€ 47.50	€ 47.70	€ 47.90	€ 48.20

Source: Citi Research. The above shows sensitivities to our DCF, which assumes a base case of a 12% buyback at €40/share, to a range of different share price and share buyback size assumptions.

At a fixed WACC of 10%, our DCF valuation model is less sensitive than EPS to the size of the share buyback, as the reduced share count is offset by higher adjusted net debt. Figure 1 shows our base-case valuation of €48.50 per share at a 12% buyback at €40/share. A 9% buyback would lower NPV by 2% to €47.70. Our DCF is included in the back of this note.

Whilst the impact to EPS of NPV of a smaller-than-anticipated buyback would be relatively limited, it could send a negative signal to the market on future cash generation, in our view, and additionally would increase the stock overhang from the strategic shareholders.

Stock Overhang

A major restructuring of strategic shareholdings will see EADS' free float rise from c55% to 72%. From a corporate governance perspective, we view this as a positive. However, there is a near-term overhang on EADS shares.

On 6 December, EADS announced a major restructuring of the strategic shareholdings — for more details [click here](#) for our note.

This process will ultimately see the company's free float rising from 49% at that time (now 55% following the subsequent sales of the Daimler stake) to an eventual 72%, with Daimler and Lagadere selling their holdings in EADS entirely. At the same time, EADS announced a proposed stock buyback of up to 15% of shares (see above), in 2 equal and simultaneous tranches — half from Lagadere and the other strategic shareholders and half from public shareholders.

This is a complicated process with a number of stages, as summarised below.

Figure 2. EADS shareholding structure will eventually see its free float rise from c55% today to 72% in a number of stages

	1) Now		2) Post EGM, Pre-Buyback		3) Post Buyback	
Lagadere	7.4%	61	0.0%	-	0.0%	-
French State	14.9%	122	15.1%	124	12.0%	87
France	22.3%	183	15.1%	124	12.0%	87
Daimler	7.4%	61	0.0%	-	-	-
KfW	8.6%	70	8.6%	70	10.1%	73
Other German Public Entities	1.6%	13	1.6%	13	1.9%	14
Germany	17.6%	145	10.2%	84	12.0%	87
Spain (SEPI)	5.4%	45	4.3%	35	4.0%	29
Strategic Shareholdings	45.4%	373	29.6%	243	28.0%	203
Free Float	54.6%	449	70.5%	579	72.0%	521
TOTAL	100.0%	822	100.0%	822	100.0%	723

Source: Company Reports

EADS free float should eventually rise from c55% currently to a final 72%. The exact overhang as a result of these proposed changes is dependent on the size of the share buyback — a larger buyback would reduce the overhang, particularly the near-term overhang from Lagadere. The above table assumes a 12% share buyback, which is also reflected in our EPS forecasts.

We believe that the near-term overhang could be c16% (130m shares), which we expect to be offset by a 12% buyback (100m shares). This gives a net overhang of 4% of EADS' stock (30m shares). The sellers are as follows:

The near-term overhang from Daimler, Lagadere and SEPI totals c16% of EADS shares, some of which we expect to be offset by a 12% shares buyback.

- **Lagadere (7.44%)** — Up to 5.5% of Lagadere's shares could be bought back directly by EADS. (The buyback will be split into 2 equal and simultaneous tranches for public and strategic shareholders of up to 7.5% each).
- **Daimler (7.44%)** — Daimler's shares look likely to be sold into the open market but the timing has not been decided. There is a possibility, in our view, that this happens at the same time as the Lagadere and SEPI disposals and the buyback.
- **SEPI (1.15%)** — Yesterday EADS announced that 1.15% (of 5.5%) owned by the Spanish government would be sold into the market by 9 April.

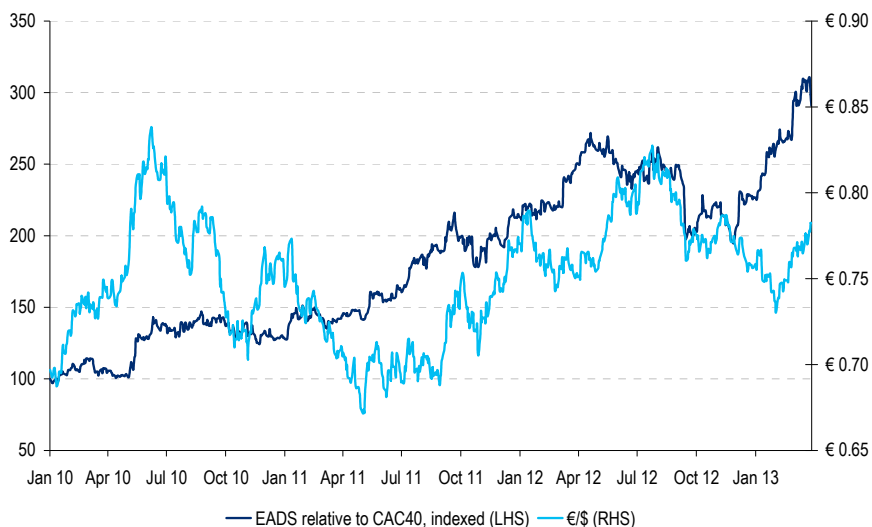
The timing and form of the above alongside the buyback could be known as soon as 2 April. In addition to the near-term overhang detailed above, we estimate that there could be an additional small overhang later this year, principally relating to the French government stake (currently 15% with an eventual target of 12%). Under the new shareholding agreement, the French government has the option to retain a larger stake in the company, but any shares in excess of 12% are placed into a warehousing facility without voting rights. So it may not necessarily sell down further shares.

FX Continues to be a Benefit

We raise our Target Price to €48.50/share, in part to reflect an FX rate assumption of \$1.28/€ (previously \$1.31/€).

We rebase our EPS forecasts and Target Price to reflect an FX rate of \$1.28/€ vs. \$1.31/€ previously. This is the principal reason for raising our Target Price as EADS is a major long-term beneficiary of € weakness vs. the dollar. For more details, [click here](#) for our report from early March.

Figure 3. EADS share price relative vs. €/€ rate



Source: DataStream

Late 2012 saw EADS shares significantly outperform the market despite the € strengthening vs. the \$. In the past week, the opposite has been the case — EADS' shares have fallen despite the € weakening vs. the \$.

Fundamentals Intact

We expect 27% EPS CAGR 2012A-2016E on 4% Sales CAGR due to margin improvements at the core Airbus Commercial division from a low base.

In our view, the EADS investment case remains very attractive and the fundamental equity story is unchanged. We continue to like EADS' combination of strong earnings growth driven by organic sales growth and margin improvements at the core Airbus Commercial division. EADS targets a margin of 10% in 2015E at Airbus Commercial (Citi 9.3%) vs. 4.5% in 2012A, before the dilutive impact of early A350XWB deliveries at an FX rate of \$1.35/€ (Citi \$1.28/€). We expect margins to improve to reflect operating leverage on rising aircraft deliveries, cost control, an FX tailwind, modest YoY pricing improvements, and closing out A380 programme losses by 2015E. We expect this, and the buyback (12%), to drive 27% EPS CAGR 2012A-2016E.

Our report entitled "[Still Bullish, Target Price Raised to €45](#)" argued that EADS could be worth up to €75/share on a 3-year view based on EV/Sales, EV/EBIT and P/E approaches. We still believe this to be the case and have refreshed our long-term valuation models and republish them in the following pages.

We still believe that EADS shares could be worth >€70 on a 3 year view.

■ **EV/Sales** — EADS is trading on 0.71x 2014E EV/Sales, which is slightly ahead of its historical average of 0.66x vs. a 2012A EBIT margin of 5.3%. Using the rule of thumb that a business with a 10% margin should trade on 1.0x EV/Sales would suggest that EADS could trade up to €54 based on our long-run margin assumption of 8.7%. If EADS could achieve a 10% margin as planned by 2015, we think it could potentially be worth €65/share (at 1.0x EV/Sales). Peer Boeing also trades at c1.0x EV/Sales vs. a current margin of 7.7% in 2012A.

Figure 4. EADS – EV/EBIT-based Valuation (€ millions)

	2013E	2014E	2015E	2016E
Clean EBIT	3,700	4,560	5,650	6,620
Target EV/EBIT Multiple	10.0x	10.0x	10.0x	10.0x
Enterprise Value	37,000	45,600	56,500	66,200
Adjusted Net Debt	-10,691	-14,721	-14,502	-13,380
Suggested Equity Value	26,309	30,879	41,998	52,820
per share	€ 33	€ 43	€ 58	€ 73
Discount Rate	10%			
Factor	1.00	0.91	0.83	0.75
Valuation	€ 33	€ 39	€ 48	€ 55
Estimated A350XWB Charges	-1,500	-1,500	-1,500	-1,500
Estimated A380 Wing Crack Charges	-100	-100	-100	-100
Total Estimated Further Charges	-1,600	-1,600	-1,600	-1,600
per share	-€ 2	-€ 2	-€ 2	-€ 2
Valuation	€ 30.99	€ 36.59	€ 45.79	€ 52.59

Source: Citi Research

■ **EV/EBIT** — If EADS were to hold a forward EV/EBIT multiple of 10x through to 2016E, we believe that the shares could be worth as much as €73 in 3 years, as shown above. A 10x EV/EBIT multiple would be broadly consistent with the multiple we use to value other civil aerospace and industrial companies. This exercise assumes no further A350XWB charges. After factoring in €1.5bn of further charges for the A350 and an additional €100m for A380 (wing cracks) and discounting back the suggested €72/share (=10x 2016E EV/EBIT), the implied valuation is still c€53/share.

■ **P/E** — EADS currently trades on c10x 2014E P/E vs. its historical average rating of c13x). Applying a 13x multiple to our 2014E EPS forecast of €3.90 suggests a valuation of €50/share. Boeing's average historical P/E has been c16x (Figure 9). Applying this to our 2014E EPS would suggest a valuation of €62/share.

At its 10% group margin target, EADS could generate almost €6/share in 2015E.

■ **Earnings Power** – EADS targets a 10% EBIT margin by 2015E. Using our revenue forecasts (and assuming a 15% buyback), we calculate a best-case 2015E EPS of €5.64 vs. our base case forecast of €4.94. Capitalising this at EADS' average P/E rating of c13x would suggest a valuation of c€73/share. Applying Boeing's average P/E of 16x would suggest €90/share.

Financial Statements

Figure 5. EADS - Income Statement 2005-2016E (€ millions)

	2005	2006	2007	2008	2009	2010	2011	2012	2013E	2014E	2015E	2016E
Airbus Commercial	22,179	25,190	25,216	26,232	26,370	27,673	31,159	36,943	38,100	41,500	43,600	46,900
Airbus Military	763	2,200	1,140	2,759	2,235	2,684	2,504	2,131	2,130	2,130	2,130	2,130
Eurocopter	3,211	3,803	4,172	4,486	4,570	4,830	5,415	6,264	6,450	6,640	6,840	7,050
Astrium	2,698	3,212	3,550	4,289	4,799	5,003	4,964	5,817	5,930	6,050	6,170	6,290
Cassidian	5,636	5,864	5,392	5,668	5,363	5,933	5,803	5,740	5,570	5,400	5,400	5,400
Other Businesses	1,155	1,257	1,407	1,338	1,096	1,182	1,252	1,524	1,520	1,520	1,520	1,520
Headquarters/Consolidation	-1,436	-2,092	-1,754	-1,507	-1,611	-1,553	-1,969	-1,939	-1,940	-1,940	-1,940	-1,940
Sales	34,206	39,434	39,123	43,265	42,822	45,752	49,128	56,480	57,760	61,300	63,720	67,350
growth	8%	15%	-1%	11%	-1%	7%	7%	15%	2%	6%	4%	6%
Airbus Commercial	2,307	2,788	2,693	2,006	1,036	281	485	1,647	2,320	3,100	4,070	4,920
Airbus Military	48	75	-155	107	36	21	49	93	90	90	90	90
Eurocopter	212	257	211	293	263	303	374	411	460	510	560	610
Astrium	58	130	174	234	261	283	290	312	350	390	430	470
Cassidian	201	348	345	408	449	477	403	340	330	320	350	380
Other Businesses	-171	-288	84	43	21	25	49	49	50	50	50	50
Headquarters/Consolidation	197	449	274	239	82	-46	144	154	100	100	100	100
EBIT Before One-Offs	2,852	3,759	3,626	3,330	2,148	1,344	1,794	3,006	3,700	4,560	5,650	6,620
Airbus Commercial	10.4%	11.1%	10.7%	7.6%	3.9%	1.0%	1.6%	4.5%	6.1%	7.5%		10.5%
Airbus Military	6.3%	3.4%	-13.6%	3.9%	1.6%	0.8%	2.0%	4.4%	4.2%	4.2%	4.2%	4.2%
Eurocopter	6.6%	6.8%	5.1%	6.5%	5.8%	6.3%	6.9%	6.6%	7.1%	7.7%	8.2%	8.7%
Astrium	2.1%	4.0%	4.9%	5.5%	5.4%	5.7%	5.8%	5.4%	5.9%	6.4%	7.0%	7.5%
Cassidian	3.6%	5.9%	6.4%	7.2%	8.4%	8.0%	6.9%	5.9%	5.9%	5.9%	6.5%	7.0%
margin	8.3%	9.5%	9.3%	7.7%	5.0%	2.9%	3.7%	5.3%	6.4%	7.4%	8.9%	9.8%
EBIT PGE (pre-goodwill/exceptionals)	2,852	399	52	2,830	-322	1,231	1,696	2,186	3,600	4,560	5,650	6,620
margin	8.3%	1.0%	0.1%	6.5%	-0.8%	2.7%	3.5%	3.9%	6.2%	7.4%	8.9%	9.8%
Exceptional Items	-140	-121	-85	-58	-58	-44	-83	-55	0	0	0	0
EBIT (Reported)	2,712	278	-33	2,772	-380	1,187	1,613	2,131	3,600	4,560	5,650	6,620
Net Interest	-155	-121	-199	36	-147	-99	13	-285	-450	-440	-440	-430
Other Financial Result	-22	-123	-538	-508	-445	-272	-233	-168	-180	-180	-180	-180
PBT (Reported)	2,535	34	-770	2,300	-972	816	1,393	1,678	2,970	3,940	5,030	6,010
Underlying PBT (EADS)	2,697	3,616	3,225	3,136	1,694	932	1,515	2,541	3,070	3,940	5,030	6,010
Underlying PBT (Citi)	2,697	3,616	3,225	3,136	1,694	932	1,515	2,541	3,070	3,940	5,030	6,010
Income Tax	-825	81	333	-703	220	-244	-356	-449	-861	-1,143	-1,459	-1,743
Underlying Tax	-809	-1,085	-968	-941	-508	-266	-379	-702	-890	-1,143	-1,459	-1,743
rate	30%	30%	30%	30%	30%	29%	25%	28%	29%	29%	29%	29%
Minority Interests	-34	-16	-9	-25	-11	-19	-4	-1	-1	-1	-1	-1
Net Income (Reported)	1,676	99	-446	1,572	-763	553	1,033	1,228	2,108	2,796	3,570	4,266
Underlying Net Income (EADS)	1,854	2,515	2,249	2,170	1,175	647	1,132	1,838	2,179	2,796	3,570	4,266
Underlying Net Income (Citi)	1,854	2,515	2,249	2,170	1,175	647	1,132	1,838	2,179	2,796	3,570	4,266
EPS (IFRS)	€ 2.11	€ 0.12	-€ 0.56	€ 1.95	-€ 0.94	€ 0.68	€ 1.27	€ 1.50	€ 2.64	€ 3.87	€ 4.94	€ 5.90
Underlying EPS (EADS)	€ 2.33	€ 3.14	€ 2.80	€ 2.69	€ 1.45	€ 0.80	€ 1.39	€ 2.24	€ 2.73	€ 3.87	€ 4.94	€ 5.90
Underlying EPS (Citi)	€ 2.33	€ 3.14	€ 2.80	€ 2.69	€ 1.45	€ 0.80	€ 1.39	€ 2.24	€ 2.73	€ 3.87	€ 4.94	€ 5.90
growth	14%	35%	-11%	-4%	-46%	-45%	75%	61%	22%	41%	28%	19%
DPS	€ 0.65	€ 0.12	€ 0.12	€ 0.20	€ 0.00	€ 0.22	€ 0.45	€ 0.60	€ 1.09	€ 1.55	€ 1.97	€ 2.36
Average Shares	795	800	803	807	810	811	813	819	797	723	723	723
Average Diluted Shares	800	804	806	808	811	811	814	821	798	724	724	724

Source: Company Reports and Citi Research Estimates

Figure 6. EADS - Cash Flow Statement 2005-2016E (€ millions)

	2005	2006	2007	2008	2009	2010	2011	2012	2013E	2014E	2015E	2016E
Clean EBIT	2,852	3,759	3,626	3,330	2,148	1,344	1,794	3,006	3,700	4,560	5,650	6,620
Depreciation and Amortisation	1,653	1,691	1,772	1,667	1,826	1,582	1,884	2,053	2,100	2,230	2,320	2,450
Tax Paid	-265	-239	-73	-393	-32	-215	-307	-376	-861	-1,143	-1,459	-1,743
Associates/JVs	-174	-106	-257	-161	-107	-104	-142	-201	-206	-218	-227	-240
Movement in Provisions	175	2,150	2,268	1	1,767	334	719	1,072	-650	-650	-650	-650
Underlying Net Interest	-155	-121	-199	36	-147	-236	-107	-285	-450	-440	-440	-430
Customer Financing	174	1,160	61	-327	-406	63	135	-146	-300	-300	-300	-300
Working Capital	1,065	-1,303	1,175	155	421	2,756	1,251	70	0	0	0	0
Capex (Gross)	-2,818	-2,708	-2,028	-1,837	-1,957	-2,250	-2,197	-3,270	-3,270	-3,100	-2,800	-2,700
Other	-153	-2,334	-3,236	141	-3,005	-487	-537	-474	-100	0	0	0
FCF (pre-Acquisition)	2,354	1,949	3,109	2,612	508	2,787	2,493	1,449	-37	939	2,095	3,007
per share	€ 2.96	€ 2.44	€ 3.87	€ 3.24	€ 0.63	€ 3.44	€ 3.07	€ 1.77	-€ 0.05	€ 1.30	€ 2.90	€ 4.16
Net Acquisitions/Disposals	59	80	245	-53	77	-80	-1,535	-201	0	0	0	0
FCF (post-Acquisition)	2,413	2,029	3,354	2,559	585	2,707	958	1,248	-37	939	2,095	3,007
Contribution to Pension Plan Assets	0	0	-303	-436	-173	-553	-489	-856	-500	-500	-500	-500
Equity Issued/Redeemed	-101	59	46	63	12	-51	-66	139	-4,340	0	0	0
Dividends	-396	-552	-98	-107	-166	-7	-183	-379	-492	-869	-1,121	-1,425
FX/Other	-388	-2,796	-204	90	346	25	-457	459	0	0	0	0
Change in Net Debt	1,528	-1,260	2,795	2,169	604	2,121	-237	611	-5,368	-430	473	1,083
Net Debt/(Cash) b/f	-3,961	-5,489	-4,229	-7,024	-9,193	-9,797	-11,918	-11,681	-12,292	-6,924	-6,494	-6,967
Net Debt/(Cash) c/f	-5,489	-4,229	-7,024	-9,193	-9,797	-11,918	-11,681	-12,292	-6,924	-6,494	-6,967	-8,050

Source: Company reports and Citi Research

Figure 7. EADS – Calculation of Adjusted Net Debt 2005-2016E (€ millions)

	2005	2006	2007	2008	2009	2010	2011	2012	2013E	2014E	2015E	2016E
Net Debt / (Cash)	-6,080	-5,133	-7,883	-9,930	-10,449	-12,450	-12,136	-12,637	-7,269	-6,839	-7,312	-8,395
Pension Provision	5,238	5,883	4,668	4,546	5,306	5,221	5,821	6,433	6,433	6,433	6,433	6,433
Government Launch Aid	5,293	5,418	5,315	4,920	5,294	6,020	5,737	6,112	6,112	6,112	6,112	6,112
Off Balance Sheet Customer Financing	644	526	440	415	382	379	323	169	169	169	169	169
Provisions on Programmes	0	0	3,300	2,700	2,500	1,850	4,000	4,400	3,750	3,100	2,450	1,800
Customer Advances	4,911	6,308	8,420	8,843	8,579	8,817	9,256	9,881	9,881	9,881	9,881	9,881
MV Dassault Stake	-2,873	-3,324	-3,166	-1,995	-2,605	-2,982	-2,828	-3,692	-4,463	-4,463	-4,463	-4,463
Minority Interests	153	137	85	104	106	95	15	25	26	27	28	29
Other	3,500	0	0	0	0	0	-700	0	0	0	0	0
Adjusted Net Debt	10,786	9,815	11,179	9,603	9,113	6,950	9,488	10,691	14,639	14,420	13,298	11,566

Source: Company reports and Citi Research

Figure 8. EADS - Discounted Cash Flow (€ millions)

	2013E	2014E	2015E	2016E	2017E	TV
Airbus Commercial	38,100	41,500	43,600	46,900	49,400	50,880
Airbus Military	2,130	2,130	2,130	2,130	2,130	2,130
Eurocopter	6,450	6,640	6,840	7,050	7,260	7,370
Astrium	5,930	6,050	6,170	6,290	6,290	6,350
Cassidian	5,570	5,400	5,400	5,400	5,400	5,400
Other Businesses	1,520	1,520	1,520	1,520	1,520	1,520
Headquarters/Consolidation	-1,940	-1,940	-1,940	-1,940	-1,940	-1,980
Sales	57,760	61,300	63,720	67,350	70,060	71,670
Airbus Commercial		8.9%	5.1%	7.6%	5.3%	3.0%
Airbus Military		0.0%	0.0%	0.0%	0.0%	0.0%
Eurocopter		2.9%	3.0%	3.1%	3.0%	1.5%
Astrium		2.0%	2.0%	1.9%	0.0%	1.0%
Cassidian		-3.1%	0.0%	0.0%	0.0%	0.0%
Other Businesses		0.0%	0.0%	0.0%	0.0%	0.0%
growth		6.1%	3.9%	5.7%	4.0%	2.3%
Airbus Commercial	2,320	3,100	4,070	4,920	5,730	5,000
Airbus Military	90	90	90	90	90	90
Eurocopter	460	510	560	610	630	590
Astrium	350	390	430	470	470	440
Cassidian	330	320	350	380	380	350
Other Businesses	50	50	50	50	50	50
Headquarters/Consolidation	100	100	100	100	100	100
EBITA	3,700	4,560	5,650	6,620	7,450	6,620
Airbus Commercial	6.1%	7.5%	9.3%	10.5%	11.6%	9.8%
Airbus Military	4.2%	4.2%	4.2%	4.2%	4.2%	4.0%
Eurocopter	7.1%	7.7%	8.2%	8.7%	8.7%	8.0%
Astrium	5.9%	6.4%	7.0%	7.5%	7.5%	7.0%
Cassidian	5.9%	5.9%	6.5%	7.0%	7.0%	6.5%
Other Businesses	3.3%	3.3%	3.3%	3.3%	3.3%	3.0%
margin	6.4%	7.4%	8.9%	9.8%	10.6%	9.2%
Taxation	-1,022	-1,260	-1,561	-1,829	-2,058	-1,829
NOPAT	2,678	3,300	4,089	4,791	5,392	4,791
Capital Expenditure	-3,270	-3,100	-2,800	-2,700	-2,800	-2,870
% of Sales	5.7%	5.1%	4.4%	4.0%	4.0%	4.0%
Depreciation	2,100	2,230	2,320	2,450	2,550	2,610
% of Sales	3.6%	3.6%	3.6%	3.6%	3.6%	3.6%
Capex/Depreciation	1.6x	1.4x	1.2x	1.1x	1.1x	1.1x
Working Capital	0	0	0	0	0	0
% Sales	0%	0%	0%	0%	0%	0%
FCF	1,508	2,430	3,609	4,541	5,142	58,830
EV	45,593					
Adjusted Net Debt (2012E)	-10,691					
Buyback	-4,340					
Further A350 Charges / A380 Charges	-1,600					
Free Cash Flow	-15,123	2,430	3,609	4,541	5,142	58,830
Shares	797	723	723	723	723	723
PV of FCF per share	-€ 18.97	€ 3.36	€ 4.99	€ 6.28	€ 88.44	€ 81.34
DCF Value per share	€ 48.50					

Source: Company Reports and Citi Research Estimates

EADS

Company description

EADS is a European aerospace and defence company centred on Airbus Commercial, which represents c60% of group sales. Airbus Commercial manufactures large commercial jet aircraft and forms half of a duopoly globally with Boeing. The other EADS businesses include Airbus Military (military transport and refueling aircraft), Eurocopter (helicopters), Cassidian (with exposure to MBDA missiles and the Eurofighter programme) and Astrium (satellites and launchers). EADS also has a 50% stake in ATR, a regional aircraft manufacturer (alongside Finmeccanica).

Investment strategy

We rate EADS Buy. We view EADS as a leveraged play on civil aerospace OE, upon which we remain positive both in the near term and as a long-term growth story. For EADS we forecast strong EPS growth from a depressed base due to rising aircraft deliveries, underpinned by the large order backlog, and margin improvements in the core Airbus business driven by higher volumes, pricing improvements, FX and reducing A380 losses. We are positive on the ability for EADS to deliver the A350XWB programme without further significant charges. EADS has a strong balance sheet, with a large net cash position, which also makes it attractive in the current environment of macroeconomic uncertainty, in our view. EADS has additionally announced a major restructuring of the strategic shareholders and a 15% buyback, which should help support further re-rating, in our view.

Valuation

Our one-year Target Price of €48.50/share is based on DCF model using a conservative set of assumptions, including a 10% WACC, 2.3% long-term growth and a mid-cycle margin assumption of c9% for the group and for Airbus Commercial (at \$1.28/€). EADS targets a 10% Airbus Commercial margin by 2015E (at \$1.30/€) before the dilutive impact of early A350XWB deliveries. Our Target Price equates to 12.5x 2014E P/E (vs. EADS' long-run average of c13x) and 10.0x 2014E EV/EBIT. Our Target Price equates to 0.74x 2014E EV/Sales vs. our mid-cycle margin assumption of c9% and 7.4% in 2014E, rising to 8.9% in 2015E.

Risks

The key risks to our investment thesis on EADS are: (1) potential further cost overruns on the A350XWB programme; (2) execution risks surrounding Airbus' plans to ramp up narrow-body production; (3) management's attempts at transformational M&A (like the now aborted merger with BAE); (4) transactional FX risk; (5) increase in demand for vendor financing, worsening cash flows, if credit markets tighten or continued export credit agency support is not forthcoming; (6) Power 8 cost cutting plan failing to achieve the targeted cost savings as incremental savings prove harder to attain; (7) continued difficulties ramping up A380 production; (8) continued cost overruns on the A400M military transporter programme; (9) the potential for a late-cycle decline in civil aircraft deliveries; (10) re-engining the A320 could prove technically and commercially risky, and lead to even higher R&D costs at Airbus Commercial; (11) the complex nature of the business, making it difficult to model and hard to value. Recurring non-recurring items can make estimating the underlying profitability of the business tricky.

If any of these risk factors has a greater downside impact than we anticipate, the share price will likely have difficulty attaining our target price. Conversely, if the impact of any of these upside risks is greater than we anticipate, the stock could exceed our target price.

Appendix A-1

Analyst Certification

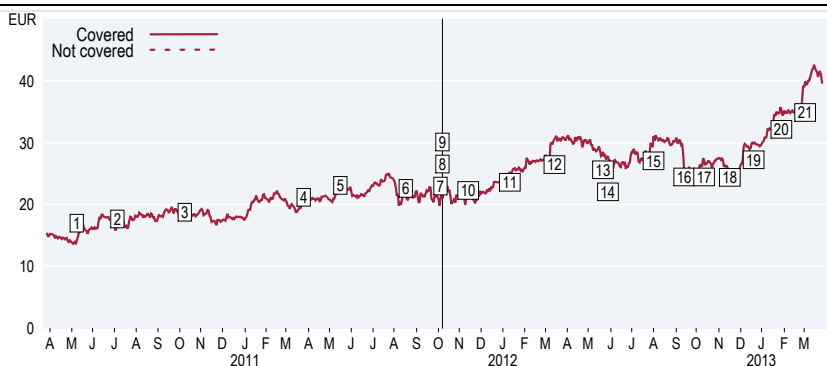
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IMPORTANT DISCLOSURES

EADS (EAD.PA)

Ratings and Target Price History Fundamental Research

Analyst: Jeremy Bragg



Date	Rating	Target Price	Closing Price
1 10-May-10	*1H	*18.50	14.16
2 6-Jul-10	1H	*22.50	16.37
3 8-Oct-10	*2H	*19.30	17.98
4 25-Mar-11	2H	*21.00	20.19
5 17-May-11	2H	*23.80	22.05
6 17-Aug-11	2H	*23.00	22.60
7 5-Oct-11	2H	*22.50	20.96

* Indicates change

Date	Rating	Target Price	Closing Price
8 7-Oct-11	Stock rating system changed		
9 7-Oct-11	*2	22.50	20.99
10 14-Nov-11	*1	*27.00	22.05
11 11-Jan-12	1	*31.00	25.17
12 14-Mar-12	1	*34.50	30.56
13 22-May-12	1	*38.00	28.51
14 29-May-12	1	*36.50	27.83

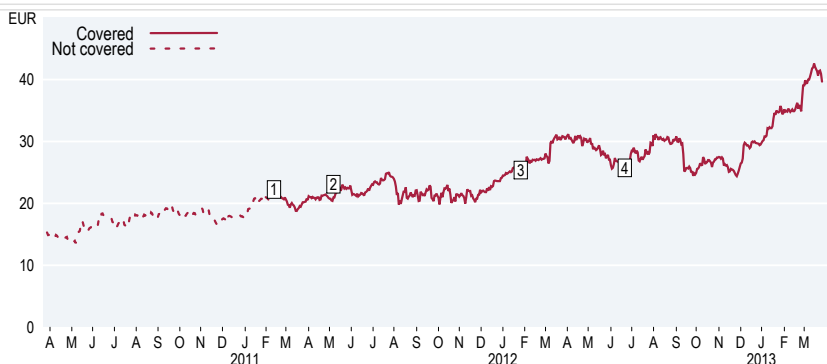
Date	Rating	Target Price	Closing Price
15 1-Aug-12	1	*40.00	31.01
16 13-Sep-12	*2	*27.00	25.15
17 11-Oct-12	*1	*33.00	27.18
18 16-Nov-12	1	*34.00	25.17
19 20-Dec-12	1	*37.50	29.87
20 29-Jan-13	1	*40.00	35.30
21 4-Mar-13	1	*45.00	39.90

Rating/target price changes above reflect Eastern Standard Time

EADS (EAD.PA)

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

Analyst: Jeremy Bragg



Date	Rating	Target Price	Closing Price
1 11-Feb-11	*ADD LP	-	21.77
2 6-May-11	*REM LP	-	20.95

* Indicates change

Date	Rating	Target Price	Closing Price
3 26-Jan-12	*ADD MP	-	25.45
4 21-Jun-12	*REM MP	-	26.90

Rating/target price changes above reflect Eastern Standard Time

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% of companies in each rating category that are investment banking clients

12 Month Rating			Relative Rating		
Buy	Hold	Sell	Buy	Hold	Sell
49%	38%	12%	7%	86%	7%
53%	49%	45%	60%	49%	55%

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