EQUITIES
EUROPE
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HSBC Global Research

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www.research.hsbc.com

European equities in 2016

Earnings underpin equities

- Upside based on positive earnings surprises and attractive valuations
- Lower bond yields and ECB policy to add further support
- We highlight four investment themes: lower rates point to higher yield, quality is risky, China - beware of a bounce, and M&A upswing to continue

Play video with Peter Sullivan

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Investment themes for 2016

Theme	Description	How to invest*
1. Lower rates point to higher yield	High-yielding equities offer resilience to macro shocks and should thrive as bond yields fall	Insurance: Generali, Prudential Real estate: Hammerson Energy: Total, Royal Dutch Shell Utilities: National Grid, Enel
2. Quality is risky	Quality is perceived by many investors as low risk, but we see it as one of the highest risk styles because both valuation and macro risks are high	Least preferred stocks: Pharmaceuticals: Novo Nordisk Health care equipment: Getinge Food & beverages: Beiersdorf Software: Dassault Systèmes
3. China – beware of a bounce	The consensus call of running with underweight positions on the China exposed sectors makes them candidates for an upside surprise	Luxury goods: Moncler, Richemont, LVMH Autos: Michelin Metals & mining: Thyssenkrupp, Glencore Capital goods: Atlas Copco, Schneider
4. M&A upswing to continue	Cash-rich companies, low debt-servicing costs and a perceived lack of growth opportunities are recipes for continued M&A	Real estate: Vonovia Telecoms: Deutsche Telekom, BT, Telecom Italia Autos: Renault Chemicals: BASF

Source: HSBC
*Note: Prudential, Total, Deutsche Telekom and National Grid are also HSBC Europe Super Ten portfolio constituents

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European equities in 2016

- Upside based on positive earnings surprises and attractive valuations
- We expect high-yielding equites to thrive as bond yields fall; for those with higher risk appetite, stocks exposed to China are very much out of favour
- Quality stocks are risky because valuations are stretched; M&A upswing to continue

Fundamentals versus risks

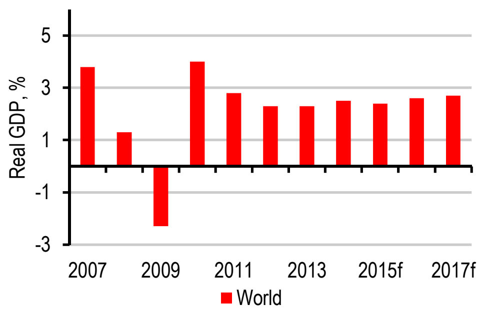
2015 has been a battle between improving fundamentals and emerging risks. Europe has been the bright spot in the global economy, and a weaker euro has boosted earnings in the eurozone. However, while these positive fundamentals have been unfolding, investors have had to grapple with the crisis in Greece, a slowdown in emerging markets, plunging commodity prices and the prospect of Fed tightening. At the time of writing, improving fundamentals seem to be outweighing risks, with European equities delivering a total return (dividends and share price appreciation) of 8% year-to-date in local currency. We see a similar battle in 2016 and we expect the same winner.

Slow growth, falling bond yields and a weaker dollar

The key to improving fundamentals is that we expect double-digit earnings growth next year. Our outlook is based on HSBC economic forecasts and the key ones are:

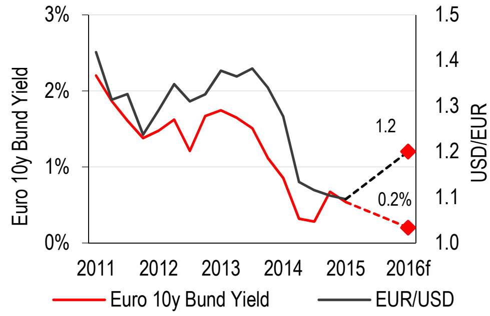
- Bund yields will fall to 0.2%, reducing corporate interest payments.
- Slow world economic growth and even slower wage growth in Europe. It is the gap between the two that is important for margins.
- We also expect the euro to strengthen to 1.20 against the dollar. This will act as a drag on earnings.

Chart 1: Economic growth stuck in a low gear



Source: HSBC, Thomson Reuters Datastream

Chart 2: Lower Bund yields and a stronger euro in prospect



Source: HSBC, Thomson Reuters Datastream

Upside earnings surprises

When we put these macro forecasts together, we estimate 15% EPS growth in 2016 in Europe ex UK, and 10% in the UK. These are both above the consensus forecasts of 8% and 5%, respectively, Table 3.

One factor boosting margins is the prospect of nominal economic growth being above wage growth. Our economists expect world real GDP growth to be 2.6% next year and inflation to be 2.5%. This is pedestrian by historical standards, but at least it implies that economic growth will be higher than wage growth, which we expect to be only 1.6% in the eurozone. Margins usually widen when economic growth exceeds wage growth, Chart 4.

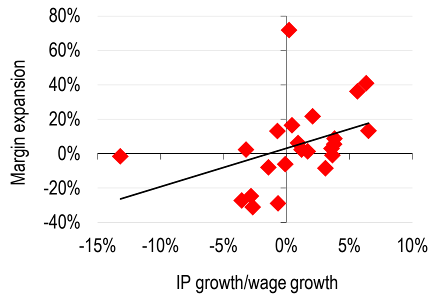
Table 3: HSBC macro forecasts point to positive earnings surprises in 2016

Europe ex UK				UK			
		2016	2017			2016	2017
Sales growth (%)	HSBC	4	6	**Sales growth (%)**	HSBC	5	6
	Consensus	3	4		Consensus	2	5
Inputs	EU Cons	1.7	1.5	**Inputs**	Energy Index	10.2	3.4
	World IP	3.4	3.8		GBP	1	-4
	Euro/USD	5	2		UK CPI	1.3	1.7
	EU CPI	0.7	1.2				
Margin expansion (%)	HSBC	11	7	**Margin expansion (%)**	HSBC	5	6
	Consensus	5	6		Consensus	2	8
Inputs	EU IP (nom)	2.0	3.0	**Inputs**	UK IP (nom)	2.5	2.9
	Wages (nom)	1.6	1.6		UK wages (nom)	3.3	3.3
	Eff. Tax rate	31	31		Eff tax rate	37	37
	Eff. Interest rate	2.1	2.0				
EPS growth (%)	HSBC	15	13	**EPS growth (%)**	HSBC	10	12
	Consensus	8	11		Consensus	5	14

Our above-consensus forecast for Europe ex UK is also based on our Fixed Income team's 0.2% Bund yield forecast. This is likely to reduce corporate interest payments and boost margins, Chart 5.

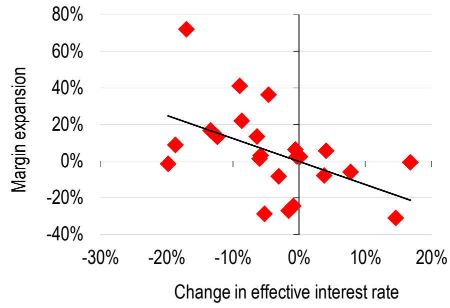
Earnings in the UK have fallen in 2015, hampered by currency strength and dragged down by the plunge in commodity prices. The UK is particularly exposed to lower commodity prices given its high weighting in commodity sectors. We expect some recovery next year but this is highly dependent on some recovery in commodity prices.

Chart 4*: Margins usually expand when economic growth exceeds wage growth



Note: *Diamonds represent years
Source: HSBC, Thomson Reuters Datastream

Chart 5*: Margins usually expand when interest rates fall



Note: *Diamonds represent years
Source: HSBC, Thomson Reuters Datastream

Valuations are not stretched

There are many risks that could blow European equities off course, but valuation, in our view, is unlikely to be one of them. We judge that European equities are somewhere between fair value and 20% undervalued. We approach this from two directions: a comparison with historical averages and a forward-looking DCF, both giving consistent signals.

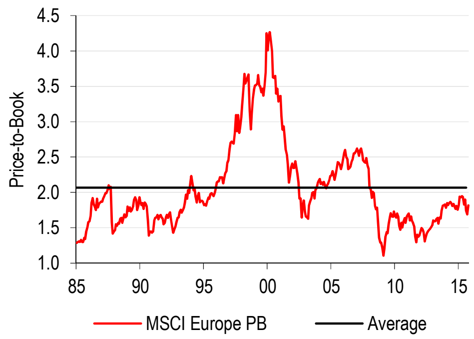
The Shiller PE and the price-to-book ratio are also below their 30-year averages (Charts 6 and 7). For our DCF we assume lower profit growth, lower returns on capital and a lower spread between returns and cost of capital. Despite this, European equities are 10% to 15% below their equilibrium value according to our estimates (Charts 8 and 9).

The right kind of risks

There are a daunting array of risks that could derail European equities, from Fed tightening to plunging commodity prices, from the slowdown in emerging markets to tensions within the eurozone. However, we do not expect them to outweigh the positive fundamentals, not least because these risks are well known to investors.

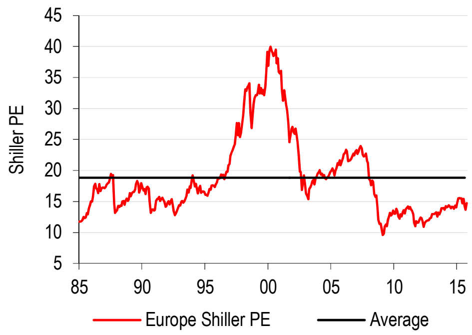
Even if these risks do cause equity markets to fall, they do not usually cause lasting damage. For example, equities usually rise in the 12 months after the first Fed rate rise, albeit after a wobbly quarter. Falling commodity prices are also a double-edged sword; they represent lower input costs for the majority of sectors and tend to increase consumer spending power. A spike in commodity prices is usually more problematic for equities. A slowdown in emerging markets is also negative for equities, but even this has been widely discussed and positioned for. These risks are one of the reasons why we favour high-yield equities. We believe this strategy will perform under a wide range of scenarios.

Chart 6: Low price to book for Europe



Source: MSCI, HSBC, Thomson Reuters Datastream, I/B/E/S

Chart 7: Low Shiller PE for Europe



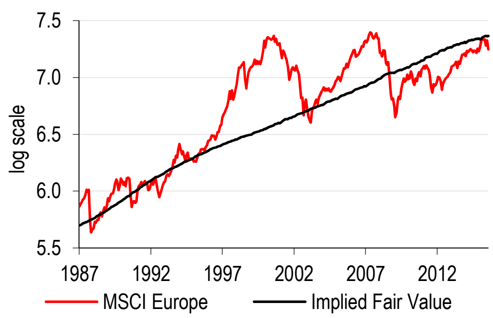
Source: MSCI, HSBC, Thomson Reuters Datastream, I/B/E/S

Chart 8: European equities are 10% to 15% undervalued according to our DCF

	History	Forecast Assumption	Expression
Return on Capital %	10.3	7.8	
Cost of Capital %	7.8	7.0	
Spread, ppt	2.5	0.8	RoC-WACC
Profit Growth %	4.5	4.0	
Retention Rate %	43.0	51.0	g/RoC
EV/NOPAT	17.0	16.2	(1-r)(WACC-g)
Current EV/NOPAT		15.5	

Source: MSCI, HSBC, Thomson Reuters Datastream

Chart 9: European equities are below our DCF value estimate



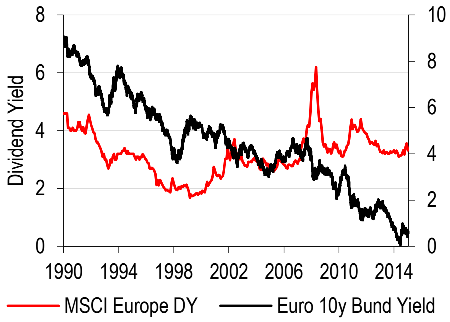
*Implied fair value is calculated using today's long-run assumptions
Source: MSCI, HSBC, Thomson Reuters Datastream

Lower rates point to higher yield

We recommend high yield equities because we believe they will outperform if bond yields fall and because we believe they could prove to be resilient to macro shocks.

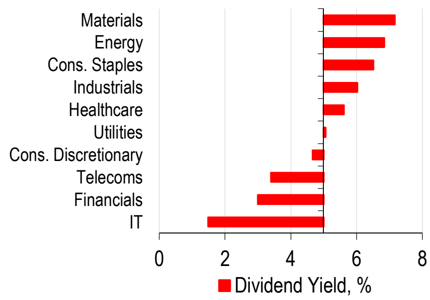
HSBC Fixed Income Research expects Bund yields to fall close to zero next year and we expect this to boost demand for all high yielding assets, including high yield equities. High yield equities outperformed during the two largest declines in bond yields in the past five years, between June and September 2011 when bond yields fell from above 3% to below 2%, and between December 2013 and March 2015 when bond yields fell from 1.9% to 0.2%.

Chart 10: Bond yields are below dividend yields in Europe



Source: MSCI, HSBC, Thomson Reuters Datastream

Chart 11: Materials and energy have the highest prospective yields



Source: MSCI, HSBC, Thomson Reuters Datastream

One of the attractions of yield is that it is found in a diverse group of stocks covering many sectors, from utilities to materials and energy to telecoms (Chart 11). In our view, this diversity is likely to make it resilient to macro developments.

The prospective dividend yield for Europe is 3.7% compared to the Bund yield of 0.5%, Chart 10. It is highly unusual for dividend yields to be so far above government bond yields and we do not expect this to persist, unless dividend growth is permanently subdued and the equity risk premium has risen permanently.

Insurance

Insurance offers attractive capital returns, backed by cash flow generation. The 2016e normal dividend yield for our coverage universe is 4.7%, relative to the Stoxx Europe 600 at 3.8%, while the total yield, including buybacks and special dividends is 5.2%. The sector's dividend credentials are backed by a 2016e cash flow yield of 7.6%. Our high conviction Buys are Generali and Prudential (an HSBC Europe Super Ten portfolio constituent).

Generali offers above sector-average growth in cash flows, dividends and earnings over the next three years. We forecast 13% pa dividend growth with positive surprise potential, given dividend cover ratios above its European composite peers, strong cash-flow growth potential and increasing comfort around its economic solvency position. This takes the current yield (2015e) of 3.9% up to 5% in 2017e.

At Prudential, under the guidance of the new CEO, we believe there could be more focus on operational efficiency than in the past, opening out the possibility of a positive dividend surprise.

Real estate

Low bond yields have been highly supportive for real estate over the last six years or so, both as a favourable yield benchmark and as an attractive price-setting comparator for credit. The danger is that weak economic fundamentals persist, negative real rates become endemic, and the risk of deflation increases significantly should further central bank action prove ineffective.

In short, falling bond yields for a cyclical sector such as real estate may well be a double-edged sword and we would recommend a selective approach.

Hammerson is one of our conviction Buy ideas that offers an attractive yield. The company's focus on growth and quality of earnings has resulted in dividend growth averaging 7.6% since 2012. We expect more to come with an average growth rate of 8% forecast for the next three years, taking the dividend yield up to 4.5% by end 2017e.

Energy (Integrated oils)
Dividend sustainability is a key area of focus for investors, given the slump in the oil price over the last 17 months. The sector's dividend yield to the wider market remains close to a 27-year high. We think this extreme reading is indicative of the level of scepticism in the market as to whether dividends are sustainable. We believe this scepticism is overdone. On our base case assumption of USD70/b Brent, we see most of the big oils broadly covering their dividends organically in 2017, and many are now targeting USD60/b organic breakevens.

Our highest conviction Buys are Total (an HSBC Europe Super Ten portfolio constituent) and Royal Dutch Shell. Total offers the best combination of volume growth and improvement in free cash yields of the big-caps. This makes the attractive prevailing 5% dividend yield sustainable, in our view. Royal Dutch Shell's commitment to the dividend is clear, and its balance sheet and potential disposals give it plenty of room to sustain it.

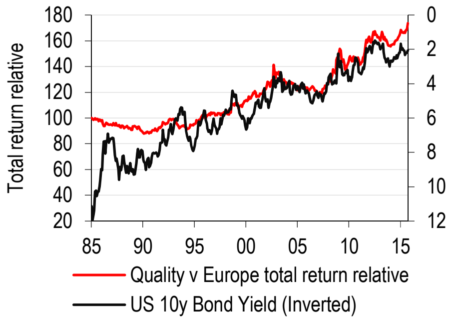
Utilities
In an environment of low bond yields and declining power prices, we continue to favour safe regulated plays with clear visibility on earnings and 2016e dividend yields above 4%. National Grid (an HSBC Super Ten constituent) and Enel are the two high conviction Buys in our coverage that offer a yield in excess of 4%. The uncertain commodity environment brings National Grid's defensive investment proposition to the fore, in our view. The company offers a sustainable yield (4.8% 2015e and growing) and scope for regulatory asset growth remains attractive.

Enel is targeting a constant increase in the pay-out (from 50% in 2015e to 65% by 2018e) sustaining a dividend growth profile that on our estimates provides a minimum yield close to 5% by 2017e assuming current prices.

Quality is risky

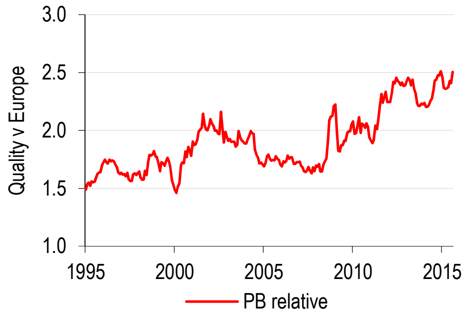
We believe many investors choose quality because it is perceived as being low risk. This may be true in terms of operating performance, but as an investment strategy we see it as one of the highest risk styles because both valuation and macro risks are high.

Chart 12: Quality has outperformed as bond yields have fallen



Note: Total return = dividends + price appreciation
Source: MSCI, HSBC, Thomson Reuters Datastream

Chart 13: Valuations are stretched for quality



Source: HSBC, Thomson Reuters Datastream

Quality has been the standout performer over the past two decades, one of the main beneficiaries of slow growth and ultra-low interest rates, Chart 12. On this basis we would expect quality to outperform if HSBC Fixed Income's forecast of lower bond yields proves to be correct. However, we also expect high yield equities to outperform and we prefer the yield strategy because we believe it has a lower valuation risk.

The strong performance of quality has taken valuations towards decade extremes, Chart 13, and makes the style vulnerable to negative shocks, in our view. Health care and the HPC/food sectors tend to have a higher concentration of quality classified companies, but this theme is a bottom-up one and our analysts also highlight stocks at risk in software and business services.

Pharmaceuticals
The US election cycle puts US drug pricing centre stage as we move into 2016. US drug prices, the magnitude of some drug price increases and the difference between drug prices inside and outside the US have all been signalled by various presidential candidates as likely discussion topics during the upcoming campaign. This opens up the likelihood of a prolonged period of unremittingly negative headlines for the sector which could result in multiple contraction in the near term.

Our least preferred company is Novo Nordisk. It is operationally the best run company in the sector and has delivered exceptional revenue and earnings growth over the last 10 years. But that operational excellence is more than reflected in the stock's significant premium to the sector on almost every valuation metric. Further, with increasing price pressure and competition in Novo's core Diabetes area, and with competition emerging for Novo's haemophilia franchise, the potential risks for Novo's growth profile are not reflected in the current valuation, in our view.

Home and personal care and food producers
We expect sales growth in HPC in 2016e to remain close to the bottom of the 3-5% growth range that the sector has historically delivered. This creates a headwind for the sector given the demanding multiples that the stocks trade on.

Beiersdorf is a case in point. We see it as a quality company that is likely to deliver EPS growth c8.0%-8.5% per annum out to 2019e on our forecasts. But this is not sufficient in our view to justify a PE of 28.3x for 2016e, a 29% premium to its global HPC sector peers.

Health care equipment
Fading FX tailwinds, tougher US reimbursement environment and continuing weak emerging market growth are key challenges for 2016. The sector trades on a 12-month-forward PE of 23.1x, a 20% premium to the average of the last 10 years. Our least preferred name under coverage is Getinge.

Least preferred (quality) stocks in other sectors
In the software space, Dassault Systèmes (Software and IT Services) is one of our analyst's least preferred names. It remains a high-quality story, but this is more than reflected in its premium valuation, in our view. EV/NOPAT of 27x 2016e needs to be supported by upgrades to consensus estimates for 2016e which are already at the high end of the company guidance. We expect guidance for 2016e to disappoint, as it has done for the past three years.

China exposure – beware of a bounce

European equities with Chinese exposure are deeply out of favour. The August slump in stocks crystallised investors' concerns regarding a hard landing in China that had been steadily building since 2012. Pessimism on anything China-related has reached such an extreme level, that we believe the consensus call of running with big underweight positions on these exposed sectors is now dangerous.

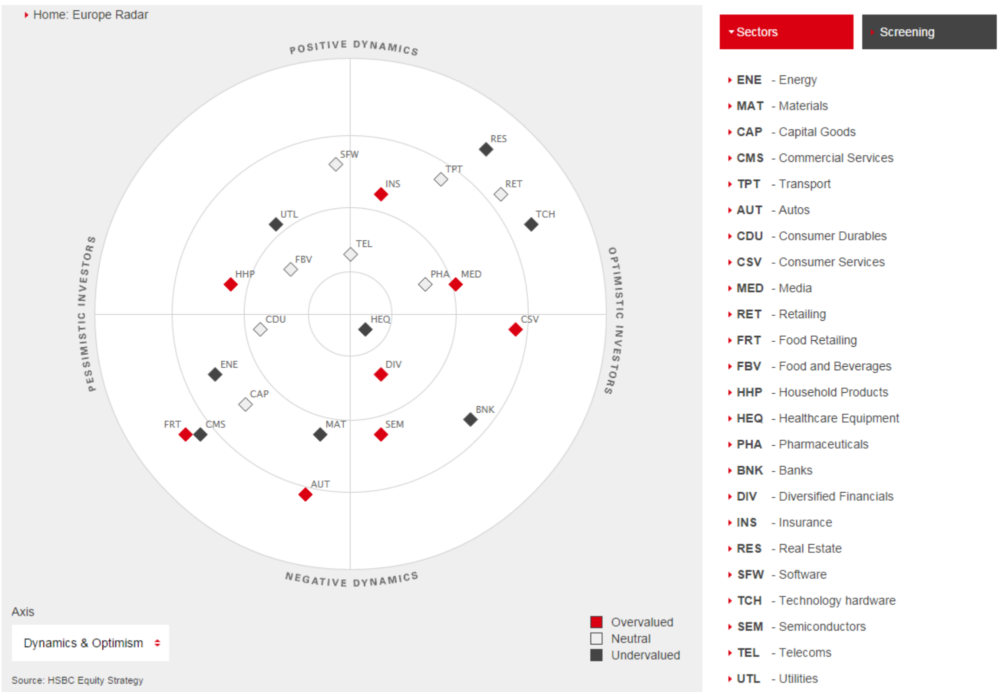
Monetary policy has been too tight in China in our view and we have argued that policy makers need to do more. But this now appears to be happening. The recent cuts to interest rates and the RRR highlight policy makers renewed efforts to stabilise growth. Our China economists are looking for another 25bps rate cut and 300bps RRR cut as we move into 2016. They also forecast a moderate recovery for economic activity in 2016. Property and infrastructure investments are to be key drivers while consumption spending is holding up too (see *Asian equities in 2016*, November 2015).

In the August update of our Radar – the framework we use to guide us to our sector and country recommendations (see *Europe Equity Insights: the great fall of China (exposed sectors)*, 19 August 2015) – we highlighted how the exposed sectors had fallen dramatically out of favour. This remains the case three months on. Materials, consumer durables, capital goods and autos remain located on the left hand side of our Radar framework, highlighting relative investor pessimism (see chart 14 and http://www.research.hsbc.com/Radar for our web tool).

Metals & Mining

The key takeaway from our sector team's recent China trip (see *Metals & Mining, China trip: implications for copper*, 6 October 2015) was that, while China is structurally slowing, there was no evidence of a recent sudden demand shock in contrast to snowballing negative sentiment. Even though a significant structural rebound looks unlikely, stability alone may be enough to trigger selective interest in the sector. And if a demand floor is established, as is our

Chart 14: HSBC Radar highlights that the China exposed sectors are out of favour (click on chart to launch our interactive web tool)



Source: HSBC, Thomson Reuters Datastream

expectation, a lowering of the risk discount on a select group of higher beta equities will present the best opportunities. We see copper working under a low positive demand growth environment, given we think the market is too optimistic on near-term supply growth.

Glencore is a high risk proposition but one that we believe is well positioned to benefit. Recently announced debt reduction measures secure the balance sheet in all but the most bearish demand scenarios. Importantly, the Glencore investment case works without needing a commodity price recovery.

While ThyssenKrupp faces the same steel pricing pressure as peers, we think that it is one of the few steel stocks that fully discounts spot steel margins and a cautious economic scenario. We think that the investment case is for a multi-year transformation with more cost cutting in 2016e. While book equity is rather low (9.4% of balance sheet total) we think that a 2016e ND/EBITDA of 1.3x indicates a solid balance sheet. The conglomerate discount has widened to previous peak values, and stripping out elevators the other assets trade at an attractive 5.0x 2016e EV/EBITDA.

Autos
We forecast a rebound in light vehicle sales in emerging markets in 2016. An acceleration in China demand (2016e: +5% y-o-y), as a result of temporary vehicle purchase tax cuts, is the driving force behind this improvement.

Michelin should benefit from this improving trend. Our positive view on the stock rests on three pillars: its defensive nature with 75% exposure to replacement tyres, its significant margin improvement potential from a low base and its relatively cheap valuation.

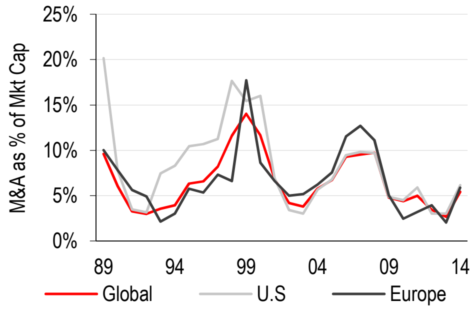
Luxury goods
China outbound travel is still in its infancy. Even though Chinese consumers already account for around 35% of global luxury consumption, there have been only about 50m trips outside of Hong Kong and Macau, less than the likely number of passport holders (65m). We forecast a mid-teen increase pa in Chinese outbound travel over the medium term, with most reasons for spending abroad still being valid.

All luxury goods companies should benefit from this trend and our three high conviction Buys are Moncler, Richemont and LVMH.

Capital goods
The slowdown in China and the capex cuts coming through in the resources space have been significant headwinds for the capital goods sector. Our coverage universe saw no like-for-like top-line growth in the first nine months of 2015 but nonetheless managed to generate like-for-like margin expansion of 50bps, underlying EPS growth of 16% and operating cash flow growth of 34%. We believe that this resilient operational performance will continue in 2016, with any stabilisation in China demand trends likely to provide an added boost.

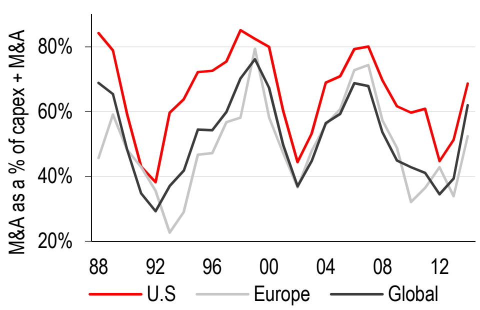
Atlas Copco and Schneider are well paced to benefit from any improvement in the macro backdrop in China.

Chart 15: M&A activity is nowhere near previous peaks



Source: MSCI, HSBC, Thomson Reuters Datastream

Chart 16: Companies prefer M&A to capital spending



Source: MSCI, HSBC, Thomson Reuters Datastream

M&A upswing to continue

The takeover of SAB Miller by AB Inbev has put M&A in the spotlight and raised questions about the sustainability of current trends, but we expect it to increase in 2016. M&A has been rising but activity is nowhere near the peaks reached in previous cycles, chart 15.

Cash-rich companies, low debt-servicing costs and a perceived lack of growth opportunities are recipes for continued M&A. Companies have the capacity to increase M&A spending because they are in surprisingly robust health given the weakness of economic growth. We believe this is because although growth has been slow it has been stable, and the clouds have a number of silver linings including low interest rates, subdued wage growth and falling corporate tax rates. These have helped to boost profits and profitability.

The health of the corporate sector gives companies the capacity to buy (M&A) or build (capital spending). We believe they will increasingly choose to buy because the macro outlook is so uncertain. Current threats to growth include a slowdown in emerging markets, Fed tightening and gyrating commodity prices. An important difference between buying and building is that buying does not add to industry capacity whereas building does. The more uncertain the macro outlook, the more we expect companies to favour buying over building.

Real estate

M&A was a very strong theme in the German real estate sector in 2015 and we see the rationale and scope for further consolidation in 2016.

Vonovia is one of our high conviction Buys that should benefit. It is a natural consolidator in a highly dynamic but still fragmented German residential market. Several sizeable portfolio acquisitions have been integrated quickly, and in line with guidance. These will deliver synergies in 2016-17 and provide VNA with strong FCF growth and a potential 13% discount to our 2017e NAV per share while peers trade at a substantial premium.

Telecoms

Consolidation remains a live theme for the telecoms sector. Two major in-market mobile consolidation deals are on the table for 2016: one in Italy (where it is proposed that Wind combines with Hutchison's 3Italia) and the other one in the UK (where Hutchison's 3UK intends to purchase O2). The decision to abandon the proposed merger in Denmark between TeliaSonera's and Telenor's Danish unit dealt a blow to investors' hopes that consolidation might improve conditions in the European telecoms market. However, we think that the Danish case was different in various important respects to previous mergers seen in countries including Germany and Austria, and we continue to believe that the European Commission will evaluate each merger proposal on its individual merits, rather than adopting a predetermined approach of forbidding mergers that reduce the number of operators to three.

Deutsche Telekom (an HSBC Europe Super Ten portfolio constituent) looks well positioned to benefit from improved regulation and consolidation in Europe, with Germany being a front-runner in several respects. The approval of mobile consolidation should lead to a more rational environment in the medium term and this should help DT's domestic EBITDA to grow again from 2016.

BT is another of our high conviction Buys that should benefit from consolidation. The UK's Competition and Markets Authority's provisional clearance of BT's proposed acquisition of mobile operator EE brings together the UK's largest fixed-line operator with its largest mobile operator, which should in turn generate substantial synergy benefits. We would also argue that BT (following the acquisition of EE) could benefit from the more rational conditions that would emerge if the proposed acquisition of O2 UK by 3 Group can secure approval on reasonable terms.

Our high conviction Buy case for Telecom Italia is based largely on it being the key passive beneficiary of Italian in-market consolidation between 3Italia and Wind – provided that this can secure approval. We believe that in-market consolidation would provide a 'win-win' outcome, in which a return to modest revenue growth (at the aggregate market level) would enable greater investment of the type that Italy needs. We would also expect consolidation to drive lower unit prices, thereby enabling more innovation and productivity growth.

Autos

We expect M&A activity to accelerate in autos with PSA and Renault in focus. We have already seen reports in the press mentioning that Fiat would explore a merger with PSA or GM (see Reuters report on 29 May 2015) and that Nissan could increase its stake in Renault (see Reuters report on 28 October 2015).

Renault is one of our high conviction Buys in autos and we see the possibility of the structure of the alliance with Nissan changing in 2016. If this happens we believe it would lead to a substantial reduction of the holding discount.

Chemicals

We believe that the sector will generate approximately USD50bn of free cash flow over the next three years, as we believe the capital expenditure cycles of most companies have peaked. There clearly remains a question over what companies will do, obviously highly leverage companies will continue to deleverage, but there are a significant number which are under capitalised. Therefore we expect to see continued M&A or management returning cash to shareholders.

One of the strongest free cash flow generators in the sector is BASF. Our forecasts the FCF yields are currently close to 10% over the next three years and it is one of our highest conviction Buy ideas in the sector. Whilst management has been very clear that there is no deal of more than EUR3bn that currently meets its financial criteria, if M&A multiples come back (say in response to rising US rates) then BASF will have cash reserves to buy quality assets.

Sectors

Automobiles

- Key themes: volume recovery in EM, and M&A activity to accelerate
- High conviction Buys are Renault and Michelin. Least preferred names are BMW and Nokian Renkaat

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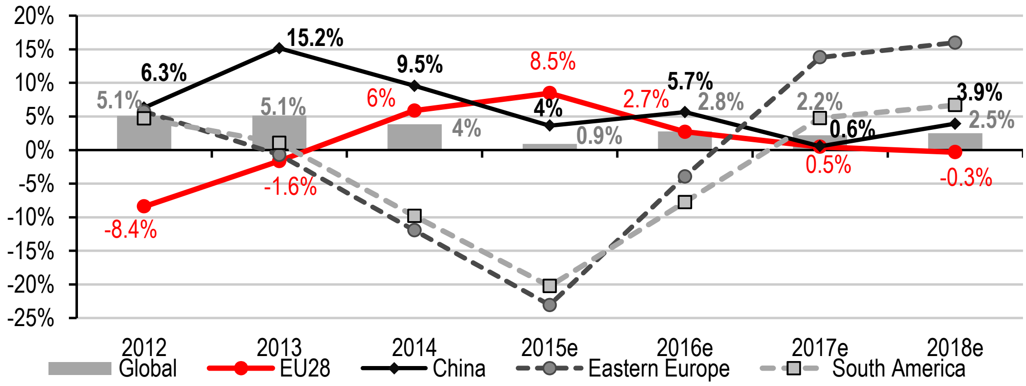
2016 investment themes

2016e global and EU light vehicle sales: around 2.7% growth in EU, with recovery in emerging markets. The global sales pattern in 2015 has been even more polarised than in 2014, with light vehicle sales (LVS) up in developed markets (2015e: +4.5% y-o-y) and down in emerging markets (2015e:-2.0%). However, this weakness in EM 2015 can become the basis for growth in 2016. While we expect EU28 countries to grow their light vehicle sales (LVS) by about 2.7% y-o-y overall in 2016, we believe the declines in Russia and South America will diminish and growth in China will pick up (2016e: +5.7% y-o-y as a result of a temporary reduction in vehicle purchase tax). This should be positive for EU car makers which generate c60-80% of their car sales in EU and China. In addition, model cycles will matter again and that's why we also prefer, amongst others, Renault (due to the launch of the new Megane, Kadjar, Talisman and Scenic) and why we like BMW less (lower sales of 3-, 5- and X3 series).

M&A activity might pick up: PSA and Renault are in focus. We expect M&A activity to increase in the auto sector in 2016. There have already been reports in the press that Fiat would explore a merger with PSA or GM (see Reuters, 29 May 2015). Furthermore, Reuters reported on 28 October that Nissan could increase its stake in Renault, and even on 6 November that both companies could merge. (For a more detailed analysis of this theme see HSBC's Global Consumer & Retail report *What's next in terms of M&A in Global Consumer & Retail post ABI-SAB?*, 22 October 2015.)

Currency developments are still important. We expect German car makers to have a more positive effect from currencies in 2016, because hedging activities limited the impact from a strong USD and weak EUR in 2015.

Resilient sales in Europe and recovery in Emerging Markets expected for 2016e



Source: HSBC estimates, IHS Automotive

Highest conviction Buys

Renault, Buy, TP EUR100
We think there is little likelihood of surprises to consensus EBIT for 2015e (due to the transition to Euro 6 compliant engines and FX losses in H2 15e among other things). However, we are (still) c30% ahead of Factset consensus for 2016e and even 40% ahead for 2017e. We expect total unit sales to increase by 11% y-o-y in 2016 due to model launches such as the Megane and Scenic, which we think will have much higher profitability than their predecessors. There is also a possibility that the structure of the alliance with Nissan might change in 2016 (Reuters, 13 November 2015), which we think would lead to a substantial reduction of the holding discount.

Michelin, Buy, TP EUR105
Q3 results showed that pricing, which was the main issue in H1 2015, is improving sequentially. Volumes and pricing should continue to improve (due to materialisation of price increases). Management is upbeat about margin development in the most important PLT (Passenger Car and Light Truck tyres) division, targeting 12.5% margin for H2 2015e (+110bps vs H1 2015) – which would be the highest margin ever posted in the segment – and targets mid-term performance well above the former 10-12% target range. Overall, our mid-term positive view on Michelin rests on three pillars: (1) its defensive nature with 75% exposure to replacement tyres while simultaneously benefiting from premiumization; (2) its significant margin improvement potential from a low base with self-help to fix its sub-peer cost structure with small plants, high-cost locations and low capacity utilisation and thus narrowing the profitability gap to industry peers; and (3) its cheap valuation relative to peers (34% discount to average of Continental and Nokian on 2016e PE) even though the 2015-17 consensus EPS CAGR is in line with its peers.

Least preferred names

BMW, Hold, TP EUR92
We expect subdued volume growth in 2016, with expanding volumes in the X1 and 7-series offset by volume declines in the 3-, 5- and X3 series, as they reach the end of their lifecycle. In our view, volume growth should remain subdued until 2018e and a real acceleration will only happen as of 2019e. With little top-line growth, the continuing increase in "other cost changes" and negative pricing, it will be difficult to increase the EBIT margin. FX effects will support earnings in 2016-17e, which helps to keep EBIT margins stable, but as of 2018e, the EBIT margin should start to fade. This is the case for other peers too, but the problem for BMW is momentum as its sales and earnings growth in 2016e will be weaker than peers.

Nokian Renkaat, Hold, TP EUR30
While Nokian's PC tyre margin has remained relatively robust at around 30% we do not see much scope for improvement in 2016e while volume and currency risks from Russia persist. Our 2016-17e EBIT is 2-8% below Factset consensus. Notwithstanding these risks, Nokian's share price has recovered very strongly since end-August, outperforming the sector by c35%. It now trades at a 2016e PE of 19.4x (34% premium to its historical 10-year average, and a 40% and 80% premium to Continental and Michelin, respectively). Nokian's exposure to Russia is now only 17% while North America and Europe account for 37%, and it remains a quality niche player (virtually 100% replacement tyres, cheapest production base, strong regional brand/positioning and distribution network, high spare capacity/low capex needs). Valuation appears stretched, however, seeing that Nokian's value proposition is not easily scalable in our view. Local competition in Russia, a new plant in a higher cost location (eg North America), entering the OE tyre segment and fewer benefits of brand and distribution in international markets represent a risk of dilution of its strong and proven business model in our view.

Banks

- We anticipate a continuing, gradual recovery in loan demand, but tougher regulations and margin compression limit the sector's upside
- Our highest conviction Buys are Barclays, CASA, Caixabank and Erste. Our least preferred name is Handelsbanken

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2016 investment themes

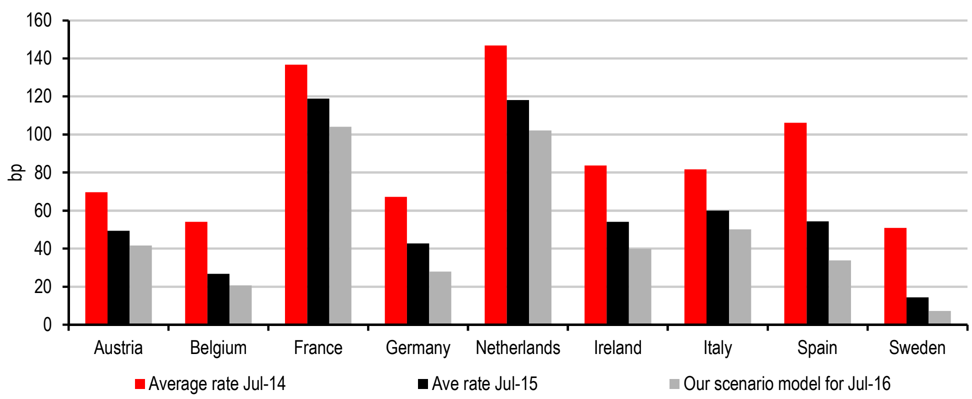
Loan demand should continue its gentle recovery. The good news for the sector is that debt overhangs are slowly being dealt with, the cost of borrowing is lower and, absent a more severe Asian slowdown, demand is picking up. We forecast 3.2% loan growth in 2016 for our European coverage universe compared with an estimated 2.2% in 2015.

Interest margins may be the biggest driver in 2016e. With deposit rates approaching zero, the scope for further cuts in 2016e is limited (see chart). That will leave interest income vulnerable to the twin effects of lower yields on securities portfolios and tighter lending competition. And while we'd hope to see some pricing discipline, historically that's not been a major strength of the banking sector. Hence, there's a very real danger that any pick-up in credit demand is offset, or more than offset, by margin compression.

Regulations redux. The good news is that we see growing signs of 'political' pushback on the ever expanding list of regulator-driven proposals. The bad news is that some degree of change is inevitable which, in the banking sector, only means one thing: more capital to run the same business. 2016e should see updates in a number of areas: credit, market and operational risk-weightings, the ECB's Pillar 2 add-ons and, towards year-end, the next EBA stress test.

Valuations undemanding, but upside is limited. Our European coverage universe trades on an undemanding 1.1x 2016e P/TNAV for a 9.8% ROTE. However, with ROTE under pressure from regulation, low rates and potential margin declines, sector upside may be capped.

Average household deposit rates: approaching floor levels over the next 12 months



Source: ECB data, HSBC Research estimates

Highest conviction Buys

Barclays, Buy, TP GBP3.15 and an HSBC Europe Super Ten portfolio constituent
We believe Barclays represents a simple, late-cycle, restructuring story. Costs are falling in absolute terms as both investment and retail banking operations are streamlined. Non-core asset disposals are running ahead of management's original targets, reducing the drag on group returns. The stock is trading on a 2017e PE multiple of 6.7x, P/TNAV of 0.72x with an ROTE of 12% (adjusted to a normalised CT1 of 12%).

Credit Agricole SA, Buy, TP EUR14.7
CASA trades at a discount to European peers (2017e PE of 7.5x, P/TNAV of 0.77x) despite being geared to a recovery in both European retail volumes and asset gathering (which should benefit from continuing low interest rates) which should allow it, over time, to earn a superior ROTE to French peers. One reason for the discounted valuation is investor concern over the removal of the 'Danish Compromise', but we anticipate the November consultation paper from the ECB will allay those fears.

Caixabank, Buy, TP EUR4.25
Caixabank is our preferred play among Spanish banks. As the biggest 'mass-market' bank in Spain, we think Caixabank will continue to benefit from industry consolidation and win market share against a backdrop of improving loan demand. Near-term catalysts include simplification of the structure and equity holdings which should both contribute towards reducing the valuation gap to peers as well as putting a floor under consensus top-line expectations.

Erste, Buy, TP EUR33 and an HSBC Europe Super Ten portfolio constituent
Erste remains our preferred play on a German and CEE economic recovery. The loan growth in the latter should help to produce both good net interest income and overall revenue growth. Erste is already earning a return above our estimate of its cost of equity (9.2%) and management guides for 10% in 2015e. The profitability should improve further as management is guiding for 2016 ROTE of 10-11% driven by strong focus on cost reductions; in part driven by the streamlining of software systems and digitalisation of the bank.

While we believe there are some concerns about the possibility of a major acquisition, during the Q3 conference call on 6 November management reiterated that it is not interested in buying another Austrian or a Polish bank. Hence we expect smaller deals to be done in markets where Erste is already operating to strengthen its market position (for example its recent deal with Citi in Hungary). Last but not least, the management intends to pay a DPS for 2015e as the group's capital ratios, with an expected fully loaded CT1 ratio of 11.2% at end 2015e, look entirely comfortable as does the leverage ratio at 5.3%.

Least preferred name

Svenska Handelsbanken, Reduce, TP SEK98
Revenue headwinds and cost growth continue to put pressure on Handelsbanken's profitability, while traditionally strong asset quality provides little room for positive upside surprises. With continuing uncertainty around the regulatory treatment of RWAs, we think returns might be under pressure, leaving the premium valuation vulnerable.

Building Materials & Construction

- Structural weakness in EM and patchy European recovery means we are selective within Building Materials
- Prefer contractors subsector: high conviction Buys ACS, Eiffage and NCC; least preferred stocks LafargeHolcim and Wienerberger

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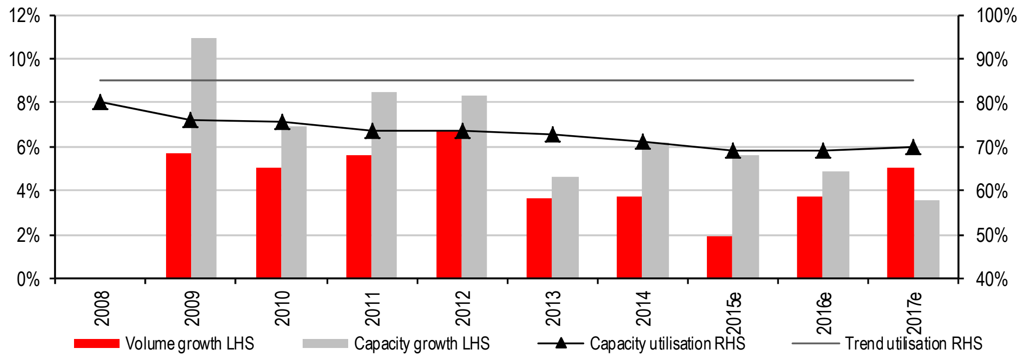
2016 investment themes

Weak EM and patchy Europe to check ROIC progression: We expect the pressure on EM volumes that started in H2 2013 to continue in 2016 with just 2.5% aggregate growth leading to a continuation of record-low cement capacity utilisation at around 70%, well below the 85% level required for equilibrium pricing power. Although the US recovery should remain robust, we expect Europe to continue to be patchy, keeping heavy-side material companies' ROICs below their costs of capital in 2016e. Heavily EM exposed LafargeHolcim is our key Reduce call.

Prefer light-side companies: These are generally better placed to improve returns due to greater exposure to developed markets and regulatory support for energy efficiency products that should benefit some of these businesses.

Contractors: Project execution and strategy implementation in focus with decent demand in 2016. We expect demand to be slightly more positive than during 2015, in particular as the important French market likely starts recovering during 2016 (see *Eiffage, Spie & Vinci: Back to growth*, 5 November 2015). Execution remains more important than volumes and with many of our covered contractors performing below their end-market margin potential, there remains plenty of earnings growth to be achieved from better execution. During 2016 this could be particularly true for Eiffage, Hochtief, Skanska, NCC and Strabag. 2016 should also see Skanska and NCC begin their new 5-year strategies. Finally, the contractors sector continues to shine with a high dividend yield, with an average 3.8% for 2015 to be paid out in 2016

Emerging market (ex-China) volume growth to remain below capacity growth until 2016e



Source: HSBC estimates

Highest conviction buys

ACS, Buy, TP EUR35
Going into 2016, ACS is at least two-thirds through its planned transformation into a more streamlined global infrastructure leader – a fact that is still underappreciated by investors, in our view. For 2015 ACS and its listed subsidiaries Hochtief/CIMIC will show a material improvement in cash flows and margins. ACS's own core business should return to moderate growth in 2016. The company's steady refinancing efforts will continue to see interest cost declining. While our 2016 net profit estimate of EUR767m stands below management's significant net profit target of EUR1bn, a continued reduction in minorities could help ACS achieve this target. The valuation screens well (PE 2016e 12.8x, or 8.0x at EUR1bn target) and dividends remain attractive (2015-17e 4.2-5.1%).

Eiffage, Buy, TP EUR64
After four years of recession (2012-15), construction output in France should recover in 2016. Contractors such as Vinci (DG FP, EUR60) and Eiffage are well placed to win large infrastructure contracts that should be tendered in the coming years, in France and also in the UK. The growing needs for energy savings, the development of zero energy building and the emergence of smart cities will add complexity to construction and building and will generate additional demand. On top of that, the nearly automatic reduction in its cost of debt will generate 15% EPS growth per annum over the next three years.

NCC, Buy, TP SEK320
NCC is set to update its strategy for 2016-20 which will focus on the growth opportunities in the Nordics and margin improvement. Moreover, to highlight the value of the group's Housing Development business management is considering a spin-off of these activities to the shareholders, which we believe could help the company see a re-rating.

Least preferred names

LafargeHolcim, Reduce, TP CHF42
The 21% share price fall since the beginning of the year reflects the weak trading environment in EM to which LafargeHolcim has 59% sales exposure. We believe it is too early to assume a rebound in the share price as we expect most EM divisions to report underlying gross margin erosion and because there is heavy exposure within Europe to markets that are declining. We expect these factors to lead to a sub-par ROIC performance in 2016e of 4.5% (from 3.7% in 2015e) against WACC of 7.3%.

Wienerberger, Reduce, TP EUR13.5
In 2015 Wienerberger's profits have benefitted from a strong pricing development in the UK, a revival of international project activities for its pipes products, and the sale of non-core real estate. Considering that these benefits could come to an end in 2016, profitability growth will slow significantly leaving the valuation at unattractive levels, particularly in light of slow underlying development in its core clay bricks and tiles activities in Europe.

Business Services

- The key theme is the stage of the cycle; a US industrials slowdown does not always mean recession, and labour demand is strong
- Our highest conviction Buys are Experian and Adecco. Our least preferred name is Aggreko

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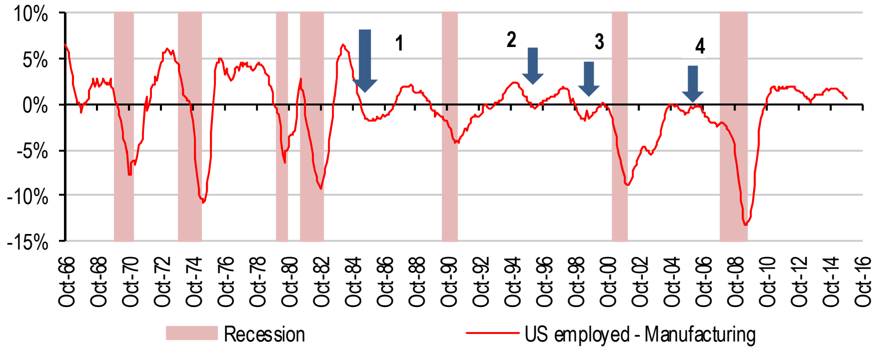
2016 investment themes

Where are we in the cycle? We, like many analysts are trying to understand where we are in the cycle; this will indicate which parts of the sector should perform best, and much else. The cycle is already the key theme for business services stocks, and will continue to be so in 2016. The market is nervous of slowing US manufacturing, and getting concerned that it might be a precursor of recession. In this sense, the staffers and other cyclicals are depressed. If recession comes they will be still more depressed in share-price terms; if recession is averted, they are cheap.

Our read of the data: A manufacturing slowdown sometimes gives false signals. Manufacturing sector growth slowed between March 1984 and August 1986 giving a false signal of recession for nearly two years. It slowed from March 1995 to June 1996, which again was a false signal. The next decline started in 1997, which was three years before the 2001 recession. And the decline that started in mid-2005 was not followed by recession until 2.5 years later. Those who follow the temp numbers, and they tend to lead GDP forecasts, are reassured that even in the US they have not turned negative, as they did as early as January 2006.

Labour demand is strong: Gross hiring, job vacancies and temps numbers are rebounding strongly, after the annual summer lull. In the US, barring manufacturing, the rest of the economy looks robust. European markets posted strong vacancies/temps growth. Growth was led by high-wage, white collar sectors. It also fits with a hypothesis that the service sector is becoming the growth engine, as it has at the mid-cycle stage before.

US industrial slowdown doesn't always matter that much



Source: Thomson Reuters DataStream, HSBC calculations

Highest conviction Buys

Experian, Buy, 1,290p
In the near term, improvement in the US Consumer division's growth and resilient performance in LatAm will continue to outperform market expectations. US velocity of credit seems to be improving. That should bode well for growth in the higher-margin Credit Services and Decision analytics divisions.

In the medium term, penetration in India and Austria (both positive credit bureau markets) should drive growth and help EMEA/ROW division to turn a profit. Current management seem to have heightened focus on driving growth whilst maintaining Capital discipline. Experian is likely to optimise its geographic footprint to focus on operations that meet this criteria. A stream of disposals and focussing the business could reduce drag on returns and margins.

Adecco, Buy, CHF90.0
Adecco is trading at a 2016e PE multiple of 13x on consensus estimates, having dropped sharply after guidance was cut by new management. If management guidance (4% growth and 5.2% margin for 2016e) is correct, the current share price is possibly broadly correct, although we note the stock trades on a 20% discount to the market despite still seeing 5%- 6% EPS growth on consensus estimates, offering a 3.3% dividend yield.

However, we believe growth can accelerate. After the seasonal lull in summer, labour market data indicated accelerating growth in Europe, including, importantly for profit growth, France. In the US, the labour market is growing well, barring industrials (c13% of the employees). Should the sales mix shift towards white collar, even at a lower growth rate, we may see more gross margin improvement. This backdrop is encouraging, and Adecco will need to capture this market growth. With changing demographics and declining churn, staffers who can find suitable candidates and have better selling-in skills will do materially better, and Adecco appears to be losing business to smaller players. If this reverses, as appears to be happening at Randstad, there is upside.

Least preferred name

Aggreko, Reduce, 800p
We see seven reasons to avoid Aggreko shares. First, the demand outlook from emerging markets (EM) and resource driven economies is weak. Second, several emerging economies have been adding permanent capacity over the past five years. This suggests that there a degree of capacity saturation relative to demand, in our opinion. Third, weaker local currencies limit the affordability of dollar-denominated temporary power contracts for government-owned EM utilities companies. They are unlikely to take the pain when manufacturing growth is weak and investments in permanent capacity are closer to fruition. Fourth, a falling oil price may increase a customer's focus on the rental component of a temporary power contract, especially a diesel contract. Fifth, the off-hire rate of 30% and contract renewals may continue to reset pricing to the economic reality of the operating environment. Our calculations suggest that these contracts generate significantly higher margins. Investors need to watch trends in the receivables, which are longer (c150 days) for EM utilities contracts, closely around contract renegotiations. Sixth, supply chain indicators from the labour markets and OEM remain unexciting and do not suggest a near-term pick-up. Seventh, we disagree with the wider market view that Aggreko's returns may have troughed.

Capital Goods

- 2016 set to be another year when bottom up (margin expansion) is a more important earnings driver than top down (revenue growth)
- Highest conviction Buys: Schneider Electric, Atlas Copco and Volvo. Least preferred names Philips, Kone and Schindler

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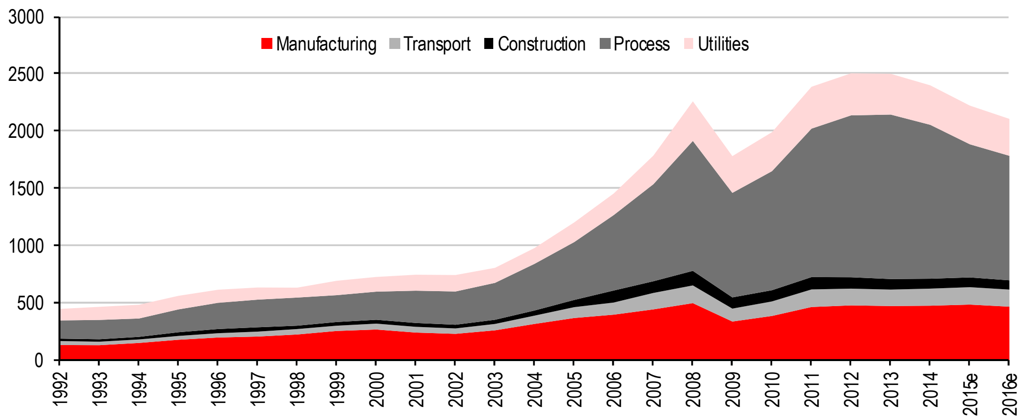
2016 investment themes

For the first nine months of 2015, our European capital goods coverage saw no like-for-like top-line growth but nonetheless managed to generate like-for-like margin expansion of 50bps, EPS (ex-items) growth of 16% and operating cash-flow growth of 34%. We think 2016 will offer more of the same. As we demonstrated in our October 2015 sector report *Show Me The Money*, estimates of global investment spending have been revised down steadily over the past six months, with analysts now looking for global capex to fall 7% in USD terms in 2015e and a further 5% in 2016e.

For listed European capital equipment suppliers, however, the market contraction will be mitigated: (1) by the fact that most are underweight the blackspots (eg oil & gas is typically only 10-15% of revenues, whilst it is over 30% of global capex); and (2) by their large, profitable and mostly still growing service businesses (typically 20-40% of revenues), which give them exposure to customers' opex not capex. Despite the weak top-line growth environment, we believe they will continue to generate double-digit earnings and cash flow growth. We see five key earnings drivers for the sector in 2016:

- **The enabler: price stability.** Despite enduring three years of declining revenue growth (2013-15) pricing remains reasonably robust for the capital goods sector at down just 0.8% y-o-y in Q3 2015. The two main drivers of price stability are (1) the oligopolistic nature of most capital equipment markets; and (2) vendors' large and growing service businesses.

Global listed company capex (USDbn) by industry group, 1992-2016e



Source: Thomson Reuters Datastream consensus estimates

- **Cutting the fat after a decade of fine dining: good old-fashioned cost cutting.** 13 of the 23 capital goods vendors in our coverage group currently have live cost-cutting programmes, 11 of them continuing through 2016. We estimate these will yield USD2.5bn of EBIT growth in 2015 (80bps in margin terms) and a further USD3.9bn (50bps) in 2016. We look for the biggest cost cuts (relative revenues) at ABB, SKF and Smiths.
- **Fixing the mix: focusing towards the more profitable parts of the business portfolio.** The poster child for this approach in the capital goods sector is SKF, which used this technique to drive margins from a 1999 low of 4.9% to a 2011 high of 14.8%. Companies from Atlas Copco to Wärtsilä are currently using the same technique to drive margin expansion.
- **From fixed to variable – outsourcing.** A dollar of variable cost is clearly better, all else equal, than a dollar of fixed cost. New technologies and new business models are helping vendors, led by Atlas Copco and Kone, to outsource ever-further.
- **Too big to succeed – divestments**. Six of the 23 vendors in our coverage group are either actioning identified divestments or have made a public commitment to identifying such opportunities. The largest of these potential divestments are the proposed carve-out of Siemens' USD16bn medtech unit, the promise of a "portfolio review" at ABB's USD15bn Power Grid division, and the ongoing breakup and divestment of Philips' USD9bn lighting business.

Highest conviction Buys

Schneider Electric, Buy, TP EUR72
Our investment case rests on the fact that management has been shifting priorities to operational efficiency and towards cost rationalization. This change in focus should drive better margins as Schneider's pricing power allows for the retention of some of the productivity gains.

Atlas Copco, Buy, TP SEK280
Atlas Copco is one of our highest conviction Buys because: its strong 10-year average Cash-ROIC of 16.0%; its world no 1 compressor franchise (45% of 2015e revenues); and a better performance by some recent acquisitions (Henrob).

Volvo, Buy, TP SEK120
We rate Volvo Buy on back of: a cyclical recovery in the core European truck market in 2015-16e; the company's major cost savings programme, which will continue to boost the earnings recovery; and increased pressure to perform from major shareholders Industrivärden and Cevian.

Least preferred names

Philips, Reduce, TP EUR19
We believe Philips lacks a strong value proposition across its core portfolio of Healthcare, Lighting and Consumer Lifestyle. Earnings forecasts have been coming down for more than a year now. Healthcare demand is under pressure because of tight public finances and a change in the Chinese market, and in Lighting, Philips has to deal with the shift from traditional lamps to LED and a weak Chinese construction market.

Kone, Reduce, TP EUR30
Kone bears the largest China risk of any of the western players (exposure of 30% of FY2014 sales). Kone is guiding for a slight decline in the new installation market in China (in orders) in 2015.

Schindler, Reduce, TP CHF125
Schindler is less exposed to China than Kone, and the share price has therefore been driven more by management's commitment to margin improvement. Given the weak Chinese market, margin expansion may stall next year. Hence, we see more downside than upside.

Chemicals

- 2016 will be a challenging year for the sector as volume growth remains subdued, net pricing power remains illusive
- Our high conviction Buys are BASF and Johnson Matthey. Our least preferred names are Umicore and Lanxess

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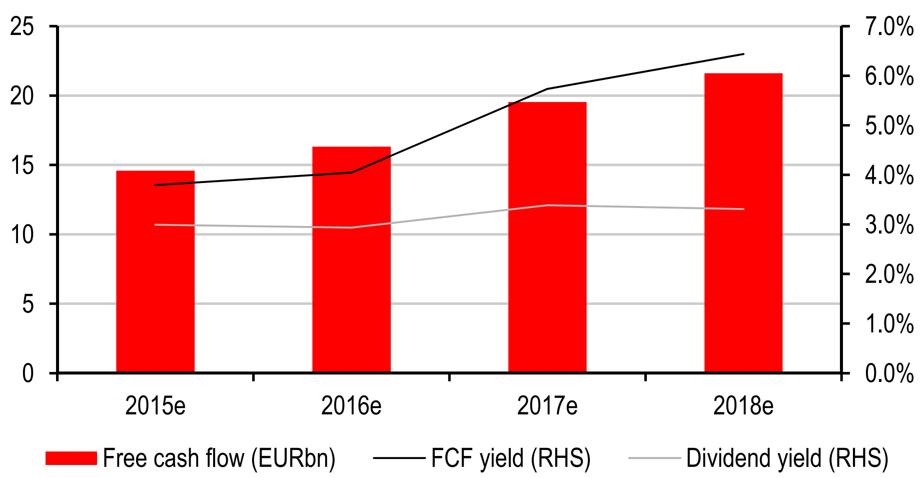
2016 investment themes

We believe that the drivers of top-line and profit growth in 2015 will start to wane, which means 2016 will be a challenging year for the European chemical sector. Despite this, we continue to see value, particularly in those companies that have strong cash generation or are cheap defensives.

Back to normal. Following a better-than-expected 2015, we believe that 2016 will be a more "normal" year for the sector, which translates into modest top-line growth of c3%, net pricing power (selling prices – input cost increases) will be negligible due to global oversupply. We therefore expect margin expansion to be minimal unless companies take action to reduce costs or transform their businesses. This outlook has not changed considerably since we outlined our views for the sector until the end of the decade in *Survival Guide – creating value in a lost decade* , in December 2014.

Slowing growth. While we expect volume growth for the sector to be c3% in 2016 we do see downside risk to this, given concerns about the slowdown in developing economies, such as China and Brazil, while the developed economies are showing few signs of significant recovery. However, we believe that the trend we have seen of robustness in consumer end markets should continue to into 2016, while the more industrial, energy and construction end markets will continue to be tough. We expect the auto end market to show some signs of recovery, particularly in the developing economies, while Europe and North America should continue to show positive auto volume growth.

European chemical sector will generate EUR30bn in FCF after dividends in 2015-18e



Source: HSBC estimates

Lack of margin expansion. With low volume growth and no pricing power we believe that margin expansion across the sector will be limited next year, particularly in a low inflation environment. We believe management could have to decide between boosting margins through cost cutting or M&A. Historically, when companies have lifted margins this has tended to lead to share price appreciation.

M&A. We believe that the sector will generate approximately USD50bn of free cash flow over the next three years, as we believe the capital expenditure cycles of most companies have peaked. There clearly remains a question over what companies will pursue M&A, obviously highly leveraged companies will continue to deleverage, but there are a significant number that are under capitalised. Therefore we expect to see continued M&A or management returning cash to shareholders.

Cash generation. We believe that one support for the sector in the medium term is cash generation, as the sector's capex cycle peaked in 2013. Looking at free cash flow yields and dividend yields, the companies with the largest net yields in 2017e are Lanxess, Arkema, Solvay and BASF, and those where cash generation is not strong include Givaudan, Air Liquide and Umicore.

Highest conviction Buys

BASF, Buy, TP EUR88
Our investment case for BASF is based on: (1) A diverse portfolio that brings sustainability of earnings. (2) Group margin recovery: we believe that margins have troughed and we should see a faster recovery than peers through the next five years driven by the benefits from the cost reduction programmes, the introduction of new high margin products and the operational leverage that BASF has given the integrated nature of its chemical assets. (3) Earnings growth faster than the sector; we believe BASF can grow EBIT faster in 2016 than the rest of the sector, 12.0% vs 9.4%. (4) Strong cash generation; we believe that BASF will be one of the strongest free cash flow generators in the sector, on our forecasts the FCF yields are currently close to 10% over the next three years.

Johnson Matthey, Buy, TP 3,500p
We see three main reasons to own Johnson Matthey's shares: (1) Earnings growth moving to c7-8% pa in the next five years, is coming primarily from the introduction of new and more stringent emission legislation in Europe and China and new products in Process Technology. (2) We forecast that Johnson Matthey will generate an average free cash flow of GBP395m pa over the next three years, which implies a free cash flow yield of approximately 6.0%; and (3) Earnings are resilient, we expect EPS growth of c10% pa in the next 5 years driven by new emission legislation.

Least preferred names

Umicore, Hold, TP EUR39
With the shares trading at 2016e EV/EBITDA of close to 9x, we believe this fully prices in the earnings growth coming from Recycling capacity expansion, growth in Catalysis and disposal of non-core assets. It does not, however, take full account of the risk from lower metal prices, particularly with gold, platinum and silver at their lowest levels for five years.

Lanxess, Hold, TP EUR45
The shares are trading at 2016e EV/EBITDA of c7x and PE of 18x, which is at a significant premium to its historical averages of the last ten years and broadly in line with the rest of the sector. While we see Lanxess as a restructuring story, in our opinion in the aftermath of the Aramco joint venture, and as the market turns its attention to the Performance Chemicals assets, we see little to get excited about at these valuation levels. We remain holders of the shares as we believe there is a possibility of further significant restructuring or portfolio transformation, which would be a positive.

HSBC

Food Retail

- Economies of scale and buying power will be major themes in 2016 while discounters and online are likely to add margin pressure
- Our highest conviction Buys are Metro, Booker and Dia. Our least preferred names are Colruyt and Sainsbury

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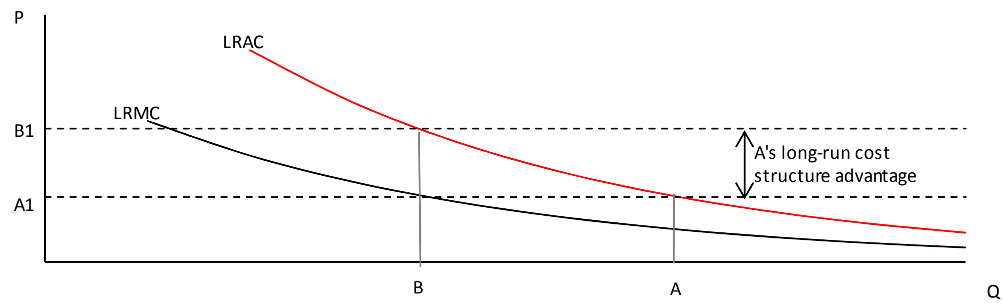
2016 investment themes

In 2015 we wrote extensively in *Retail Digest* and in other publications about the importance of economies of scale and buying power. These features are important because we view food retail as a natural monopoly, with continually falling marginal costs (see figure below), and as a low margin and highly operationally geared industry. In 2016 we believe the implications and consequences of these themes are likely to drive share prices performances: Companies that should benefit from scale and growth are: Ahold/Delhaize, Booker, Carrefour, Dia and Tesco.

Economies of scale: We believe scale economies are a major advantage in an industry with thin margins and where customers are price sensitive, mobile, and have little brand loyalty. Retailers will always play down economies of scale, as smaller retailers do not want to admit they are disadvantaged, and larger ones do not want to admit they are structurally advantaged. We believe there are many scale economies in retailing, with buying power a major one, along with cost spreading and logistic economies, but it is buying power that attracts most attention.

Buying Power: Buying power is a function of the structure of food retailing and manufacturing and for it to exist, there is a series of conditions that must be met. Amongst these conditions are high operational gearing, excess manufacturing capacity, and an oligopoly in food retailing. If these economic conditions are met then scale economies will be significant in our view. Carrefour, Metro and Tesco are the ones in our coverage with the most buying power in their domestic or most important markets, while Dia has grown significantly notably due to acquisitions. Looking ahead, growth companies are best positioned to benefit from scale.

Food retailing as a natural monopoly: continually falling long-run marginal costs



Source: HSBC

Highest conviction Buys

Metro, Buy, TP EUR36

In 2015, Metro's share price has been adversely impacted by the Kaufhof disposal and by its Russian exposure, even though the Kaufhof deal was positive for the group's financial structure and Russian performance has been resilient. In 2016, we expect investor focus to return to Metro's strengths in Consumer Electronics (CE). We believe Metro has a competitive advantage in CE over the pure online players thanks to its size. It is, #1 in Europe, has leadership positions in 9 countries, and offers choice, prices and convenience via click & collect options. With most of its re-investment in pricing now completed, we see Metro rebuilding its CE margins to around 3% within the next three years from 1.6% in FY2014 (ending September) and 2.0%e in FY2015.

Booker, Buy, TP 230p

Booker has world class management, relevant scale for its industry and a very clear strategic plan. It operates in the less glamorous world of cash and carry, but its strategy of being cash focussed has served it well. It is a growth company based on maintenance capex. It competes against many disadvantaged competitors in the UK and has long-term potential from its embryonic Indian venture.

Dia, Buy, TP EUR7.0

We believe the market underestimates the resilience of Dia's franchise driven model. Although we forecast a 120bp margin fall over 2015-16, due to newly acquired businesses and remodelling of Dia Maxi, we expect EBITDA margins to stabilise at 8.4% thereafter. We believe the market tends to underestimate: (1) the leverage impact when Dia returns to positive LFL (which we expect from 2016e); (2) economies of scale Dia has built while growing market share by 200bp; and (3) the potential to convert more stores to franchises. Between 2009 and 2015, and despite a LFL sales decline since 2013, the Iberian EBITDA margin grew 300bp to 9.56%, owing to the conversion of stores to franchises, bringing franchises to 51% of the network from 31%.

Least preferred names

Colruyt, Reduce, TP EUR37

The Belgian market (95% of Colruyt sales) is price sensitive and space growth opportunities are limited. Colruyt is prepared to match competitors' price investments, meaning its operating margin is likely to be under pressure for a while. Although Colruyt remains a top class retailer, we have concerns about the business model becoming more capital intensive, margins coming under pressure and the company possibly not seeing LFL growth despite its price investments. As well as facing tough competition in Belgium, Colruyt lacks new sources of growth, as it is opening only a few new stores per year (5 to 10). A slight premium could be justified given good execution and the highest margin in the sector but the operating margin is under pressure and Colruyt's growth profile is not as compelling as it was. A c30% premium to European peers' EV and PE multiples is therefore difficult to justify, particularly as Ahold may raise competitive intensity in Belgium and as there may be better opportunities elsewhere in the sector.

Sainsbury, Reduce, TP 200p

Sainsbury remains very vulnerable to either a recovery at Tesco and/or further deterioration in industry margins and continued deflation. Sales have held up a bit better than we expected, but two years of LFL declines in sales are leading to a c30% two-year fall in profits. Sainsbury also has a stretched balance sheet, with a rental bill that is greater than its operating profits, meaning it is highly operationally geared and therefore vulnerable to continued competitive deterioration. The company will come under increasing pressure throughout 2016.

General Retail

- Key areas of focus for 2016 will be recovery in Europe, continued channel shift to online and structural growth in selected categories
- Highest conviction Buys are H&M, M&S and GrandVision. Least preferred names are Inditex and Kingfisher

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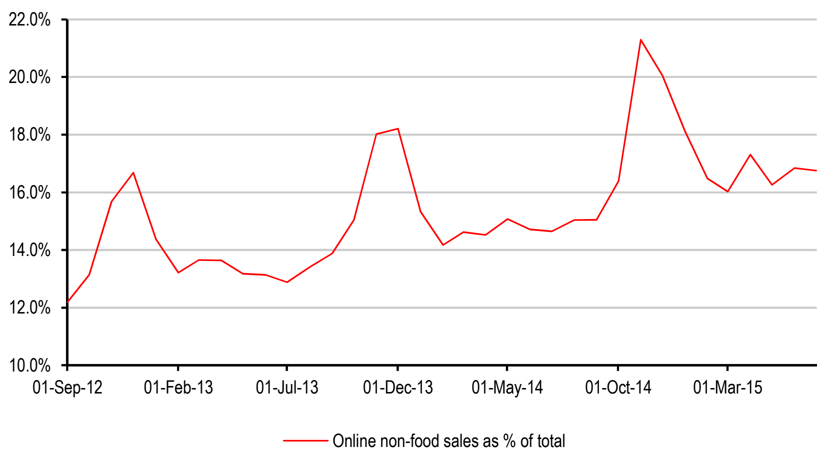
2016 investment themes

European recovery: European consumer spending has been an area of increasing strength driven by disposable income growth and improving confidence. As highlighted in HSBC European Economics research (see '*Unfinished business, Q3 2015'*), a combination of lower oil prices, QE, a weak Euro and policy reform is driving economic recovery. The recovery in consumer confidence seen in 2015 should be a precursor to sustainable recovery in consumer spending. H&M, where c40% of sales is in European markets, is a key play on this trend.

The shift online. Online penetration varies significantly by category with electronics, toys and clothing at or above 20% while food and pet care have taken longer owing to more challenging economics. However, across all categories online is gaining share as customers demand it and technology enables it. A relevant platform offering a seamless shopping experience and competitive fulfilment options is now a prerequisite to access structurally faster growth in online.

Structural growth in optical retail and premiumisation in pet care. The sector also offers some structural growth opportunities in selected categories. Optical retail is one such category and offers defensive structural growth given aging developed market populations and chronic under-penetration of eye care in emerging markets. GrandVision is the global leader in optical retail and offers attractive long-term growth prospects on this theme. In addition, pets are increasingly being treated like members of the family supporting penetration of specialist and premium products and services.

Online non-food sales as % of the total



Source: ONS

Highest conviction Buys

H&M, Buy, TP SEK375
H&M is a high margin, global growth story with multi-year expansion potential. We expect the larger European markets to which H&M is exposed by revenue (Germany 20%, UK 7%, France 7%, Sweden 5% and Spain 4%) to benefit from rising GDP growth, declining unemployment and rising consumption in 2015 and 2016. In the longer term H&M's potential to more than treble its global store count and the development of multi-channel/multi-brand capabilities support a compelling growth opportunity.

Marks & Spencer, Buy, TP 700p and an HSBC Europe Super Ten portfolio constituent
Marks & Spencer offers a specific and attractive self-help opportunity. It has already demonstrated considerable progress on this front, as indicated by consistent gross margin expansion. Yet it has been given little credit for this progress to date. We identify up to c500bps of gross margin potential via increased free on board (FOB), an increase in direct design and reduced markdowns.

GrandVision, Buy, TP EUR28
GrandVision is the global leader in eyecare retail. This sector benefits from powerful structural growth drivers in the form of an aging population in developed markets (with eyesight deteriorating from the age of 40, and sophistication of treatments getting more complex with age) and considerable underpenetration of eyecare solutions in developing markets (over 50% of people who need an eyecare solution don't have access to it). Fragmented markets offer GrandVision attractive consolidation opportunities it is well placed to capitalise on, given leading positions and a lengthy track record in successfully identifying, buying and integrating acquisitions.

Least preferred

We have no negative ratings, and our caution on these names reflects either valuation or less favourable category exposure.

Inditex, Hold, TP EUR29
Inditex is one of the best positioned companies for capitalising on growth in the global apparel market, in our view. This is achieved via the rollout of a multi-brand, multi-channel model in new and existing markets (88 in FY2015), and in which the group has limited share (typically <1% albeit with a small number of exceptions). However, we struggle to justify current share price levels given valuation metrics at extreme levels and hence have a preference for the likes of H&M which offers similar exposure at a more reasonable valuation.

Kingfisher, Hold, TP 355p
The strategy update from new CEO Veronique Laury at the FY2015 results indicated a willingness to tackle key investor concerns head-on. However, these initiatives will take time to implement before any benefit can be extracted. Also they do little to address some of our long-term structural concerns over the UK market (increasing competition and shifting away from DIY in favour of trade-based services).

Health Care Equipment & Services

- Fading FX tailwinds, a tougher US reimbursement environment and continuing weak emerging market growth key challenges for 2016
- Our highest conviction Buys are Straumann, Sartorius and Amplifon. Our least preferred name is Getinge

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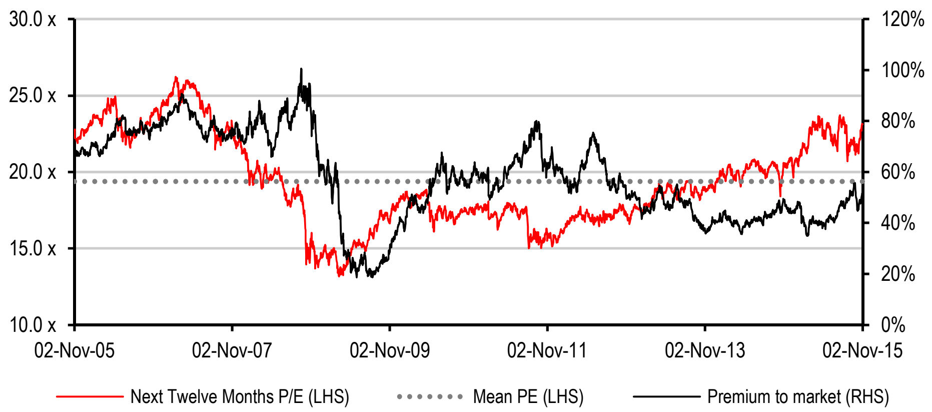
2016 investment themes

Challenging environment set to continue in 2016: In 2014, the sector faced a significant decline in emerging market demand (particularly from China and Russia), and expectations of a recovery in 2015 have not proven correct. Looking in 2016, we believe there is no reason to get overly constructive on an emerging market recovery, given economies continuing to struggle (Russia and Brasil), political instability (Middle East) and further restrained order behaviours (China). In addition, the considerable FX tailwind experienced throughout 2015 (mainly from a stronger USD) should peter out in the next couple of months. Hence, and together with recently received negative data points in connection with the US reimbursement environment, we spot several challenges for the sector's earnings growth potential in 2016.

Sector re-rating finally coming to an end, selectivity now key: The sector's four-year rally and rerating process finally stopped in Q2 2015 with a forward PE range of 22-23x over the last months. However, trading at a 12-month forward PE of 23.1x, the sector is still at a premium of 20% compared to the average of the last 10 years. Hence, and with the above described growth challenges, we do not expect further multiple expansions in the short term. This said, decent and visible earnings growth should be the main source of upside throughout 2016, and selective stock investments should be key, in our view.

Sector* valuation: 12-month forward PE (last 10 years)



*STOXX Europe Health Care Equipment & Services Index
Source: Factset

Highest conviction Buys

Straumann, Buy, TP CHF315
Straumann is the leading dental implant manufacturer in the CHF3bn dental implant market with a share of c24% in 2015. We see Straumann in a good position to deliver 6-9% revenue growth over the next years, due to a number of product launches in the fields of implants, regenerative and CAD/CAM solutions, as well as further regional expansion in yet untapped markets in APAC. In addition, recently announced collaborations with large dental equipment suppliers (Patterson and Sirona) should strengthen Straumann's position as market leader. We believe Straumann offers substantial operating leverage going forward, along with strong top-line growth, leading to our estimated 13% EPS CAGR from 2014 to 2017.

Sartorius, Buy, TP EUR225
Sartorius is a leading supplier of production equipment for the biopharmaceutical and laboratory industry. With its Bioprocess Solutions division (69% of sales), the company holds dominant market positions in fluid management as well as fermentation (c40-50% market share) and a No.3 position in filtration (c25% market share). We believe Sartorius will be one of the main beneficiaries of the increasing trend towards biopharmaceutical drug approvals and the biosimilar market which is finally developing. In addition, we believe consensus still underestimates the operating leverage potential of the company, which has c50% of COGS fixed (our 2017e EPS is 12 % ahead of the Street).

Amplifon, Buy, TP EUR8.10
Amplifon is the leading hearing aid retailer in the global cEUR15bn hearing aid market, with a 9% market share, benefitting from a sustained 4-5% market growth per year. As the retail share of the market is highly fragmented, with about 50% of the market still in the hands of small independent retailers and buying groups, we see Amplifon in a unique position to gain scale by active consolidation and given its ability to build a global brand. We believe that increasing scale and continuous re-negotiations of agreements with suppliers should drive margin expansion for Amplifon. Along with top-line growth sustained at 6-7% (organic growth + M&A); we estimate an attractive 19% EPS CAGR from 2014 to 2017.

Least preferred names

Getinge, Reduce, TP SEK192
Getinge is a Sweden based global medtech company with strong market positions throughout most of its product offering (eg operating room equipment, cardiovascular surgery, patient handling and disinfection/sterilisation equipment). However, following an aggressive rate of M&A, margins have suffered considerably in the last four years. As a response, management recently initiated a comprehensive efficiency programme, which implies a return to peak margin levels in 2019. Given that the market environment has deteriorated (eg stricter reimbursement, increasing pricing pressure), we believe this is an ambitious target. This and an anticipated rise in R&D costs, puts our 2016-17 EPS forecasts 6-10% below the Street. In addition, considerable challenges with the FDA (consent decree signed in February 2015) constitute a further source of uncertainty, in our view.

Home & Personal Care and Food Producers

- We expect global category growth rates to remain muted, with EM improving slowly, so a key theme is geographic expansion opportunities
- Our high conviction Buys are AB Foods, Greencore and Hilton Foods. Our least preferred name is Beiersdorf

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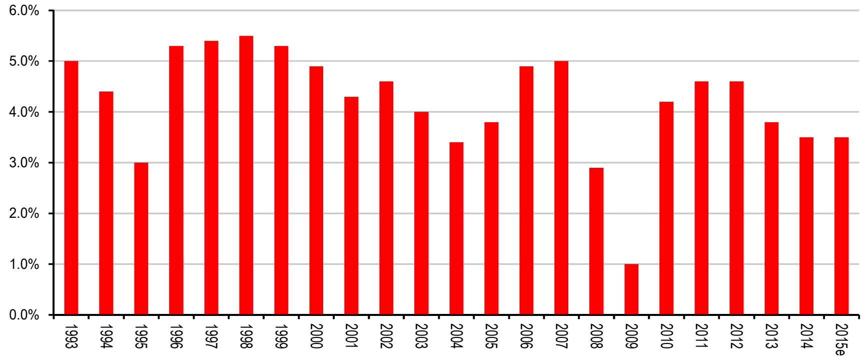
2016 investment themes

Category growth rates to remain below average. The chart below shows L'Oreal's estimated growth rates for its global categories from 1993 to 2015. The chart is specific to L'Oreal's categories, but we think holds true for Home & Personal Care (HPC) in general. What it shows is a stable picture of 3-5% growth, with growth in 2014 and 2015 towards the bottom of the range at 3.5%. We expect growth to be only slightly better in 2016, as the emerging market consumer environment only slowly improves.

Look for international growth stories to deliver stronger growth. Given relatively muted market growth rates, we favour companies that have an international expansion angle and we flag ABF (with Primark), Greencore (with the US) and Hilton Foods (with Australia).

Input costs benign, although currency volatility is offsetting some of the benefit. That said, we would expect trend of steadily improving margins in HPC companies to continue.

Global Cosmetics market growth 1993-2015e



Source: L'Oreal, Personal Care market excluding razors, blades, soaps and deodorants

Highest conviction Buys

Associated British Foods, Buy, TP 3,760p
Whilst EPS growth is likely to remain depressed in 2016e, due to both currency translation and transaction issues, the key attraction of the stock, namely the international expansion of Primark, remains undiminished in our view. It is early days in the US for Primark, but the initial shopper reception has been positive. We think Primark still has huge roll-out potential in Europe, and its new store openings are trading very strongly, whether they are in France, Spain, Germany or Benelux. We forecast sales space rising from 11.2m sq ft in 2015a to 32.1m sq ft in 2025 and to 50.9m sq ft by 2035, and this is a key driver of our target price.

Greencore, Buy, TP 360p
In the UK, we expect Greencore to continue to grow its market share in the fast-growing UK Food to Go market, aided in part by the store expansion plans of its key customers M&S (Buy, 700p TP) and the Co-Operative Group. In the US we expect the Food to Go strategies of its key customers, namely Starbucks (not covered) and 7Eleven (not covered), to drive volume growth, improving operating leverage and in turn increasing US profitability. The shares trade on 14.5x PE and 9.9x EV/EBITDA for calendar 2016e, representing what we believe is an undeserved discount to its peers on a PE basis.

Hilton Food Group, Buy, TP 545p
Hilton has grown organically with leading retailers across Europe and most recently Australia. We forecast 22% EPS growth in 2016e as it benefits from first full-year trading at its expanded facility in the UK and its new plant in Melbourne, Australia combined with a much lower level of start-up costs. It is trading on 15.5x PE and 7.2x EV/EBITDA for calendar 2016e, which in our view looks attractive. Our DCF-driven target price does not assume any further business wins, although, given Hilton's strong track record and substantial balance sheet capacity, we would be surprised if further opportunities did not arise in the next few years.

Least preferred name

Beiersdorf, Hold, TP EUR81.5
We think Beiersdorf has one of the best Personal Care brands in the world in Nivea, which should be capable of driving better organic growth for the group than it has over the past five years. We also believe it has the opportunity to significantly raise margins in its Consumer business and improve working capital management. That said, EPS growth c.8.0%-8.5% from 2016e to 2019e is not sufficient, in our view, to justify a PE of 28.3x for 2016e a 29% premium to its global HPC sector peers.

HSBC

Insurance

- Attractive capital returns, clarity around Solvency II capital positions and managing interest rate and macro exposures are key themes for 2016
- Our highest conviction Buys are Prudential and Generali. Our least preferred names are PZU and Euler Hermes

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2016 investment themes

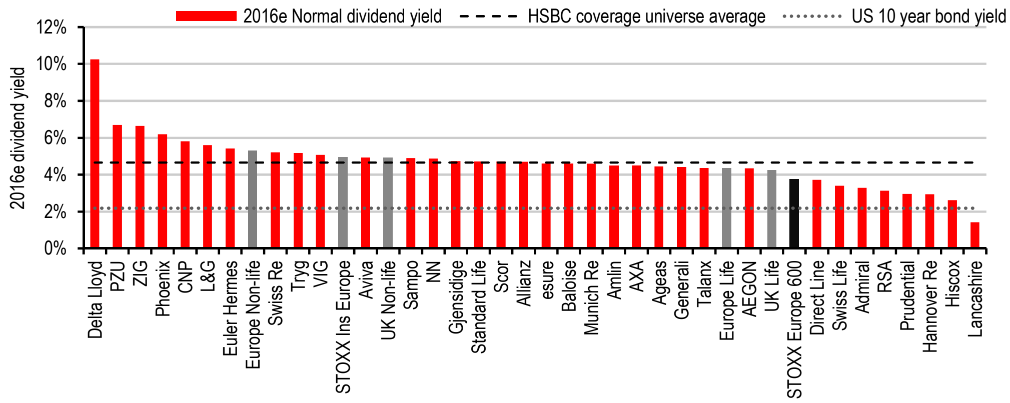
Attractive capital returns, backed by cash flow generation. The 2016e normal dividend yield for our coverage universe is 4.7%, relative to the Stoxx Europe 600 at 3.8% (chart below), while the total yield including buybacks and special dividends is 5.2%. The sector's yield is attractive given HSBC Fixed Income's view that 10-year UST yields will be 1.5% and German 10-year Bunds will be 0.2% by end-2016. The sector's dividend credentials are backed by a 2016e cash flow yield of 7.6%.

Clarity around Solvency II could be a positive catalyst, but there remain risks around comparability and capital levels. Capital positions around Solvency II will be disclosed over the coming quarters. However, there remain significant concerns around the comparability of Solvency II disclosures across the sector due to inconsistent assumptions and methodologies. There could also be volatility in share prices if the reported capital levels or ratios are not as strong as anticipated. On the other hand, disclosure around Solvency II models and capital positions could also involve more transparency around insurers' future capital management policies, which could be a positive catalyst.

Insurers continue to manage exposure to interest rates and macro volatility. Insurers have taken steps to reduce interest rate exposure by moving away from traditional products, reducing guarantees and crediting rates, reducing asset-liability duration mismatches, improving underwriting or diversifying their investments. Furthermore, reducing financial and asset leverage has helped reduce balance sheet volatility. However, the scope for further actions is now limited, in our view.

Top-line growth is limited but insurers have other options to improve profitability. While we expect premium growth in Europe to be subdued in 2016, insurers are targeting further cost saving programmes, increasing exposure to higher growth markets outside Europe and capitalising on positive trends for their respective asset management businesses to improve profitability. That said UK life and motor should experience above average growth over coming years, in our view.

European insurers offer attractive dividend yields



Note: Consensus IBES data used for FTSE and STOXX Europe indices. Individual company dividend yield based on HSBC forecasts for normal dividends only. Priced as at close on 02 November 2015. Source: IBES, Thomson Reuters Datastream, HSBC estimates

Highest conviction Buys

Prudential, Buy, TP 1,985p
Prudential is a core holding in the sector given its attractive strategic positioning in insurance and asset management in Asia, the US and the UK. Prudential offers above sector-average returns on equity and sector-leading growth on all metrics, while its current valuation does not fully reflect its above-average returns and growth, in our view. For example, the shares currently imply earnings growth of 2% relative to our forecast of 12% growth in operating earnings over 2014-17e. Furthermore, we think there will be no major change in strategy under the new CEO Mike Wells, but there could be more focus on operational efficiency than in the past. Prudential also offers positive dividend surprise potential, in our view, given dividend cover above 2.5x on a range of earning and cash metrics. Lastly, its financial targets also leave some room for positive surprises, in particular Asia's IFRS earnings and underlying free surplus generation. Prudential is a HSBC Europe Super Ten constituent.

Generali, Buy, TP EUR21.5
Generali offers above sector-average growth in cash flows, dividends and earnings over the next three years. We forecast 13% pa dividend growth with positive surprise potential, given dividend cover ratios above its European composite peers, strong cash-flow growth potential and increasing comfort around its economic solvency position. Concerns around the Group's Solvency position should continue to ease over time as management continues to optimise its internal model, which could result in further strengthening of its solvency surplus and a reduction in the economic sensitivities of its capital position. Generali's business strategy is focused on its core strengths and it aims to become a retail leader in European insurance. In terms of its sales mix, the group has actively shifted towards unit-linked and protection products, which is likely to translate into higher quality, fee-based earnings over time. Furthermore, Generali is targeting EUR1.0bn in gross cost savings over 2014-18e in order to retain a flat cost base, which would see it move into the top quartile for both life and non-life admin cost ratios among European insurers, based on our analysis.

Least preferred names

PZU, Reduce, TP PLN359
PZU is a well-capitalised insurer with an attractive 6.7% 2016e dividend yield and a strong brand in Poland. However, we are concerned about the ability of the group to grow its earnings. The shares currently imply around 1% earnings growth versus our forecasts for no growth in earnings or book value over 2014-17e. Furthermore, we remain concerned about a further rise in body injury claims in the Polish motor segment, given that current regulation is not as clear and specific as other European countries, while lower investment income remains a drag on earnings.

Euler Hermes, Reduce, TP EUR80
Euler Hermes is a global credit insurer and offers industry-leading underwriting performance. However, the deterioration of the economic environment, notably in some emerging markets has increased volatility in the group's combined ratio and reduced the earnings visibility on the stock in the short term. This earnings deterioration was serious enough in Q3 2015 for management to take voluntary underwriting actions to prevent a further deterioration of the profitability of the book in the coming quarters. These measures are likely to have a short-term negative earnings impact. Furthermore, we see greater risks from Solvency II capital models for credit insurers than for the rest of the industry due to differing assumptions in terms of capital intensity calibration. The stock offers a 5.4% 2016e dividend yield, which is above the sector average but we forecast no dividend growth for 2015.

Integrated Oils

- Oil prices look unsustainably low, but recovery will be gradual. Sharply improving free cash flow supports dividend sustainability
- Our highest conviction Buys are Royal Dutch Shell and Total. Our least preferred names are ENI and Repsol

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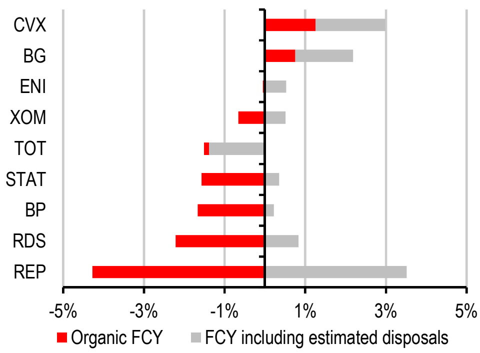
2016 investment themes

The macro environment remains challenging. Global oil markets look set to remain oversupplied in 2016, but the imbalance should narrow substantially. We expect demand growth to stay healthy at over 1mbd for the year; while non-OPEC supply should decline in absolute terms in the face of severe industry spending cuts. However, we see no let-up in the supply pressure from OPEC, including the potential for increased crude exports from Iran next year. Overall, the market may take until 2017 to move fully back to balance and is meanwhile beset by historically high inventory levels. Nevertheless, we continue to believe current oil prices are unsustainably low and expect them to grind higher over the next few years. We assume an average Brent price of USD60/b in 2016, rising to USD70/b in 2017 and USD80/b in 2018.

Big Oils: sharply improving breakeven levels. As bad as the macroeconomic backdrop has been – and may remain for a while – we have been extremely encouraged by the scale of response from the integrated oils. We have seen a combination of aggressive capital discipline and sharp cuts in operating costs virtually across the board and in many cases there is evidence of a willingness to completely reassess some of the historical processes of upstream project design, contracting and execution. We think this points to a more structural reduction in costs which should be much more sustainable than in the last down-cycle, and we expect to see further evidence of this in the 1Q strategy season. We think the market is underestimating the degree of free cash improvement in the sector over the next two to three years. In the meantime, balance sheets are showing remarkably little stress, a function also of low gearing going into this cycle and the significant additional flexibility from disposals and in some cases scrip dividends.

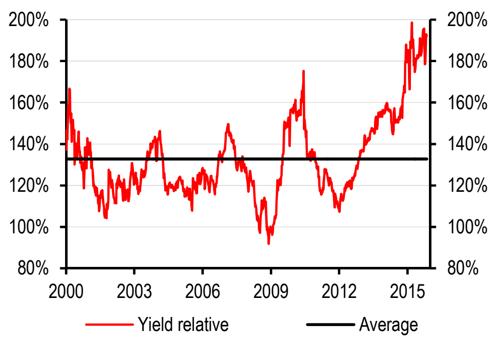
Dividend sustainability a key focus. The sector's dividend yield relative to the wider market remains close to a 27-year high, which we think is indicative of the level of scepticism in the

2017e free cash yield after dividends at USD70/b Brent



Source: HSBC estimates

European integrated oils – dividend yield relative to market



Source: Thomson Reuters Datastream

market as to whether dividends are sustainable. We believe this scepticism is overdone. At our base case assumption of USD70/b Brent, we see most of the big oils broadly covering their dividends organically in 2017, and many are now targeting USD60/b organic breakeven levels.

Downstream support has waned. Strong refining margins helped offset some of the effect of sharply weaker upstream earnings for much of the sector through 2015. However, refining margins have fallen sharply thus far in Q4 (2 November) to levels more consistent with historical averages. If this persists into 2016, a key source of earnings support would be eroded.

We still like the sector for the medium term. Although downstream weakness could create a near-term headwind to estimates, we still think the medium-term outlook for the sector is good. Sentiment toward the big oils remains highly negative, and it seems to us that the market is still pricing in an overly pessimistic outlook for the companies' free cash flow and dividends in particular. This view is reflected in the predominance of Buy ratings in our coverage.

Highest conviction Buys

Royal Dutch Shell, Buy, TP (A/B shares) 1,960p
The prospective BG deal should resolve one Shell's critical issues – a relative lack of growth prospects – but the resulting near-25% increase in Shell's share count will restrict growth in per-share metrics. We have recently seen welcome data points indicating that management is now tackling some of the key issues around capital discipline. Moreover, we think the prospect for incremental newsflow in the coming year is as good as any in the sector, particularly around the closure of the BG deal and subsequent portfolio actions. The company's commitment to the dividend is clear, and its balance sheet and potential disposals give it plenty room to sustain it.

Total, Buy, TP EUR51 (HSBC Europe Super Ten portfolio constituent)
Total remains one of our top sector picks and an HSBC Europe Super 10 constituent as we see it offering the best combination of volume growth and improvement in free cash yields of the big-caps. Despite a cut to 2017 volume target we still see output growing about 4-5% pa over 2016-18. In addition, the underlying cash margin accretion that has helped Total to show the smallest y-o-y decline in cash flow so far in 2015 should remain a key feature. Combined with sharply lower capex as the company concludes a multi-year growth investment phase, we see one of the most impressive turnarounds in free cash flow in the sector in 2016-17e.

Least preferred names

ENI, Hold, TP EUR15.9
ENI's dividend rebasing in 2015 removed a historic overhang for the stock, while its balance sheet should be de-risked by the transaction to deconsolidate Saipem. The volume growth outlook is healthy with guidance of 3.5% growth per annum through to 2024. However, cash flow growth is more muted given high historic upstream margins – year-to-date, ENI's decline in underlying cash flow was the worst of the big-caps (-52% y-o-y). ENI's prospective capex reductions should also be more modest than peers'. Finally, geographical risk in ENI's portfolio is above average, with a third of 2015e volumes from North Africa (Libya 15%).

Repsol, Hold, TP EUR13.0
Repsol recently presented its 2016-20 strategic plan following closure of the Talisman acquisition. If well executed, the plan should drive an impressive turnaround in its free cash generation, but the near-term free cash remains under pressure. Repsol will have to realise significant efficiency gains, synergies and large-scale asset sales to balance its cash cycle. Refining margins will also need to hold up better than in the 2009-14 period. Thus we see risks around delivery of upside from the deal which we think warrant a valuation discount vs peers.

Luxury Goods

- Chinese outbound travel still in its infancy slower yet healthier industry growth; increased brand volatility in soft luxury; star category jewellery
- Our highest conviction buys are LVMH, Richemont and Moncler. Our least preferred name is Swatch

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2016 investment themes

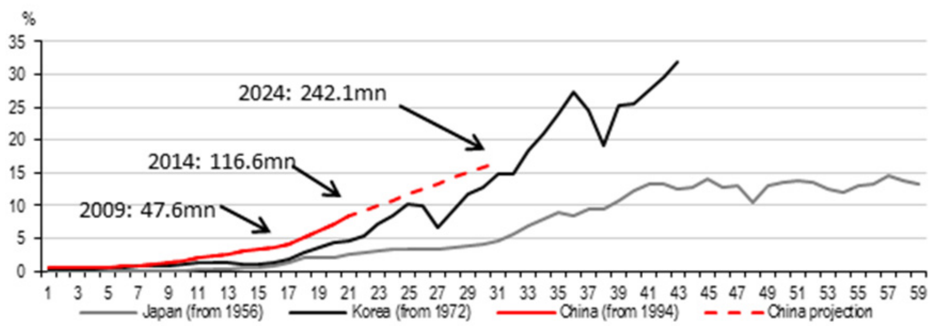
Chinese outbound travel: still the tip of the iceberg; even though Chinese consumers already account for 35% of global luxury consumption, there have only been about 50m trips outside of Hong Kong and Macau, a lower number than the likely number of passport holders (about 5% of the population, or 65m). We forecast a mid-teen increase pa in Chinese outbound travel over the medium term, with still most reasons for spending abroad being valid.

Slower, yet healthier industry growth as companies allocate investment to digital, services and more efficient targeting of different consumers rather than ramping-up bricks-and-mortar stores. In turn, capex to sales will likely continue to fall sharply, and margins should be supported by the prospect of sales being driven more by like-for-like growth than by space expansion.

Increased volatility of brand momentum in soft luxury: for brands focusing on apparel and accessories, the need for greater differentiation means being bolder in terms of innovation, leading to higher risk. We anticipate volatility for individual brands, and it will become increasingly difficult for investors to anticipate when the momentum of a soft luxury brand will change direction. This implies investors should favour mono-brand companies with a distinctive positioning and/or at a less mature stage of development (eg Moncler) and larger groups not too dependent on one brand (LVMH).

Jewellery star category driven by branding process: We expect branded jewellery to be one of the fastest growing luxury segments as brands are taking market share from non-branded jewellery, which still accounts for about 75% of the total market. In Asia in particular, we believe that branded jewellery has entered a sort of super-cycle of growth with consumers.

Resident departures as a percentage of total population



Source: CEIC, HSBC Economics forecasts

Highest conviction Buys

LVMH, Buy, TP EUR195

The recently achieved 7% organic growth in Q3 is a feat in the current environment and demonstrates the resilience of most of LVMH's businesses. Management and the creative team at Louis Vuitton put in place in 2013 are ahead of the competition in reacting to less favourable market dynamics in the handbags segment. In Cognac, we expect a two-stage recovery: in H2 2015, sell-in to Chinese distributors should pick up on the back of very easy comps, and in 2016, the end-demand should bottom out even for higher-margin products. With regards to other businesses, strength in perfumes & cosmetics, Champagne, Bulgari and Sephora more than offset issues with some of LVMH's less well performing names (DFS, Marc Jacobs and Berluti).

Richemont, Buy, TP CHF100

We remain very positive about the growth of jewellery (a third of Richemont's sales), the underdeveloped nature of Cartier in that segment and the pricing power of specialist watch brands. With a few exceptions (Dunhill, Lancel and Piaget), we believe the health of Richemont's brands is good and as of H2, operating margin should start improving again on the back of better growth.

Moncler, Buy, TP EUR20

Moncler still has plenty of opportunities to open new stores outside Italy without jeopardising like-for-like sales growth. The performance in H1 was very strong with retail LFL up 25% in Q1 and 18% in Q2 2015. While retail LFL growth should normalise to mid-single digits as from Q3 2015, we believe the contribution from new stores is still underestimated by the market and we expect more than 20% in H2 2015 and, FY2016. Overall constant FX sales growth of 16% in H2 2015e and 19% in 2016e should support Moncler as the fastest-growing luxury company.

Least preferred names

Swatch, Hold, TP CHF410

The stock has been a value trap for a while, and we remain reluctant to become more constructive "just because the stock looks cheap". Valuation may indeed appear undemanding (14.9x 2016e PER), but in light of the current macro/market backdrop, the group's exposure to Greater China (37% of sales, of which 22% in mainland China, 11% in Hong Kong and 4% in Taiwan and Macau), which is the highest in our coverage, is a deterrent, in our view. In addition, market concerns about the exact impact of the launch of "smart watches" on group sales are unlikely to wane, even though management announced the Swatch Group would launch its own "smart watches". Finally, the small size of Swatch's jewellery business (only 5% of sales) is a relative weakness versus other hard luxury players such as Richemont and Tiffany.

Media

- Sector theme is defensive vs cyclical, but we see stock-specific triggers as more important in the short term
- Our highest conviction Buys are Publicis, ProSiebenSat1 and GfK. Our least preferred stocks are Vivendi and JC Decaux

2016 investment themes

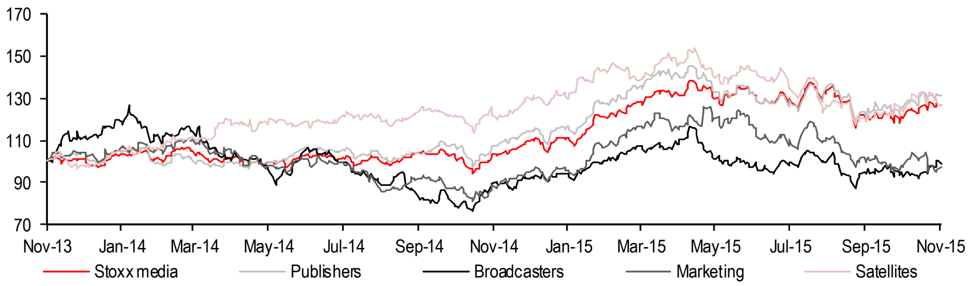
More than just macro: At this stage of the cycle, defensive names within media should be preferred, but we think stock-specific triggers outweigh sector themes. Our analysis suggests that the long-recognised cyclicality of most advertising-driven names is unlikely to be a tailwind in the coming quarters, and we prefer stocks with attractive dividend yields together with a company-specific angle.

Broadcasters: we expect sizable performance differences between European TV names to continue into 2016 and prefer a stock-picking approach in the sub-sector, as each is fundamentally different (eg, due to differences in strength of TV ad market, position in the ad cycle, advertising vs diversification exposure and of course operational performance). ProSiebenSat.1 is one of our highest convictions Buys.

Agencies and Market Research: beyond a clear macro/FX uncertainty, 2015's themes (media budget reviews, quest for transparency, ad-blocking), and disparity in how agencies record revenues, are impeding equity stories and comparability. We focus on profit growth prospects instead of potentially misleading top lines, company-specific triggers and cash return to shareholders.

Satellites: The prospect of re-accelerating organic growth for each player, driven by the implementation of new capacities, could restore interest in the satellite operators sub segment. However, we see several themes (completion vs OTT, overcapacity due to HTS emergence, pricing pressure) creating doubts for investors and generating volatility. Beyond fundamentals, Q1 should provide key detail on SES (more colour about O3b) and Inmarsat (LightSquared to adjust its strategy and business model for its inflight broadband business across Europe).

Stock performance: Media



Source: Thomson Reuters Datastream; Note: Values rebased as on 2 November 2013

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Highest conviction Buys

Publicis, Buy, TP EUR77
Except perhaps for the share of revenues generated with consumer products (27% over 9M, including food), we do not see any company-specific obstacle that would prevent Publicis from delivering decent organic growth again after two disappointing years. The French group should also take advantage of the contribution of Sapient, both for organic (fairly favourable 2015 base) and cost synergies. All in all, we expect the group, currently discounted to peers, to gradually restore confidence during 2016 and rerate: a commitment to an increased return of cash to shareholders could be another catalyst.

ProSiebenSat.1, Buy, TP EUR55
We believe the market underestimates Pro7's ability to keep organic growth at accelerated levels, particularly for its Digital&Adjacent segment where we expect 15%+ organic sales growth to be maintained for several years. Why are we so confident about this? Pro7's digital story is largely opaque as Pro7 only discloses sub-segment performance within 'Digital & Adjacent' despite sizable differences among its 20+ key assets. We believe this opaqueness creates an opportunity (we provide detailed estimates for all key digital assets in *Another strong delivery* (30 October 2015).

GfK, Buy, TP EUR43
Being at the tail-end of restructuring and having multiple new products lined up (new panels, mobility, new audience measurement contracts), GfK is likely to start reaping the benefits from 2016. The current soft valuation, based on estimates more cautious than group guidance, offers an opportunity for long-term investors (limited liquidity makes trading on the name difficult).

Least preferred names

Vivendi, Hold, TP EUR21
Vivendi is at a crossroads: if the direction of travel has been stated (towards building a content and media group), the mean of transport is still to be defined (what vehicle to buy next) and the re-investment required to prepare the current business units for future growth is uncertain. The management team has engaged in a portfolio clean-up over the last 12 months (selling SFR, GVT and most of the stake in Activision) but has also built a 20% stake in Telecom Italia and invested in Ubisoft and Gameloft. Investors may therefore feel like they are contemplating pieces of a complex jigsaw with little clue about what the final picture might be, despite an engaged and experienced management team and a large pile of cash (HSBCe – EUR8.1bn December 2015,) that in turn allows it to be creative. In the meantime, Vivendi will face the difficult task of managing its two business units, Canal+ (Pay-TV in France, Poland, Viet Nam and Africa) and UMG (global music leader), which both face structural challenges and require investments. Vivendi is confident that it could positively impact the revenue in the longer run but we are of the view that it will take time to establish certainty on that matter.

JC Decaux, Hold, TP EUR35
The leading outdoor operator has several obvious qualities: strong leadership with a global footprint, the capacity to innovate and take advantage of the most recent innovations (small cells, digital panels), a solid balance sheet enabling the M&A required to reach critical mass in new markets. We think these are already well priced in by the market however (2016 EV/adj EBITDA above 10x), that recent acquisition/wins will trigger operational leverage only in the long term and that any weakness in one of the group's markets could drive significant pullback on the stock price.

Metals & Mining

- China – broken or bottomed? Our China trip suggests bottomed
- High conviction buys are ThyssenKrupp, and copper plays Glencore and Freeport. Our least preferred name is Rio Tinto

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2016 investment themes

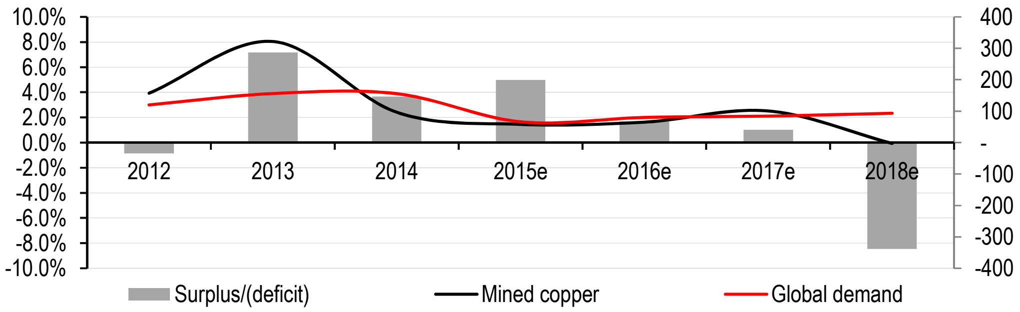
China – broken or bottomed? We think conviction on China's commodity demand outlook is near an all-time low. Given China typically accounts for around 50% of global metals demand, this presents a roadblock to investor appetite for many. Almost everyone we've spoken to recently is sitting on the sidelines, waiting for firmer signals that China has broken or bottomed – indeed, the data is mixed enough that bears and non-bears alike can justify their view.

Our China trip suggests stability: On our recent China trip we sensed that, while China is structurally slowing, there was no evidence of a recent sudden demand shock (in contrast to snowballing negative sentiment). That said, while some market concerns of a sharp downturn look misplaced, we think a significant structural rebound also looks unlikely. See *China trip – implications for copper*, 6 October 2015.

An "L shape" China works for some commodities and equities: We think the next 12 months will be very interesting. If a demand floor is established, as is our expectation, a lowering of the risk discount on a select group of higher beta equities will present the best opportunities.

Copper – amongst the best: We see copper working under a low positive demand growth environment, given we think the market is too optimistic on near-term supply growth. While there remains short-term downside price risk, we think further price-related production cuts would support the copper price around current levels. Supply growth turns negative after 2017 – if new supply is needed, the price will need to rise as no projects generate a return at today's spot price. This is a consideration we think the market will increasingly turn to as 2016 progresses.

Global refined copper: demand and supply growth, implied surplus/deficit (RHS, kt)



Source: WoodMackenzie, HSBC estimates

Highest conviction Buys

Glencore, Buy, TP 190p
Glencore remains a high risk/high return proposition, given its leverage and high earnings sensitivity to commodity prices. Recently announced debt reduction measures secure the balance sheet in all but a sustainably bearish demand scenario. Importantly, the Glencore investment case works without needing a commodity price recovery. Spot prices generate positive annual free cash flow after capex, while multiple catalysts (asset sales, precious metal streams) will further buffer the balance sheet pinch point. After equity issue proceeds, H1 2015 net debt was USD27.1bn. A spot case EBITDA corresponds to a net debt ceiling (3x EBITDA) which can be met through cash flow, working capital release and asset sales.

Freeport McMoran, Buy, TP USD19
Similar to Glencore, the Freeport investment case does not require a commodity price improvement in our view. Current spot prices point to cash-flow breakeven under conservative near-term production assumptions, while near-term low-cost production growth (Cerro Verde, Grasberg) will boost EBITDA and steer the company away from the 4.75x net debt/EBITDA ceiling.

ThyssenKrupp, Buy, TP EUR23.8
While TKA faces the same steel pricing pressure as peers, we think that it is one of the few steel stocks that fully discounts spot steel margins and a cautious economic scenario. We think that the investment case is for a multi-year transformation with more cost cutting in 2016e. While book equity is rather low (9.4% of balance sheet total) we think that a 2016e ND/EBITDA of 1.3x indicates a solid balance sheet. The conglomerate discount has widened to previous peak values, and stripping out elevators the other assets trade at an attractive 5.0x 2016e EV/EBITDA.

Least preferred name

Rio Tinto, Hold, TP 2,690p
More than 70% of Rio's earnings stem from iron ore and aluminium – the two commodities for which we expect zero positive price momentum for 2016e. This leaves a strong balance sheet (gearing 23% at year-end) a decent FCF and the potential of putting dividends first as reasons to hide in the stock. However, we project that iron ore marks new lows in 2016e and think that the market underestimates the risk that the yield story could break and see these as sound reasons to remain cautious. The stock discounts an iron ore price above USD60/t and at 6.5x EV/EBITDA trades in line with the historical average.

Oilfield Services

- The downturn extends into 2016 – we prefer defensible names with self-help trading at attractive valuations at a low point in the cycle
- Our highest conviction buys are Petrofac and AMEC Foster Wheeler. Our least preferred stocks are Saipem and Lamprell

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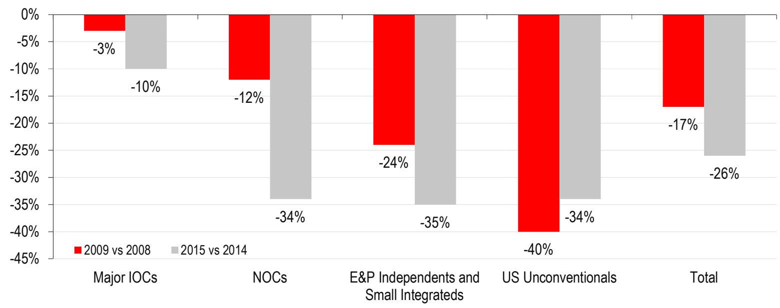
2016 investment themes

In our September 2015 sector publication *Gimme Shelter from the Storm* our analysis of industry capex trends, rig counts and pricing pressures confirmed our earlier view that the oilfield services sector downturn would be harsher than in 2009. We have seen incremental cutbacks to E&P capex budgets and further oil price turbulence while North American rig counts have double-dipped and we do not see any near-term catalysts that could drive a meaningful uptick in drilling activity, and international drilling activity has fallen at unprecedented rates. "Mediocrity will be eliminated in these market conditions… best in class will survive…" (source: Hunting H1 2015 results)

The industry is planning for a 'lower for longer' scenario, and we expect a second year of industry E&P capex cuts (for the first time since the 1980s) in 2016, at 10-15%, before recovering somewhat in 2017 when we believe oil companies will be more comfortable with project economics and more concerned with falling organic production. We also expect oil prices to be significantly higher than prevailing prices (HSBC estimates USD70/bbl for 2017).

We see growing prospects for industry consolidation – supply chain integration may be necessary to lower the industry's cost structure, and we see potential for classic sector consolidation as well as deals aspiring to integrate across verticals. Our overall sector stance remains neutral and our ratings profile is balanced. We favour relatively defensible business models with self-help programmes trading at attractive valuations at a low point in the cycle.

Upstream Capex Cuts in the last vs. current cycle



Source: Company data, HSBC calculations

Highest conviction Buys

Petrofac, Buy, TP 1,025p
Laggan Tormore's problems should be consigned to history in 2015, and it now appears to be largely de-risked as first production approaches. October's cancellation of the vessel newbuild contract reduces both PFC's capex burden and its medium-term capital intensity. Importantly, the wider OEC portfolio continues to deliver solid profitability as difficult commercial close-outs are offset by self-help and PFC's own supply chain savings. A record OEC backlog is supported by a healthy pipeline of opportunities and the competitive environment is surprisingly stable with no signs of irrational competitor behaviour. Against this backdrop we anticipate a healthy win rate for OEC, while the IES business continues to focus on execution and opportunities to reduce capital intensity including the farm out/sell out of contracts. There is some uncertainty around dividend sustainability and a possible medium-term move to a higher pay-out ratio, but balance sheet deleveraging and a 2016 earnings recovery provide some comfort.

AMEC Foster Wheeler, Buy, TP 800p
The step-up in AMFW's net leverage is somewhat concerning to us, but we take comfort in its inherently cash-generative business model, and potential disposals can accelerate balance sheet deleveraging. Management also felt it necessary to rebase the dividend by 50%, but after the share price fall, the valuation looks appealing to us – a 2016e PE <10x and EV/Sales of around 0.5x both appear attractive relative to peers and at a marked discount to AMFW's long-run averages. 2016 is also likely to see trough earnings for this cycle, based on our forecasts. Revenue synergy opportunities from the Foster Wheeler deal are gathering momentum, particularly in LNG, petrochemical and brownfield, and notably in the Middle East, strengthening recovery prospects. We believe AMFW offers investors a diversified, low-risk/reimbursable, asset light and cash generative business, which is undergoing a significant self-help programme.

Least preferred names

Saipem, Reduce, TP EUR5.5
Should it go through as planned, Saipem's EUR3.5bn capital raising should resolve the balance sheet issue, ensure more independence and according to management, allow Saipem to "seize opportunities the downturn may present". We can expect some change – modest divestments (FPSO/infrastructure/yard capacity) and diversifications (MMO, and more FEED, EPCM and technology). However, broadly speaking, Saipem as we know it today – with its blend of (inherently more risky) onshore/offshore E&C and relatively more stable cash flows from drilling is also the Saipem of the future. We remain concerned about the corruption probe in Algeria (and possibly Brazil), execution issues in the legacy backlog and some non-legacy contracts such as the EUR4bn Kaombo contract. We continue to see an unfavourable risk/reward profile.

Lamprell, Reduce, TP 110p
Lamprell is in the peculiar position of being the only major yard to have secured a newbuild jackup rig contract in 2015, and the group has about 60% revenue coverage for 2016. However it will need to convert a number of prospects from its USD5.2bn pipeline to fill the gap in a market where projects are shifting to the right and competition is intensifying. Lamprell's attempts to diversify away from jackups and form alliances to capture a wider cross-section of EPC work makes strategic sense, but will not be easy to achieve and may change the risk profile of the organisation – something that was vastly improved under outgoing CEO Jim Moffat. For the foreseeable future, we believe a worsening jackup market will continue to weigh on sentiment for Lamprell, and we see a lacklustre market continuing for several years.

Pharmaceuticals

- US drug pricing likely to be a key theme in a US election year; pricing changes unlikely, but headlines could be unhelpful
- Our highest conviction Buys are Novartis, GlaxoSmithKline and Shire; Novo Nordisk is the least preferred name

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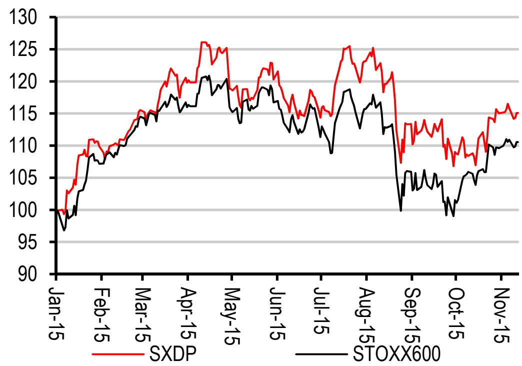
2016 investment themes

US election year puts US drug pricing centre stage. US drug prices, the magnitude of some drug price increases, and the difference between US and ex-US drug prices have all been signalled by various presidential candidates as likely discussion topics during the upcoming election campaign.

Although we do not believe that there is likely to be any change to the drug pricing regime in the US, negative headlines for the sector or for individual companies could be unhelpful for some share prices.

2016 a major year for new product data and approvals. Despite any headwinds for share prices created by headlines on US drug pricing, 2016 is a year when newsflow on late-stage clinical programmes or approval decisions at most of the major European pharma companies is likely to be significant. Expected approvals include lifitegrast (Shire, dry eye disease), alectinib (Roche, ALK+ve NSCLC), venetoclax (Roche, 17p del CLL) and BKM120 (Novartis, breast cancer). Expected clinical trial read-outs include the APHINITY and Goya studies (Roche, Perjeta and Gazyva), LEE011 (Novartis, breast cancer) CTL019 (Novartis, ALL).and Fovista (Novartis, wet AMD). That may provide a catalyst for the share prices of different companies at different times during the year, but any disappointments at such events are likely to be negative catalysts for share prices.

EU Healthcare Index vs STOXX600 Index



Source: Thomson Reuters DataStream

Highest conviction Buys

Novartis, Buy, TP CHF118

2016 will be a year of pushes and pulls for the group. On the negative side, Glivec will face generic competition and Alcon is likely to remain a drag on earnings. However, with Entresto and Cosentyx still in the launch phase, a full-year contribution from the acquired GSK Oncology business and a significant amount of likely positive late-stage pharma pipeline news flow, the stock is well placed – on fundamentals – to outperform the peer group. With one of the largest, but arguably underutilised, balance sheets, the group has ample firepower to support a growing dividend, for potential share buybacks and for acquiring growth, should such opportunities arise at reasonable prices.

GlaxoSmithKline, Buy, TP 1,700p

GSK has come through a period where serial disappointments, especially in its US Respiratory business, led to serial estimate cuts. With the three-part Novartis transaction now being incorporated, giving the group a lower risk profile and with a new chairman on board, the outlook in the near-term should have stabilised. With a 2020 guidance that is unlikely to be met, as it is likely too low in our view, the company has a lot of wiggle room to meet, or more likely, beat, its guidance of an EPS CAGR of mid to high single digits from 2015 to 2020. In our view, that profile deserves a higher multiple than a sector average rating provides, especially as the R&D pipeline provides a degree of optionality as well.

Shire Pharmaceuticals, Buy, TP 6,200p

In our coverage universe, Shire has one of the highest sales and earnings growth rates. It has diversified its business, making it less reliant on its ADHD/ADD franchise than in previous years and it has grown its Rare Disease franchises both organically and by acquisition. Although we remain concerned that its proposed acquisition of Baxalta is a deal to acquire scale for the sake of it, we see the likelihood of a deal going through as low and rather expect Shire to focus its efforts on its Rare Disease franchise and on deploying its prodigious cash generation on the acquisition of growth assets. The proposed acquisition of Dyax, which we view as being value-accretive, is not yet reflected in the valuation of the stock.

Least preferred name

Novo Nordisk, Reduce, TP DKK300

We see Novo as operationally the best-run company in the sector, which has delivered exceptional revenue and earnings growth over the last ten years. However, in our view, that operational excellence is more than reflected in the stock's significant premium to the sector on almost every valuation metric. Further, with increasing price pressure and competition in Novo's core Diabetes area, which could intensify if Lantus (Sanofi) biosimilars gain traction and with competition emerging for Novo's haemophilia franchise, the potential risks for Novo's growth profile are not reflected in the current valuation, in our view.

Precious Metals Miners

- Gold and silver prices to rebound off 2015 lows driven by dovish central bank behaviour supported by robust Asian demand
- Our highest conviction Buys are Fresnillo and Polymetal

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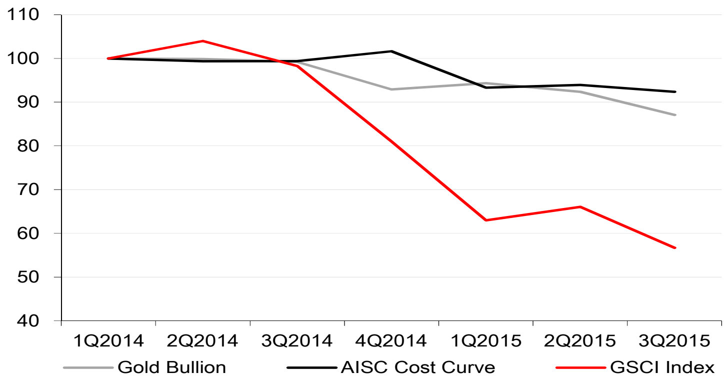
2016 investment themes

Gold: direction is up in 2016, but may be a tough climb – At time of writing, in late 2015, gold is down about 7% on average y-o-y, but continues to outperform most other commodities. We expect gold to move up modestly in 2016 (to an average USD1,205/oz) as the Fed's predicament (it can't normalise rates without risking a recession) begins to come back into focus, and the world of cheap money looks set to continue, running the risk of a severe currency devaluation. Meanwhile Asian demand is likely to remain robust (helped by ongoing purchases by the Chinese central bank and others), while mine supply looks like it has peaked. However, while we think significant selling pressure on gold will abate, apparently low inflation could delay a move back into gold for many investors and hence, although the general direction is up, the extent of upside in the metal is likely limited for 2016, at least.

Favourable cost trends help offset low metals – Weakness in producer currencies (for example the Russian rouble, Mexican peso and Tanzanian shilling), low oil prices, and declines in other mining industry cost inputs have had a favourable impact on many gold and silver miners, offsetting lower metals prices. This trend is likely to continue into 2016, but may slow as the pace of devaluation of producer currencies slows and as oil prices potentially rise.

Balance of stable cash flow and growth is key – The market favours companies that can balance a stable/growing cash flow profile with cost-effective growth and solid balance sheets. There are some good examples in the UK market, and we should expect these to perform well relative to other miners and versus the FTSE index in 2016.

European gold miners – Gold outperforms other commodities, and miners lower costs



Source: HSBC, Data Stream, Company data; AISC is aggregate for Randgold, Polymetal, Acacia, Hochschild and Fresnillo on a GEO basis

Highest conviction Buys

Fresnillo, Buy, TP 810p
Fresnillo is a high-quality gold and silver miner with a strong management team, a portfolio of low-cost assets and the ability to fund its sector-leading pipeline of growth projects mainly through operating cash flow (please see our recent note, *Buy: Site visit confirms positive outlook*, 8 October 2015). It arguably has the best growth profile of any of the major metals and mining companies, with 60% growth in GEO (gold equivalent ounce) production between 2014 and 2018, on our estimates. It should deliver additional low-cost production growth in 2016e as the new San Julian mine comes into production. We estimate that after extensive growth-related spending in 2015-2017, at spot gold and silver prices, Fresnillo will generate USD510m in FCF in 2018, implying an attractive 6.1% FCF yield. Fresnillo also continues to make exciting new discoveries from its exploration programme which should boost asset values going forward and enable the company to continue to grow.

Polymetal, Buy, TP 660p
Polymetal is a UK-domiciled, London-listed gold miner with operations in Russia and Kazakhstan. Amongst our global precious metals coverage, it has become the lowest-cost producer, largely as a result of the devaluation of the Russian rouble, although the low costs also reflect a higher-than-average quality suite of assets, marked by higher-than-average grades. We believe the weak rouble will help boost cash-flow generation, supporting the company's relatively high dividend (yielding 4.6% for payments in 2015) and also its plans to build a new mine in Kazakhstan, the Kyzyl project. We believe the market should react favourably to the strong planned economics of the new mine, which should allow modest production growth plus substantial mine life extension to POLY's production by 2018/19, and, being particularly high grade, the mine should fit well with the company's low-cost positioning. In the longer term, we believe POLY is very well placed to continue rapid growth at low entry cost, as it is one of only a few well-established, well-funded gold miners willing and able to operate in Russia, an area that we consider holds significant potential for new gold discoveries.

Real Estate

- Between a rock and a hard place – higher or lower real interest rates could both prove worrisome for real estate
- Our high conviction Buys are Vonovia and Hammerson. Our least preferred stocks are Capital & Counties and Immofinanz

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2016 investment themes

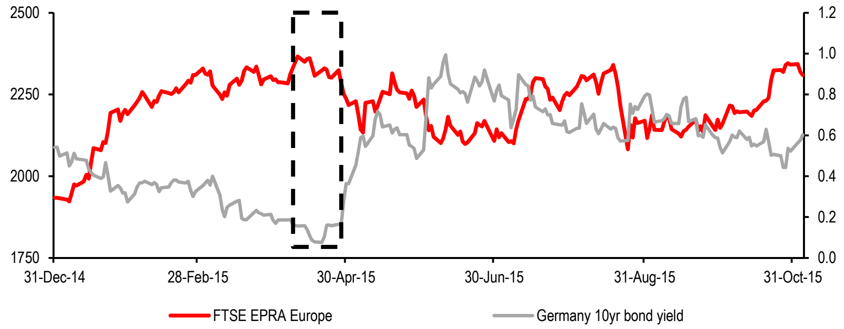
Higher, or, conversely, negative real interest rates in 2016 could prove to be a tipping point for real estate at this later stage of the cycle. Low bond yields have been highly supportive for real estate over the last six years or so, both as a favourable yield benchmark and as an attractive price-setting comparator for credit. However, markets are now pricing in a US rate rise over the next three months despite weak economic fundamentals persisting and the eurozone's yield curve increasingly resembling that of Japan. Listed real estate is unlikely to react positively as this will signal the end of a supra-low rates era. However, should a rate rise 'not stick' and central banks find they need to revert to a strategy of negative real rates (move away from QE due to having reached peak liquidity) this is not necessarily better for real estate.

Negative real rates could be construed as a positive as this re-inflates the yield gap. However if negative real rates become endemic within the major global economies then the risk of deflation should the stimulus prove impotent increases significantly. If so, a period of negative real rates could shape investment trends, or more pertinently for real estate, divestment trends, were viewpoints to move increasingly towards pending deflation. The bund will likely reflect this potential, as seen in the correlation breakdown earlier in 2015.

The dynamics of the eurozone's real estate markets vary considerably by country. Our European real estate coverage has exposure to the majority of the eurozone countries either by domicile or portfolio footprint. Broadly, the most prominent themes in 2016 are as follows.

Mergers & Acquisitions – a very strong theme throughout 2015 in the German residential market, and more recently to a lesser degree within the German office segment. Despite the

European Real Estate sector vs German bund



Source: Thomson Reuters Datastream

segment now representing one of the largest sub-sectors in the European listed real estate sector we can still see the rationale and scope for further consolidation in 2016.

Europe's EUR1.1trn QE programme – Because of the programme's size, 2016 will be another year with QE throughout. However, inflation is well below target and this is a problem, but also a differentiator. Annual CPI indexation of leases strongly favours prime retail over office portfolios.

The shift from cap rate compression to rental growth is under way in Europe's most advanced economy, the UK. However, we believe this could dampen share price momentum after what has been a very strong 2014 and 2015 YTD, leaving capitalisation yields materially below previous peak-cycle levels and GDP growth waning after a 2014 peak year. We turned cautious on the UK real estate sector in March 2015 (*Real Estate Digest 8*). Of additional note, the potential ramifications of a Brexit are as yet not evident.

Highest conviction Buys

Vonovia, Buy, TP EUR35
A natural consolidator in a highly dynamic but still fragmented German residential market. VNA's growth appetite has built a highly efficient and tested asset management platform with a nationwide portfolio (EUR24bn GAV and 380,000 residential units). Several sizeable portfolio acquisitions have been integrated fast, and in line with guidance. Currently, VNA is attempting to take over its local rival Deutsche Wohnen, which would substantially expand its footprint, particularly in Berlin. Recent acquisitions will deliver synergies in 2016-17e and provide VNA with strong FCF growth (around 50% for 2015-17e), and with likely yield compression it trades at a potential 13% discount to our 2017e NAV p/s versus peers' substantial 7% premium.

Hammerson, Buy, TP 677p
A somewhat atypical strategy within the UK REIT sector, HMSO has prioritised growth and quality of group earnings in recent years. As a result, dividend growth has averaged 7.6% since 2012 and we forecast average growth of 8% for the next three years to end-2017. We consider HMSO offers an income fund qualifying headline dividend yield with a potentially superior growth rate. HSBC Strategy team's view is that companies offering above average income yield profiles should outperform those that do not.

Least preferred names

Capital & Counties, Reduce, TP 394p
Capital & Counties has navigated its way impressively through land assembly in West London and re-positioning Covent Garden. However, we consider due to the lack of evidence of unlocked development profit at the Earls Court scheme with barely 3% of the residential component 'monetised', a prioritised social housing agenda at the forefront of the London Mayoral elections in May 2016 and the low level of cash rent conversion at Covent Garden, the share is pricing in too much of a blue sky outlook (in excess of a 25% book premium) when headwinds are gathering.

Immofinanz, Reduce, TP EUR1.8
One of the largest investors in Eastern European property markets, IIA is a complex company that lacks visibility. Its 30% exposure to the Moscow shopping centre market and an underperforming office portfolio with a 25% vacancy rate (CEE/SEE capital cities) remain problematic. In both segments we believe there is a sizeable disconnect between reported and market yields, and so we forecast a substantial write down (EUR1.4bn by FY2018).This would result in a NAV fall from EUR4.3 p/s, to EUR3 by end-FY2018 leaving the stock at a P/NAVPS discount of 20% (versus the historical range of 30-50%).

Software & IT services

- The key themes of 2016 in Software and IT services sector are the strengthening of Big Data/Analytics, mobile, cloud and security
- Our highest convictions Buys are Capgemini and Gemalto. Our least preferred names are Dassault Systèmes and Software AG

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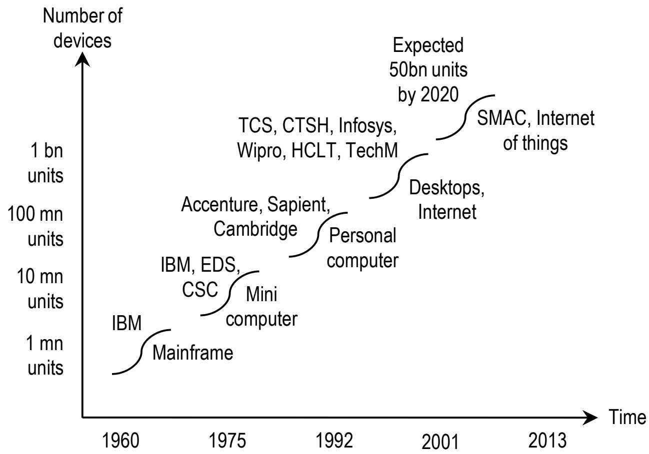
2016 investment themes

Big data, analytics and mobility. The amount of data is increasing at an exponential rate, and extracting the nuggets of information that can benefit businesses is becoming a strategic issue for many companies. While the most apparent examples of data proliferation are in business-to-customer, similar trends are visible in business-to-business. Storage, mining, analytics, trend analysis and intelligent, informed decision-making from these data are the realm of "big data" solutions and analytics (the "A" in SMAC). This has been a strong growth area for software and IT services companies in 2015, and should remain so in the coming years, in our view.

Cloud computing. We see the cloud as an opportunity for all the Software and IT services segment to accelerate top-line growth. Cloud and Software as a Service (SaaS – platform-based business process outsourcing) addresses the need for chief information officers to perform run-the-business tasks at the minimum TCO (total cost of ownership) and at the same time make costs more variable. There are opportunities to provide infrastructure or to provide cloud-related services that will be the potential accelerators of growth for IT providers like Capgemini.

Security. Deployment networks for business (cloud) or e-m-commerce (internet and mobile payment) creates a complex ecosystem. It increases the need for digital security and identity management solutions to make sure these high value data are accessible online only to the right users. This creates a significant potential market for companies like Gemalto.

Increasing intensity of IT spending



Source: HSBC

Highest conviction Buys

Capgemini, Buy, TP EUR105
Q3 2015 revenue growth has confirmed an accelerating growth trend (+1.5% at constant currencies y-o-y, +4.5% excluding the ramp down of the contract with HMRC in the UK). All indicators look good for Q4 and 2015. The investment environment in Europe is stabilised and the company will benefit from the traction in the US (31% of sales, improvement of the win rate, good traction from traditional ERP and S4HANA) and the UK (18% of sales), and the group's position in the fast-growing business Cloud, Analytics, Mobility (SMAC 20% of sales, +21% y-o-y in Q3 2015).

Capgemini is trading at 15x EV/NOPAT 2016e, which appears unchallenging if we take into account an EPS CAGR of +16% pa 2014-17e, with the possibility of the company surprising on the upside and strong FCF generation (yield 6% in 2016e).

Gemalto, Buy, TP EUR95
Gemalto has been penalised since 2014 by an increasingly complex environment in the mobile payment area. At the same time, H1 and Q3 results were lower than consensus expected, impacted by the closure of Softcard in the US (SIM NFC), validating the bear case. Beyond the mechanical impact of the Softcard contract (EUR120m on revenues, EUR50m of EBITA on a full year basis), the company enjoys strong top-line growth fuelled by migration of the US to EMV standards, expansion of M2M and recovery of government programmes. Combined with a stable cost base, it would create strong operating leverage from 2016. We believe that the operating profit target of EUR660m in 2017 remains achievable, implying an EBITA +25% pa.

The current share price appears to us to be an good opportunity to enter the long-term growth story. EV/NOPAT is at 13.5x 2016e while we expect an EPS CAGR at +23% pa for 2014-17.

Least preferred names

Dassault Systèmes, Hold, TP EUR75
Growth momentum stabilised at a high level in Q3 2015, at +9% excluding FX. Consensus already appears at the high end of the new guidance. Taking into account cost discipline and growth momentum in Americas and Asia, we see a good chance that Dassault Systèmes will beat consensus expectations in Q4 2015, especially on the operating margin side (we are at the high end of full-year guidance). However, the guidance for 2016 should remain cautious, thus disappointing consensus as it has for the past three years.

Dassault Systèmes remains a high-quality story, but at very high valuation. EV/NOPAT of 27x 2016e and 24x 2017e, with an EPS CAGR of 10% 2015-17e, more than prices in a potential upgrade of consensus estimates in our view.

Software AG, Hold, TP EUR28
For 9M 2015, the company published results broadly in line with consensus expectations. However, the performance did not come from where we expected it. The strategic growth driver business (Digital Business Platform – DBP) continues to underperform. This is compensated by a better-than-expected (by HSBC and the company) resilience of declining cash cow business A&N, and more precisely its support/maintenance part.

At 13x EV/NOPAT 2016e, Software AG presents one of the lowest valuations of the European software segment with a discount which we estimate at 30-40%. On a more fundamental view, we are waiting for more evidence on the recovery of top-line growth, especially in the DBP segment, more regularity in the broad performance and a more sustained long-term strategy.

Telecoms

- Regulation remains the sector's main driver. Only consolidation can maximise investment to consumers' benefit
- Our high conviction Buys are Deutsche Telekom, BT, Orange, Telecom Italia and NOS. We have no least preferred names

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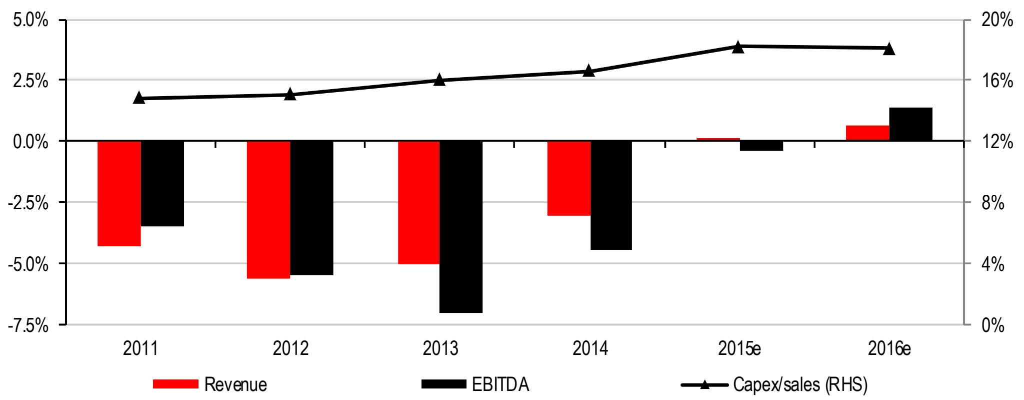
2016 investment themes

Regulation is the key driver: As we have argued since 2012 (see, among others, *A proposal for progressive consolidation*, December 2012 followed by *Supercollider*, February 2014 and *Supersonic*, February 2015), we believe regulation is the main driver for the investment case of the telecom sector. Recent developments in the regulation of fixed-line broadband have been positive: in order to encourage investment in fibre, incumbents have been given the flexibility to determine (within certain constraints) their wholesale pricing. In mobile, we think consolidation is necessary if operators are to generate the returns necessary to sustain investment. The higher investment that consolidation would enable is necessary, in our eyes, for higher speeds and would lead to lower rather than higher prices, as capex is the most powerful mechanism to reduce unit pricing.

Consolidation: further possible deals remain on the table. Two major in-market mobile consolidation deals are on the table for 2016: Italy (Wind- 3Italia) and the UK (3UK-O2). We think that the Danish case (where the proposed merger was abandoned) was different in various important respects. We continue to believe that the European Commission (EC) will evaluate each merger proposal on its individual merits, rather than adopting a predetermined approach of forbidding mergers that reduce the number of operators to three.

We see continued recovery for European telecoms in 2016: We believe that capex is critical if the telecoms industry is to maintain competitiveness and grow. European operators have increased capex in 2015 (19% capex/sales after 17% in 2014). Capex and better regulation have led to better revenue and EBITDA trends in 2015 and we expect further improvements in 2016 (see chart below).

European incumbents: Domestic revenue & EBITDA trends improving



Source: Company reports, HSBC estimates

High conviction Buys

Deutsche Telekom, Buy, TP EUR19.0 (an HSBC Europe Super Ten constituent)
Deutsche Telekom looks well positioned to benefit from improved regulation and consolidation in Europe, with Germany being a front-runner in several respects. In Germany, the regulator, BNetzA, has established a more constructive regulatory regime for NGA fibre networks and the recent decisions on wholesale fibre pricing flexibility further reinforce our view. As a result, we expect DT's German business to turn around revenue erosion over the next two years. We also expect the German market would be more rational post-consolidation and domestic EBITDA should return to growth from 2016. Further, in the US, regulation is shifting towards a pro-challenger approach that should benefit T-Mobile US.

BT Group Plc, Buy, TP 520p
Recently BT's proposed acquisition of EE (largest mobile operator), was provisionally cleared by CMA. We expect this merger to generate substantial synergy benefits. Also, the combined entity could benefit from the proposed acquisition of O2 UK by 3 Group, if approved on reasonable terms. On the fixed-line side of the business, BT looks well placed in the UK's bill inflationary (but price deflationary) environment. With best-ever TV net adds reported in Q2 2016, we think that the group's TV strategy is working. This should help both consumer ARPU and churn over the coming years.

Orange, Buy, TP EUR18
We believe that Orange is on the right track: quarter after quarter, the company has shown improvements in its organic revenue trends, and returned to growth in Q3 2015. Orange's better performance has been driven by it adopting the right commercial strategy – a mix of FTTP and quad-play supported by good quality networks combined with continuous cost cutting (a mix of lower headcount and other efficiency gains). We expect Orange's revenue and EBITDA to start growing again from 2016e, which we believe could lead to a re-rating of the shares.

Telecom Italia, Buy, TP EUR1.35
Our Buy case for TI is based largely on it being the key passive beneficiary of any Italian in-market consolidation between the proposed merger of 3Italia and Wind (see our report, *TI passive beneficiary of WIND-3Italia merger*, 10 August 2015). We believe that consolidation would provide a 'win-win' outcome, in which a return to modest revenue growth (at the aggregate market level) would enable the greater investment that Italy needs and drive lower unit prices. As a result of consolidation (our base case), we expect TI's mobile ARPU to grow by 1.8% in 2017e which would result in domestic EBITDA margin of 46.7% in 2017e (vs 45.1% in 2015e).

NOS, Buy, TP EUR9.0
Our Buy case for NOS is driven by: (1) strong execution post-merger with the company returning to revenue and EBITDA growth in 2015; (2) we expect NOS to be a beneficiary of further in-market consolidation as we see disposal of Cabovisao by Altice to Apax France a temporary solution – in the medium term we would still consider Vodafone as a plausible buyer (*Diario Economico*, 6 May 2014); (3) we expect NOS to continue to deliver strong shareholder returns, not only from price appreciation but also from its high dividend pay-out. We forecast that NOS will increase its dividend by 36% in 2015, and then by an annual average of 35% in 2016-18, once its network footprint expansion is completed (see *NOS-Buy: Harvest time*, 24 September 2015 for more details).

Least preferred names

Regulatory cycles are long duration. Regulatory policies can easily last a decade or more (the corrosive regulation to which Europe has been subject has been present since the late 1990s, and in some instances longer). The recent positive inflection is therefore a very rare event, and should be to the benefit of almost all European market participants – provided, of course, it persists. By contrast, we believe that regulatory trends are often deteriorating elsewhere on the planet, such as in the Americas. This should entice a net inflow into European operators.

Transport

- Falling oil and weakening yields shape airline profitability. Volume growth boosts infrastructure. Bus/rail impacted by regulatory change
- Highest conviction Buys are Eurotunnel, Air France-KLM and Wizz. Least preferred liquid stocks are EasyJet, Zurich Airport and Firstgroup

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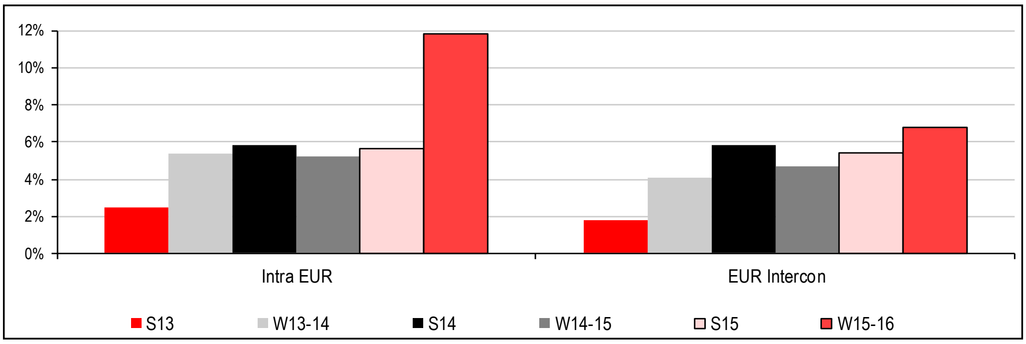
2016 investment themes

Airlines will be shaped by fuel vs yield, restructuring and possible consolidation. As out of the money fuel hedges drop away the effective fuel price will drop for European airlines. We expect the fuel price to be passed through to consumers, but the pace of the pass-through will vary depending on the competitiveness of the market. Flag carrier fortunes will be shaped by their success in restructuring. We see the low-cost carrier sector facing excess capacity growth and unstable fragmentation. At some stage this must switch to a trend of consolidation – when and how is, however, less clear.

Infrastructure will benefit from volume growth: We expect Eurotunnel and the listed airports to benefit from solid volume growth. Regulatory developments will continue to be hard to predict, with broader political developments shaping the outlook. Airport retail benefitted from windfall gains due to EUR weakness in 2015 that mitigated weakness in the source markets of top-spending passengers. Notwithstanding ever-improving execution, this momentum will be tough to sustain.

Bus and Rail sector will be influenced by changing regulation. The comprehensive spending review in November will likely detail potential subsidy cuts, which operators will then feel in 2016 and beyond. To some extent, this could be offset by a benefit from lower fuel costs. However, 2016 is also the year when changes to the regulatory structure of the industry will likely be pushed through parliament in the form of the Buses Bill. This will give local councils greater powers to regulate buses and could mean that margins are squeezed over time. Stagecoach and Firstgroup look most exposed.

Airline yields destined to face pressure as y-o-y capacity growth accelerates



Source: CAPSTATS ASK Growth

Highest conviction Buys

Eurotunnel, Buy, TP EUR15.50
The migrant crisis in Calais has disrupted operations, but had limited impact on the group's profitability. This is because, following the closure of MyFerryLink, capacity has exited the cross-channel ferry market, and this is feeding through into a more robust pricing environment for the ferry operators and Eurotunnel alike. We expect this structural improvement to continue. Management remains confident that additional costs incurred as a result of the crisis will be recouped from the British and French governments in time. Further structural benefits should show through in the form of additional routes, with London-Amsterdam in 2016. We see improving cash flows.

Air France-KLM, Buy, TP EUR8.45 (an HSBC Europe Super Ten portfolio constituent)
Air France-KLM faces a highly challenging battle to drive labour restructuring at Air France. We believe the management will make more progress than the market generally expects, given the lapse of key labour agreements in 2016, political support for management and the restructuring already undertaken at KLM. The balance sheet could be improved by disposals of slots, Amadeus and potentially the catering business.

Wizz Air, Buy, TP 2,250p
Since its February 2015 IPO Wizz has consistently seen upward earnings revisions. We see Wizz's core East-West Europe market as unattractive to most low-cost carriers, contested by very weak flag carriers. Ryanair is interested in the market, but is currently focussed on repositioning upmarket into primary Western European airports. The management team is experienced, stable and aligned with shareholder interests. We see the European low-cost market being far from equilibrium, expecting the current fragmentation to revert to consolidation at some stage. We see Wizz as well placed, with its high profitability, tightly defined market niche and very low costs as and when the industry looks to consolidate.

Least preferred names

easyJet, Reduce, TP 1,600p
We are cautious towards easyJet: the low-cost sector faces a step-change in capacity growth from around 6% y-o-y in the past 18 months to around 10% from this winter, which will weaken yield trends. The fragmentation of the industry means new bases, such as Lisbon and Amsterdam, are markedly more competitive than the existing network. Established markets are facing fresh entry from the likes of Transavia in Paris and Norwegian in Gatwick. Ryanair is driving its market position towards that of easyJet, whilst second-tier names Eurowings, Transavia, Vueling and Norwegian are all positioned in easyJet's market area.

Zurich Airport, Reduce, TP CHF600
We continue to see Zurich Airport as vulnerable to pressure from the strength of the CHF, which we expect to pressure inbound winter traffic volumes more so than outbound summer volumes. We do expect the introduction of Swiss 777s to increase capacity, but the C Series introduction remains vulnerable, as is the mid-term outlook for the Swiss operation of Air Berlin.

Firstgroup, Hold, TP 100p
While we would expect to see Firstgroup win new rail franchises in time, which would help the shares, the problem remains the US operations. Most recently, it has been the long-distance bus business (Greyhound), but we also harbour lingering concerns around the school bus business, given wage cost pressure. We are fearful that further downgrades could emerge, meaning that a turnaround and return to cash generation remain distant. The group is also exposed to pressures in UK bus (such as subsidy cuts and bus reregulation).

Utilities

- Prefer regulated stocks with clear visibility on earnings; French water and renewable exposed stocks offer attractive growth opportunities
- Our highest conviction Buys are National Grid, Enel and Veolia. Our least preferred names are RWE and Drax

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2016 investment themes

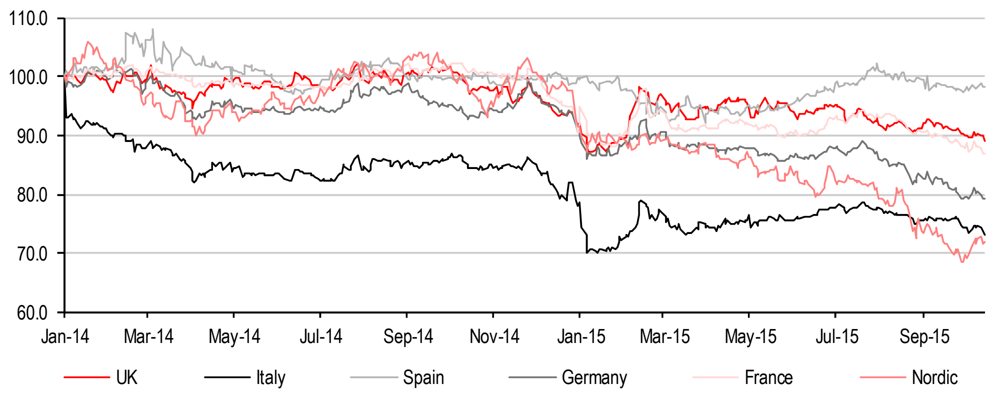
Declining power prices – a major concern for generators: Power prices across major economies in Europe have been in decline for many months (see chart below). Given our expectations of low economic growth in 2016 (c1.5%), coupled with electricity oversupply and focus on energy efficiency across key EU markets, we expect power prices to remain under pressure during 2016.

Prefer regulated stocks with good visibility and dividend yield: In an environment of low bond yields and declining power prices, we continue to favour low-risk regulated plays with clear visibility on earnings and 2016e dividend yields above 4%.

Significant investment requirements support water growth story: Significant investment needs in the water sector across markets such as the US (estimated USD2trn over next 25 years) and China (RMB5bn expected during 2016-20) provide growth opportunities for French stocks. In the UK, the companies are in the first year of a five-year regulated price control with scope for operational and financial outperformance.

Paris Climate conference to provide momentum for renewables: We expect the UN Climate Conference in Paris in December 2015 to provide momentum to the renewable industry in 2016.

European 1 year forward power price performance since January 2014 (%)



Source: Thomson Reuters Datastream

Highest conviction Buys

National Grid, Buy, TP 1,000p and an HSBC Europe Super Ten portfolio constituent
In an uncertain commodity environment, we believe National Grid's defensive investment proposition with a secure yield and scope for regulatory asset growth remains attractive. The company is continuing to outperform operationally and financially in its regulated business, asking state regulators for increased regulated revenues in order to drive up US returns and developing non-regulated opportunities such as new interconnectors. With involvement in four out of the six new interconnectors that are expected to commence operations by 2022, National Grid would emerge as the biggest beneficiary of the increase in net imports among our covered stocks, in our view. In addition management is exploring the potential to crystallise value by selling a stake in its UK Gas Distribution assets and returning the proceeds to shareholders.

Enel, Buy, TP EUR5.0
Despite the integrated nature of Enel, we think that the stock offers an appealing equity story. The balance sheet is largely under control, allowing the company to offer a solid capex plan to unlock medium-term earnings growth. On top of this, Enel offers a global footprint to crystallise organic growth from the renewable industry (renewables still enjoy high demand), ongoing cost efficiency to limit the pressure on returns from liberalised assets, self-help strategy focused on LatAm restructuring and improved cash-flow generation. The uncertainties from the LatAm and power price exposure could be offset by cheaper cost of debt and greater efficiency. Enel is now targeting a constant increase in the pay-out (from 50% in 2015e to 65% by 2018e) sustaining a dividend growth profile that on our estimates provides a minimum yield close to 5% by 2017e assuming current prices.

Veolia, Buy, TP EUR23.0
Veolia offers an attractive value proposition given: its well-diversified portfolio that may provide a natural hedge against slowing economic activities; China's waste and water growth story remains intact, in our view; waste still offers specialist opportunities despite commodity exposure; Veolia outperforms its cost savings target, which could further improve its margins. The next catalyst is its strategic presentation on 14 December in which we expect Veolia to set out its intentions for balancing cash redeployment for dividends and growth capex.

Least preferred names

RWE, Reduce, TP EUR10.5
Underlying conditions have continued to deteriorate with no sign of a recovery in RWE's markets of Germany, Benelux and the UK. Given falling power prices, squeeze on lignite mining and a thin equity base (lowest in the sector as a percentage of total balance sheet), our rating is Reduce on RWE. The share seems unattractive even in terms of yield at 4.0% for 2016e versus the average for HSBC utilities universe of 5.1% for 2016e.

Drax, Reduce, TP 190p
In our view, Drax looks unattractive for several reasons. We are negative about power prices and assume an achieved price of GBP38MWh for 2017 giving an EPS of 6.3p, 28% below consensus. There are significant concerns about the future of its three remaining coal units not converted to biomass. The UK government assumes no coal generation in the UK after 2027. Uncertainty also remains about the level of enhanced support for one of Drax's three biomass units under a Contract for Difference with the UK government. This is currently under discussion by the EU under the state aid rules.

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Valuation and risks

Automobiles

	Valuation	Risks
Renault RNO FP Current price: EUR89.35 Target price: EUR100 Rating: Buy Up/downside: 12%	We value Renault using a multiples-driven, sum-of-the-parts model, based on our 2016 estimates. Core drivers are the value of the stakes in other companies (mainly Nissan at cEUR17bn), automotive net cash (EUR3.9bn in 2016e), and multiples for the automotive division (20% EV/sales and 2.0x EV/EBITDA). We value the stakes in Nissan and Daimler at current market value and apply a 20% holding discount. Despite the recent strong decline of the Renault stub value, we think the holding discount should not be higher as there remains some chance that the alliance structure will change in the mid-term. This would reduce the holding discount substantially. Net cash, dividends, book value for financial services: We discount these values back to today's fair value by using a cost of capital of 9%. We value Financial Services at 90% of its 2016e book value.	Renault's main downside risks are macro-related. Any unexpected negative shifts in volumes, prices or raw material prices could have a significant effect on the company's earnings and cash outlook, given its high operating leverage. Renault's high exposure to the volatile markets of Russia and Brazil also pose risk to volumes and profitability. Furthermore, Renault's valuation is greatly influenced by the value of its associates – particularly Nissan. Any change in Nissan's share price and the Japanese yen would have a direct, positive or negative effect on our valuation of the stock.
Michelin ML FP Current price: EUR92.0 Target price: EUR105 Rating: Buy Up/downside: 14.1%	We value Michelin using a 60-20-20-weighted average of, respectively, (1) A sum of the parts, based on peer multiples (EV/sales, EV/EBIT, P/E and FCF yield), (2) ROIC/WACC versus EV/IC and (3) Discounted cash flows (DCF). Our assumptions are RFR of 3.5%, ERP of 5.5%, beta of 1.0 and terminal growth rate of 2.0%. For SOTP we derive fair multiples for Michelin implying 0-50% premiums for its divisions over the simple peer group averages of EV/sales, EV/EBIT and P/E multiples to reflect its superiority in terms of earnings growth and capital efficiency. Based on this methodology we arrive at our fair value target price of EUR105.	**Downside risks:** Main downside risks include: (1) further sharp deteriorations in LatAm tyre markets and general global tyre volume weakness, given that Michelin is basically a proxy for the market, as one of the biggest and most international tyre makers; (2) a potential margin squeeze from a sharp recovery in raw material costs without the simultaneous ability to pass on the higher costs to consumers; (3) execution risks in relation to narrowing the profitability gab to competitors – which is a major part of our positive investment case; and (4) further weakness in the Specialty Tyre segment with no normalisation in volumes by 2017e.
BMW BMW GR Current price: EUR94.36 Target price: EUR92 Rating: Hold Up/downside: -2.5%	We value BMW using a multiples-driven, sum-of-the-parts model, which we base on our 2016 estimates. Core value drivers for BMW remain its automotive division, value of the China JV, the automotive net cash (EUR14.1bn) and the pension provisions (EUR4.5bn). We value the automotive division at 35% EV/Sales and 3.5x EV/EBITDA, reflecting a 10% discount to BMW's peer Mercedes-Benz Cars, mainly because we expect weaker clean EBIT growth at BMW. China JV: We value BMW's China JV in line with the current 2016e (Factset) consensus PE multiple of Brilliance (1114 HK, Hold, HKD10.1), which stands at 8.5x. Net cash, dividends, book value for financial services: We discount these values back to today's fair value by using a cost of capital of 8%. We value the Financial services division at 0.9x its 2016e book value.	BMW is exposed to the usual macro risks as other stocks in our universe. If premium car demand trends are better or worse than expected, this will have an impact on our estimates. At BMW Autos, car pricing remains a downside risk. The high exposure to China has been a benefit in the past few years, but the business is becoming more difficult. Particularly in China, we see the risk that the currency tailwind will be partially passed on to customers. Currency risks seem to be currently on the upside, but this could quickly reverse.
Nokian Renkaat* NRE1V FH Current price: EUR33.7 Target price: EUR30 Rating: Hold Up/downside: -11.1%	We value Nokian using a 60-20-20-weighted average of, respectively, (1) A sum of the parts, based on peer multiples (EV/sales, EV/EBIT, P/E and FCF yield), (2) ROIC/WACC versus EV/IC and (3) Discounted cash flows (DCF). Our assumptions are RFR of 3.5%, ERP of 5.5%, beta of 1.1 and terminal growth rate of 2.0%. For SOTP we derive fair multiples for Nokian implying 30% and 15% premiums for its PC tyre and Heavy tyre divisions, respectively, over the simple peer group averages of EV/EBIT and PE multiples to reflect its superiority in terms of revenue growth and capital efficiency. For EV/Sales our fair multiples imply a premium of 150% for PC and 100% Heavy tyres, which is lower than the 200% premium Nokian has traded at versus peer historically (to account for short- to medium-term risks from Russia). Based on this methodology we arrive at our fair value target price of EUR27 which implies 11% downside to the current share price. We rate the stock as Hold as Nokian's long-term structural potential is high, but short-term visibility and transparency are very limited.	**Downside risks:** Main downside risks include (1) a later-than-expected recovery of the Russian tyre market, (2) a continued margin deterioration in Russia due to a dilution of mix (regional mix, brand mix, summer/winter tyre mix) and (3) increasing competition in Russia with competitors building local capacity and Russian import duties on tyres fading to 10% by 2017. **Upside risks:** Upside risks include (1) a sooner and/or stronger than expected volume recovery in Russia, (2) a reversal/recovery of the margin dilution in Russia towards historical levels (c40-50% EBIT margin in Russia) despite Nokian's business model evolution and (3) economic factors, including in particular sooner and/or stronger than expected recovery in Russian consumer spending and/or a recovery (i.e. appreciation) of the RUB (as this boosts Russian ASPs in EUR terms).

Priced as at close on 2 November 2015, * except for Nokian Renkaat for which TP changed on 13 November with the stock priced at 12 November. Source: HSBC estimates

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Banks

	Valuation	Risks
Barclays BARC LN Current price: GBP2.36 Target price: GBP3.15 Rating: Buy Up/downside: 33%	We use a 2017e sum-of-the-parts model, discounted back to present value, to set our target price for Barclays (GBP3.15). Key components of this SOTP are P/TNAV multiples of 1.3x for the Investment Bank, 1.4x for the UK Retail/Commercial bank and 2.0x for Barclaycard with the different multiples reflecting varying forecasts for 2017e ROTE.	Main downside risks are revenue disappointment within the investment bank, possibly driven by a weaker macro environment, the failure of management to deliver on current cost targets and regulatory risks, with the Basel Committee looking to revise how capital is allocated to markets-based products.
Credit Agricole SA ACA FP Current price: EUR11.6 Target price: EUR14.7 Rating: Buy Up/downside: 26%	Our EUR14.7 target price is set using a 2016e sum-of-the-parts model discounted back to present value terms. As a general rule we use PE multiples for non-balance sheet intensive activities (Asset Management 12x, Insurance 10.5x) and P/TNAV for banking operations (1.1x for Corporate Finance, 1.7x for LCL). We also adjust our SOTP for the capital deficit (ex-Switch transaction) versus a 10% CT1 benchmark	We believe the key downside risks for CASA come from two sources. The first is regulatory; while we believe the ECB has opted to leave the Danish compromise in place (which CASA relies on), the bank is vulnerable to any tightening in capital requirements elsewhere (mortgage floors, operational risk weightings). Second, as a large 'asset gatherer', group earnings would be vulnerable to any further weakness in equity markets.
CaixaBank CABK SM Current price: EUR3.49 Target price: EUR4.25 Rating: Buy Up/downside: 22%	Our EUR4.25 target price is set using a 2017e sum-of-the-parts model discounted back to present value terms. We use a WEV (warranted equity value) equation to value the Banking and Investment divisions (using a 9% CoE and zero growth), that produces P/TNAV multiples of 0.8x and 2.4x, respectively. Surplus capital above a benchmark 12% CT1 (including deductions related to financial investments) is also added into the valuation.	Downside risks could arise from a significant deterioration in the real estate portfolio or a worse-than-expected intensification of lending competition in Spain (leading to a drag on margins).
Erste Group EBS AV Current price: EUR26.7 Target price: EUR33 Rating: Buy Up/downside: 24%	We use our equity value model to calculate our target price of EUR33 which is based on our 2017 estimates. We divide the adjusted ROE of 12.8% by our CoE of 9.2%, which we calculate by using the CAPM approach and which includes a risk-free rate of 3.5%, a 5.5% risk premium and a beta of 1.04. We multiply this value by our estimate of the tangible book value of EUR27.52 per share and discount it back with our cost of equity back to reflect a current fair value and arrive at our rounded target price of EUR33.	The biggest downside risk, in our view, is a severe downturn in the global and German economies that could spill over to Austria and CEE, leading to more corporate defaults. Other downside risks include further interest rate cuts by the ECB, which would hurt the bank's deposit margins even more or an even higher charge for Croatian FX mortgages could be negative for sentiment as well. The introduction of a Czech banking tax, although unlikely, could harm profits of the most important business unit, while a potential placing of the 9.1% stake owned by Spain's CaixaBank could have a negative impact on the shares (however, no statement on this has been made by either company).
Svenska Handelsbanken SHBA SS Current price: SEK116.6 Target price: SEK98.0 Rating: Reduce Up/Downside: -16%	Our target price is set using a 2017e WEV (warranted equity value) equation discounted back to present value terms. We assume a 9% cost of equity and zero growth, and for 2017e we estimate an ROTE of 13.5%. This gives us a P/TNAV of 1.5x. We also adjust our valuation for surplus/deficit CT1 capital versus a benchmark level of 20%.	We see potential upside risks to our target price coming from stronger-than-expected growth in core markets outside Sweden or better-than-expected Swedish export growth which could positively impact SHB's domestic corporate segment.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Building material and construction

	Valuation	Risks
ACS ACS SM Current price: EUR31.4 Target price: EUR35 Rating: Buy Up/downside: 11.5%	We value ACS based on a SOTP valuation where we apply peer group-derived adjusted EV/EBITA multiples of 7x to 12x to our 2016e estimates for all the different contracting activities. We value ACS's stake in Hochtief (HOT GR, EUR83.8) at our target price of EUR84 and all the Iberdrola (IBE SM, EUR6.516) derivatives and direct exposure at market price. All other assets are valued on book values or announced cash proceeds. Finally, our aggregate equity value for all segments is adjusted for intra-year working capital swings and minorities on group level. Our target price implies 11.5% upside and we rate the stock Buy. Our target price for Hochtief is based on a SOTP where we apply peer group-derived adjusted EV/EBITA multiples of 7x to 10x to our 2016e estimates for all contracting activities. We value Hochtief's real estate development activities and concessions at adjusted book values. Our enterprise value is adjusted for net cash, working capital swings, pension liabilities and minorities. Our target price is EUR84 and we rate Hochtief Buy. Key downside risks: (1) Weaker-than-expected demand, particularly at Hochtief Asia-Pacific; (2) poor project execution; (3) inability to drive a sustainable turnaround at Hochtief Europe; (4) a significant strengthening of the euro vs AUD/USD; (5) a slower and more costly scaling down of the remaining real estate development activities; (6) poor cash flow from operations including the collection of legacy receivables.	Downside: (1) a deterioration of economic activity as well as sentiment in and towards key markets such as Spain, the US, Australia and Mexico; (2) declining share prices of Hochtief and Iberdrola, which could result in a reduced value contribution to ACS; (3) project execution problems; (4) expensive acquisitions and a lack of further debt reduction momentum; (5) foreign currency tailwinds; and (6) lack of ability to continue to grow international activities.
Eiffage FGR FP Current price: EUR56.99 Target price: EUR64 Rating: Buy Up/downside: 12.3%	We value Eiffage based on a SOTP valuation where we value its contracting activities at peer group-derived adjusted EV/EBITA 2016e multiples of 6x to 9x. Its concessions activities are valued at DCF using a WACC of 5.5%. At the group level we adjust for pensions, pre-payments and non-strategic assets. Our target price implies 12.3% upside and we rate the stock Buy.	Downside: (1) inability to increase margins in underperforming Infrastructure and Energy division; (2) a lack of recovery in the construction sector in France in 2016; (3) inability to gain sizable contracts in the UK; (4) lower than expected traffic on motorways in the years to come on its portfolio of concessions (APRR, Area, A65); (5) much higher interest rates which would reduce the benefits of refinancing.
NCC NCCB SS Current price: SEK270.1 Target price: SEK320 Rating: Buy Up/downside: 18.5%	We value NCC based on a SOTP valuation where NCC Construction is valued at 10.0x EV/EBITA 2016e (in line with its closest peer Skanska), NCC Housing is valued based on the 2014 year-end book value, NCC Property Development is valued at market value, while the more capital-intensive NCC Roads business is valued at 12.0x EBITA 2016e, equivalent to 7.0x EV/EBITDA 2016e. The combined value is adjusted for holding costs, adjusted net debt, working capital fluctuation, pensions and minorities to derive at a rounded fair value of SEK320. Our target price implies 18.5% upside and we rate the stock Buy.	Downside: (1) deterioration in economic activity and consumer confidence in key markets, including St. Petersburg; (2) overestimation of demand at specific housing sites; (3) weaker land bank quality than expected; (4) poor project execution in Construction; (5) deviation from the disciplined pricing in Roads; (6) investor appetite for capital-intensive development activities may deteriorate if ROCEs achieved are unsatisfactory; (7) a new strategy could limit the dividend potential if growth is targeted in the development businesses; (8) a significant devaluation of key currencies (RUB, EUR, NOK) against the SEK.
LafargeHolcim LHN VX Current price: CHF56.2 Target price: CHF42 Rating: Reduce Up/downside: -25.3%	We derive our CHF42 target price using 7.0x 1-year forward target EV/EBITDA, a 19% discount to sector average, as we expect ROIC (5.3%) in 2017 to fail to exceed the cost of capital (7.3%) due to a weak geographical footprint. Our target price implies 25.3% downside and we rate the stock Reduce.	Upside: (1) European markets (24% of 2014 sales) stronger than expected; (2) emerging markets (59% of 2014 sales) start growing at stronger rate and price growth meets cost inflation; (3) New CEO maintains or increases existing standalone self-help programme.
Wienerberger WIE AV Current price: EUR16.365 Target price: EUR13.5 Rating: Reduce Up/downside: -17.5%	We apply a 7.5x 1-year-forward EV/EBITDA multiple to our 2017 estimate broadly representing a 15% discount to our sector reference level. The discount is at the high-end of the spread versus the sector in the last years. Our target price implies 17.5% downside and we rate the stock Reduce.	Upside: (1) better-than-expected demand and pricing for clay blocks, bricks and tiles in key residential construction markets; (2) better-than-expected demand for pipes & pavers which could outperform expectations (limited track record), particularly if public infrastructure spending is picking up again; (3) a new cost-cutting programme or better operating execution than currently assumed; (4) improved sentiment towards European residential construction; (5) further industry consolidation.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Business Services

	Valuation	Risks
Experian EXPN LN Current price: 1,114p Target price: 1,290p Rating: Buy Up/downside: 15.8%	Our fair value target price of 1,290p is derived by applying a calendarised 2016 PE multiple of 20x which is akin to the multiples its US peer trade at. For a defensive business such as Experian, we think the upside is fairly attractive.	Key downside risks: (1) FX risk from Brazil. (2) banking and retail sector mergers in the US, UK and Brazil; (3) increased regulator pressure; and (4) expensive looking acquisitions.
Adecco* ADEN VX Current price: CHF67.90 Target price: CHF90 Rating: Buy Up/downside: 32.5%	We think Adecco's share price, in essence, is pricing in low growth and static margins; barring a recession, we believe there is little downside risk. We see more profit growth, and guidance set to be beaten. Our fair value target price of CHF90 is derived by applying the average mid-cycle FY2 PE multiple of 15.7x to our 2016e EPS estimate of EUR5.3 (CHF/EUR spot exchange rate of 1.08).	Key downside risks: (1) As for all staffers, the advantages of tight supply can only amplify the advantages of solid demand; should labour demand weaken not much will help. (2) Time-to-hire expands more than expected, as finding staff is more difficult, and slows profit growth. (3) Adecco has a multi-brand strategy but has flirted with single brand approaches in some markets; a single brand approach may damage candidate draw, and as such growth.
Aggreko AGK LN Current price: 929p Target price: 800p Rating: Reduce Up/downside: -13.8%	Aggreko's multiples imply that the market expects the business to be ex-growth but with stable returns. Further pressure on returns should drive multiple de-rating. We arrive at our fair value target price of 800p for Aggreko by applying a PE multiple of 15x to our 2016 EPS estimate. This equates to an EV/EBITDA of 5.0x (pre-structural growth), and EV/CE of 1.6x (consistent with RoCE 12%, 8% WACC and lower growth environment).	Key upside risks: (1) a recovery in Power Projects order income; (2) a turn in new orders for turbines and power equipment; (3) a recovery in mining exploration; (4) a recovery in the oil price; (5) turnaround in situation in Yemen; (6) better outlook for EM markets; and (7) stronger EM currency.

Priced as at close on 2 November 2015 * except for Adecco for which TP changed on 13 November with the stock priced at 11 November. Source: HSBC estimates

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HSBC

Capital Goods

	Valuation	Risks
Schneider Electric SU FP Current price: EUR55.27 Target price: EUR72.00 Rating: Buy Up/downside: 30.3%	Our target price of EUR72 is driven by a through-cycle cash-ROIC projection of 9.5% and a target MACC of 8.5%, equating to an exit 2017e PE of 14.2x.	Key downside risks include: Weaker-than-expected recovery in the North American market and a steeper decline in construction markets in DM. Schneider may not be able to execute the smaller transactions it has planned.
Atlas Copco ATCOA SS Current price: SEK222.70 Target price: SEK280.00 Rating: Buy Up/downside: 25.7%	We use a market assessed cost of capital approach (MACC) to value stocks in our sector. This is essentially a reverse DCF, although the model is driven by a through-cycle Cash-ROIC assumption. Our target price of SEK280 is driven by a through-cycle cash-ROIC projection of 16% and a target MACC of 6%, equating to an exit 2017e PE of 21.3x.	Key downside risks include: (1) any further deterioration in pricing power; and (2) any significant recovery in the SEK and/or EUR.
Volvo VOLVB SS Current price: SEK89.55 Target price: SEK120.00 Rating: Buy Up/downside: 34.0%	Our target price of SEK120 is driven by a through-cycle cash-ROIC projection of 9.0% and a target MACC of 12.8%, equating to an exit 2017e PE of 13.0x.	Key downside risks include: (1) weaker-than-expected progress on cost-cutting; and (2) any reversal of the current strong FX tailwinds.
Philips PHIA NA Current price: EUR24.67 Target price: EUR19.00 Rating: Reduce Up/downside: -23.0%	Our target price of EUR19 is driven by a through-cycle cash-ROIC projection of 7.0% and a target MACC of 10.2%, equating to an exit 2017e PE of 10.9x.	Key upside risks include: the ACCELERATE! programme may prove to be much more self-sustaining, and hence lower costs may accrue, associated with a sustainable improvement.
Kone KNEBV FH Current price: EUR39.00 Target price: EUR30.00 Rating: Reduce Up/downside: -23.1%	Our target price of EUR30 is driven by a through-cycle cash-ROIC projection of 16.0% and a target MACC of 5.8%, equating to an exit 2017e PE of 14.8x.	Key upside risks include: (1) stronger growth in China and North America than we expect, and (2) moderation of competition and pricing pressure in the services sector.
Schindler SCHN SW Current price: CHF163.10 Target price: CHF125.00 Rating: Reduce Up/downside: -23.4%	Our target price of CHF125 is driven by a through-cycle cash-ROIC projection of 13.0% and a target MACC of 8.5%, equating to an exit 2017e PE of 16.8x.	Key upside risks include: (1) stronger growth in China and in North America than we expect; (2) a moderation of competition and pricing pressure in the services sector.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Chemicals

	Valuation	Risks
BASF BAS GR Current price: EUR75.2 Target price: EUR88 Rating: Buy Up/downside: 17.1%	Our fair value target price of EUR88 is based on peer group multiples (two thirds) and DCF (one-third). Our DCF valuation – risk-free rate: 0.6% in 2015e-19e and 3.5% thereafter, equity risk premium: 5.2%, beta: 1.0 – yields a fair value of EUR98 reflecting lower long term forecasts. We use the relationship between EV/sales and EBITDA margin in 2015e relative to the European chemical sector. Based on our 2015e EBITDA margin of 14.4%, generates a fair value of EUR85, implying an EV/sales multiple of 1.2x.	Downside risks: (1) a significant slowdown in the global economy as for any Classic chemicals company; (2) 2015 targets not being met; (3) mega acquisitions – one of the temptations that the chemical industry has succumbed to in the past is boosting growth through large acquisitions; (4) oversupply – if the capacity additions we see coming online over the next two to three years happen, we believe a number of products will be oversupplied, putting pressure on margins, particularly polyurethane intermediates.
Johnson Matthey* JMAT LN Current price: 2690p Target price: 3500p Rating: Buy Up/downside: 30.1%	Our fair value target price of 3,500p is based on the equal-weighted average of our DCF and multiple approaches. Our DCF valuation – risk-free rate: 0.6% in 2015-19e and 3.5% thereafter, equity risk premium: 5.2%, beta: 1.0 – yields a fair value of 3627p. We calculate our multiples fair value using the long-term relationship between EV/IC and ROIC, with a 2016e ROIC of 13.8%. This generates a fair value of 3,423p and implies an EV/IC of 2.9x. The equal weighted average is a value of 3525p, which we have rounded down to 3,500p to set our target price.	Downside risks to our rating include less favourable auto and truck volume/mix growth as well as new technologies. Diesel engines tend to need more complex auto catalyst systems, so any change in Europe to the gasoline/diesel mix would have a detrimental impact on Emission Control Technologies' earnings. Moreover, any new technology that could significantly reduce the use of platinum group metals (PGM) in autocatalysis would be a significant risk. A reduction in the supply of platinum; the recent industrial action in the South African platinum industry has raised concerns about the shortage of platinum, particularly in sponge form. Any new technology that could significantly reduce the use of platinum group metals (PGM) in auto catalysts would be a significant risk.
Umicore UMI BB Current price: EUR38.7 Target price: EUR39 Rating: Hold Up/downside: 0.8%	Our fair value target price of EUR39 is based on the equal-weighted average of our DCF, relative sector regression and multiple approach. Our DCF valuation – risk-free rate: 0.6% in 2015-19e and 3.5% thereafter, equity risk premium: 5.2%, beta: 1.0 – yields a fair value of EUR43.6. Our sector relative valuation approach (EV/IC vs ROIC/WACC regression) indicates a fair value of EUR37.5 using an EV/IC multiple of 1.8x. We calculate our multiples fair value using the long-term relationship between EV/IC and ROIC/WACC, with a 2016e ROIC of 12.2%, which generates a fair value of EUR37.7, implying an EV/IC multiple of 1.8x.	Downside risks to our rating include longer shutdowns in the Hoboken smelter as new capacity is added, lower metal prices and declines in auto volumes. Upside risks to our rating include stronger economic growth, particularly in the construction and electronic end markets, and a spike in the gold, platinum, palladium and silver price, which would significantly benefit profitability in Recycling.
Lanxess LXS GR Current price: EUR49.8 Target price: EUR45 Rating: Hold Up/downside: -9.6%	Our fair value target price of EUR45 is based on an equal weighted average of our DCF, relative sector regression and relative multiple approaches. Our DCF valuation – risk-free rate: 0.6% in 2015-19e and 3.5% thereafter, equity risk premium: 5.2%, beta: 1.1 – yields a fair value of EUR55 (vs EUR61 on lower mid-term growth assumptions). Our sector relative valuation approach (EV/IC vs ROIC/WACC regression) indicates a fair value of EUR33 based on ROIC/WACC of 1.02x (unchanged). We use a sector EV/EBITDA multiple approach, which yields a fair value of EUR47. The peer group multiple is 7.6x (from 7.8x) for the Classic sub-sector for 2015e. We adjust for Lanxess' historical discount of 6% to the Classic peer group but add a 10% restructuring premium.	Downside and upside risks include lower/higher supply discipline; stronger/weaker than expected pricing pressure from new supply; a stronger/weaker euro; windfall losses/gains from sudden changes in raw material costs; failure to deliver on cost reduction targets; customer destocking or restocking; value dilutive/accretive changes to the portfolio.

Priced as at close on 2 November 2015, * except for Johnson Matthey for which TP changed on 20 November with the stock priced at 19 November. Source: HSBC estimates

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Food Retail

	Valuation	Risks
Metro MEO GR Current price: EUR28.03 Target price: EUR36.00 Rating: Buy Up/downside: 28.4%	We believe a sum of the parts remains the most appropriate way to value Metro. Applying sector multiples to each of Metro's business units and taking into account our current estimates we derive fair value per share of EUR36. Multiples include: European food retail sector average EV/EBITDA of 7.0x applied to the Food Retail/Cash & Carry; sector average of the consumer electronics peers (Fnac, BestBuy, Darty, and Dixons) of 6.0x EV/EBITDA to the Consumer Electronics business.	Downside risks: (1) a worsening environment in Europe, (2) deterioration in Russia and increasing political pressure, and (3) an unfavourable currency effect from international operations.
Booker BOK LN Current price: 186p Target price: 230p Rating: Buy Up/downside: 23.5%	We use a DCF model to derive our target price of 230p. Our main DCF assumptions include a WACC of 6.7% based on a risk-free rate of 3.5%, equity risk premium of 4.0% and a beta of 1.0. Our terminal margin stands at 4.3%, while our terminal growth is 1%.	Downside risks include: (1) increase in competitive activity, (2) deflation becoming firmly embedded, (3) unexpected management change.
DIA DIA SM Current price: EUR5.86 Target price: EUR7.00 Rating: Buy Up/downside: 19.4%	We use a DCF model to arrive at our fair value target price of EUR7.0. Our main assumptions include a WACC of 9.0%, based on a risk-free rate of 3.5%, an equity risk premium of 5.5%, a beta of 1.1 and a terminal margin assumption of 4.2%.	Downside risks include: (1) macroeconomic risks as DIA derives 90% of EBIT from Iberia, (2) tougher pricing environment, (3) increased labour costs in EM, and (4) input cost inflation.
Colruyt COLR BB Current price: EUR44.97 Target price: EUR37.00 Rating: Reduce Up/downside: -17.7%	We use a DCF model to derive our target price of EUR37. Our main DCF assumptions include a WACC of 8.77%, based on a risk-free rate of 3.5%, an equity risk premium of 5.5% and a beta of 1.1. Our terminal margin stands at 5.2%, while our terminal growth is 1%.	Upside risks include: (1) a return to significant food inflation, (2) a recovery in consumer spending, (3) lower wage indexation, (4) a higher shareholder return than the recurrent share buyback, (5) a strategic acquisition in France to achieve critical mass, (6) an improvement in French profitability.
Sainsbury SBRY LN Current price: 267p Target price: 200p Rating: Reduce Up/downside: -25.1%	We use a DCF model to arrive at our fair value target price of 200p. Our main DCF assumptions include a WACC of 7.3%, based on a risk-free rate of 3.5% an equity risk premium of 4.0%, a beta of 1.0 and a terminal margin assumption of 2.2%.	Upside risks include: (1) any potential full bid from QIA (IBTimes UK); (2) significant market share gains and (3) a strong margin improvement.

Priced as at close on 2 November 2015. Source: HSBC estimates

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General Retail

	Valuation	Risks
Hennes & Mauritz HMB SS Current price: SEK331 Target price: SEK375 Rating: Buy Upside: 13.3%	We have a target price of SEK375. Our target price is based on our APV (adjusted present value) analysis. We assume an unchanged risk-free rate of 3.5%, equity risk premium of 5.5% for Sweden and beta of 0.84.	Downside risks: (1) adverse weather; (2) adverse FX; (3) significant increase in input costs; (4) structural increase in competition in key markets.
Marks & Spencer MKS LN Current price: 520p Target price: 700p Rating: Buy Upside: 34.6%	Our TP of 700p is based on an adjusted present value (APV) analysis. We assume a risk-free rate of 3.5%, an equity risk premium of 4%, a stock-specific beta of 0.9x, terminal growth of 1% and an implied WACC of c7%.	Downside risks include: (1) deterioration in UK consumer confidence; (2) increase in sector promotional activity; (3) faster-than-expected increase in interest rates. .
GrandVision GVNV AS Current price: EUR24.9 Target price: EUR28.0 Rating: Buy Upside: 12.4%	We have a Buy rating and a fair value target price of EUR28, based on APV (adjusted present value) analysis. Our APV analysis assumes a risk-free rate of 3.5%, an equity risk premium of 5.5%, a company specific beta of 0.6 and terminal growth of 3.0%.	Downside: (1) potential impact of new market entrants in major/existing developed markets; (2) the development of new channels to market; (3) the adoption of alternative eye care solutions.
Inditex ITX SM Current price: EUR34.1 Target price: EUR29.0 Rating: Hold Downside: -14.9%	We have a target price of EUR29. Our target price is based on APV analysis in which we assume a risk-free rate of 3.5%, an equity risk premium of 5.5%, a beta of 0.8 and terminal growth rate of 1%.	Upside risks: stronger-than-expected contribution from online; faster-than expected recovery in pan-European consumer spending trends. Downside risks: adverse weather, adverse FX, tough comparatives, economic slowdown in eurozone/EM.
Kingfisher KGF LN Current price: 356p Target price: 355p Rating: Hold Downside: -0.1%	We have a target price of 355p based on APV (adjusted present value) analysis. We assume a risk-free rate of 3.5%, an equity risk premium of 4%, a beta of 1.03 and a terminal growth rate of 0.5%.	Upside risks: (1) short-term rebound in France industry data; (2) broad-based improvement in the UK and French macroeconomic outlook; (3) increase in cash returns to shareholders; (4) bid speculation. Downside risks: (1) adverse weather; (2) increased pricing pressure in key end-markets; (3) the reversal of recent positive UK housing market trends; (4) further material deterioration in French consumer confidence/housing market trends.

Priced as at close on 02 November 2015. Source: HSBC estimates

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Health Care Equipment & Services

	Valuation	Risks
Straumann STMN SW Current price: 283.75 Target price: CHF315 Rating: Buy Up/downside: 11%	Our valuation is based on a DCF model (ERP 4.0%, RFR 3.5%, beta 0.9), which yields a target price of CHF315.	Primary risks to our Buy rating are sluggish growth in Europe and a slowdown in the US, China and Latin American markets and falling consumer confidence as the industry is fairly cyclical, as this is primarily an out-of-pocket market. In addition, in the medium term the ongoing competition from value/discount players and increasing competition by Zimmer/Biomet and Nobel Biocare/Danaher could imply risk.
Sartorius SRT3 GR Current price: EUR206 Target price: EUR225 Rating: Buy Up/downside: 9.2%	Our valuation is based on a DCF model (ERP 5.5%, RFR 3.5%, equity beta 0.85), which yields a target price of EUR225.	Downside risks to our rating include the failure to identify and integrate suitable acquisition targets, failure to gain market share in the US and lower-than-anticipated operating leverage.
Amplifon AMP IM Current price: EUR7.10 Target price: EUR8.1 Rating: Buy Up/downside: 14.1%	Our valuation is based on a DCF model (ERP 5.5%, RFR 3.5%, equity beta 0.9), which yields a target price of EUR8.1.	Downside risks include stronger competition from large retail chains (including retail managed by manufacturers, shop-in-shop store providers, pharmaceutical chains) which could lead to weaker operating leverage and margin development.
Getinge* GETIB SS Current price: SEK217 Target price: SEK192 Rating: Reduce Up/downside: -11.5%	Our valuation is based on a DCF model (ERP 5.5%, RFR 3.5%, beta 0.9), which yields a target price of SEK192.	Upside risks: higher/faster-than-expected margin improvements from the efficiency programme, lower-than-expected R&D costs, faster-than-expected progress with the FDA and lower-than-anticipated pricing pressure.

Priced as at close on 2 November 2015 * except for Getinge on which we initiated coverage on 11 November with the stock priced at 5 November. Source: HSBC estimates

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Home & Personal Care and Food Producers

	Valuation	Risks
Associated British Foods ABF LN Current price: 3,434p Target price: 3760p Rating: Buy Up/downside: 9.5%	We have a 3750p TP, based on our (rounded) SOTP analysis. Critical in that is our valuation of Primark which we value at c.GBP24bn, which equates to over 80% of the ABF group value. Our Primark valuation is based on our DCF analysis which uses a 7.5% cost of equity and 10-year explicit forecasts to 2025e, followed by a 10 year holding period when we assume 40 new stores pa and 1% LFL growth. Grocery is valued at c.GBP4.1bn, Sugar at GBP1.2bn and Ingredients at c.GBP1.2bn.	Downside risks: 1) Primark store roll-out is slower than expected; 2) unsuccessful launch of Primark in the US; 3) margin pressure due to competitor or market issues; 4) EU Sugar regime reform leading to excess supply in EU sugar markets.
Greencore GNC ID Current price: 306p Target price: 360p Rating: Buy Up/downside: 18%	We have a 360p TP, based on our DCF analysis. We use a cost of equity of 7.5%, made up of a risk free rate of 3.5%, an equity risk premium of 4.0% and a Beta of 1.0x. We use explicit 3 year forecasts including the assumption that EBITA margins rise by c.60bp to 7.1% by 2017e. We have a 10-year holding period with sales growth of 5% and flat margins and a perpetuity growth rate of 2%.	Downside risks to Buy rating include: 1) slower-than-anticipated category growth rates; 2) operational issues negatively affecting margins which could include health and safety, start-up costs, higher impact of national living wage in the UK; 3) a protracted downturn in employment particularly in the service sector; 4) loss of major supply agreement with key customers.
Hilton Food Group HFG LN Current price: 484.5 Target price: 545p Rating: Buy Up/downside: 12.5%	We have a 545p TP, based on our DCF analysis. We use a cost of equity of 7.5%, made up of a Risk Free Rate of 3.5%, an equity risk premium of 4.0% and a Beta of 1.0x. We use explicit 3 year forecasts including the assumption that EBITA margins rise by c.50bp to 2.9% by 2017e. We have a 10 year holding period with sales growth of 4% and flat margins and a perpetuity growth rate of 2%.	Downside risks include: 1) contracts not being renewed with retailer, or renewed at less-favourable terms; 2) customer sales falling below expectations; 3) unfavourable exchange rate movements; 4) outbreaks of disease, feed contamination, product adulteration, general food scares or negative media stories related to red meat consumption.
Beiersdorf* BEI GR Current price: EUR87.7 Target price: EUR81.5 Rating: Hold Up/downside: -7%	We have a EUR81.5 TP, based on our DCF analysis. We use a cost of equity of 7.3%, made up of a risk free rate of 3.5%, an equity risk premium of 4.75% and a Beta of 0.8x. We use explicit five-year forecasts including the assumption that EBITA margins rise from 13.7% in 2014 to 16.7% by 2020e. We have a 10 year holding period with sales growth of 4% and flat margins and a perpetuity growth rate of 2%.	Upside: 1) Acquisitions which boost earnings and growth 2) Faster organic growth driven by successful brand innovation or more favourable market conditions 3) Higher than expected margins 4) Further EUR weakness. Downside: 1) Deterioration in organic growth or margins in either Consumer or tesa 2) Over-priced acquisitions, or a failure to integrate acquisitions 3) EUR strength

Priced as at close on 2 November 2015, *except Beiersdorf which was upgraded to Hold on 5 November and it is priced at 4 November. Source: HSBC estimates

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Insurance

	Valuation	Risks
Prudential PRU LN Current price: 1,529p Target price: 1,985p Rating: Buy Up/downside: 30%	Our 1,985p TP is based on a weighted average of five different methodologies. We apply a 20% weighting to each of the P/TNAV, P/EV, PE, P/Op FCF and Appraisal value methodologies. We assume a 10.1% cost of equity. A detailed explanation of our valuation methodology and target price derivation is provided in *European insurance: The yield conundrum*, 20 April 2015.	Downside risks: (1) Change in focus and priorities under a new CEO; (2) worse-than-forecast life sales and margins; (3) undisciplined inorganic expansion; (4) rising regulatory standards, particularly across Asia – we think this is a competitive advantage for PCA, but markets may take time to recognise this; (5) risk management failure; (6) Solvency II and G-SII outcomes being worse than currently anticipated.
Generali G IM Current price: EUR17.3 Target price: EUR21.5 Rating: Buy Up/downside: 24%	Our EUR21.5 TP is based on a weighted average of five different methodologies. We apply a 20% weighting to each of the P/TNAV, P/EV, PE, P/Op FCF and Appraisal value methodologies. We assume a 9.3% cost of equity. A detailed explanation of our valuation methodology and target price derivation is provided in *European insurance: The yield conundrum*, 20 April 2015.	Downside risks: (1) Italian sovereign risk; (2) non-life operating earnings being less resilient than expected; (3) property portfolio performs poorly; (4) a significant rise in lapse and surrender rates; (6) risk management failure; (7) Solvency II and G-SII outcomes are stricter than currently anticipated.
PZU PZU PW Current price: PLN377.5 Target price: PLN359.0 Rating: Reduce Up/downside: -5%	Our PLN359.0 TP is based on a weighted average of five different methodologies. We apply a weighting of 30% to P/TNAV, 5% to P/EV, 45% to PE, 5% to P/Op FCF and 15% to Appraisal value methodologies. We assume a 9.5% cost of equity. A detailed explanation of our valuation methodology and target price derivation is provided in *European insurance: The yield conundrum*, 20 April 2015.	Upside risks: (1) better-than-expected earnings; (2) further initiatives on cost savings; (3) capital repatriation to shareholders better than expected.
Euler Hermes ELE FP Current price: EUR84.0 Target price: EUR80.0 Rating: Reduce Up/downside: -5%	Our EUR80 TP is based on a weighted average of four different methodologies. We apply a weighting of 20% to P/TNAV, 20% to PE, 20% to P/Op FCF and 40% to Appraisal value methodologies. We assume a 9.2% cost of equity. A detailed explanation of our valuation methodology and target price derivation is provided in *European insurance: The yield conundrum*, 20 April 2015.	Upside risks: (1) Acceleration in the group's top line above our expectations, thanks to better-than-expected GDP growth; (ii) faster development of its trade credit products in high-growth markets and a successful strategy to broaden its product mix; (3) Euler Hermes' portfolio continuing to perform better on the underwriting side and the group achieving a better calendar-year loss ratio, or reserve releases exceeding our expectations; and (4) any clarification by the group on its capital management strategy.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Integrated Oils

	Valuation	Risks
Royal Dutch Shell RDSA LN Current price: 1,712p Target price: 1,960p Rating: Buy Up/downside: 14%	Our estimate of Shell's SoP value is USD195bn, or 2027p/share. As with all the large integrated oils, we do not include any exploration upside in this figure. Our SoP estimates are based on DCF, with a 9% discount rate which is based on: (1) a global risk-free rate of 3.5%, (2) a sector beta of 1.0, (3) a 6% average equity market risk premium, (4) an average pre-tax cost of debt of 5% and 25% target gearing, (5) an average sector tax rate of 45%, and (6) a 2% inflation adjustment. For downstream and other perpetuity businesses we assume a 2% long-term growth rate in line with historical rates of global energy demand growth. For the upstream, given the wasting nature of the assets we assume no perpetuity but estimate the value of commercial resources until produced to full depletion. Shell's current share prices represent discounts of 16% and 15% to our SoP valuations for the A and B shares, respectively. We apply a 5% discount, consistent with that of the other super majors (apart from Exxon), which generates an implied fair value of 1925p/share. Shell's forward PE relative to the European market has averaged 76% over the past three years. Our fair value is based on an average 85% target PE relative, as we believe recent multiples are being overly depressed by sentiment towards the sector in general. Our forward estimates imply an average fair value of 1970p. Taking this in conjunction with our SoP approach gives us implied target prices which we round to 1,960p for both the A and B shares. These target prices indicate share price upside of 14% respectively vs the current share prices on both stocks. We rate both Shell A and B shares as Buy due to our positive view of the sector's risk/reward balance and Shell's attractive prospective return including its c7% prospective dividend yield	In addition to the broad risks from macro conditions, we see the following main company-specific risks. Downside: (1) the North American upstream business is under severe pressure and losses are likely to be extended in the current environment; (2) there are regulatory and other risks that could come in the way of completion of the proposed acquisition of BG.
Total FP FP Current price: EUR46.2 Target price: EUR51.0 Rating: Buy Up/downside: 10%	Our estimate of Total's SoP value is USD142bn, or EUR53/share. Our SoP estimates are based on DCF, with a 9% discount rate which is based on: (1) a global risk-free rate of 3.5%; (2) a sector beta of 1.0; (3) a 6% average equity market risk premium; (4) an average pre-tax cost of debt of 5% and 25% target gearing; (5) an average sector tax rate of 45%; and (6) a 2% inflation adjustment. For downstream and other perpetuity businesses, we assume a 2% long-term growth rate in line with historical rates of global energy demand growth. For the upstream, given the wasting nature of the assets, we assume no perpetuity, but estimate the value of commercial resources until produced to full depletion. Total's current share price represents a discount of 13% to our SoP valuation, in line with the super major average. We think on a 12-month view this discount should close as the free cash turnaround becomes more apparent. We apply a 5% discount, which generates an implied fair value of EUR50.2/share. Based on Bloomberg consensus estimates, Total's forward PE relative to the European market has averaged 72% over the past three years. Our target PE relative is 90% as recent evidence of cash generation has reinforced our view that improving free cash flow should result in a re-rating of the stock; on this basis, our forward estimates imply a fair value of EUR51.6/share. Taking this in conjunction with our SoP approach gives us an average target price of EUR51, equivalent to USD55/ADR (TOT US, CP USD50.0). The target price implies upside of 10% vs the current share price. We rate Total Buy due to our positive view of the sector's risk/reward balance and Total's attractive prospective return including its c5% prospective dividend yield. Total is an HSBC Europe Super Ten portfolio constituent.	Downside: General risks include oil and gas prices or refining, marketing or chemicals margins below our modelling assumptions. Company-specific risks include Total's asset concentration in certain countries, notably Libya, Russia and Yemen. Unrest in Yemen has halted output at Yemen LNG and could affect sentiment. Total's dividend is uncovered by organic cash flow, which may lead to investor perceptions of risks to the dividend in case of continued crude price weakness. Finally, as the largest component of the French CAC40 Index, Total could be exposed to downside in the case of a correction in French or broader Eurozone markets.

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	Valuation	Risks
ENI ENI IM Current price: EUR14.9 Target price: EUR15.9 Rating: Hold Up/downside: 6%	Our estimate of ENI's SoP value is USD73bn, or EUR18.1/share. As with all the major integrated oils, we do not include any exploration upside in this figure. Our SoP estimates are based on a DCF, with a 9% discount rate which is based on: (1) a global risk-free rate of 3.5%; (2) a sector beta of 1.0; (3) a 6% average equity market risk premium; (4) an average pre-tax cost of debt of 5% and 25% target gearing; (5) an average sector tax rate of 45%; and 6) a 2% inflation adjustment. For downstream and other perpetuity businesses, we assume a 2% long-term growth rate, in line with historical rates of global energy demand growth. For the upstream, given the wasting nature of the assets, we assume no perpetuity, but estimate the value of commercial resources until produced to full depletion. ENI's current share price represents a discount of 18% to our SoP valuation. We apply a target price discount to SoP of 5%, equivalent to that for the supermajors (except Exxon) to reflect reduced balance sheet with the impending deconsolidation of Saipem's debt. This discount yields a fair value of EUR17.1/share. Based on Bloomberg consensus estimates, ENI's two-year forward PE relative to the European market has averaged 88% for the past three years. We target a PE relative of 95% to reflect ENI's reduced balance sheet risk. This would imply a fair value of EUR15.2/share vs EUR13.8 previously. Taking this in conjunction with our SoP approach gives us a target price of EUR15.9, equivalent to USD34/ADR (E US, CP USD32.3). Our target price is 7% above the current market price and we rate the stock Hold given ENI's above-average geographical risk and what we believe to be less capex flexibility than most peers.	Upside: In our view, some of the biggest risks to our investment view on ENI are variances in crude oil and natural gas prices, as well as downstream margins, relative to our assumptions. From a company-specific perspective, we think the main upside risks could come from: (1) more rapid progress towards monetising Mozambique LNG or potentially the Congo; (2) more significant exploration success; or (3) a more rapid recovery in the Italian gas market as a result of the weakness in crude prices. Downside: (1) delays to the key Mozambique LNG project; (2) political risk, which looks above average given the geographic spread of ENI's assets, notably its exposure to North Africa and Venezuela.
Repsol REP MC Current price: EUR12.3 Target price: EUR13.0 Rating: Hold Up/downside:6%	Our estimate of Repsol's SoP value is USD26.4bn, or EUR17.6/share. Our SoP estimates are based on a DCF, with a 9% discount rate, which is based on: (1) a global risk-free rate of 3.5%; (2) a sector beta of 1.0; (3) a 6% average equity market risk premium; (4) an average pre-tax cost of debt of 5% and 25% target gearing; (5) an average sector tax rate of 45%; and (6) a 2% inflation adjustment. For downstream and other perpetuity businesses, we assume a 2% long-term growth rate in line with historical rates of global energy demand growth. For the upstream, given the wasting nature of the assets, we assume no perpetuity but estimate the value of commercial resources plus technical resources until produced to full depletion. We use a 15%target price discount to reflect balance sheet and integration risks around the Talisman acquisition. This implies a fair value of EUR14.9/share. Repsol's two-year forward PE relative to the European market has averaged around 91% in the past three years. We use a 75% PE relative to account for integration and balance sheet risks from the Talisman acquisition given the weak prevailing crude price environment. On the basis of our estimates for 2016-17, this implies a fair value of EUR12.0. Taking this in conjunction with our SoP approach and rounding gives us an average target price EUR13.0/share. This implies upside of 6%. We rate the stock Hold given the above average balance sheet risks in the current environment, and the likelihood of negative near-term earnings momentum from weaker refining margins.	Upside: Apart from the risk of crude prices and downstream margins being above our assumptions, the main company-specific risks to our investment stance, in our view, are: (1) a rapid delivery of a significant portion of the EUR6.2bn of planned disposals, (2) quicker-than-expected delivery of the synergy and efficiency benefits targeted, (3) a return of refining margins to recent high levels. Downside risks include 1) further weakness in refining margins, given Repsol's above average exposure and 2) integration and balance sheet risks arising from the Talisman transaction

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Luxury Goods

	Valuation	Risks
LVMH MC FP Current price: EUR167.9 Target price: EUR195 Rating: Buy Up/downside: 16%	We have a DCF-based target price of EUR195. Our DCF assumptions are: risk-free rate of 3.5%, equity risk premium of 5.5%, sector beta of 1.1 and specific beta of 0.85, EBIT growth 2015-25e CAGR of 9%, EBIT growth 2025-45e CAGR of 4%, fade period 2045-53e, and a WACC of 8.43%. We rate the stock a Buy as we think the diversified nature of its asset portfolio should translate into greater earnings resilience.	Downside risks include LV brand momentum deteriorating, much greater destocking within the wholesale businesses (Wines & Spirits, Watches and Perfumes) and value destruction linked to M&A activities (past and future).
Richemont CFR VX Current price: CHF84.3 Target price: CHF100 Rating: Buy Up/downside: 19%	We have a DCF-based target price of CHF100. Our DCF assumptions are: risk-free rate of 3.5%, equity risk premium of 4%, sector beta of 1.1 and specific beta of 1.2, EBIT growth 2015-25e CAGR of 8.3%, EBIT growth 2025-45e CAGR of 4%, fade period 2045-53e, and a WACC of 8.78%.	Downside risks include adverse currency changes, the Cartier watch launch Clé de Cartier generating lower-than-expected sales, underperforming divisions (such as Lancel and Dunhill) weighing more heavily than we forecast, further corruption crackdowns in China reducing demand, and any threats to travel. Operating deleverage from tough business in Hong Kong could also affect margins more than we expect.
Moncler MONC IM Current price: EUR14.76 Target price: EUR20 Rating: Buy Up/downside: 36%	We have a DCF-based target price of EUR20. Our DCF assumptions are: risk-free rate of 3.5%, equity risk premium of 5.5%, sector beta of 1.1 and specific beta of 1, EBIT growth 2015-25e CAGR of 12.6%, EBIT growth 2025-45e CAGR of 4%, fade period 2045-53e, and a WACC of 9.45%.	Downside risks include high dependence on one product category (outerwear accounted for c85% of sales in 2014), marked seasonality (Autumn/Winter c75% of annual sales), management departures and any further placement from Eurazeo, which owns a 16% stake (RF FP, EUR56.87, Buy).
Swatch UHR VX Current price: CHF382.3 Target price: CHF410 Rating: Hold Up/downside: 7%	We have a DCF-based target price of CHF410. Our DCF assumptions are: risk-free rate of 3.5%, equity risk premium of 4%, sector beta of 1.1 and specific beta of 1.3, EBIT growth 2015-25e CAGR of 6.3%, EBIT growth 2025-45e CAGR of 4%, fade period 2045-53e, and a WACC of 9.22%.	Downside risks to our rating include weaker-than-expected trends in Greater China, market share losses to 'smart watches', value destruction on the Harry Winston acquisition, a stronger CHF and stronger gold prices. Upside risks include stronger-than-expected trends in Greater China, market share gains to 'smart watches', value creation on the Harry Winston acquisition, a weaker CHF and weaker gold prices.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Media

	Valuation	Risks
Publicis Groupe PUB FP Current price: EUR59.43 Target price: EUR77.00 Rating: Buy Up/downside: 29.6%	Our target price of EUR77 for Publicis is DCF-based. Our main assumptions are a risk-free rate of 3.5%, a weighted equity risk premium of 4.6% (based on a geographical revenue breakdown), a beta of 1.2, a cost of debt (pre-tax) of 3.5% (implying a WACC of 8.4%), and perpetual growth at 2%.	**Downside risks:** Difficulty in regaining organic momentum; an uncertain macro environment; loss of major clients or a key manager; client pressure on fees; difficulties in the merger process of acquisitions; and euro strength versus the US dollar.
ProSiebenSat.1 PSM GR Current price: EUR49.20 Target price: EUR55.00 Rating: Buy Up/downside: 11.8%	We value Pro7 based on a DCF methodology. We use a risk-free rate of 3.5%, an equity risk premium of 5.5% and beta of 1.1 with a WACC of 7.3%. Our target price is EUR55, which implies nearly 12% upside. We rate the stock Buy as we are conservatively c4% above consensus 2016-17e EPS and see material surprise potential on the top-line as well (5-6% above 2016-17 Street estimates).	**Downside risks:** (1) a worse-than-expected development in the German-speaking TV ad market; (2) failure to execute on its Digital & Adjacent strategy (10-25% digital growth CAGR with set 2018 targets); (3) failure to deliver on distribution/retransmission growth expectations (HSBCe EBITDA delta of EUR100m in 2018e vs 2012); (4) de-rating of broadcasters, for example driven by fear of a cyclical downturn or a loss of competitiveness versus online video; and (5) on-demand consumption by OTT player grabbing a bigger-than-expected share of free to air (FTA) viewing, putting ad dollars at risk.
GfK GFK GR Current price: EUR34.16 Target price: EUR43.00 Rating: Buy Up/downside: 25.9%	We value GFK using our standard DCF methodology with the following assumptions: risk-free rate of 3.5%, risk premium of 5.0%, cost of debt (pre-tax) at 3.5%, perpetual growth rate of 2%, beta of 1.2, long-term debt to assets at 12.5%, implying a WACC of 8.6%.	**Downside risks** include intensified price pressure from new market entrants (particularly in custom research), failure to restructure the entity to achieve the desired synergies, and a decrease in global advertising spending, resulting in lower research spending.
JC Decaux DEC FP Current price: EUR37.11 Target price: EUR35 Rating: Hold Up/downside: -6%	We derive our target price from a sum-of the parts and DCF model, based on an adjusted (non-IFRS) breakdown. We value JC Decaux's three divisions independently, as each features different growth rates, normalised margins and long-term potential. We use discount rates ranging from 8.7% to 9.1% as we use betas of 1.15x for Street Furniture, 1.2x for Transport and 1.25x for Billboard but the same RFR (3.5%) and RPM of (5.1%, geographically weighted).	**Downside risks:** (1) Sharp deceleration in advertising momentum; (2) sharp rebound of the EUR, or a worsening business climate in the eurozone; (3) increasing uncertainties in key emerging markets, especially Russia and China. **Upside risks:** (1) sharp acceleration in advertising momentum, especially in Europe, at fixed costs; (2) good track record in terms of contract gains; (3) appealing acquisitions at a fair price, to strengthen existing positions or facilitate entry into fast-growing markets.
Vivendi VIV FP Current price: EUR21.8 Target price: EUR21 Rating: Hold Up/downside: -3.7%	We value Vivendi using a sum-of-the-parts (SOTP) methodology. We value UMG and Canal+ businesses using DCF methodology (WACCs of 9%, risk free rate of 3.5%, MRP of 5.5% and a Beta of 1.25 times, for both). We value Vivendi's minority shareholdings in Activision Telecom Italia and Telefonica at the current market price.	**Upside risks** include a quicker turnaround in TV or music trends than currently expected or a sizable acquisition that would put the cash sitting on the balance sheet at work. **Downside risks** include further deterioration in business conditions in pay-TV in France or a rapid deterioration of the music business driven by the difficulty of monetising the content in a business model of streaming.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Metals and Mining

	Valuation	Risks
Freeport Mc Moran FCX US Current price: USD11.82 Target price: USD19.0 Rating: Buy Up/downside: 61%	We value Freeport on a 50:50 blended average of our DCF (USD23.72/share; risk-free rate 3.5%, risk premium 5.5%, beta 1.5,) and EV/EBITDA peer group multiple (USD14.27). We use a 12-month forward EBITDA peer group multiple of 6.0x).	Downside risks include a worse-than-expected outcome in the Grasberg negotiations with the Indonesian government (e.g. higher negative valuation impact from smelter construction, prolonged higher export duties, significant delays in resolution leading to material reduction in production profile); material delays or capex blowouts at major project expansions; and lower-than-expected commodity prices (most notably copper, gold, and oil).
Glencore GLEN LN Current price: 116p Target price: 190p Rating: Buy Up/downside: 64%	We value Glencore on a combination of our DCF model for the Industrial assets (NAV of USD22.9bn, risk-free rate of 3.5%, 6.5% risk premium, beta of 1.5) and an 11.0x 2015e PE for Marketing. Our target prices for Glencore's Hong Kong and Johannesburg listings of HKD23.0 and ZAR39.4 respectively are based on our UK target price of GBP1.90 converted at FX rates of 12.1 HKD/GBP and 20.7 ZAR/GBP. Our HKD and ZAR target prices imply upside of 67.9% and 56.0%, respectively, and we have a Buy rating on these listings.	Downside risks to our Buy rating include a 'perfect storm' in Marketing oor marketing conditions in all commodity sectors); adverse moves in ımmodity prices; material delays or increased capex at key projects; ›parture of key management and/or CEO.
ThyssenKrupp* TKA GR Current price: EUR18.54 Target price: EUR23.80 Rating: Buy Up/downside: 28%	We value TKA on a sum-of-the-parts, using market multiples of calendar 2016e EBITDA of peer companies, applied to the steel, elevator, industrial solutions, components and materials services divisions. We then apply a 10% conglomerate discount to the implied value per share to arrive at our fair value target price.	Downside risks include: deterioration in the Industrial Solutions business; greater competitive pressure in elevators; and a stalling recovery in the European steel market or EU recession.
Rio Tinto RIO LN Current price: 2,322p Target price: 2,690p Rating: Hold Up/downside: 16%	We value Rio on a 50:50 blended average of our discounted cash flow model (USD49.0 from USD48.4; risk-free rate 3.0%, risk premium from 4.5%, beta 1.4 and one-year forward EV/EBITDA (USD34.3, multiple 6.0x), translated at a USD/GBP rate of 1.55. Our target price implies upside of 16% and we have a Hold rating on the stock, as we project that iron ore marks new lows in 2016e and think that the market underestimates the risk that the yield story could break. We set a fair value target price for Rio Tinto Ltd, the Australian listed entity (RIO.AX, AUD50.61), of AUD58.2. Our target price is based on our Plc target price of 2,690p and applying the prevailing discount of Rio Tinto Ltd. to Rio Tinto Plc shares (currently 1.2%) and the current spot GBP/AUD exchange rate of 0.47. Our target price of AUD58.2 implies upside of 15% and we have a Hold rating on the stock.	Downside risks: The major downside risk relates to economic growth, especially in China. As a high-beta commodity play, another leg to the economic downturn could result in the stock underperforming the market. In addition, price expectations for iron are growing and an unexpected drop in spot prices could lead the stock to underperform the market and its peers. Upside risks: The upside risk to our rating include risks relating to commodity prices: if metal prices strengthen, the stock may outperform the market.

UK lines priced as at close on 2 November 2015, non-UK lines priced as at close 3 November 2015, except for ThyssenKrupp for which TP was changed on 17 November with the stock priced at 13 November.
Source: HSBC estimates

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Oilfield Services

	Valuation	Risks
Petrofac PFC LN Current price: 828p Target price: 1,025p Rating: Buy Up/downside: 23.8%	Our target price is based on the equal-weighted average of our fair values from the averages of our 2015e and 2016e DCFs, 2015e and 2016e sum-of-the-parts analyses (we value Integrated Energy Services using NAV and multiples-based valuation for services businesses), and 2015e and 2016e EV/Sales multiples based valuation using 1.1x for 2015e and 1.0x for 2016e (a blend of trough and through-cycle averages).	**Downside risks:** cost overruns or material project delays for which there is no contingency; increases in payment accruals, lower-than-expected E&P and downstream capital expenditures by oil companies, production risk from IES contracts, and slower-than-expected pace of contract awards from NOCs.
AMEC Foster Wheeler* AMFW LN Current price: 574p Target price: 800p Rating: Buy Up/downside: 39.4%	Our target price is based on the equal-weighted average of our fair values from the averages of our 2015e and 2016e DCFs, 2015e and 2016e sum-of-the-parts analyses and our EV/Sales multiples based valuation which uses 0.82x for 2015e and 0.78x for 2016e (balance of trough and through-cycle averages).	**Downside risks:** lower oil prices; lower than expected order intake and book-and-turn work, higher level of competitive pressures; unexpected problems with the Foster Wheeler integration, failure to achieve targets specified in its plan through cost reductions and/or organic and inorganic growth.
Saipem SPM IM Current price: EUR8.36 Target price: EUR5.5 Rating: Reduce Up/downside: -34.2%	Our target price is based on the equal-weighted average of our fair values from the averages of our 2015 and 2016e DCFs, 2015e and 2016e sum-of-the-parts analyses and 2015e and 2016e EV/Sales multiples based valuation using 0.85x and 0.81x for 2015e and 2016e (a moderate discount to trough cycle averages).	**Upside risks:** strong execution of the company's legacy backlog, a favourable outcome in the ongoing Algeria corruption probe, a less fierce competitive environment, a more resilient offshore drilling cycle than we currently expect, positive resolution to contractual issues and improved working capital/cash positions.
Lamprell LAM LN Current price: 116.75p Target price: 110p Rating: Reduce Up/downside: -5.8%	Our target price is based on the equal-weighted average of our fair values from the averages of our 2015e and 2016e DCFs, 2015e and 2016e sum-of-the-parts analyses and 2015e and 2016e book value multiples based valuation.	**Upside risks:** these include higher-than-expected order intake for rig refurbishment and newbuilds, unexpected awards outside of the drilling market, stronger than anticipated execution on existing backlog, and a more benign competitive environment.

Priced as at close on 2 November 2015 * except for AMFW for which TP changed on 6 November with the stock priced at 5 November. Source: HSBC estimates

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Pharmaceuticals

	Valuation	Risks
Novartis NOVN VX Current price: CHF89.45 Target price: CHF118 Rating: Buy Up/downside: 31.9%	Our long-term, product-by-product risk-adjusted DCF valuation, which takes account in detail of Novartis' commercially significant late-stage Pharma R&D pipelines, suggests the shares are notably undervalued and our fair value target price is CHF118. This is based on a WACC of 7%, using a long-term risk-free rate of 3.5%, an equity risk premium of 3.5% and a beta of 1.	Downside risks include: the potential for any manufacturing issues to recur in any part of the group's newly streamlined businesses, the growth rate in various parts of the generics market that Sandoz is active in, especially biosimilars, increasing competition in various parts of the eye care segment for Alcon, a greater-than-expected decline in sales of Exforge and more importantly, Glivec due to genericisation, any issue relating to the integration of the acquired GSK Oncology business, any issues relating to the Consumer Health business over which Novartis no longer has operational control (GSK runs it), a slower-than-expected ramp-up in sales of key new drugs such as Cosentyx and Entresto (LCZ696), high-profile, late-stage development failures (such as serelaxin, although we expect this to fail and have it at zero in our sales forecasts), and any intensification of US pricing pressure in Pharma.
GlaxoSmithKline GSK LN Current price: 1,397p Target price: 1,700p Rating: Buy Up/downside: 21.7%	We base our fair value target price of 1,700p on a DCF, with a WACC of 7%, using a long-term risk-free rate of 3.5%, an equity risk premium of 3.5% and a beta of 1.	Downside risks include: a faster erosion of established Respiratory drug revenues and a slower replacement of those revenues and profits by newer Respiratory products, increased competition in the Respiratory area, especially the threat of a substitutable generic Advair in the US, any issues in integrating the Vaccines and Consumer Health businesses, acquired as part of the major three-part transaction with Novartis, any failure to significantly improve working capital metrics relative to many peers which could restrain cash generation, any intensification of US pricing pressure in Pharma, the ability of the group to grow the dividend faster than its peers over the long-term given the already high pay-out ratio and the possibility of US and/or UK legislative action following the group's fine in China related to alleged sales malpractices.
Shire Pharmaceuticals SHP LN Current price: 4,885p Target price: 6,200p Rating: Buy Up/downside: 26.9%	Our target price of 6,200p is based on a long-term risk-adjusted DCF valuation (WACC 8%). Our WACC of 8% is based on a long-term risk-free rate of 3.5%, an equity risk premium of 4.5% and a beta of 1. We include DX-2930 in our forecasts, assuming the Dyax deal is completed and the drug is approved and launched by 2018.	Downside risks include an FDA rejection of lifitegrast or a delay in its approvability, the failure of DX-2930 to be approved, failure to close the Dyax acquisition; an increase in the value of the proposed Baxalta bid and any further US political headlines that could negatively impact companies that sell high-priced drugs, such as Shire.
Novo Nordisk NOVOB DC Current price: DKK363.5 Target price: DKK300 Rating: Reduce Up/downside: -17.5%	Our risk-adjusted DCF valuation, with forecasts that have Tresiba launched in the US in 2016 and with peak sales above USD2bn (and Xultophy sales above USD4bn at peak), reaches DKK300/share. Our fair value target price uses a WACC of 7%, based on a long-term risk-free rate of 3.5%, an equity risk premium of 3.5% and a beta of 1.	Upside risks to our view, target price and rating include: faster-than-anticipated growth in sales of Tresiba, Ryzodeg and Xultophy, a slower-than-expected sales trajectory of competitor products such as Toujeo and LixiLan, greater-than-expected sales of Saxenda, the failure of long-acting GLP-1 agonists currently in development to reach commercialisation, success in phase III development with oral semaglutide, a lower impact of new competitor products in the haemophilia space.

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Precious Metals Miners

	Valuation	Risks
Fresnillo FRES LN Current price: 722p Target price: 810p Rating: Buy Upside: 12.2%	We see gold and silver prices able to, respectively, reach and sustain levels of USD1,200/oz and USD17/oz within the next 12 months, and therefore believe that the stock valuation, at that point, will reflect these metal prices. Using these target gold and silver prices, we derive our target stock price using a modified DCF valuation approach, and we discount it back at real WACC to current terms. We rate the stock a Buy as we view it as a high-quality gold and silver miner with a strong management team, a portfolio of low-cost assets and the ability to fund its sector-leading pipeline of growth projects mainly through operating cash flow	Downside risks, in our view, include weaker-than expected precious metals prices, poor performance at the core assets, particularly, lower than expected silver grades at the Fresnillo mine, further increases in taxation, security issues, higher costs associated with mining, environmental disasters or political risk related issues. Delay in commissioning and ramp-up of key projects such as San Julian may also pose a risk to our thesis. Land access is a growing concern in Mexico, and may pose a risk; however, we do not expect any land access issues at the core Fresnillo and Saucito operations as the necessary development land is already owned by the company.
Polymetal International POLY LN Current price: 573p Target price: 660p Rating: Buy Upside: 15.2%	We see gold and silver prices able to, respectively, reach and sustain levels of USD1,200/oz and USD17/oz within the next 12 months, and therefore believe that the stock valuation, at that point, will reflect these metal prices. Using these target gold and silver prices, we derive our target stock price using a modified DCF valuation approach, and we discount it back at real WACC to current terms. We rate Polymetal Buy as we believe it is very well placed to continue rapid growth at low entry cost, as it is one of only a few well-established, well-funded gold miners willing and able to operate in Russia, an area that we consider holds significant potential for new gold discoveries	Downside risks, in our view, include weaker-than-expected prices of precious metals, poor performance at core assets, higher costs associated with mining, environmental disasters, and political risk-related issues, particularly as all of the company's key assets are in Russia, , although we do not expect any significant direct impact on the company at this point.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Real Estate

	Valuation	Risks
Vonovia VNA GY Current price: EUR30.3 Target price: EUR35.0 Rating: Buy Up/downside: 15.5%	Our EUR35.0 target price is based on average of: (1) a EUR34.4 DCF valuation which is based on a WACC of 5.9%, CoE of 9%, beta of 1, RFR of 3.5% and FCF growth of 2.75%; and (2) our 24M-rolling adj. NAV (incl. cumulative dividend payment) of EUR37, to which we do not apply any company-specific discount. We have a Buy rating as we see strong cash flow growth momentum due to synergies on recent acquisition materialising in 2016/17e.	**Downside risks include**: (1) lower-than-guided synergy effects would reduce the FFO 1 projection and lower the valuation; (2) dilutive capital raise; (3) strong rise in interest rates would lower the free cash generation and the ability to pay attractive dividends.
Hammerson HMSO LN Current price: 631p Target price: 677p Rating: Buy Up/downside: 7.3%	Our 677p target price comprises a 25% weighted contribution from: (1) a 561p DCF valuation, which is based on a WACC of 7.0%; and (2) a 75% weighted contribution from a 716p NAV valuation based on our estimated 24M-forward NAVPS with a 16% discount applied (consistent with what we apply to all the non-Central London specialists) and adding back the dividend pay-out. We have a Buy rating on the stock as we deem the company's dividend profile to be attractive which is also consistent with the HSBC Strategy team's view that companies offering above average income yield profiles should outperform those that do not.	**Downside risks include**: (1) cap rate expansion to a greater extent than assumed; (2) weaker rental growth than we have assumed; (3) a steeper increase in interest rates than expected.
Capital & Counties CAPC LN Current price: 445p Target price: 394p Rating: Reduce Up/downside: -11.5%	Our 394p target price comprises a 25% weighted contribution from: (1) a 254p DCF valuation, which is based on a WACC of 7.0%; and (2) a 75% weighted contribution from a 441p NAV valuation based on our estimated 24M-forward NAVPS with an 8% premium applied (consistent with what we apply to all of CAPCO's peer group) and adding back the dividend pay-out. We have a Reduce rating on CAPC because we see potential in 2016 for an escalation in addressing London's affordable housing crisis, which if enacted by a newly elected London Mayor in that year, could undermine CAPC's premium valuation.	**Upside risks include**: (1) greater on-going yield compression than we have assumed; (2) stronger than expected rental growth than we have assumed; (3) greater development profits than we have assumed.
Immofinanz IIA AV Current price: EUR2.4 Target price: EUR1.8 Rating: Reduce Up/downside: -24.7%	Our EUR1.8 target price is based on average of: (1) a EUR1.4 DCF valuation, which is based on a WACC of 7.9%, a beta of 1.3, CoE of 10.8%, ERP of 6%, RFR of 3% and FCF growth of 0.5%; and (2) our 24-month rolling NAV (plus cumulative dividend payments) of EUR3.07, to which we apply 30% company-specific discount to factor in uncertainties in Russia and the fragile outlook for property markets in CEE/SEE leading to our NAV value per share of EUR2.15.	**Upside risks include**: (1) lower-than-expected capital value decline, (2) faster-than-expected recovery of the Russian economy.

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HSBC

Software and IT Services

	Valuation	Risks
Capgemini CAP FP Current price: EUR81.87 Target price: EUR105 Rating: Buy Up/downside: 28%	Our DCF-based target price is EUR105 (risk-free rate 3.5%, risk premium 5.5%, beta 0.9 and WACC 9.0%).	Downside risks include: (1) lower economic growth than we expect, especially in Europe, which could hurt our top-line growth and margin estimates; (2) an unfavourable increase in the headcount-to-business ratio, squeezing margins in a scissor effect; (3) the company using net cash to finance acquisitions that are overpriced, oversized or have a high integration risk; and (4) risk of integration linked to the acquisition of Igate.
Gemalto GTO NA Current price: EUR58.87 Target price: EUR95 Rating: Buy Up/downside: 61%	Our DCF-based target price is EUR95 (WACC 8.5%; beta of 1.0, 3.5% risk-free rate, 5.5% risk premium).	Downside risks include: (1) Slowdown in SIM business segment that represents 25% of the revenues, but 47% of profit from operation. (2) The equity story is focused on EMV migration in the US and NFC deployment around the world. Postponement of some contracts, or lower-than-expected growth of these technologies, could lead to lower growth and leverage on margins, which could hurt the share price. (3) Managing consensus reactions and expectations: consensus is regularly surprised by releases, owing to misunderstandings concerning the seasonal nature of the group's business. This was also true in Q3 2014.
Dassault Systèmes DSY FP Current price: EUR71.91 Target price: EUR75 Rating: Hold Up/downside: 4%	Our DCF-based target price is EUR75 (WACC 7.0%; beta of 0.6, 3.5% risk-free rate, 5.5% risk premium).	Upside risks include: (1) stronger-than-expected recovery of organic top-line growth; (2) overestimating the impact of the rental licensing on group sales of new licence sales in 2015/16; (3) the group's ability to leverage its cost structure further and generate higher margins than we expect (and favourable impact of rental licensing, which appears accretive for margins in the long term); and (4) quicker recovery of dilutive acquisitions and new self-financed acquisitions. Downside risks include: (1) lower organic top-line growth; (2) unfavourable FX; (3) multiplication of dilutive acquisitions.
Software AG SOW GR Current price: EUR26.89 Target price: EUR28 Rating: Hold Up/downside: 4%	Our DCF-based target price is EUR28 (WACC 10.0%; beta of 1.2, 3.5% risk-free rate, 5.5% risk premium).	Upside risks include: (1) stronger-than-expected recovery in DBP deals; (2) more leverage than expected on fixed cost base, especially in the DBP segment. Downside risks include: (1) lower growth than expected in the Digital Business Platform (DBP) segment, which is the main driver of the equity story; (2) lack of control over the cost base, especially sales & marketing costs in the BPE segment; (3) negative impact from macroeconomic conditions on customer investment in DBP solutions – particularly in the banking and public sectors, which accounted for 21% and 20% of sales, respectively; (3) a major acquisition that carries the risk of overpayment and integration, especially in the memory analytics field; (4) a stronger-than-expected decline in mature/subscale activities (A&D Adabas & Natural + Consulting 54% of sales in 2014).

Priced as at close on 2 November 2015. Source: HSBC estimates

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Telecoms

	Valuation	Risks
Deutsche Telekom DTE GR Current price: EUR17.00 Target price: EUR19.00 Rating: Buy Up/downside: 11.8%	Our target price is derived from an EV/EBITDA based SOTP, with the exception of listed T-Mobile US, which we incorporate at current market value. We assign a target 2015e EV/EBITDA multiple to DT's German business and other European integrated assets of 8.2x. We see fair value for DT's mobile-only assets at 5.0x, (given their more difficult strategic position) and DT's smaller divisions T Systems at 3.0x and the GHS cost centre at 2.0x 2015e EV/EBITDA.	Downside risks include: (1) a less positive approach to regulation in Germany and Europe; (2) DT becoming less financially disciplined.
BT Group Plc BT/A LN Current price: 464p Target price: 520p Rating: Buy Up/downside: 12.2%	We value BT using a FCFF-based DCF. We use a RFR of 3.5% and ERP of 4.0%, leading to a WACC of 7.8%. We assume a terminal growth rate of 2%, in line with peer growth estimates. We note that the stock will go ex-div in December 2015.	Downside risks include: (1) adverse regulatory decisions from Ofcom; (2) entry into mobile sparking a renewed bout of price competition; and (3) low visibility on Global services revenue.
Orange ORA FP Current price: EUR15.91 Target price: EUR18.00 Rating: Buy Up/downside:13.2%	We use DCF methodology for France, Spain, the other Europe, Enterprise segment, Africa & Middle East and ICSS divisions (WACC of 8.3% for France, 8.4% for Spain and the other Europe & Enterprise segment, and 9.4% for the Africa & Middle East segment). We value Orange's 50% stake in EE based on the transaction price with BT. We value Poland and Belgium based on our target prices for Orange Polska (OPL PW, PLN7, reduce, TP PLN6.20, 5% of group EV) and Mobistar (MOBB BB, EUR21.6, Hold, TP EUR18), respectively.	Downside risks include: (2) higher-than-expected ARPU declines in France (in both fixed line broadband and mobile), (2) Orange being fined related to the competition law in the B2B segment in France at a cost that is higher than what we already have in our sum of-parts; and (3) higher commercial costs in Europe.
Telecom Italia TIT IM Current price: EUR1.27 Target price: EUR1.35 Rating: Buy Up/downside: 6.3%	We use a DCF methodology to derive our valuation for the domestic business of Telecom Italia (88% of the EV). We assume a risk-free rate of 3.5%, market risk premium of 5.5% and levered beta of 1.5. For the purposes of valuing TI, we consider TIM Brasil (66.7% stake held by TI) at its last six-month average share price.	Downside risks include: (1) the lack of regulatory approval for a WIND-3Italia merger would imply persisting competitive pressure, translating into revenue and EBITDA pressure not in our forecasts; (2) a disposal of TIM Brasil at an unattractive valuation or overpaying for an acquisition.
NOS NOS PL Current price: EUR7.57 Target price: EUR9.00 Rating: Buy Up/downside:18.9%	We value NOS on a consolidated basis (including synergies) to derive a DCF-based fair value target price. Our key DCF assumptions are: risk-free rate of 3.5%, market risk premium of 5.5%, beta of 1.0 and terminal growth rate of 2.0%.	Downside risks include: (1) a deterioration of the competitive environment through higher promotions and discounts; and (2) a deterioration of macro with a negative impact on disposable income, which would likely affect appetite for more advanced telecoms services.

Priced as at close on 2 November 2015. Source: HSBC estimates

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Transport

	Valuation	Risks
Groupe Eurotunnel GET FP Current price: EUR12.78 Target price: EUR15.50 Rating: Buy Up/downside: 21.3%	We use DCF to derive our target price. Our enterprise value is calculated by applying WACC of 7.4% based on RFR of 3%, ERP of 5.2% and sector beta of 1.0. We value new routes at EUR0.8 per share as we include the Lyon, Marseille and Amsterdam routes in our core DCF valuation. This gives us the target price of EUR15.5.	Downside risks: Eurotunnel is a single asset company, and as such, it is risky. Any event that forced a closure (temporary or otherwise) such as accidents/fire etc. could have an immediate impact on valuation. Other risks include technological changes in transport modes, UK/France tax changes, economic weakness, damaging trade between UK and France, value destructive acquisitions and changes to regulatory structure.
Air France-KLM* AF FP Current price: EUR6.46 Target price: EUR8.45 Rating: Buy Up/downside: 30.7%	We derive our target prices from a three-stage DCF analysis. Our three-stage DCF based target price of EUR8.45 is based on our assumed WACC of 8.3%, mid-term EBIT margin of 4.5%, sector beta of 1.1, risk-free rate of 3.5% and equity risk premium of 5.5%.	In terms of downside risks, the most obvious risk is further terror incidents. Thereafter the risk remains labour, potential industrial action or at least the failure to deliver meaningful change. We are concerned about trading to Brazil, Japan and North Africa, which is an important market for Transavia. While management suggests that it is working around the constraints of the political challenges in Holland, this continues, at the very least, to be a potential management distraction.
Wizz Air WIZZ LN Current price: 1,917p Target price: 2,250p Rating: Buy Up/downside: 17.4%	Our three-stage DCF-based target price of GBP22.50 is based on our assumed WACC of 8.2%, mid-term EBIT margin of 12%, sector beta of 1.1, risk-free rate of 3.5% and equity risk premium of 4.0%. We rate Wizz Buy seeing its strategic niche and low costs to be powerful attributes as the industry heads into a period of instability.	Key downside risks include disappointing unit revenues as a result of the impact of higher capacity growth and increasing competition. Political instability in the Ukraine and Russia has had little negative impact on the company to date, but contagion to other regional markets could depress demand, yields and profitability. The weakening of the EUR relative to the USD will put upward pressure on fuel costs, maintenance and lease costs, dampening the benefit falling fuel prices.
easyJet EZJ LN Current price: 1,713p Target price: 1,600p Rating: Reduce Up/downside: -6.6%	Our three-stage DCF-based target price of 1,600p is based on our assumed mid-term EBIT margin of 14.4%, WACC of 8.5%, sector beta of 1.1, risk-free rate of 3.5% and equity risk premium of 4.5%. We rate EZJ Reduce reflecting our concerns that the company faces building competitive pressures form Ryanair as well as second tier low cost carriers.	Key upside risk comes from better than expected yields, industry consolidation, outperforming Q4 revenue guidance or dividend increases.
Zurich Airport FHZN SW Current price: CHF752.5 Target price: CHF600.0 Rating: Reduce Up/downside: -20.3%	We derive our target prices from a three-stage DCF analysis. Our three-stage DCF target price of CHF600 is based on our assumed WACC of 7.2%, mid-term EBIT margin of 31%, risk free rate of 3.5%, equity risk premium of 4.0% and sector beta of 1.0x.	Upside risks include positive developments in commercial revenues, if the price cuts on the airside can drive more spending. Strengthening traffic volumes from Swiss, value creation from positive news on new tenants for the Circle project and industrial unrest at Lufthansa potentially diverting Lufthansa group traffic flows through Zurich could all support the share price.
Firstgroup FGP LN Current price: 99p Target price: 100p Rating: Hold Up/downside: 0.9%	We use a multiple based SOTP to derive our TP, giving different weights to the earnings stream of each division. We value the UK rail division on an assumed market share, which we believe is logical given that we expect the operators to have a long-term future in the industry. We assume 6.25% UK Rail market share (half of current market share) for FGP in perpetuity, which may be harsh. We apply target multiples to various road assets and derive one year forward price. Our theoretical SOTP valuation is 108p, which is derived by discounting (at a WACC of 7.0%, risk-free rate of 3% and risk premium of 4.5%) the sum of our one-year forward price and dividend. While this suggests that there is some value available, we aren't yet fully convinced by the turnaround and we continue to apply a 10% discount. So our rounded TP is fixed at 100p.	Upside risks include a better-than-expected margin recovery in the US School Bus and UK bus, and a new franchise win. Downside risks include margin pressure in the US school bus market owing to high competition/ budget pressure. Other risks include subsidy/regulatory risk in UK bus and any change in capital structure.

Priced as at close on 2 November 2015, * except for Air France-KLM for which TP changed on 20 November with the stock priced at 18 November. Source: HSBC estimates

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Utilities

	Valuation	Risks
National Grid NG/ LN Current price: 923p Target price: 1,000p Rating: Buy Up/downside: 8%	We value National Grid via three methodologies – DCF, Dividend Yield and SOTP. Under this methodology, we assign a 50% weight to yield (969p assuming 4.5% dividend yield) and 25% each to DCF (1,190p based on WACC of 4.3%) and SOTP (875p based on 2015e average peer group multiples) to arrive at our rounded target price of 1,000p.	Downside risks: NG fails to achieve the agreed returns which could damage its reputation and threaten future growth opportunities and regulatory arrangements. In particular, the risk is that Grid fails to deliver the growth implicit in our forecasts; it may fail to increase regulatory returns in the US; it may not be able to achieve the efficiencies implicit in its UK price controls; and its investment in UK electricity transmission may be re-phased further than our assumptions. As National Grid also has significant US assets it may suffer in the short term from a negative correlation with higher US government bond yields. It has put a stake in its UK Gas Distribution assets up for sale but may fail to find buyers.
Enel ENEL IM Current price: EUR4.24 Target price: EUR5.00 Rating: Buy Up/downside: 18%	Our target price for Enel is based on the average of DCF (EUR5.7 assuming WACC of 6.0% and terminal growth rate of 1%), yield implied valuation on 2015e DPS (EUR3.8 based on 4.5% yield) and sum-of-parts (EUR4.8, after 10% discount related to political and conglomerate risk). We apply a 40% weighting to the DCF, 40% weighting to the SOP and 20% weighting to yield (slightly below peers reflecting lower yield appeal as the pay-out is lower).	Downside risks: political instability in Italy, negative regulatory changes in Spain or uncertainties linked to the general elections, additional decline in Spanish or Italian power prices, lack of success in divestments and portfolio rationalisation, deterioration in the cash-flow profile of the group from negative working capital requirements, deterioration in LatAm (economy and currencies) where Enel has a strong presence, negative update in the allowed returns of the domestic regulated assets on lower risk free rate.
Veolia Environnement VIE FP Current price: EUR21.4 Target price: EUR23.0 Rating: Buy Up/downside: 8%	We value Veolia via three methodologies – DCF, dividend yield and sum-of-the -parts based on 2015e average peer group multiples. Under this methodology, we assign a 50% weight to yield (EUR21.4 based on 3.5% dividend yield) and 25% each to DCF (EUR27.1 based on WACC of 5.6%) and SOTP (EUR23.1 based on 2015e average peer group multiples) to arrive at our rounded target price of EUR23. We have a Buy on the stock as we expect to hear good news at the strategy day on 14 December, where we expect Veolia to increase its cost cutting targets, give new guidance and increase its dividend for 2016.	Downside risks: failure to deliver cost cutting; failure to increase the dividend in 2016 from its current floor of EUR0.70; failure to meet FCF guidance for 2015; a lack of growth in European water and waste volumes and prices; and low organic growth in international water.
RWE RWE GR Current price: EUR13.2 Target price: EUR10.5 Rating: Reduce Up/downside: -20%	Our target price for RWE is based 50% on yield based valuation (EUR10.0 at 5% yield), 25% on DCF (EUR11.5 from EUR12.6, WACC of 6.6%) and 25% on SOP valuations (EUR10.3 from EUR11.9 after 40% discount).	Upside risks: external fund recommended by the government for nuclear waste storage liabilities; negotiations with a Gulf-based investor (Reuters, 27 March 2015) lead to an injection of capital into RWE; German Constitutional Court rules against the nuclear tax; and RWE reassures on its dividend.
Drax* DRX LN Current price: 227p Target price: 190p Rating: Reduce Up/downside: -16%	Our DCF-based valuation assumes a WACC of 7.34%, comprising a 4.0% cost of debt and 8.6% cost of equity. Unlike the other utilities above, we no longer use a yield valuation in calculating our target price as we do not believe yield is a consideration for investors given the current challenging environment.	Upside risks: The key risk is higher than anticipated power prices reflecting a tightening market. In addition the December capacity auctions could see higher capacity payments from 2019 onwards. There could be upside if the Secretary of State concludes her review and decides there is a place for unabated coal in the UK's generation mix. If the EU agrees to a CfD of GBP105MW/h this could underpin the stability on one unit of biomass generation in a falling power price environment..

Priced as at close on 2 November 2015 * except for Drax for which TP changed on 19 November with the stock priced at 17 November. . Source: HSBC estimates

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Notes

Disclosure appendix

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Important disclosures

Equities: Stock ratings and basis for financial analysis

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 20 November 2015, the distribution of all ratings published is as follows:

Buy	45%	(31% of these provided with Investment Banking Services)
Hold	41%	(29% of these provided with Investment Banking Services)
Sell	14%	(17% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see “Stock ratings and basis for financial analysis” above.

Information regarding company share price performance and history of HSBC ratings and target prices in respect of long-term investment opportunities for the companies that are the subject of this report is available from www.hsbcnet.com/research.

HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
AGGREKO	AGGK.L	9.92	19-Nov-2015	4, 7
AIR FRANCE-KLM	AIRF.PA	6.65	19-Nov-2015	1, 2, 4, 5, 7
AMEC FOSTER WHEELER	AMFW.L	4.79	19-Nov-2015	6, 7
ASSICURAZIONI GENERALI	GASI.MI	17.69	19-Nov-2015	4, 5, 6, 7
ATLAS COPCO	ATCOa.ST	227.30	19-Nov-2015	6, 7
BANK OF IRELAND	BKIR.I	0.32	19-Nov-2015	1, 5, 6, 7
BARCLAYS PLC	BARC.L	2.30	19-Nov-2015	2, 4, 6, 7
BASF	BASFn.DE	77.32	19-Nov-2015	2, 4, 5, 6, 7
BEIERSDORF	BEIG.DE	88.82	19-Nov-2015	6
BMW	BMWG.DE	98.73	19-Nov-2015	1, 2, 4, 5, 6, 7
BOOKER GROUP	BOK.L	1.82	19-Nov-2015	7
BT GROUP PLC	BT.L	4.91	19-Nov-2015	4, 6, 7
CAIXABANK SA	CABK.MC	3.55	19-Nov-2015	1, 5, 6, 7
CAP GEMINI	CAPP.PA	84.37	19-Nov-2015	1, 2, 4, 5, 6
CAPITAL & COUNTIES PROPERTY	CAPCC.L	4.34	19-Nov-2015	1, 6
CREDIT AGRICOLE S.A.	CAGR.PA	11.52	19-Nov-2015	6, 7
DASSAULT SYSTEM	DAST.PA	74.25	19-Nov-2015	2, 6
DEUTSCHE TELEKOM	DTEGn.DE	17.16	19-Nov-2015	4
DIA	DIDA.MC	6.04	19-Nov-2015	4, 7
DRAX GROUP PLC	DRX.L	2.28	19-Nov-2015	2, 7
EASYJET	EZJ.L	17.14	19-Nov-2015	4, 6, 7
EIFFAGE	FOUG.PA	57.55	19-Nov-2015	7
ENI	ENI.MI	14.93	19-Nov-2015	1, 4, 5, 6, 7
ERSTE GROUP BANK	ERST.VI	28.66	19-Nov-2015	1, 4, 5, 6, 7
EULER HERMES	ELER.PA	83.50	19-Nov-2015	2, 6
EXPERIAN LTD	EXPN.L	12.17	19-Nov-2015	4, 5, 6, 7
FIRSTGROUP	FGP.L	1.06	19-Nov-2015	5
FREEPORT MCMORAN	FCX.N	8.41	19-Nov-2015	7
GEMALTO	GTO.AS	57.80	19-Nov-2015	4, 7
GFK	GFKG.DE	34.84	19-Nov-2015	2, 6, 7
GLAXOSMITHKLINE	GSK.L	13.47	19-Nov-2015	1, 2, 4, 5, 6, 7
GLENCORE	GLEN.L	0.94	19-Nov-2015	2, 5, 6, 7
GRANDVISION NV	GVNV.AS	25.44	19-Nov-2015	1, 5, 6, 7
GREENCORE	-	-	-	5, 6, 7
GROUPE EUROTUNNEL SA	GETP.PA	12.18	19-Nov-2015	2
HAMMERSON	HMSO.L	6.12	19-Nov-2015	1, 2, 5, 6
HILTON FOOD GROUP PLC	HFG.L	5.19	19-Nov-2015	7
HOCHTIEF	HOTG.DE	88.70	19-Nov-2015	7
INDITEX	ITX.MC	32.72	19-Nov-2015	6
JC DECAUX	JCDX.PA	35.86	19-Nov-2015	5
JOHNSON MATTHEY	JMAT.L	26.94	19-Nov-2015	7
KINGFISHER PLC	KGF.L	3.56	19-Nov-2015	4, 5, 6, 7
KONE	KNEBV.HE	39.99	19-Nov-2015	6, 7
LAFARGEHOLCIM	LHN.VX	55.55	19-Nov-2015	1, 2, 5, 6, 7
LAMPRELL PLC	LAM.L	1.07	19-Nov-2015	1, 5, 7
LANXESS	LXSG.DE	47.15	19-Nov-2015	6
LVMH	LVMH.PA	162.40	19-Nov-2015	5, 6
MARKS & SPENCER GROUP	MKS.L	5.20	19-Nov-2015	4, 5, 6
METRO	MEOG.DE	29.80	19-Nov-2015	2, 5, 6, 7
MICHELIN	MICP.PA	94.68	19-Nov-2015	1, 2, 4, 5, 7

MONCLER	MONC.MI	14.97	19-Nov-2015	1
NATIONAL GRID	NG.L	9.40	19-Nov-2015	1, 4, 5, 6
NOVARTIS	NOVN.VX	90.00	19-Nov-2015	6
NOVO NORDISK	NOVOb.CO	379.20	19-Nov-2015	7
ORANGE	ORAN.PA	16.84	19-Nov-2015	2, 4, 5, 6, 7
PETROFAC LTD	PFC.L	7.88	19-Nov-2015	4, 5, 6, 7
PHILIPS	PHG.AS	25.14	19-Nov-2015	1, 4, 5, 6, 7
PROSIEBENSAT.1	PSMGn.DE	50.70	19-Nov-2015	4
PRUDENTIAL CORP	PRU.L	15.18	19-Nov-2015	1, 5, 6, 7
PUBLICIS	PUBP.PA	58.63	19-Nov-2015	1, 2, 4, 5, 6
PZU	PZU.WA	393.50	19-Nov-2015	6
RENAULT	RENA.PA	92.57	19-Nov-2015	1, 2, 5, 6, 7
REPSOL	REP.MC	12.26	19-Nov-2015	2, 4
RICHEMONT(CIE FIN)	CFR.VX	77.70	19-Nov-2015	6
RIO TINTO	RIO.L	22.90	19-Nov-2015	1, 2, 5, 6, 7
ROYAL DUTCH SHELL A SHS	RDSa.L	16.66	19-Nov-2015	1, 4, 5, 6, 7
ROYAL DUTCH SHELL B SHS	RDSb.L	16.82	19-Nov-2015	1, 4, 5, 6, 7
RWE	RWEG.DE	11.61	19-Nov-2015	1, 2, 4, 5, 6
SAINSBURY	SBRY.L	2.53	19-Nov-2015	1, 4, 5, 6, 7
SAIPEM	SPMI.MI	8.10	19-Nov-2015	2, 6
SARTORIUS	SATG_p.DE	212.65	19-Nov-2015	6, 7, 11
SCHINDLER	SCHN.S	165.00	19-Nov-2015	6, 7
SCHNEIDER	SCHN.PA	58.35	19-Nov-2015	1, 4, 5, 6, 7
SHIRE PHARMACEUTICALS	SHP.L	47.18	19-Nov-2015	4, 7
SOFTWARE AG	SOWG.DE	25.76	19-Nov-2015	6, 7
SVENSKA HANDELSBANKEN	SHBa.ST	118.90	19-Nov-2015	6
SWATCH	UHR.VX	362.60	19-Nov-2015	4, 5, 7
TELECOM ITALIA	TLIT.MI	1.16	19-Nov-2015	1, 2, 4, 5, 6, 7
THYSSENKRUPP	TKAG.DE	19.65	19-Nov-2015	4, 5, 7
TOTAL	TOTF.PA	46.60	19-Nov-2015	1, 4, 5, 6, 7
VEOLIA ENVIRONNEMENT	VIE.PA	22.26	19-Nov-2015	2, 5, 6, 7
VIVENDI	VIV.PA	20.26	19-Nov-2015	4, 6, 7
VOLVO	VOLVb.ST	88.25	19-Nov-2015	1, 2, 5, 6, 7

Source: HSBC

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Additional disclosures

1 This report is dated as at 23 November 2015.

2 All market data included in this report are dated as at close 02 November 2015, unless otherwise indicated in the report.

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6 HSBC is acting as Financial Adviser regarding the announced disposal of METRO Cash & Carry Vietnam to Thailand based Berli Jucker Public Company Limited

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