Deutsche Bank

19 September 2007

Benetton

Reuters: **BNG.MI** Bloomberg: **BEN IM** Exchange: **MIL** Ticker: **BNG**

Upgrading to Buy on upside potential

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Turnaround progressing - Upgrade to Buy

The share price is now back to where it was one year ago and has shed 25% since the beginning of the year, in sharp contrast with its fundamentals trends. The Group's turnaround is already visible in the good interim performance and in the solid outlook for A/W 07-08, and this also indicates that it is sustainable. BNG shares show substantial upside vs. our Euro 14.8 TP. Upgrading to Buy. Dividend yield >3% and reasonable multiples provide defensiveness.

Playing the second phase of the turnaround

Benetton is one of the leading casualwear players in Italy and around the world. We believe that the turnaround achieved over the recent couple of years should allow the Group to show top line and margin improvements over the medium term. Delivery of the second phase of the relaunch, including a re-focus on retail performance, should improve credibility on margin recovery and could give higher visibility and appeal to the shares, particularly should BNG exceed our forecasts (the group's recent strategic re-focus must have been driven by renewed profitability ambitions, ie taking the medium-term operating margin back at least to mid-teens, which compares with our <13% assumption). This leaves the new CEO with a challenging task, but would allow him and the shareholders good rewards.

Reasonable bottom line growth ahead

We expect a 14% 3-year EPS CAGR driven by a 6-7% top line growth (50-60% the growth from new openings) and an average 80bp margin expansion thanks to the operating efficiencies, better sales mix and the end of the mark-up policy.

Where is the downside? Moving to Buy – Key risk is execution

Our Euro 14.8 TP is based on a DCF (7.4% WACC -4.5% RP, 4.5% RFR, 80% equity based capital structure, beta 0.9, 1.3% perpetuity, which is consistent with a deflationary environment). A number of factors provide support to the shares (dividend yield, Euro 535m of distributable reserves, c. 30% of the market cap represented by property value). On our numbers, BNG is trading at acceptable multiples with real-estate adjusted multiples at a c.15% discount to reported ones. The discount implicitly attributed by the market for low management visibility will in our view soon prove inappropriate. In addition to macroeconomic risks, the main risks are i) the execution of the re-launch strategy, including possible margin erosion from potential aggressive pricing decisions, ii) low transparency on commercial capex; iii) low visibility on retail progression. More on pages 4 and 10.

Forecasts and ratios

Year End Dec 31	2005A	2006A	**2007E**	2008E	2009E
P/E (DB EPS) (x)	13.3	17.3	**13.2**	11.4	10.5
DB EPS (EUR)	0.63	0.70	**0.82**	0.95	1.03
DB EPS growth (%)	-9.4	11.1	**17.2**	16.3	8.3
Yield (%)	4.1	2.9	**3.7**	4.3	4.8

Source: Deutsche Bank estimates, company data

Rating Upgrade

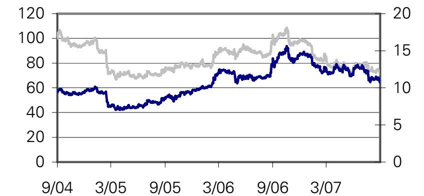
Buy

Price at 18 Sep 2007 (EUR)	**10.85**
Price Target (EUR)	**14.80**
52-week range (EUR)	**15.61 - 10.77**

Key changes

Rating	Hold to Buy ↑	
Target Price	14.90 to 14.80 ↓	**-0.7%**

Price/price relative



Performance (%)	1m	3m	12m
Absolute	*-1.0*	*-8.2*	*-16.4*
Dow Jones EURO STOXX Price		*2.8*	*-7.2*

Stock & option liquidity data

Market cap (EUR)(m)	1,969.9
Shares outstanding (m)	182
Free float (%)	–
Option volume (und. shrs., 1M avg.)	–

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DISCLOSURES AND ANALYST CERTIFICATIONS ARE LOCATED IN APPENDIX 1

Model updated: 18 September 2007

Running the Numbers

Europe

Italy

Retail-Non Food

Benetton

Reuters: BNG.MI Bloomberg: BEN IM

Buy

Price as of 17 September	EUR 10.77
Target price	EUR 14.80

Company website

http://www.benetton.com

Company description

Benetton Group S.p.A. manufactures and retails clothing, sportswear and accessories for men, women and children, with a global brand name (United Colours of Benetton) and with the Sisley, Killer loop and Playlike brands. The company markets its products worldwide, with Europe being the main market. Benetton still distributes most of its casualwear and sportswear products through a network of franchising partners, but has recently embarked on a direct retailing strategy with the opening of directly operated stores and megastores. The Benetton family is the core shareholder.

Research Team

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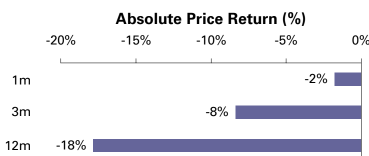
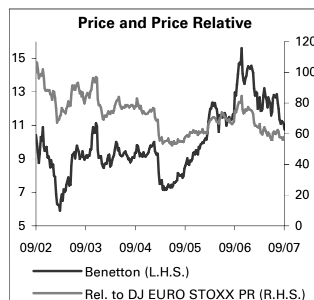
Absolute Price Return (%)

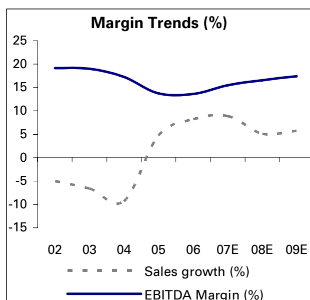


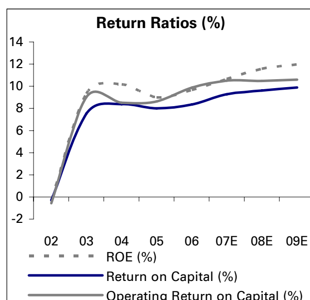
52-week Range:	EUR 10.77 - 15.61
Market Cap (m)	EUR 1,955
	USD 2,711

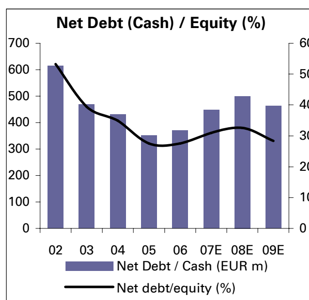
Company identifiers	
Cusip	NA
SEDOL	7128563

Year Ending 31 December	2002	2003	2004	2005	2006	2007E	2008E	2009E
SUMMARY								
DB EPS (EUR)	0.95	0.74	0.70	0.63	0.70	0.82	0.95	1.03
P/E (x)	12.8	11.8	13.2	13.3	17.3	13.1	11.3	10.4
DB EPS growth (%)	1.3	-22.4	-5.6	-9.4	11.1	17.2	16.3	8.3
Reported EPS (EUR)	-0.02	0.60	0.67	0.62	0.69	0.81	0.94	1.03
P/E (Reported) (x)	nm	14.6	13.7	13.6	17.6	13.3	11.4	10.4
CFPS (EUR)	0.51	2.02	1.36	2.03	1.28	0.89	1.55	1.61
P/CFPS (x)	23.9	4.3	6.8	4.1	9.5	12.1	6.9	6.7
Free CFPS (EUR)	0.59	1.21	0.50	1.40	0.09	-0.74	0.03	0.47
DPS (EUR)	0.35	0.38	0.34	0.34	0.35	0.40	0.47	0.52
Dividend Yield (%)	2.9	4.3	3.7	4.1	2.9	3.8	4.4	4.8
BV/Share (EUR)	6.28	6.47	6.77	6.95	7.26	7.90	8.37	8.88
Price/BV (x)	1.35	1.41	1.44	1.38	1.99	1.36	1.29	1.21
Weighted average shares (m)	182	182	182	182	182	182	182	182
Average market cap (EUR m)	2,214	1,574	1,670	1,525	2,197	1,955	1,955	1,955
Enterprise value (EUR m)	2,909	2,109	2,162	1,942	2,639	2,486	2,377	2,285
EV/Sales	1.46	1.13	1.28	1.10	1.38	1.19	1.09	0.99
EV/EBITDA	7.6	6.0	7.4	8.0	10.1	7.7	6.6	5.7
EV/EBIT	11.7	9.1	11.3	12.3	14.9	11.2	9.5	8.2
EV/Operating Capital	1.6	1.3	1.3	1.4	1.8	1.4	1.3	1.1
INCOME STATEMENT (EUR m)								
Sales revenue	1,992	1,859	1,686	1,765	1,911	2,081	2,186	2,312
Operating EBITDA	381	353	291	242	261	323	362	402
Depreciation	66	61	59	61	66	75	86	0
Amortisation	66	60	41	24	18	25	25	124
EBIT	249	232	191	157	177	223	251	278
Net interest income(expense)	-40	-32	-23	-23	-18	-27	-24	-22
Associates/affiliates	0	0	0	0	0	0	0	0
Investment/other income(expense)	9	3	0	0	0	0	0	0
Exceptionals/extraordinaries	-162	-38	-3	0	0	0	0	0
Income tax expense	57	56	44	20	31	47	54	67
Minorities/preference dividends	2	1	-1	2	3	2	2	2
Net income	-4	108	122	112	125	147	171	188
CASH FLOW (EUR m)								
Cash flow from operations	93	367	246	369	232	162	282	292
Movement in net working capital	-80	155	-63	215	53	-108	-19	-37
Capex	-163	-147	-158	-122	-220	-300	-280	-210
Free cash flow	108	220	91	254	16	-134	6	85
Other investing activities	147	-5	15	-105	34	132	32	4
Equity raised(bought back)	0	0	0	0	0	0	0	0
Dividends paid	-64	-68	-62	-62	-64	-73	-85	-94
Net inc(dec) in borrowings	0	0	0	0	0	0	0	0
Other financing cash flows	12	0	0	0	0	0	0	0
Total cash flows from financing	-52	-68	-62	-62	-64	-73	-85	-94
Net cash flow	25	147	41	80	-18	-79	-51	-8
Movement in net debt(cash)	-25	-147	-41	-80	18	79	51	8
BALANCE SHEET (EUR m)								
Cash and other liquid assets	311	401	402	217	144	-35	-187	-249
Tangible fixed assets	706	714	742	743	837	972	1,086	1,142
Goodwill	27	27	24	17	13	9	5	1
Other intangible assets	228	204	186	135	156	205	243	257
Associates/investments	43	82	95	278	270	190	180	150
Other assets	1,319	1,320	1,176	1,018	1,039	1,156	1,206	1,275
Total assets	2,634	2,747	2,624	2,407	2,460	2,497	2,532	2,576
Interest bearing debt	926	869	833	568	513	413	313	213
Other liabilities	554	675	553	564	605	636	684	731
Total liabilities	1,480	1,544	1,386	1,132	1,119	1,049	997	945
Shareholders' equity	1,141	1,174	1,230	1,262	1,319	1,434	1,519	1,613
Minorities	14	13	7	13	22	14	16	18
Total shareholders' equity	1,155	1,187	1,237	1,275	1,341	1,448	1,535	1,631
Net working capital	876	737	784	569	515	623	642	679
Net debt(cash)	615	468	431	351	369	449	500	462
Capital	1,770	1,655	1,668	1,626	1,710	1,896	2,035	2,093
RATIO ANALYSIS								
Sales growth (%)	-5.0	-6.6	-9.3	4.7	8.2	8.9	5.1	5.7
EBITDA Margin (%)	19.2	19.0	17.3	13.7	13.6	15.5	16.5	17.4
EBIT Margin (%)	12.5	12.5	11.3	8.9	9.3	10.7	11.5	12.0
Payout ratio (%)	nm	63.2	50.7	55.3	51.3	50.0	50.0	50.0
ROE (%)	-0.3	9.3	10.2	9.0	9.7	10.7	11.6	12.0
Return on Capital (%)	-0.3	7.5	8.4	8.0	8.4	9.3	9.6	9.9
Operating Return on Capital (%)	-0.6	9.0	8.5	8.6	9.9	10.5	10.5	10.6
Capex/sales (%)	8.2	7.9	9.4	6.9	11.5	14.4	12.8	9.1
Capex/depreciation (x)	1.5	1.3	1.6	1.5	2.7	3.1	2.6	1.7
Net debt/equity (%)	53.2	39.4	34.8	27.5	27.5	31.0	32.6	28.3
Net interest cover (x)	6.2	7.3	8.3	6.8	9.8	8.2	10.7	12.7









Source: Company data, Deutsche Bank estimates

Investment thesis

Outlook

After a series of disappointing quarters, in March 2005 BNG announced a change in its commercial strategy with a drastic increase of its mark-up policy towards its franchising partners and a re-focus of its business model. The key features of the turnaround focused on the supply chain (Dual Supply Chain, featuring a bottom-up, pull-driven process to maximise sell-out and service to the network, and more flexible delocalisation of production) and on the reshaping of the collections resulting in an updated and timely offer.

This strategy appears to have worked and earnings releases over the last 12 months indicate an improvement of the volumes trend at sell-in and sell-out. The Group's turnaround will prove sustainable, we believe, and the renewed interest in wholesale new openings (+348 stores in the last twelve months, after a few years of network contraction, which have contributed for 5 pp to the c. 12% volumes growth in 2007) and the strong same store orders growth (+7% yoy) represent the health of BNG's current fundamentals. This is an initial achievement which should help to win back the favour of investors, while improvements in retail will represent the new management next challenge. The organic performance at wholesale should signal that more focus on retail management could result in similar improvements in performance.

All in all, we expect BNG continue to deliver high single digit volume and mid-single digit sales growth over the next three years. As in 2007 we expect neutral price policy impact, we assume a rebound in margins from 2007. BNG's current thirst for top-line is materialising in high capex mostly dedicated to commercial investments. We expect net profits to show a 14% 3-year CAGR on the back of a 6-7% top line growth and an average 100bp margin p.a. expansion thanks to efficiencies, better sales mix and the end of the mark-up policy.

True, there are a few issues still pending before a final settlement with investors i): visibility on the new management is still low; ii) retail execution must be improved; iii) credibility that the wholesale recovery is sustainable must be restored. We expect numbers over the next few quarters to remain encouraging thus fuelling investors' confidence.

Valuation

We favour a DCF based valuation for BNG vs. a multiples based valuation as the former better captures the improving margin and cashflow generation that we envisage while a multiples approach is too short-term in our view. Our DCF yields a TP of Euro 14.8, based on 1.3% perpetuity (consistent with the deflationary pressures to which BNG is subject) and our WACC is at 7.4% (4.5% RP, 4.5% RFR, 80% equity based capital structure, beta of 0.9). We assume a partial success of the strategy (exit EBIT margin of 12.8%). On multiples, BNG is trading at an average 25% discount vs. its retail peers. This level might seem appropriate based on current profitability differentials. However over 3-5 years BNG should partly close the profitability gap moving from the current 10-11% Ebit margin towards mid-teens while we think room for improvements for most peers is limited given current high levels. This would exceed our forecasts. True, an act of faith is involved, but we suggest that downside is limited. Indeed, on property adj. multiples the discount vs. peers would widen by 15%. This together with a sustainable >3% dividend yield offers good downside protection.

Risks

In addition to macroeconomic risks, the main risk is linked to the successful execution of the re-launch strategy. In particular, should BNG decide to be more aggressive on prices and fight a price war with the competition, there could be visible margin erosion. On the upside, earlier-than-expected delivery of results and better-than-expected trends in margins could result in earnings upside.

Valuation

Excessive discount?

Figure 1: Trading comparable multiples

	FX	Current Price	TP	DB rec.	EV/Sales 2007	EV/Sales 2008E	EV/EBIT 2007	EV/EBIT 2008E	EV/EBITDA 2007	EV/EBITDA 2008E	Adjusted P/E 2007	Adjusted P/E 2008E
Benetton	EUR	10.8	14.8	Buy	1.2	1.1	11.2	9.5	7.7	6.6	13.1	11.3
Hennes & Mauritz	SEK	368.5	470.0	Buy	3.6	3.1	15.3	12.9	13.8	11.7	23.0	19.0
Inditex	EUR	42.9	50.0	Buy	2.7	2.3	15.7	13.3	12.1	10.3	22.4	19.2
Marks & Spencer	GBP	574.5	815.0	Buy	1.2	1.1	9.6	8.6	7.6	6.8	12.4	11.0
NEXT	GBP	1,880.0	2,650.0	Buy	1.4	1.3	8.8	8.3	7.2	6.7	11.5	10.4
Gruppo Coin	EUR	5.7	7.2	Buy	0.8	0.7	10.3	8.4	7.1	6.0	18.5	14.4
Esprit	HKD	112.9	130.2	Buy	3.7	3.1	16.9	13.7	15.5	12.6	21.8	17.9
GAP	USD	17.9	22.0	Buy	0.8	0.8	11.0	10.7	7.4	7.4	19.3	17.1
Abercrombie & Fitch	USD	78.5	75.0	Hold	1.7	1.4	8.8	7.4	7.5	6.3	15.1	13.3
Guess	USD	45.7	62.0	Buy	2.4	2.0	16.4	13.0	13.8	10.9	23.8	19.8
Average					**2.0**	**1.7**	**12.4**	**10.6**	**9.9**	**8.5**	**18.1**	**15.3**
Benetton Disc/ premium					*-38.8%*	*-37.9%*	*-8.5%*	*-12.4%*	*-26.6%*	*-29.5%*	*-27.4%*	*-26.8%*

Source: Deutsche Bank

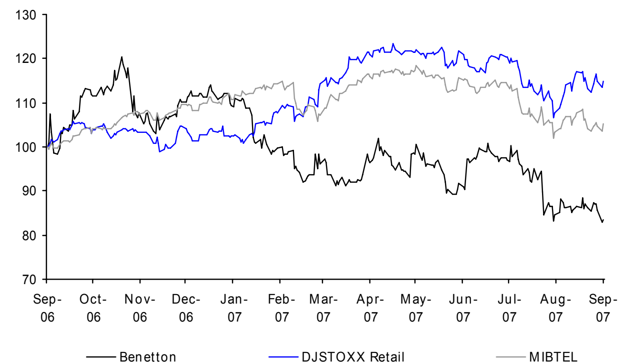
BNG is currently trading at an average 20-25% discount vs. its retail peers. We do believe the stock continues to discount an excessively high execution risk, considering that the bulk of the restructuring efforts have already been completed, but we believe the situation could improve as the CEO (who only started on 1 June) becomes more visible.

The strong underperformance has occurred despite a stable or even improving outlook (see Figure 4 and Figure 5).

Figure 2: BNG forward PE

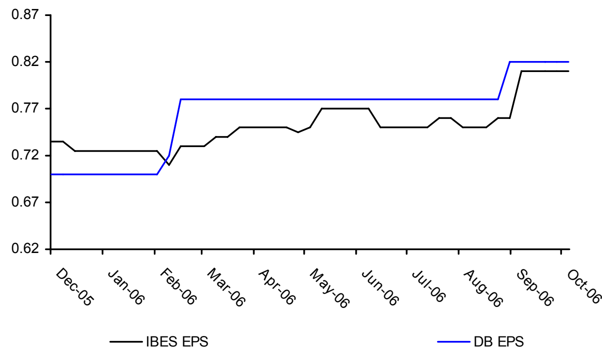
Source: Datastream

Figure 3: BNG Share price performance



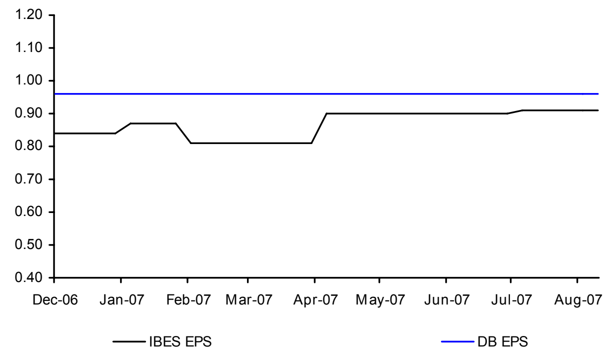
Source: Datastream

Figure 4: IBES/DB EPS 2007E



Source: Deutsche Bank and IBES

Figure 5: IBES/DB EPS 2008E



Source: Deutsche Bank and IBES

However is this level fair or is it excessive? The company is already delivering results:

- apparel sales have been growing in the last eight quarters;
- operating profitability has started to revert in Q2;
- the network has reacted positively to company's efforts and after a high-single-digit growth in S/S 07 volume mix, the Company has recorded a similar performance in A/W 07 despite the end of the mark-up policy

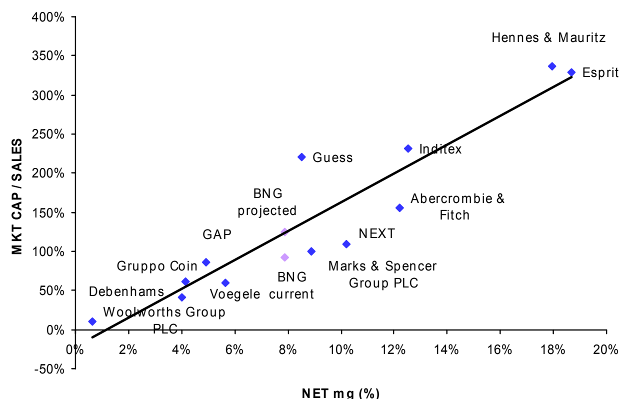
On the other hand, levels of margins at BNG are structurally lower than many of its competitors also due to the different business model (BNG is 80% wholesale):

Therefore in theory people would be tempted to justify the current level of discount, which broadly mirrors the profitability differentials existing between BNG and many of its peers. However, we would bring the following arguments to sustain our view that the current valuation is penalizing for BNG:

- BNG apparel business margin used to be in the high teens -low twenties until 2001
- The turnaround efforts have been extremely demanding both in terms of investments and in terms of strategic re-thinking. Hence BNG must have ambitious profitability targets, which we understand would be at least in the mid-teens area
- The market (including ourselves) is at best only discounting an improvement of up to 12% margin over the next 3-4 years
- The comparison between BNG and the retailers peer group does not take into account the real estate owned by BNG. The property-adjusted multiples offer a more interesting picture, as the average discount to the sector would widen by an average of 15%

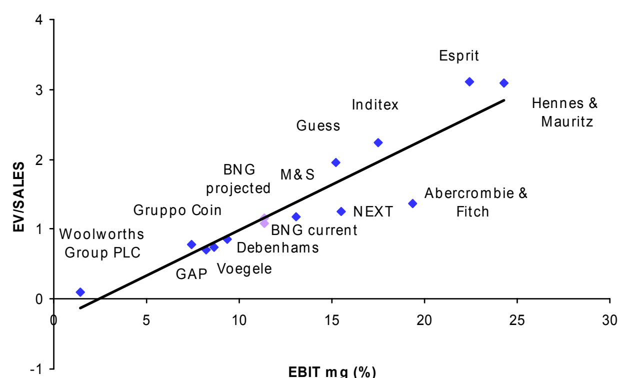
All in all we therefore believe that a multiples comparison offers a threshold for the BNG re-rating potential, and certainly suggests limited downside.

Figure 6: Market Cap/Sales vs. net margin (2008E)



Source: Deutsche Bank

Figure 7: EV/Sales vs. EBIT Margin (2008E)



Source: Deutsche Bank

Accounting for the value of properties

There is a key feature that undermines the comparison as shown above, which is the real estate portfolio at BNG. European retailers have very little property value in their balance sheets, and they tend to have leaseholds on the stores that they run. This means that only a very small percentage of their stores are owned and real estate represents only a small proportion of their capital employed. Of course this excludes leaseholds.

Figure 8: Importance of property assets for selected retail peers

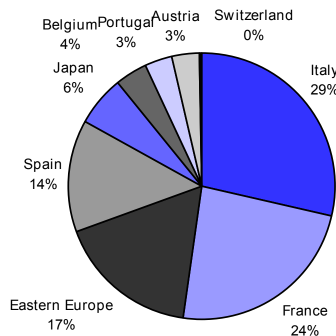
	Properties as % of Tangible Fixed Assets	Properties as % of Sales	Properties as % of Market Value
Hennes & Mauritz	8.5%	0.8%	0.2%
Inditex	23.3%	4.9%	1.7%
Next	13.9%	2.1%	1.8%
Marks & Spencer	59.1%	25.6%	24.9%
BNG	**75.30%**	**30.8%**	**32%**

Source: Company data, Deutsche Bank

BNG's real estate portfolio consists of retail stores (50 locations owned with an overall book value of Euro 508m) as well as headquarters and production plants (an additional c. Euro 120m).

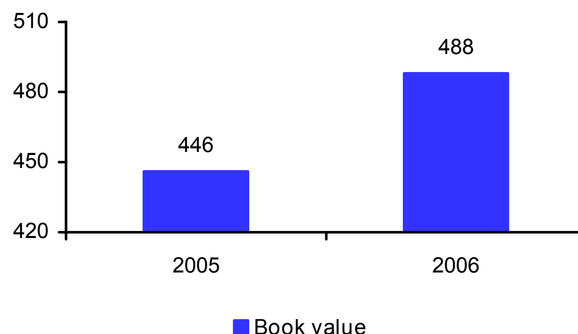
The retail assets are mainly located in prime locations, in Europe but increasingly more in Eastern Europe and the Far East, which have been acquired mainly over the last decade. The market value of such assets could be close to Euro 1billion, we believe. In the past, the company has always reiterated its intention of retaining its commercial real estate portfolio, which is considered a strategic asset by the company. We present below a geographical breakdown of the real estate portfolio. We understand most of the growth was driven by growing involvement in Eastern Europe.

Figure 9: : BNG – Real estate breakdown by market 2006



Source: Deutsche Bank

Figure 10: Real estate Value (Euro m)



Source: Deutsche Bank

In order to achieve better comparability between BNG and the other retailers we have broadly speaking two options: (i) to consider the value of the capitalized leases for the other retailers in their multiples; (ii) to adjust BNG's numbers and multiples to reflect its high exposure to retail while imputing to the P&L the difference between a notional lease charge (6% est.) and the depreciation charge (on 30-years).

We choose the second procedure because it is simpler, given that both methods should lead to similar conclusions, i.e. the widening of the valuation gap between BNG and the average.

Also we note that as shown in Figure 13 and Figure 14 below, adjusting retailers' ROCE to include capitalised leases brings the peers returns back in scale with BNG.

Figure 11: Benetton Group Real-estate adjusted multiples, with real estate @ book

	2007	2008	2009
Market Cap	1961	1961	1961
EV	2409	2461	2423
Less real estate (est. value)	-600	-600	-600
Residual Equity Value for casual	1361	1361	1361
Residual EV for casual	1809	1861	1823
- Implied EV/sales	**0.9**	**0.9**	**0.8**
- Implied EV/EBITDA	**6.7**	**6.1**	**5.3**
- Implied EV/EBIT	**8.6**	**7.9**	**7.0**
- Implied PE	**10.1**	**8.5**	**7.7**
EBITDA adj	268.7	304.6	344.1
EBIT adj	209.4	234.8	262.1
Net profit adj	135.3	159.7	176.4

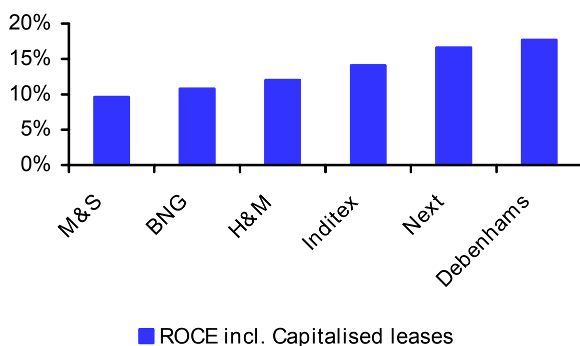
Source: Deutsche Bank

Figure 12: : Benetton Group Real-estate adjusted multiples, with real estate @ market

	2007	2008	2009
Market Cap	1961	1961	1961
EV	2409	2461	2423
Less real estate (est. value)	-1000	-1000	-1000
Residual Equity Value for casual	961	961	961
Residual EV for casual	1409	1461	1423
- Implied EV/sales	**0.7**	**0.7**	**0.6**
- Implied EV/EBITDA	**5.8**	**5.2**	**4.4**
- Implied EV/EBIT	**7.0**	**6.4**	**5.6**
- Implied PE	**7.5**	**6.3**	**5.7**
EBITDA adj	244.7	280.6	320.1
EBIT adj	202.5	227.9	255.2
Net profit adj	127.7	152.1	168.8

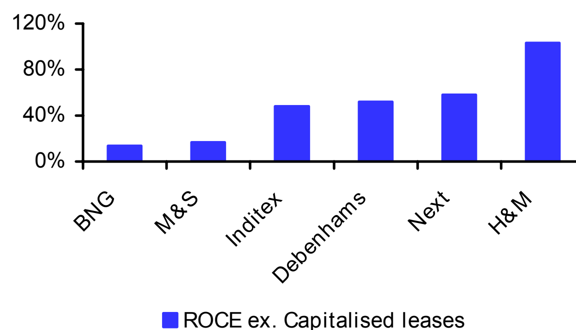
Source: Deutsche Bank

Figure 13: ROCE inc. Capitalised leases



Source: Deutsche Bank estimates

Figure 14: ROCE ex. Capitalised leases



Source: Deutsche Bank estimates

Discounted Cashflow

We believe the DCF valuation approach allows to better capture the margin recovery and cashflow generation potential for BNG. As such we use it as our primary valuation tool and we embed a reasonable margin progression scenario, which is not too aggressive (we reach 12.8% as the exit Ebit margin level, while we believe that the Company has more ambitious internal targets).

Our DFC analysis is based on the following summary assumptions …

Figure 15: Benetton Group DCF Summary Assumptions

	2006-09E	2009E-2015E
Sales CAGR	6.6%	4.8%
EBIT CAGR	15.7%	6.6%
EBIT Margin EOP	12.0%	From 11.7% to 12.8%
Capex % of sales	14.4% in 07, 12.8% in 08, 9.1% in 09	7% down to 5-6%
NWC as % sales	c. 25%	c. 25%
Tax rate	25%	Growing to 30%

Source: Deutsche Bank

…and yields the results shown in the table below. We believe this represents a fair valuation assuming that the execution of the group strategy does not lead to any major further margin erosion; indeed, in our model we assume a gradual margin improvement to 12.8% as the exit margin. We believe that the market is now requiring an increasingly lower discount factor for visibility as the first benefits of BNG's turnaround are starting to materialise.

Figure 16: Benetton Group Summary DCF Valuation

Risk free	4.5%
Risk premium	4.5%
beta	0.9
WACC	**7.4%**
Perpetuity	**1.3%**
Sum of NPV	990
TV	2249
EV	3239
NFP	-449
Other liabilities	-103
Equity	2687
Nr shares	181.5
Fair price	**14.8**

Source: Deutsche Bank

Corporate Issues

Finally in this section we address a few issues that we believe are significant for BNG's share price performance.

- **Shareholders**. True, the family will likely remain a cumbersome presence however we feel that as Mr. Alessandro Benetton is gradually taking the responsibilities of Chairman Luciano. We sense that Mr. Alessandros' decision to be the spokesman for the Company is also a sign of commitment and great responsibility that he is taking vis-à-vis the group's stakeholders. Continuity in the vision will be kept while more freedom is increasingly granted to the management in the execution phase. The Company has performed a transition and today is more a managerial company than it was before.
- **Management**. We sense that the vast international experience in a tough sector (Mr. Caccia Dominioni was previously Vice Chairman and COO of Warner Music International) should allow the new CEO to be competitive in his new task. We believe that his first contacts with the market will be critical in order to strengthen investors' confidence in the execution of the Group's relaunch phase.
- **Real estate.** Despite the analysis presented above regarding the influence of real estate on BNG's returns and valuation multiples, we are not expecting BNG to decide on a disposal of these properties in the medium term. BNG majority shareholders and its management regard the real estate assets currently in BNG's portfolio as strategic, given that most of the 51 properties are in primary locations. We believe the company to be fully aware of the issue, and we also believe the company has explored a wide range of options (from securitisation to spin-off to sale & lease-backs), none of which we believe provided enough long-term control over these assets. We cannot rule out that a valorisation of these assets could take place as the market creates more flexible financial instruments (including real estate funds)

- **Ordinary payout**. BNG has been able to maintain its committed 50% pay-out even during difficult times without any major balance sheet disruption. This has translated into a nice >3% dividend yield, which we believe will be preserved.
- **Reserves**. BNG has approximately Euro 535m of distributable reserves (June-07). Given the health of the balance sheet and the low level of financial gearing (debt/equity ratio below 30%, net debt/EBITDA of 1.4x) we would look favourably at the partial distribution of these reserves, which would improve the financial structure as well as provide a healthy dividend (the Euro 600m represent more than 8x the yearly dividends payment of the group).

Risks

- Macroeconomic variables and in particular GDP and consumption growth in Italy, Europe and globally
- The apparel retail sector is mature: a decision to pursue more aggressive commercial policies to respond to competitive threats might eventually lead to deterioration in the company's profitability
- The apparel retail sector is characterized by low entry barriers and companies' strategies tend to address similar goals in terms of sourcing, and of new markets opportunities
- The heavy commercial real estate investments might dilute the Company's margins and returns if the Company does not manage to produce the expected top line contribution
- The end of the favourable mark-up policy that has supported the network might lead to a more cautious ordering by the franchised stores partners resulting in lower sell ins and potential working capital risks
- The new business model is increasingly more focused on lower contribution of the base collections resulting in greater inventories risk at BNG. We believe that as BNG progresses in its learning curve, and lead time declines, this risk could gradually decrease over time.

Phase 1: increasing volumes through mark-up: done

A recap of major evolution in the business model

After a series of disappointing quarters, in March 2005 Benetton announced a change in its commercial strategy with a drastic increase of its mark-up policy towards its franchising partners and a re-focus to its business model with a view to improving its relationships with the network of franchised partners.

The more favourable commercial terms granted to the commercial network were only one of the ingredients of a more complex strategy. The other key features of the turnaround focused on i) the supply chain (Dual Supply Chain, featuring a bottom-up, pull-driven process to maximise sell-out and service to the network, and greater and more flexible delocalisation of production) ii) the reshaping of the collections with product and mix enrichment and more frequent shipments to the stores resulting in an updated and timely offer and iii) higher involvement in direct retail.

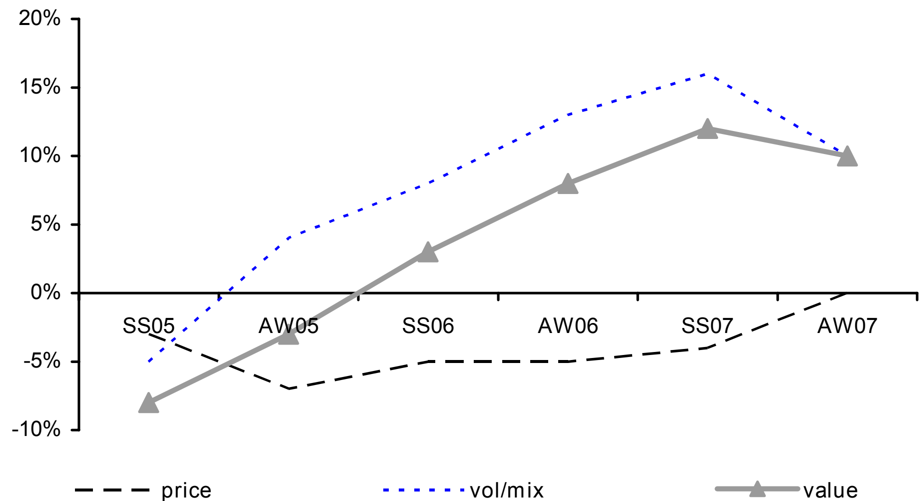
BNG was driven by the need to tackle the following issues:

- reverse the negative trend of its commercial partners. Not only numbers declined (stores from >5,300 in 2000 to c. 4,900 in 2004), but also the orders per store were reduced.
- tackle the increasing competition, and the deflationary pressures in its main markets (Italy and Germany, 55% of sales) and the cautious network ordering
- address the fact that the products were less appealing for consumers boasting old-fashioned collections structure (2-season format, with base assortments covering 80-90% of all orders in two shipments per year) and a simplistic, unsophisticated pricing policy (no nice price items, for example)
- improve efficiency of the supply chain though a better sourcing mix and lower weight of Italian manufacturing
- the retail structure was generating a growth in retail costs (rents, personnel, capex)

The chart below clearly marks the time of the decision: following the unsuccessful S/S 2005 collection. It also shows the positive impact that changes have triggered on Group's sales. Figure 17 below also shows, however, that more generous commercial terms and an overall improved level of service and quality of collections have translated into an increasing confidence of the franchising partners, who have reverted their orders trend, highlighting that the repositioning of the brands has produced the desired effect, i.e. that of volumes pick-up, even without the incentives to the network (for F/W 2007 there mark up incentives are zero, and we believe that product and mix improvements could start to drive average prices up).

Better rotation of the products, more attention to commercial activities and visual merchandising, lower initial orders commitments for the base collections thanks to the possibility of re-assortments and the special projects has created a positive mood among store-runners and among consumers.

Figure 17: Evolution of sell-in sales (% YoY change)



Source: Deutsche Bank on Company data.

The new strategy had some implementation costs:

- mark-up efforts for a total Euro 180m negative impact on the contribution margin in three years,
- investments in retail/infrastructure/IT/logistics/manufacturing for a total of gross capex of Euro 427m (of which Euro 319m for commercial investments, Euro 60m for operations and the remaining 48 for other investments)
- On the other hand, attention to the cost structure and higher delocalisation have translated into some cost savings (savings at an average of Euro 1-2m at gross margin for every 1% of delocalized production), which have not been enough to compensate for the negative impact of mark-ups.

Figure 18: Summary Impact of mark-up policy vs. delocalization benefits – 2004-07 cumulative

Euro m	M/up	Delocalisation
2005	80	20
2006	80	30
2007	20	15-16
Total cumulated	**180**	**65-66**
Net negative impact on a 3 years period		**105**

Source: Company data, Deutsche Bank estimates.

Brand, product and collections at the core

The mark-up policy was only an ingredient of the new BNG's recipe which mostly revolves around the product, the collection and the service. More importantly, BNG's strategy to relaunch the brand and regain competitiveness vs. other retail players included brand revitalisation actions aimed at enhancing the UCB brand appeal with consumers, to increase the frequency of customer visits and attract new clients. BNG commercial strategy is now closer to that of its main competitors, and this should be the major revenue driver for the group going forward.

BNG used to work on the basis of a 2-season format (Spring/Summer and Autumn/Winter) with a base collection, delivered to the stores around 6 months before starting of the sell-out accounting for 80-90% of total orders. This structure had the benefit of optimizing Castrette's logistics efficiencies but: i) obliged the franchisees to place the bulk of its orders too early, when visibility on fashion trends was still limited; ii) granted no or only limited opportunity to adjust the collections while in-season; and iii) did not allow to respond to commercial feedbacks.

The key change at BNG has been the strengthening of the product appeal by using a different approach to collections and updating them more frequently.

- **Number of collections.** BNG has gradually started to offer four collections plus one per season (starting with A/W 2006) instead of two as well as special projects with an in-season monthly roll-out schedule in order to continuously refresh the offering and to take advantage of the season's hottest trends, all with the aim of increasing in-store traffic and eventually raise brand appeal, via offering a renewed product range and image. The base collection is hence lighter and should continue to gradually decrease as a percentage of total. This new collections-roll out is now possible thanks to improved lead times which are now five to six weeks for flash collections and seven days for special projects. Collections now feature the following:
  - Contemporary 1 (8 to 6 months to sellout): the earliest collection marketed to the network, based on the main trends highlighted by fashion fairs.
  - Contemporary 2 (6 to 4 months to sellout): a first alternative
  - Trends (4 to 2 month to sellout): incorporate most recent fashion trends
  - Just-in-Time/Flash (2 months to 2 weeks):
  - Evergreen (2 to 1 week): recurrent base items.
- **On-line ordering**. The possibility of ordering on-line, 24 hours a day and seven days a week, the continuative products (so called, never-out-of-stock) with timely deliveries. Delivery is granted within 7 days in Italy and 14 abroad. This is possible as the company keeps a higher degree of inventories for this collection, allowing the network to carry lower inventories.
- **Communication**. A stronger link between visual merchandising, communication on the pos, events and promotions, and corporate communication and the roll-out of collections.
- **Product mix**. A richer product mix to increase the average ticket (hanging garments, menswear and accessories).
- **Accessories**. A focused and extensive accessories project covering both UCB and Sisley, ranging from bags to luggage to office products. BNG is enlarging the product range and building proper accessories collections Accessories guarantee a higher gross margin, and translate into incremental revenues. Ultimately it is in the interest of the group's commercial partners to have a rich sales mix which delivers them a higher gross margin. A step forward is the creation of corners in the stores dedicated to accessories. In the creation of the collections BNG is also placing a great attention to materials and particular features which could differentiate the product in terms of quality and usability while keeping a very competitive price positioning. Accessories could indeed represent a new important growth opportunity as accessory sales are expected to increase from 3-4% of total sales to 10% (today 7%), which would be in line with its competitors.
- **Pricing**. A more sophisticated pricing, including also the introduction of 'nice prices' which is the result of a 'target cost' approach to production and which allows now a more complete coverage of all price points for each product category.

Not a price strategy

Price is now a less relevant variable in BNG's strategy: The Euro180m mark-up policy investment was mostly directed to the network of commercial partners to improve their profits. If any, very little of these benefits was passed on to retail prices. This makes sense given that price would be the most dangerous variable to move. We believe that entering a price war with its competitors would not be a solution: reducing prices translates negatively into margins, and if BNG were to consider reducing retail prices, they would need to do that by a large amount, given the existing price differential with competition. That would put BNG in a lose-lose situation.

Indeed, price cuts required to reduce the average selling price gap vs. competition would need to be of a substantially different magnitude (Euro 100m would mean a 3-4% decline in average retail price, much lower than the current retail price differential between UCB brand and some of its competitors). Management has thus been unwilling to follow this road and has been devoting greater efforts on the denominator of the price/quality ratio (by keeping good quality fabrics, design and cut, enlarging collections, improving time to market, the shopping experience and service etc).

Attention to retail

Retail ranks among the group's top priorities. Although BNG is still dependent on its network of commercial partners, it also has 348 DOS, which should generate an estimated Euro 420m of sales in 2007E, representing nearly 25% of the group's apparel revenues vs. 15% three years ago.

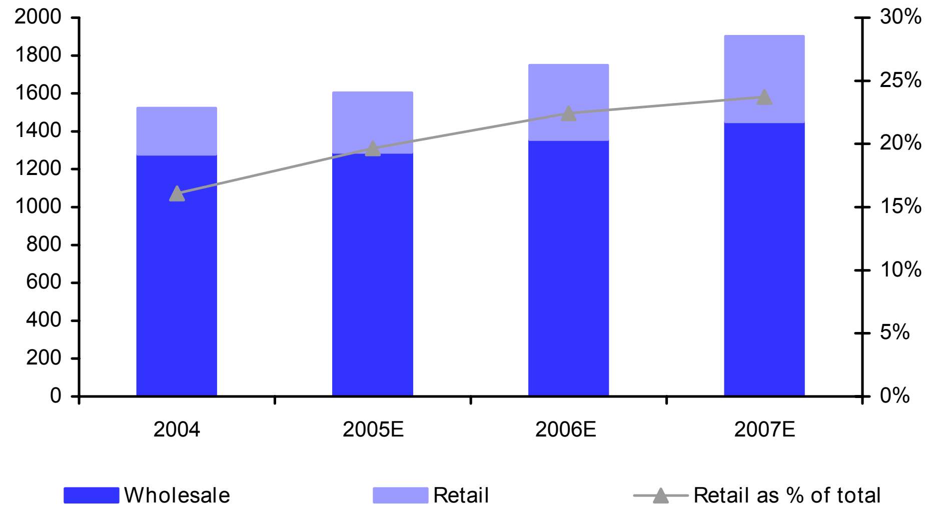
One of the key changes is that BNG is becoming increasingly involved in retail through more effective management of its own stores and through more intense collaboration with the network of its commercial partners.

The refocus on retail has required considerable efforts on the part of the team and the organisation, and as this has been completed attention has moved to the improvement of the sell-out and the real-time monitoring of stores performance. Greater sophistication in retail techniques, use on the whole network of detailed information gathered at DOS, and proactive management of stores and network should all drive to an improvement in store performance.

In this respect BNG has also been introducing new software to monitor sell-out performances at its DOS. Although they only represent ca. 6% of the total stores base, this information allows BNG to better predict reorders of the entire network, which should reduce unsold stock and improve overall efficiency. In addition to its DOS network, BNG is also rolling out this software to a number of independent stores. More than 300 wholesale stores (the number is constantly evolving) and all DOS are now on line offering immediate reading of the sell-out (in any case 40% of total sales are realized by the 50 top accounts making the reading of sell-out data easy).

We expect the critical mass at retail and the maturing store network to translate into growing profitability. We expect FY2007 to close with positive profitability in the 7% EBIT margin range, despite new openings continuing. This is because the scale of the business is increasing, and so is the number of 'older' stores, i.e. stores with positive profitability.

Figure 19: Benetton Group – Casualwear sales breakdown by channel (Euro m)



Following adoption of IFRS accounting, Retail includes S. Korea corners

Source: Company data, Deutsche Bank estimates

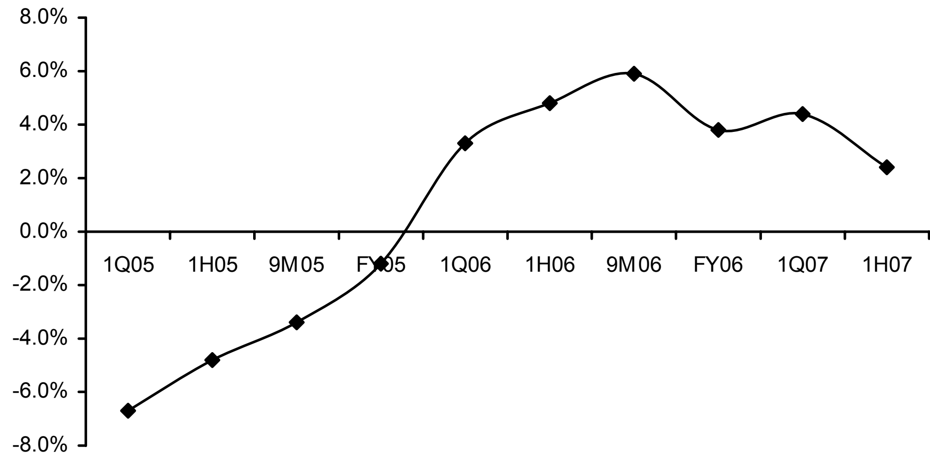
Attention to sales densities

Attention is on increasing sales per square meter as a key growth driver. This is true for both the DOS and the network of franchising stores.

BNG is focusing on reorganising and improving store lay-outs and visual merchandising (in addition to better products and collections) to attract increasing traffic and improve conversion rates to raise revenues. An improvement of the product mix with more hanging garments, menswear collections and upgrade of core products should also help raising the average ticket per customer therefore improving sales/sqm.

The lack of indications on the selling surface per channel (we know that total selling area in 2004 was close to 790-800k sqm), and on the selling area per store (wholesale vs. retail) does not allow us to perform any grounded analysis of sales/sqm performance or benchmarking it to its competitors.

Figure 20: Benetton Group – Retail like-for-like sales (% YoY chg)



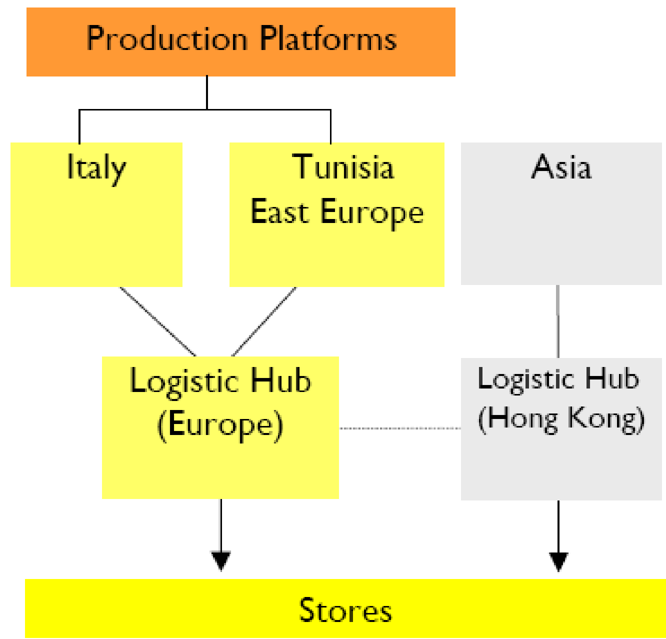
Calculated on stores opened at least 12 months.

Source: Company data.

New supply chain management

Six years ago 80% of the production was taking place in Italy and logistics was centralised in Castrette. Today the company relies on greater (owned) infrastructure in foreign countries. Benetton's process of delocalising production started in 2004. Production is now only 15% realised in Italy (including Istria and Croatia), c. 30% is now in the Far East including India and the bulk in other Mediterranean areas. 75% of the production is however realized in BNG plants to assure quality. The Company has three hubs in the Far East (Hong Kong, Shenzen and the new Shangai) in addition to the historical facility in Castrette.

Figure 21: Benetton Group – A snapshot of operations



Source: Company data.

To support its changes to the commercial strategy, BNG had to readapt its supply chain and has therefore invested in its manufacturing and logistics processes to achieve higher flexibility, speed and efficiency.

- **Flexibility**: pursued the geographic allocation of production according to time to market (eg early collections mostly in the Far East, just-in-time products in Europe to be as close as possible to the final market).
- **From Push to Pull.** BNG has moved from the old "Push" model of a business based on a one-way direction from design and production down to the final customer to a "Pull" model, ie a two-way, integrated approach responding to the inputs coming from commercial and retail operations
  - Better production planning
  - Accelerate the time to market. This is to be achieved by leveraging on a new supply and logistics system made of sub-hubs based mostly in low-cost countries with more modest manufacturing still taking place in Italy. In this effort the fully centralised procurement of raw materials with internalisation of supplies is clearly a key advantage. In this respect while early deliveries of the base collections still mostly respond to a Pull system targeting the minimisation of the costs (outsourcing in the Far East), in-season deliveries respond to a Pull system and therefore target the optimisation of timing and service
  - Focus on higher product quality, new materials, focus on comfort, quality and easiness of care, better product finishing.

New cost structure

These investments also add to the group's commercial investment, which are part of the strategy to upgrade the network and the shopping experience (larger stores) and to facilitate investments in the stores for its franchised partners. In this framework BNG has made investments in a total number of >600 stores out of a network of ca. 5,000 as follows:

(i) acquiring the property of some stores (51); of these 51 stores, 12 are DOS, the remaining 39 are rented to and managed by third parties

(ii) paying rents and in some instances key money on 336 stores which are DOS (adding to the 16 above thereby making a total of 346 stores)

(iii) Paying rents and in some instances key money on additional 346 stores for which BNG is the counterpart in the rental agreement. These stores are then sub-rented to third parties

The above has involved the following types of costs, which have been weighing on the group's accounts:

(i) amortization charges on refurbishments made (on all 346 stores)

(ii) amortisation charges on key money (when paid) and on the purchase of 'ramo d'azienda'

(iii) The gap between rents received and rents paid. BNG is basically implementing vendor financing mechanisms in order to facilitate the renewal of stores or the opening of new stores.

The cumulated investments to accomplish the above commercial project for the stores have exceeded Euro 1bn in the past five years, of which >Euro 508m invested in real estate (51 locations) and the rest spent on the key money and refurbishment for the other stores.

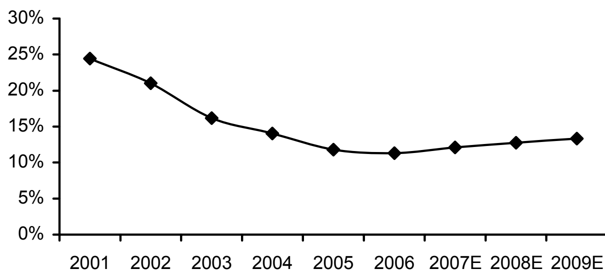
To take a very simplified approach, it is self-evident that this has raised the break-even point for the group: assuming for sake of simplicity a 20-years amortisation timeframe for the above, that means Euro 50m additional D&A per year (or roughly 3% of sales).

In addition over the same period of time BNG has invested some Euro 25m on average per year on IT and on operations.

In order to have the full picture on BNG's current margins (vs. the historical wholesale EBIT margin in excess of 20%) we need to account for significant deflationary pressures from changes in the market which have translated into a 2 pp erosion of the margin per year over the last five years, including the more recent mark up policy and the extension of the product range to include nice prices.

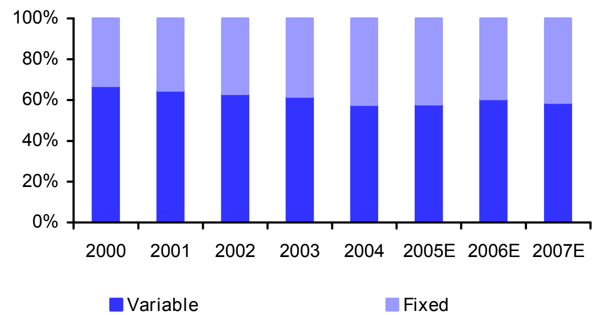
This explains why BNG today has a much heavier cost structure, resembling that of a retailer without being a retailer. This, however, offers a much greater opportunity in terms of operational gearing in the event of strong volume growth.

Figure 22: Benetton Group – Wholesale Casual EBIT margin (est)



Source: Company data, Deutsche Bank estimates

Figure 23: Benetton Group –Variable vs. fixed costs (est)



Source: Company data, Deutsche Bank estimates

Phase 2: Resuming Growth

Top line growth resuming

Alessandro Benetton has set a challenging 6-8% annual sales growth target over the medium term. This should come from both like for like (50%) and the rest from new openings (DOS or franchised stores).

Like for like performance

Like for like performance should be driven by increasing sales/densities in existing stores as a result of improved brand perception and improved products and collections (translating into higher traffic and higher conversion rates) plus a better sales mix and a better service.

- **Service**: Cluster collections built according to a standard to facilitate the selection by the store runners. It is reasonable to expect that it could represent 60-80% of each orders' size. This will shorten the number of weeks required to collect orders, translating into easier management of the supply chain, and should allow to have a more uniform presence on the market with similar best-selling items in all markets. It should also be a further step to reduce complexity of the collections: complexity was cut by 20-30% in the 2007 collections vs. A/W 2004.

- **Sales mix becoming richer**:
  - **Menswear** represents still only 20% of BNG collections, up from 11% a couple of years ago, but still below the industry average of around 30%. The biggest impact on menswear was given in the past two collections.
  - **Hanging garments** are also a growing percentage of sales as opposed to the basics
  - **Back to origin**. The Company is again pushing on the sale of woollen products/knitwear which presents a richer mix and offers unique competitive advantages being more difficult to process
  - **Accessories** should raise their contribution to 10% of sales at least although it is not unreasonable to expect a higher 15% level. This compares with 3-4% two years ago, and with 9% already in A/W 2006 (7% in S/S 2007).
  - **Children**: this is a lower contribution margin/mix area. In this respect the introduction of Sisley Young which has price points 20% above UCB children should translate into an improvement in the overall contribution of childrenswear
  - **Sisley**, the weakest performer to date is also starting to pick up (recent agreement with Chinese partner Hembly for the roll out of 250 stores, and with Tata in India).
  - **Playlife**, a dormant brand, has undergone a full revision, with a change the brand's identity and market positioning. Since the 2007 Spring/Summer, the Playlife brand operates in the lifestyle casual apparel segment (American WASP college positioning), similar to Polo Ralph Lauren or Abercrombie & Fitch, J Crew or Tommy Hilfiger. This segment is less competitive than traditional casualwear. Since the first store featuring the new concept and image was opened in Milano in Q107 the Group has already opened >30 more beating in H1 its FY target (the FY target has become 50). We believe that Playlife with this new identity could grow fast and even become a c. Euro 100m brand.

- **Undercolors**: launch of a new concept "Gloss" for both the domestic and international market to re-focus on and reap the opportunities of the appealing underwear segment with a dedicated offering and distribution.

New openings
BNG is still mainly a European retailer (86% of sales), and above all a domestic player with 48% of its sales coming from Italy.

BNG is now actively seeking new growth opportunities in new markets. New openings will be mostly concentrated in Eastern Europe and in the Far East.

- **Retail**. The company should leave the DOS number flattish at around 354 and increase shop-in-shops by some 40-50 units, and is adding 300 wholesale locations in 2007, on a total number of locations which is close to 5,100 presently. 10% of the existing BNG locations are now controlled by the Group via rents or real estate ownership.
- **China**. Stores presence in China, to be accomplished mainly through direct stores, should move from 100 to 250 in three years. In China BNG obtained the authorization last year for direct development.
- **India.** The company already has over 140 stores, of which two are flagships, which could also increase rapidly. India is already BNG's fifth market outside Europe. The recent agreement signed with Tata for the commercial development of the Sisley brand should fuel growth in this area, which is running at +40% growth.
- Within the **Far East**, South Korea (whose operations are fully consolidated into BNG's retail sales) is a particularly appealing for BNG representing 4% of sales
- In **Eastern Europe** the Company has >350 stores, and over 200 points of sales, and the number is also growing fast.
- **Turkey**. Further reinforce presence in the Turkish market, where since May 2005 BNG operates through a joint-venture including retail (they bought 50% of the company that used to manage BNG)

This expansion will be funded by capex of Euro 300m in 2007E and also in 2008E, and we expect capex to remain sustained in the >Euro 200m area also in the medium term. Capex will be devoted to both DOS and wholesale stores through forms of vendor financing for example, thereby generating a burden on overall consolidated D&A charges.

2007: margin expansion materialising:

As already visible in Q2 numbers, 2007 should be the year of the change in margins trend, and we see steady improvements going forward on the back of:

- The end of the mark-up policy with the 2007 S/S collection
- Volume gains and learning curve driving sourcing efficiencies
- Retail growing in the sales mix by channel. The increasing contribution of retail should drive gross margin (c. 65% at retail vs. 43% consolidated) and contribution margin (54-55% at retail vs. 35% at consolidate) expansion
- Improving the quality of the top line: higher sell-though (thanks to a better structuring of the collections, good products, customers service, store deliveries, in-season collections, replenishments etc)
- Enriching the product mix with accelerating contribution of: menswear; accessories; licensees; Sisley

- Fixed cost leverage will be mixed: on one hand higher productivity and efficiencies on growing volumes should produce a positive operational leverage. On the other hand however higher investments for stores expansion will translate into higher D&A, higher G&A and higher personnel costs which will partly eat up these operating improvements. This explains while EBIT margin expansion could be capped in the short and medium term

We believe our >11% EBIT margin estimate for the apparel business is challenging but achievable in 2007:

Figure 24: Benetton Group divisional sales and margin estimates (Euro m)

	2005	2006	2007E	2008E	2009E
Retail sales	315.0	392.2	423.5	449.0	475.9
EBIT	5.4	16.0	29.6	35.9	42.8
EBIT Margin	*1.7%*	*6.0%*	*8.0%*	*9.0%*	*10.0%*
Wholesale sales	1314.5	1379.8	1513.9	1633.1	1729.6
EBIT	154.9	155.8	188.7	210.3	230.6
EBIT Margin	*11.8%*	*11.3%*	*12.5%*	*12.9%*	*13.3%*
Total casualwear	1629.5	1772.0	1937.5	2082.1	2205.5
EBIT	160.3	171.8	218.3	246.2	273.5
EBIT Margin	*9.8%*	*9.7%*	*11.3%*	*11.8%*	*12.4%*
Textiles/Other	136.0	139.0	143.3	104.3	106.3
EBIT	-3.0	8.0	5.3	4.8	4.9
EBIT Margin	*-2.2%*	*5.8%*	*3.7%*	*4.6%*	*4.6%*
Consolidated	1765.5	1911.0	2080.8	2186.3	2311.8
EBIT	157.3	179.8	225.6	251.0	278.3
EBIT Margin	*8.9%*	*9.4%*	*10.8%*	*11.5%*	*12.0%*

Source: Deutsche Bank

Summary financial expectations

We expect Benetton's revenues to increase at a 6.6% CAGR over the 2006-09 period, in line with company's guidance of a 6-8% yearly top-line growth. Wholesale sales should to rise by an average 8% compound, while retail revenues should grow at a 6.7% CAGR, of which we believe two-thirds could be driven by like-for-like performance and the rest by additional selling area, also reflecting the sizeable investments in commercial real estate assets

Our EBITDA growth of estimate of c. 17% is below the Co's guidance of a +20% increase in 2007. We expect EBIT to rise at a 15.7 % CAGR over the next three years despite D&A rising due to capex.

The tax rate should stabilise around 25%. We forecast net income to increase at a 13.7% CAGR in the next three years.

FCF generation will be under pressure in 2007 and 2008, due to the sizeable investments plan (we expect Euro 300m of capex, in line with company's guidance). As such the Net financial position will move to c. Euro 450m in 2007E to some Euro 500m in 2008, however with positive FCF of Euro 34m in 2008 and assuming a payout of 50% in line with the Company's long-term guidance.

Consolidated Forecasts

Figure 25: Benetton Group: IFRS Income Statement (Euro m)

	FY2004	FY2005	FY2006	FY2007E	FY2008E	FY2009E
Revenues	**1704.0**	**1764.8**	1911.0	2080.8	2186.3	2311.8
Materials and 3rd parties	-779.0	-831.2	-962.2	-1007.1	-1049.4	-1098.1
Payroll	-87.0	-91.8	-81.0	-110.3	-113.7	-117.9
Industrial depreciation	-21.0	-21.0	-18.0	-21.0	-21.0	-22.0
Other industrial costs	-42.0	-42.2	-44.0	-48.0	-49.4	-51.1
Gross Profit	**775.0**	**778.6**	**805.8**	**894.3**	**952.8**	**1022.7**
Gross Margin	45.5%	*44.1%*	*42.2%*	*43.0%*	*43.6%*	*44.2%*
Distribution & transport	-48.0	-47.6	-63.0	-66.6	-67.8	-71.7
Sales commissions	-73.0	-77.7	-74.0	-77.0	-80.9	-83.2
Contribution margin	**654.0**	**653.3**	**668.8**	**750.8**	**804.1**	**867.8**
% of sales	38.4%	*37.0%*	*35.0%*	*36.1%*	*36.8%*	*37.5%*
Payroll	-126.0	-132.4	-153.0	-164.4	-172.7	-182.6
A&P	-54.0	-59.1	-72.0	-67.4	-70.0	-74.0
D&A	-74.0	-81.2	-66.0	-79.1	-89.6	-101.7
Other	-242.0	-200.6	-198.0	-214.3	-220.8	-231.2
EBIT	**158.0**	**180.1**	**179.8**	**225.6**	**251.0**	**278.3**
% of sales	9.3%	*10.2%*	*9.4%*	*10.8%*	*11.5%*	*12.0%*
Other & extraordinaries	0.0	0.0	0.0	0.0	0.0	0.0
Interest charges net	-22.0	-25.0	-18.0	-27.0	-23.5	-22.0
FX	0.0	0.0	0.0	-3.0	0.0	0.0
EBT	**136.0**	**155.1**	**161.8**	**195.6**	**227.5**	**256.3**
Taxes	-28.0	-43.4	-31.0	-46.9	-54.5	-66.6
Minorities	1.0	0.0	-3.0	-2.0	-2.0	-2.0
Net Profit	**109.0**	**111.6**	**127.8**	**146.6**	**171.0**	**187.7**
D&A	-95.3	-102.2	-84.0	-100.1	-110.6	-123.7
Other non-cash	-59.1	0.0	0.0	0.0	0.0	0.0
EBITDA	**312.4**	**282.2**	**276.0**	**325.7**	**361.6**	**402.1**
% of sales	18.3%	*16.0%*	*14.4%*	*15.7%*	*16.5%*	*17.4%*
% of sales						
Materials and 3rd parties	45.7%	47.1%	48.0%	48.4%	48.0%	47.5%
Payroll	5.1%	5.2%	5.4%	5.3%	5.2%	5.1%
Sales commissions	4.3%	4.4%	4.4%	3.7%	3.7%	3.6%
Payroll	7.4%	7.5%	7.2%	7.9%	7.9%	7.9%
A&P	3.2%	3.4%	3.5%	3.2%	3.2%	3.2%
Other	14.2%	11.4%	10.4%	10.3%	10.1%	10.0%

Source: Company data, Deutsche Bank estimates

Figure 26: Benetton Group: Balance Sheet (Euro m)

	FY2004	FY2005	FY2006	FY2007E	FY2008E	FY2009E
Inventories	255.5	287.2	330.8	331.9	348.8	368.8
Trade receivables	658.0	655.4	627.0	744.9	780.5	825.3
Trade payables	-285.1	-315.0	-403.0	-374.5	-393.5	-416.1
Operating working capital	**628.4**	**627.7**	**554.8**	**702.3**	**735.7**	**777.9**
Other current assets	262.3	74.9	81.1	79.1	76.5	80.9
Other current liabilities	-107.0	-133.8	-120.4	-158.1	-170.5	-180.3
Working capital	**783.7**	**568.8**	**515.5**	**623.2**	**641.7**	**678.5**
Tangible assets	741.6	743.0	836.9	971.5	1085.9	1141.5
Intangible assets	185.1	134.8	156.5	205.3	242.6	256.6
Goodwill	23.9	16.9	13.0	9.2	5.3	1.4
Financial assets	94.7	277.6	270.0	190.0	180.0	150.0
Fixed assets	**1045.3**	**1172.3**	**1276.4**	**1376.0**	**1513.7**	**1549.5**
Retirement provisions	-51.5	-49.8	-47.0	-63.0	-80.0	-90.0
Tax provisions	-50.1	-9.6	-5.0	0.0	0.0	0.0
Other provisions	-59.0	-56.2	-30.0	-40.0	-40.0	-45.0
Funds	-160.6	**-115.5**	**-82.0**	**-103.0**	**-120.0**	**-135.0**
Capital employed	**1668.4**	**1625.6**	**1709.9**	**1896.2**	**2035.4**	**2093.0**
Sharehoders' equity	1230.0	1261.9	1319.0	1433.6	1519.1	1612.9
Minorities	7.0	13.1	22.0	14.0	16.0	18.0
Equity	**1237.0**	**1275.0**	**1341.0**	**1447.6**	**1535.1**	**1630.9**
Cash and cash equivalents	402.0	217.2	144.4	-35.4	-187.1	-248.8
Short-term liabilities	-332.0	-54.5	-100.0	-100.0	-100.0	-100.0
Long-term liabilities	-501.0	-513.3	-413.3	-313.3	-213.3	-113.3
Net financial position	**-431.0**	**-350.6**	**-368.9**	**-448.6**	**-500.4**	**-462.1**

Source: Company data, Deutsche Bank estimates

Figure 27: Benetton Group: Statement of Cashflow (Euro m)

	FY2005	FY2006	FY2007E	FY2008E	FY2009E
Net profit	112.1	124.8	146.6	171.0	187.7
Minorities	2.0	3.0	2.0	2.0	2.0
Depreciation and amortisation	85.0	84.0	100.1	110.6	123.7
Cash flow	**199.1**	**211.8**	**248.7**	**283.6**	**313.4**
Change in working capital	214.9	53.3	-107.7	-18.5	-36.8
Change in funds	-45.1	-33.5	21.0	17.0	15.0
Operating cash flow	**369.0**	**231.6**	**162.0**	**282.1**	**291.6**
Change in tangibles	-72.3	-160.0	-210.0	-200.0	-150.0
Change in intangibles	-49.7	-60.0	-90.0	-80.0	-60.0
Change in goodwill	7.0	3.9	3.9	3.9	3.9
Change in financial assets	-182.9	7.6	80.0	10.0	30.0
Other	71.2	23.0	48.0	18.0	17.0
Free cash flow	**142.2**	**46.1**	**-6.1**	**34.0**	**132.5**
Dividends	-62.0	-64.0	-73.3	-85.5	-93.8
Changes in equity	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Cash flow	**80.2**	**-17.9**	**-79.5**	**-51.5**	**38.6**

Source: Company data, Deutsche Bank estimate

Appendix 1

Important Disclosures

Additional information available upon request

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Company	**Ticker**	**Recent price***	**Disclosure**
Benetton	BNG.MI	10.85 (EUR) 18 Sep 07	2,6,8

*Prices are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank and subject companies.

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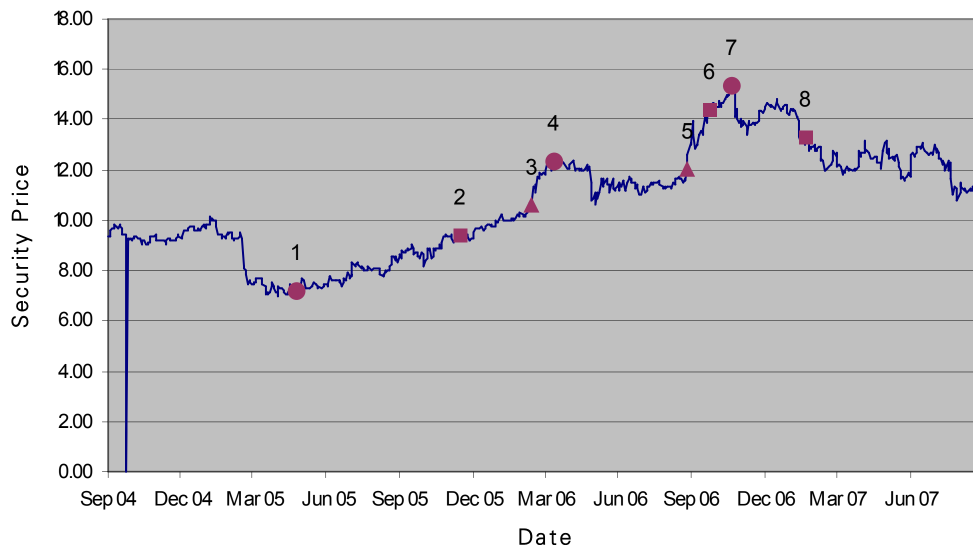
Historical recommendations and target price: Benetton (BNG.MI)

(as of 9/18/2007)



Previous Recommendations

Strong Buy
Buy
Market Perform
Underperform
Not Rated
Suspended Rating

Current Recommendations

Buy
Hold
Sell
Not Rated
Suspended Rating

*New Recommendation Structure as of September 9, 2002

1.	12/5/2005:	Downgrade to Hold, Target Price Change EUR7.60	5.	14/9/2006:	Upgrade to Buy, Target Price Change EUR13.80
2.	2/12/2005:	Hold, Target Price Change EUR9.50	6.	12/10/2006:	Buy, Target Price Change EUR15.60
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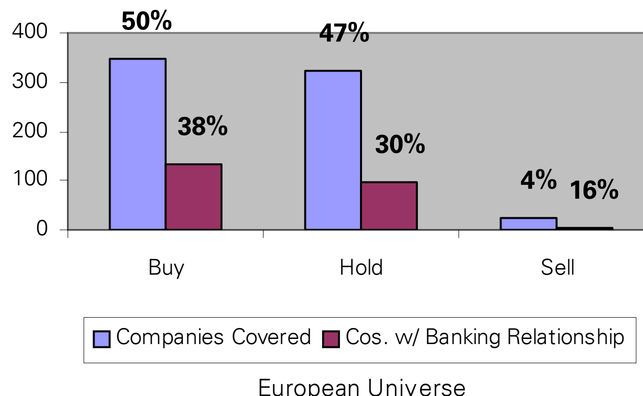

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