

#### Company Note

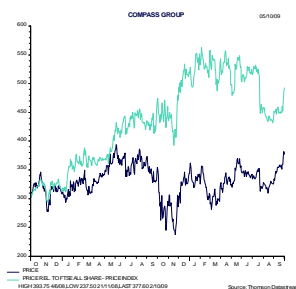
CPG.L

05 October 2009

12m Range	386-235p
Net Debt	£1.1bn
Weight in Sector (350)	18.0%
Weight in Index (100)	0.5%
Basic Shares	1,853m

#### Trading Update

In the year ending 30 September 2009, organic revenue growth will be “broadly flat” and the Group expects to deliver a strong margin improvement of 60 basis points (bps) in the year with 70 bps in Q4. Confirmation of a flat revenue outcome for the year appears to indicate that Q4 organic revenue growth has stabilised and this is reassuring. Efficiencies are driving profit margin growth and this will continue into 2010. Cash conversion remains strong. On a constant currency basis, underlying EPS is expected to show an increase of 14% in 2009. Actual reported results will benefit from a favourable impact of £120m on operating profit from currency movements.



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#### Company Activities

Compass Group is the world's largest foodservice company. By sector, revenue is divided between Business & Industry (45% of Group revenue), Healthcare (19% of Group revenue), Education (18% of revenue), Sports & Leisure (9% of revenue) and Defence, Offshore & Remote (9% of revenue).

**Year End Comments.** Compass reports its results through four geographical divisions, North America (44% of Group revenue), UK & Ireland (14% of revenue), Continental Europe (26% of revenue) and the Rest of World (16% of revenue). In North America, trading has continued strongly with organic revenue growth of 1.5% and a 50 bps improvement in the margin is expected for the year. The Healthcare (26% of divisional sales) and Education (25% of sales) sectors have performed well in terms of new contracts. In Continental Europe, organic revenue growth for the full year is expected to decline by about 1% and margin growth of 20 bps is anticipated for the full year. In Continental Europe, the Business & Industry (B&I) sector is about 60% of divisional sales and Healthcare is the next largest at 14%. In the UK & Ireland division, organic revenue growth is expected to decline by 5.5% for the year. A 60 bps improvement in the margin has been achieved. Also, the UK has a high proportion of revenue exposed to industry e.g. B&I is 55% of divisional revenue. Rest of the World is expected to show 2% organic revenue growth for the year. A 100 bps margin improvement reflects efficiency gains in the Australian and Japanese markets.

**Operational Leverage.** During the recession, Compass has managed to secure new business wins but organic revenue growth has been hit by the decline in like for like volumes. Organic revenue growth is the combination of net new business and like for like revenue growth. In total, B & I accounts for about 45% of Group revenue and here factory closures, lay-offs and shorter working hours impacted like for like volumes. Also, LFL volumes in B & I and Sports & Leisure have been impacted by a reduction in event catering and corporate hospitality. The impact of these sharp LFL declines can be seen in the quarterly progression of Group organic revenue growth which grew by 4% in Q1, declined by 1% in Q2 and appears to have been -2.5% in Q3 and Q4 respectively. As the Group has successfully reduced costs, once volumes begin to improve it should provide some operational leverage to profitability.

**Conclusion.** The year-end comments on margins were encouraging and the Group is confident about driving further efficiencies from the business. In terms of organic revenue growth, it could still be negative in Q1/2010 but we expect it to recover in H2/2010. Overall, in 2010, we expect flat organic growth and further profit margin enhancement. The share valuation looks attractive compared to its main competitor Sodexo and the wider equity market though as the share price moved higher on the publication of the trading update (29 September) we moved our recommendation to **Buy** (from Strong Buy).

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Year to September	2007A	2008A	2009E	2010E	2011E
Sales (£m)	10,268	11,440	13,920	13,980	14,200
Pre-tax Profit (£m)	442	589	788	828	889
EPS (p)	15.2	22.0	29.9	31.4	33.2
DPS (p)	10.8	12.0	13.2	14.2	15.5
PER	24.8	17.2	12.6	12.0	11.4
Net Div Yield	2.9	3.2	3.5	3.7	4.1

Source: Charles Stanley Estimates

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