CATÓLICA LISBON
BUSINESS & ECONOMICS

Equity Valuation

Distribuidora Internacional de Alimentación (DIA)

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Distribuidora Internacional de Alimentación (DIA)

Buy

Target Price: €7,6

Closing Price (Dec 31, 2014): €5,6

Potential Upside: 36%

Market capitalization (€M): 3 274

Food Retail

January 2015

Portugal

Attractive store format, robust model, smart use of capital

DIA is a Spanish based convenience discount player in the food retail market. It operates more than 6.700 stores in five countries, including Spain, Portugal, Brazil, Argentina and China.

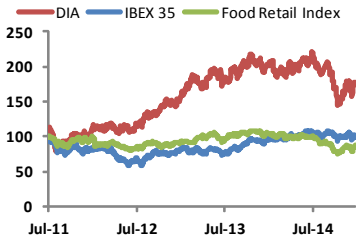
A low cost operator who seek profitable growth… The story of DIA is based on margins, cutting costs, margins, efficiencies and more margins… Its profit driven management team has been able to cut losses and improved EBITDA margins by 120bp since 2010 and it is expected to improve another 90bp due to the sale of DIA France in 2014. This was only possible due to a mix of three factors: divestment of loss making operations (Beijing, Turkey and France); continuous search for operational efficiencies; and higher contribution of franchisees.

The concept of the future: Price, Proximity… The current world trends, ageing population and lower income in developed countries, and the rise of a modernized middle class and decrease in poverty in emerging markets, favor both price and proximity attributes. Moreover, people became more price sensitive and no longer want to go to a hypermarket and make a "one-stop shopping".

…**Franchise...** Furthermore, due to its risk/profit sharing characteristic, franchising is becoming desirable, combining the financial strength and know-how of a big retailer with the personalized service and local expertise of the entrepreneur.

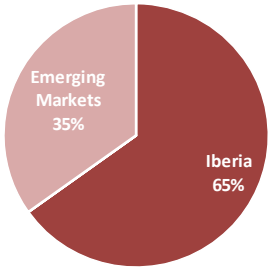
…Online. Finally, alternative channels, such as online and the "click and collect" system, are gaining market share, especially in non food products. Currently DIA has a website and a mobile app, in Spain, where customers can order online and pick up their groceries at one of the more than 4.150 locations available.

Private label products, what else? In order to be truly low price and be able to offer "quality at affordable prices" and "value for money" products, soon DIA started to developed private label brands. This way the company not only managed to offer quality products at very competitive prices but created a competitive advantage and a loyalty factor.



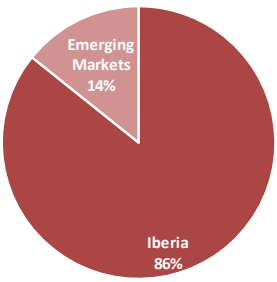
Source: Bloomberg

Sales by segment 2014e



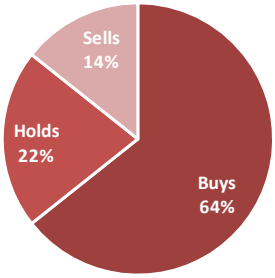
Source: Own estimations

EBITDA by segment 2014



Source: Own estimations

Anaysts recommendations



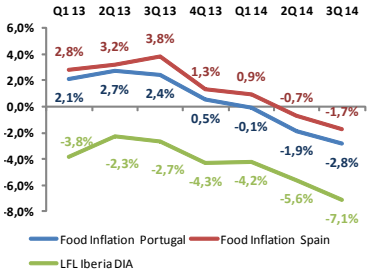
Source: Bloomberg

Performance	2012	2013	2014
DIA	37,6%	35,1%	-13,4%
IBEX 35	-4,7%	21,4%	3,7%
Food retail index	-7,1%	15,6%	-17,1%

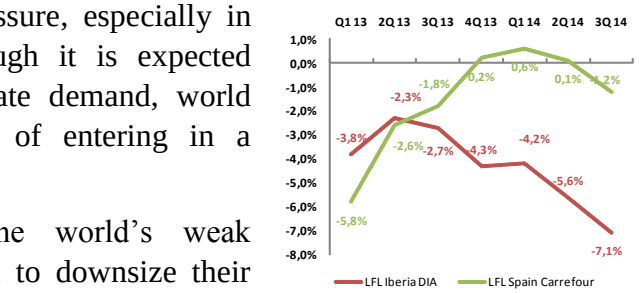
Source: Bloomberg

Iberia

The light at the end of the tunnel *vs* the cloud rising… Europe in general and Iberia in particular have been suffering from austerity and sluggish growth since the 2008 financial crisis. The economy is finally giving signs of recovery with unemployment declining in 2013 and GDP growth to be expected in 2014. However, government debt is still at alarming levels and food retailers face another threat: **Deflation.** Iberia was hit by a deflationary pressure, especially in food products dragging retailers down. Although it is expected inflation to be fueled by the increase of private demand, world institutions have already alerted for the risk of entering in a deflationary spiral.

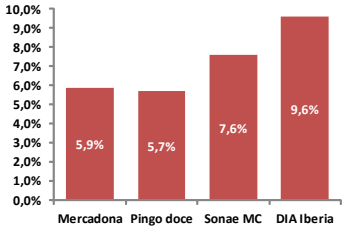


Source: Company data & OECD



Source: Company data & Carrefour data

EBITDA margin



Source: Companies data

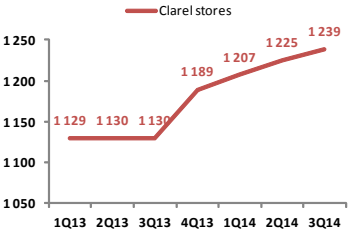
	El Árbol	Eroski
Amount invested (1)	125	146
Number of stores (2)	444	160
Net sales in 2013 (1)	825	443
EBITDA margin in 2013 (3)	-0,6%	3,0%
Average selling area (Sqm)	700	800
Total area (Sqm)	310 800	128 000
Sales per Sqm	2 654	3 459
EV/Sales multiple	0,15	0,33

(1) In Million Euros
(2) Eroski stores are subject of adjustments
(3) Estimatimations
Sqm = Square meters

Source: Company data and own estimations

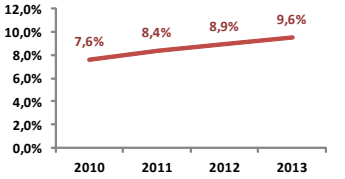
…Welcome El Árbol and Eroski. In contrast, DIA is using almost half of the proceeds from the sale to acquire assets in the Spanish fragmented market. In this context the company bought 444 El Árbol stores and 160 Eroski stores. In total, acquisitions are expected to increase DIA's 2015 sales by more than €1.100 million. Moreover, these acquisitions are expected to carry significant **synergies**: on one hand, DIA's low cost and extremely efficient operating model, applied to the new stores, would make them boost profitability by reducing logistic and administrative costs and improving buying conditions; on the other hand, DIA will increase its market share and take advantage of El Árbol's know how in perishables and fresh food.

The source of diversification: Clarel. The acquisition of Shlecker's stores in Iberia, in 2013, opened the door for DIA to diversify its portfolio to home and personal care. This way the company not only started a new source of growth but also managed to improve the home and personal care assortment in DIA's banner stores. Moreover, the company is currently remodeling Shlecker stores to a new banner: Clarel. A more modernize and with a better offer store. Furthermore, the €70,5 million investment made the number of stores to increase by 1.130 and around €241 million in sales. Additionally, Clarel stores are expected to have high EBITDA margins: 10%.



Source: Company data

EBITDA margin evolution - Iberia



Source: Company data

To summarize: DIA manages an extremely profitable store network in Iberia with increasing EBITDA margin even in a deflationary environment. However, the company is now facing deflation and high levels competition in Portugal. These two effects pressured sales and like-for-like down.

Negative scenarios were constructed. In order to incorporate the risk of a macroeconomic slowdown on the valuation, a scenario of deep deflation in Iberia and another of hyperinflation together with recession in Emerging Markets was constructed.

Base Scenario

€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	5 117	5 284	5 106	5 953	6 142	6 166	6 165	6 176	6 194	6 226	6 259	6 305	6 340
of which Spain	4 317	4 293	4 152	5 008	5 195	5 206	5 193	5 191	5 195	5 211	5 226	5 252	5 279
of which Portugal	800	749	693	657	642	637	631	627	628	630	632	635	638
of which Clarel	0	241	261	288	306	324	341	358	371	386	401	417	424
EBITDA	**457**	**505**	**495**	**474**	**489**	**502**	**512**	**530**	**553**	**573**	**588**	**597**	**603**
EBITDA margin (%)	8,9%	9,6%	9,7%	8,0%	8,0%	8,1%	8,3%	8,6%	8,9%	9,2%	9,4%	9,5%	9,5%
EBIT	**300**	**352**	**335**	**304**	**303**	**314**	**321**	**337**	**359**	**378**	**393**	**402**	**407**
Capex	157	152	190	366	221	216	216	210	204	202	200	195	196
Changes in working capita	12	0	-50	86	19	2	0	1	2	3	3	4	4
Free cash flow			**155**	**108**	**211**	**210**	**216**	**237**	**260**	**279**	**293**	**306**	**309**

Deflationary Scenario

€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	5 117	5 284	5 084	5 787	5 457	5 298	5 216	5 183	5 178	5 182	5 194	5 218	5 248
of which Spain	4 317	4 293	4 131	4 714	4 589	4 444	4 362	4 322	4 304	4 296	4 296	4 304	4 326
of which Portugal	800	749	692	614	569	539	524	517	517	517	517	518	521
of which Clarel	0	241	261	283	299	315	329	344	356	369	382	396	402
EBITDA	**457**	**505**	**493**	**340**	**299**	**304**	**309**	**337**	**372**	**388**	**421**	**437**	**444**
EBITDA margin (%)	8,9%	9,6%	9,7%	5,9%	5,5%	5,7%	5,9%	6,5%	7,2%	7,5%	8,1%	8,4%	8,5%
EBIT	**300**	**352**	**333**	**170**	**113**	**115**	**119**	**144**	**178**	**193**	**226**	**241**	**248**
Capex	133	187	190	366	221	216	216	210	204	202	200	195	196
Changes in working capital	12	0	-52	77	-29	-16	-8	-3	-1	0	1	2	3
Free cash flow			**151**	**3**	**21**	**43**	**56**	**87**	**122**	**138**	**166**	**184**	**189**

Weighted Scenario

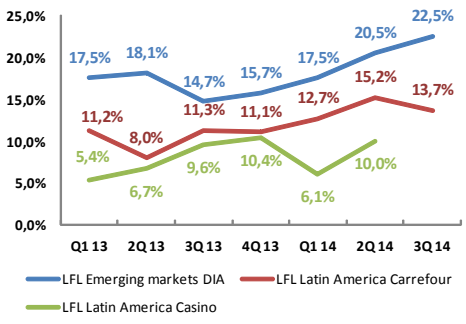
€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	5 117	5 284	5 100	5 912	5 971	5 949	5 928	5 928	5 940	5 965	5 993	6 033	6 067
of which Spain	4 317	4 293	4 147	4 935	5 043	5 015	4 985	4 974	4 972	4 982	4 994	5 015	5 040
of which Portugal	800	749	693	646	624	612	604	600	600	602	603	606	609
of which Clarel	0	241	261	287	304	322	338	354	367	382	396	412	418
EBITDA	**457**	**505**	**494**	**440**	**441**	**453**	**461**	**482**	**507**	**526**	**546**	**557**	**563**
EBITDA margin (%)	8,9%	9,6%	9,7%	7,5%	7,4%	7,6%	7,8%	8,1%	8,5%	8,8%	9,1%	9,2%	9,3%
EBIT	**300**	**352**	**334**	**271**	**256**	**264**	**271**	**289**	**313**	**332**	**351**	**361**	**367**
Capex	133	187	190	366	221	216	216	210	204	202	200	195	196
Changes in working capita	12	0	-50	83	7	-2	-2	0	1	2	3	4	3
Free cash flow			**154**	**82**	**163**	**169**	**176**	**199**	**226**	**244**	**261**	**275**	**279**

Rd	**2,3%**
Rf	0,7%
Beta	1,1
Market risk premium	5,5%
Re	**6,9%**
Tax	30,0%
E/EV	80,0%
D/EV	20,0%
Wacc	**5,8%**

Iberia Base scenario		Iberia Deflationary scenario		Iberia Weighted scenario	
Perpetual Growth	0,6%	Perpetual Growth	0,6%	Perpetual Growth	0,6%
Wacc	5,8%	Wacc	5,8%	Wacc	5,8%
Enterprise Value (Iberia)	5 114	Enterprise Value (Iberia)	2 742	Enterprise Value (Iberia)	4 521
# Shares	645	# Shares	645	# Shares	645
Price	7,92	Price	4,25	Price	7,00

Emerging markets

Not so emerging after all? Although carrying additional risks, emerging markets have the fame of being good sources of growth and opportunities. For instance, countries like Argentina and Brazil experienced a fast recovery from the 2008 financial crisis and China "almost didn't fell it". However these countries are currently facing headwinds. Argentina and, although with lesser extent, Brazil, are witnessing high inflation and negative GDP growth and the Chinese GDP is expected to decelerate.

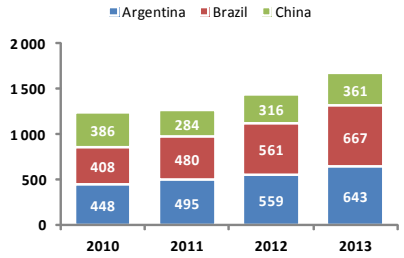


Source: Company data

FX can be devastating. The macroeconomic uncertainty lived in Argentina and Brazil has an extremely negative impact on the perceived risk of the country. As a consequence the local currencies have been devaluating at a fast pace. Especially in Argentina, where sales during the first nine months of 2014, despite an increase of 54% in constant rates, decreased by 1,7% in Euro terms.

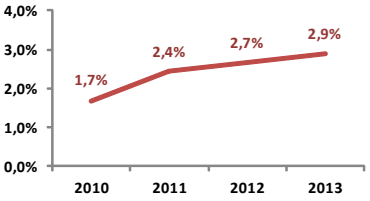
Any way… Emerging markets will still provide good sources of growth! Despite of the recent deterioration of some emerging economies it is still expected these countries to outperform developed countries in terms of growth. Even though the difficult macroeconomic environment, DIA is growing above inflation in Argentina with very healthy LFL. Therefore, the company is expected to continue investing in these countries. It is also important to note that EBITDA margins have been gradually increasing.

Stores in emerging markets



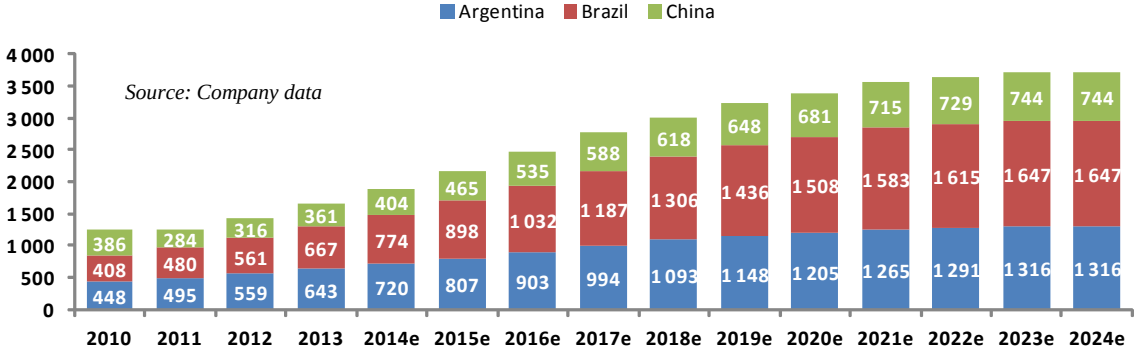
Source: Company data

EBITDA margin evolution - Emerging markets



Source: Company data

Emerging markets stores evolution



Base Scenario

€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	2 450	2 662	2 732	2 953	3 269	3 609	3 927	4 235	4 506	4 767	4 958	5 106	5 208
of which Argentina	952	1 052	1 058	1 089	1 182	1 273	1 371	1 442	1 517	1 596	1 660	1 710	1 744
of which Brazil	1 351	1 441	1 498	1 666	1 866	2 094	2 297	2 520	2 701	2 869	2 983	3 073	3 134
of which China	148	169	176	197	221	242	260	273	287	302	314	324	330
EBITDA	**65**	**77**	**82**	**92**	**105**	**119**	**134**	**148**	**171**	**191**	**208**	**230**	**232**
EBITDA margin (%)	2,7%	2,9%	3,0%	3,1%	3,2%	3,3%	3,4%	3,5%	3,8%	4,0%	4,2%	4,5%	4,5%
EBIT	**33**	**40**	**42**	**38**	**43**	**50**	**57**	**66**	**83**	**98**	**111**	**129**	**130**
Capex	106	128	135	154	160	155	153	152	153	143	139	128	103
Changes in working capital	-45	-14	9	-23	-31	-34	-32	-30	-27	-26	-19	-15	-10
Free cash flow			**-76**	**-52**	**-39**	**-19**	**-7**	**4**	**17**	**41**	**52**	**74**	**97**

Hyperinflation and Recession Scenario

€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	2 450	2 662	2 732	2 661	2 607	2 732	2 975	3 243	3 440	3 610	3 744	3 856	3 933
of which Argentina	952	1 052	1 058	1 015	975	975	1 064	1 173	1 263	1 329	1 382	1 424	1 452
of which Brazil	1 351	1 441	1 498	1 468	1 454	1 566	1 702	1 850	1 946	2 038	2 109	2 172	2 216
of which China	148	169	176	177	178	192	209	220	231	243	253	260	266
EBITDA	**65**	**77**	**82**	**64**	**65**	**77**	**89**	**104**	**114**	**126**	**139**	**154**	**165**
EBITDA margin (%)	2,7%	2,9%	3,0%	2,4%	2,5%	2,8%	3,0%	3,2%	3,3%	3,5%	3,7%	4,0%	4,2%
EBIT	**33**	**40**	**42**	**11**	**6**	**12**	**19**	**27**	**31**	**39**	**48**	**61**	**70**
Capex	106	128	135	125	125	137	152	156	141	130	124	120	96
Changes in working capital	-45	-14	9	6	5	-12	-24	-27	-20	-17	-13	-11	-8
Free cash flow			**-76**	**-71**	**-67**	**-52**	**-45**	**-34**	**-18**	**0**	**13**	**26**	**54**

Weighted Scenario

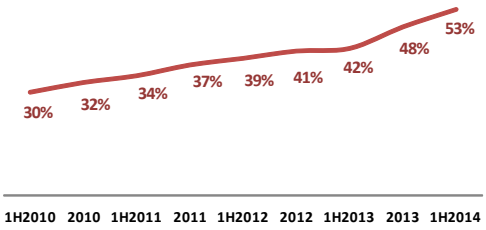
€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	2 450	2 662	2 732	2 807	2 938	3 171	3 451	3 739	3 973	4 188	4 351	4 481	4 571
of which Argentina	952	1 052	1 058	1 052	1 078	1 124	1 218	1 308	1 390	1 463	1 521	1 567	1 598
of which Brazil	1 351	1 441	1 498	1 567	1 660	1 830	1 999	2 185	2 324	2 453	2 546	2 622	2 675
of which China	148	169	176	187	200	217	234	246	259	273	284	292	298
EBITDA	**65**	**77**	**82**	**78**	**85**	**98**	**111**	**126**	**142**	**159**	**173**	**192**	**199**
EBITDA margin (%)	2,7%	2,9%	3,0%	2,8%	2,9%	3,1%	3,2%	3,4%	3,6%	3,8%	4,0%	4,3%	4,3%
EBIT	**33**	**40**	**42**	**24**	**25**	**31**	**38**	**47**	**57**	**68**	**79**	**95**	**100**
Capex	106	128	135	139	143	146	152	154	147	136	131	124	99
Changes in working capital	-45	-14	9	-8	-13	-23	-28	-29	-23	-21	-16	-13	-9
Free cash flow			**-76**	**-61**	**-53**	**-35**	**-26**	**-15**	**0**	**21**	**32**	**50**	**76**

EM Base Scenario		EM Hyperinflation scenario		EM Weighted scenario	
Perpetual Growth	2,0%	Perpetual Growth	2,0%	Perpetual Growth	2,0%
Wacc	5,8%	Wacc	5,8%	Wacc	5,8%
Enterprise Value (EM)	1 541	Enterprise Value (EM)	631	Enterprise Value (EM)	1 086
# Shares	645	# Shares	645	# Shares	645
Price	2,39	Price	0,98	Price	1,68

The DIA Group

The secret of franchising. DIA argues that franchises are able to increase their margins. This is due to the fact that the standard franchise is located in more rural areas and it is a family owned business where the entrepreneur might work with his/her family. This way DIA benefits from the local expertise of the entreperneur and the store network benefits from greater flexibility that a large corporation cannot afford. Furthermore, shrinkage and utilities cost tend to decrease when the owner works in store.

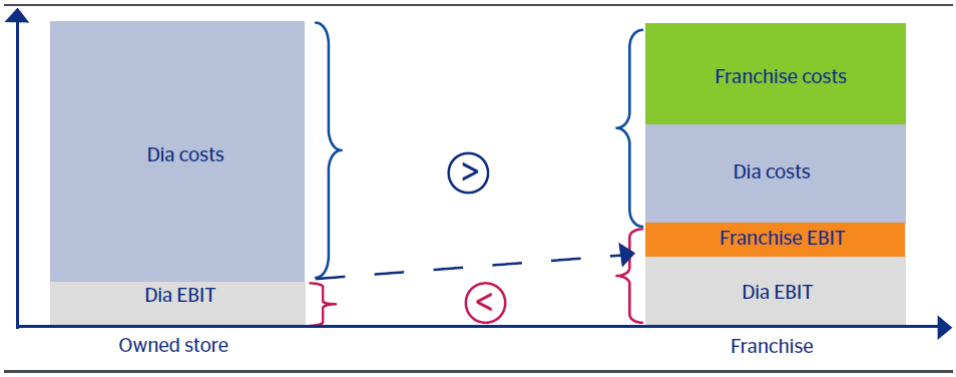
Percentage of Franchise stores in total stores



Note: excluding Shlecker/Clarel stores

Source: Company data

DIA owned vs. franchise cost structure (illustrative)



Source: Company data

Swot

Strenghts	Weaknesses
- Attractive format: Price, Proximity & Franchise; - Price leadership perception; - Strong private label penetration; - High margins;	- Dependence on the Iberia market; - Negative "Like-for-Like" in Iberia; - Dependence on the convenience discount format;
Opportunities	**Threats**
- Emerging markets growth prospects; - Consolidation in the Spanish market; - Clarel as a source of differentiation and growth in new segment;	- Deflationary environment in Iberia; - Hyperinflation and decelerating growth in emerging countries; - Very hostile competitive environment in Portugal; - Exchange rate volatility; - Loss of control over the franchisees

Source: Own estimations

Fresh is on the spotlight. Global trends are favoring fresh products and perishables as a response of higher demand for quality and healthier products. In order to keep update to consumer habbits DIA lauched a new store format: DIA fresh and Fresh by DIA. These stores are smaller than riginal DIA stores and are focused on fresh produce and perishables. Furthermore, the company is remodeling its main banner: DIA Market for a more oriented and specialized fresh offer.

Likely outperformer. Taking into consideration DIA's impeccable track record, including increasing margins in a difficult deflationary environment, it is for sure an attractive company and has good chances of being a winner.

	Market Cap (€ Million)	P/E 2014	P/E 2015	EV/EBITDA 2014	EV/EBITDA 2015	EV/EBIT 2014	EV/EBIT 2015
Ahold	13 107	16,5	14,5	7,1	6,8	12,0	11,4
Jerónimo Martins	5 185	15,6	15,3	8,0	7,7	12,7	12,6
Colruyt	6 020	17,0	16,5	8,3	8,2	11,6	11,7
Carrefour	18 428	16,4	14,2	6,9	6,4	11,0	10,2
Harmonic Average	8 171	16,3	15,1	7,5	7,2	11,8	11,4
DIA	3 724	14,8	14,5	8,0	7,9	12,3	12,6
DIA's implied share price (€)		**6,27**	**5,65**	**5,84**	**5,44**	**5,99**	**5,17**
Average (€)				**5,73**			

To summarize, DIA has an attractive store format, suitable for the world market trends; is present in emerging countries, which might provide good sources for growth; has been able to increase its margins, even in a deflationary environment; and its offer is well perceived by the customers. In contrast, DIA is highly depended on its Iberia operations, which are currently facing a competitive and deflationary environment; its emerging operations might face macroeconomic headwinds and with the increase share of franchise DIA might lose some control over operations and potential unhappy franchisees can deeply affect the company's performance.

Enterprise Value Iberia	4 521
Enterprise Value Emerging Markets	1 086
Total Enterprise Value	5 607
Non-recurring Items	-99
Net Debt	-543
Provisions	-61
Equity	4 904
# Shares	645
Target Price	7,60

Price at December 31, 2014	5,6
Potential Upside	36%
Rating	Buy

Source: Own estimations

DIA's P&L (Own estimations)

€ million	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	9 708	9 844	7 838	8 906	9 411	9 775	10 092	10 411	10 700	10 993	11 217	11 411	11 549
% gowth	*-0,2%*	*1,4%*	*-20,4%*	*13,6%*	*5,7%*	*3,9%*	*3,2%*	*3,2%*	*2,8%*	*2,7%*	*2,0%*	*1,7%*	*1,2%*
p.m. Iberia	5 117	5 284	5 106	5 953	6 142	6 166	6 165	6 176	6 194	6 226	6 259	6 305	6 340
% gowth	*3,4%*	*3,3%*	*-3,4%*	*16,6%*	*3,2%*	*0,4%*	*0,0%*	*0,2%*	*0,3%*	*0,5%*	*0,5%*	*0,7%*	*0,6%*
p.m. Emerging markets	2 450	2 662	2 732	2 953	3 269	3 609	3 927	4 235	4 506	4 767	4 958	5 106	5 208
% gowth	*21,8%*	*8,6%*	*2,6%*	*8,1%*	*10,7%*	*10,4%*	*8,8%*	*7,8%*	*6,4%*	*5,8%*	*4,0%*	*3,0%*	*2,0%*
Gross Profit	2 085	2 166	1 709	1 924	2 033	2 111	2 180	2 249	2 311	2 375	2 423	2 465	2 495
% of Sales	*21,5%*	*22,0%*	*21,8%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*
EBITDA	615	642	577	566	593	621	646	678	724	763	796	827	835
% of Sales	*6,3%*	*6,5%*	*7,4%*	*6,3%*	*6,3%*	*6,4%*	*6,4%*	*6,5%*	*6,8%*	*6,9%*	*7,1%*	*7,2%*	*7,2%*
p.m. Iberia	457	505	495	474	489	502	512	530	553	573	588	597	603
% of Sales	*8,9%*	*9,6%*	*9,7%*	*8,0%*	*8,0%*	*8,1%*	*8,3%*	*8,6%*	*8,9%*	*9,2%*	*9,4%*	*9,5%*	*9,5%*
p.m. Emerging markets	65	77	82	92	105	119	134	148	171	191	208	230	232
% of Sales	*2,7%*	*2,9%*	*3,0%*	*3,1%*	*3,2%*	*3,3%*	*3,4%*	*3,5%*	*3,8%*	*4,0%*	*4,2%*	*4,5%*	*4,5%*
EBIT	347	375	377	342	346	364	379	403	442	475	504	531	537
% of Sales	*3,6%*	*3,8%*	*4,8%*	*3,8%*	*3,7%*	*3,7%*	*3,8%*	*3,9%*	*4,1%*	*4,3%*	*4,5%*	*4,7%*	*4,6%*
p.m. Iberia	300	352	335	304	303	314	321	337	359	378	393	402	407
% of Sales	*5,9%*	*6,7%*	*6,6%*	*5,1%*	*4,9%*	*5,1%*	*5,2%*	*5,5%*	*5,8%*	*6,1%*	*6,3%*	*6,4%*	*6,4%*
p.m. Emerging markets	33	40	42	38	43	50	57	66	83	98	111	129	130
% of Sales	*1,4%*	*1,5%*	*1,5%*	*1,3%*	*1,3%*	*1,4%*	*1,5%*	*1,6%*	*1,8%*	*2,0%*	*2,2%*	*2,5%*	*2,5%*
Associated companies	1	1	0	0	0	0	0	0	0	0	0	0	0
Financial results	-26	-40	-40	-21	-21	-21	-21	-21	-21	-21	-21	-21	-21
Non-recurring items	-38	-49	-50	-50	-50	-50	0	0	0	0	0	0	0
EBT	**283**	**286**	**287**	**272**	**276**	**293**	**358**	**383**	**421**	**455**	**483**	**510**	**516**
Taxes	-102	-96	-87	-78	-72	-77	-94	-101	-112	-121	-130	-138	-139
Net Profit (from continuing operations)	**182**	**191**	**200**	**194**	**203**	**216**	**264**	**282**	**309**	**333**	**353**	**372**	**377**
Income from discontinued operations	-35	5	76	0	0	0	0	0	0	0	0	0	0
Minority interest	12	13	0	0	0	0	0	0	0	0	0	0	0
Net Profit Attributable to the Company	**158**	**209**	**276**	**194**	**203**	**216**	**264**	**282**	**309**	**333**	**353**	**372**	**377**
Underlying Net Profit	**204**	**228**	**250**	**244**	**253**	**266**	**264**	**282**	**309**	**333**	**353**	**372**	**377**
Underlying EPS			0,387	0,378	0,393	0,412	0,409	0,436	0,479	0,516	0,548	0,577	0,583
% growth				*-2,4%*	*4,0%*	*4,9%*	*-0,7%*	*6,7%*	*9,8%*	*7,7%*	*6,1%*	*5,3%*	*1,2%*
Dividend payout ratio	41%	45%	45%	49%	50%	75%	75%	75%	75%	75%	75%	75%	75%
Dividend	83,9	103,4	112,4	118,2	126,7	199,4	198,0	211,3	232,0	249,9	265,1	279,3	282,5
Dividend per share	0,13	0,16	0,17	0,18	0,20	0,31	0,31	0,33	0,36	0,39	0,41	0,43	0,44
% growth	*15,7%*	*23,2%*	*8,7%*	*5,2%*	*7,2%*	*57,4%*	*-0,7%*	*6,7%*	*9,8%*	*7,7%*	*6,1%*	*5,3%*	*1,2%*

DIA's Balance Sheet (Own estimations)

€ million	2012	2013	2014e	2015e	2016e	2017	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Goodwill	423	454	308	308	308	308	308	308	308	308	308	308	308
Net property plant and equipment	1 619	1 602	1 357	1 653	1 788	1 901	2 003	2 091	2 167	2 224	2 271	2 297	2 297
Cash & cash equivalents	350	262	370	263	264	276	270	298	348	421	500	600	711
Inventory	527	545	429	489	516	536	554	571	587	603	616	626	634
Trade receivables	180	210	215	244	258	268	276	285	293	301	307	313	316
Other assets	306	298	378	378	378	378	378	378	378	378	378	378	378
Assets available for sale	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Assets	**3 405**	**3 371**	**3 057**	**3 336**	**3 512**	**3 668**	**3 790**	**3 931**	**4 082**	**4 236**	**4 380**	**4 523**	**4 645**
Financial dept	980	913	913	913	913	913	913	913	913	913	913	913	913
Trade payables	1 759	1 787	1 418	1 616	1 707	1 773	1 831	1 889	1 941	1 994	2 035	2 070	2 095
Provisions	101	81	61	61	61	61	61	61	61	61	61	61	61
Other liabilities	418	406	309	309	309	309	309	309	309	309	309	309	309
Liabilities associated with asset held for sale	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Liabilities	**3 257**	**3 187**	**2 701**	**2 899**	**2 990**	**3 056**	**3 114**	**3 172**	**3 224**	**3 277**	**3 318**	**3 353**	**3 378**
Total Equity	**148**	**184**	**356**	**437**	**522**	**612**	**676**	**760**	**858**	**959**	**1 063**	**1 170**	**1 267**
Retained earnings			184	356	437	522	612	676	760	858	959	1 063	1 170
Net profit			276	194	203	216	264	282	309	333	353	372	377
Dividends			-103	-112	-118	-127	-199	-198	-211	-232	-250	-265	-279
Total Liabilities & Shareholders Funds	**3 405**	**3 371**	**3 057**	**3 336**	**3 513**	**3 668**	**3 790**	**3 932**	**4 082**	**4 237**	**4 381**	**4 523**	**4 646**

Abstract

This paper aims to evaluate the Spanish food retail company, Distribuidora Internacional de Alimentacion, DIA, and ultimately set a price target and a buy/sell recommendation. In order to complete this goal the state of the art of valuation was discussed by briefly describing the different valuation models, in order to access the most accurate method to evaluate DIA. Furthermore, both DIA's historical financials and future strategy were deeply analyzed and a set of consistent projections constructed. Using the sum of parts method together with the multiples analysis, a target price of €7,6 was computed, suggesting that the stock is undervalued in the market, with a potential upside of 36%. Finally, the estimations and results, presented is this paper, were compared with an analyst's report from Morgan Stanley.

Acknowledgements

This dissertation is the culmination of four and half hard working years at Católica Lisbon.

It was an interesting challenge where I had to combine the theory I have learned at the university, with the skills I have already acquired in my internship in a food retail company, and with the difficulty of obtaining information in the real market.

A journey with ups and downs, but with a positive overall, because it made me more confident of my background knowledge, and my capacity to apply it in a subject that I am passionate about: equity valuation.

This journey would not be possible without the solid support of my family and friends. I also would like to thank, professor Tudela Martins, for his valuable and timely inputs, and DIA´s Investor Relations for the information that I got.

Finally, I embrace the challenges ahead of me with motivation and enthusiasm once I'm sure Católica Lisbon gave me what it takes to succeed on the job market.

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1. Introduction

This paper is the outcome of the academic thesis of a Catolica Lisbon's master student. The broad subject is finance and the seminar specific topic is equity valuation with professor José Tudela Martins. The aim of this thesis is to evaluate a public company listed on a stock exchange and ultimately present a price target and a buy/sell recommendation. Moreover the executive summary should have the same structure as an analyst's financial report in order to be suitable for publishing. The comparison between the present valuation and a report from a major investment bank, Morgan Stanley, was also made. Accordingly with the assumptions and methods used the author came up with a target price of €7,6, suggesting that the stock is undervalued in the market, with a potential upside of 36%, considering the price closing on December 31, 2014 of €5,6 per share.

The company analyzed in this article is Distribuidora Internacional de Alimentación, hereon referred as "DIA", and is traded on the main Spanish stock Exchange, IBEX 35. This company was chosen because:

- It operates in a sector which the author has professional interest: food retail market;
- Its international scope: it is present in five countries in three continents, including Portugal with the Minipreço banner;
- It has a very interesting store format and strategy accordingly with the trends in the market: "Price, Proximity and Franchise" and great focus on private label;
- Its track record is impeccable, especially after the spin off with Carrefour in 2011, with an EBIT margin increase of 80 basis points, and the successful sale of underperforming operations such as its operations in Turkey, in Beijing and more recently in French;
- DIA provides a substantial amount of public information and has an investor's relation department ready to help;
- It is a challenging and complex case of valuation, with the sale and purchase of businesses during the explicit period.

The rest of the paper is structured in the following way: on the next section the state of the art of valuation will be presented with a brief description of the discount factors and main valuation methods. On the third section the macroeconomics indicators which affect the business are discussed and the food retail market is analyzed. The fourth section describes the company. Then, the valuation assumptions and methods used are presented in the sixth

section. The comparison with a valuation made by a top financial bank is on the seventh section, and finally the last section contains the main conclusions taken from this thesis.

2. Literature Review

In this section the main valuation methods are summarized and their advantages and disadvantages discussed, in order to find the reasoning behind the chosen approaches: **the sum of parts method, and the multiples analysis to complement the valuation.**

2.1. Why is valuation important?

"Price is what you pay. Value is what you get." Warren Buffet

This famous quote from one of the most respectful investors, Warren Buffet, seems simple and obvious but it has an important teaching. It suggests that the concepts of price and value are not the same. Price is something objective (is the amount paid for a product or service) while value is subjective to personal interpretation. Therefore, **valuation is important in order to access the value, decide about the reasonability of the price and help the decision making.**

In accordance, Mauboussin (2006) defends that investors' objective is: "Buying a stream of cash flows for less than what it is worth", reinforcing the importance of valuation.

"Today valuation is the financial analytical skill that general managers want to learn and master more than any other." Luehrman 1997

Valuation has high practical relevance by helping the decision making process. For instance, when deciding to buy something, the buyer asks himself "is this worth the money?". This question suggests a process of analyzing and accessing whether the price is higher or lower than the value, a process of valuation.

Moreover, valuation models are very useful for computing a target price on a listed company or for an IPO, to evaluate inheritances and wills, to build compensation schemes based on value creation, to indentify value drivers, to help strategic decisions and to influence strategic planning (Fernández 2013).

2.2. Approaches to valuation

"The goal of company valuation is to give owners, potential buyers and other interested stakeholders an approximate value of what a company is worth. There are different approaches to determine this value but some general guidelines apply to all of them." Steiger 2008

Accordingly to Fernandez (2002) the discount valuation models based on the same assumptions should be equivalent, however Kruschwitz and Loffler (1998) defend that Weighted Average Cost of Capital (WACC) and Adjusted Present Value (APV) methods will provide necessarily different values. Furthermore, Demirakos, Strong and Walker (2009) state that, although in theory price-to-earnings and discount models should produce similar valuation if implemented consistently, in practice these methods usually output different results.

The discount model is generally considered as the best valuation method and is widely used (Luehrman 1997), but **there is no one method that is best suited for every situation**.

To concluded, there are a vast number of valuation methods and there is a fierce discussion between analysts and academic researchers about which model outputs the best estimation of the "true" value. Furthermore, **it is fair to say that there is no right or wrong method and the "best one" will depend on the characteristics of the firm being analyzed, and the analysts' personal perspective** (Demirakos, Strong & Walker 2009)

Finally, five main groups of methods were identified: Discounted Cash flow valuation, value creation approach, relative valuation, contingent claim valuation and asset-based valuation (Fernandez 2007).

Discount Cash Flow Valuation	Value Creation Approach	Relative Valuation (Multiples)	Contigent Claim Valuation (options)	Asset-based Valuation
- Dividend Discount Model (DDM)	- Economic Value Added (EVA)	- Enterprise Value-to-EBIT (EV/EBIT)	- Binomial Model	- Book Value
- Free Cash Flow For the Equity (FCFE)		- Enterprise Value-to-EBITDA (EV/EBITDA)	- Black-Scholes	- Liquidation Value
- Free Cash Flow For the Firm (FCFF)		- Enterprise Value-to-Sales (EV/Sales)		
- Adjusted Present Value (APV)		- Price-to-Earnings (PER)		

Exhibit 1: Valuation methods

2.2.1. Discount cash flow models

"Cash is king". This is one of the most known quotes in finance and it suggests that cash generation is an essential concept in valuation.

In accordance, Fernandez (2013) defends that, "the most suitable method for valuing a company is to discount the expected future cash flows, as the value of a company's equity - assuming it continues to operate - arises from the company's capacity to generate cash for the equity's owners."

Taking Fernandez words in consideration, all the variants of discount cash flow model have the same basic mechanic behind them: **a stream of future cash flows actualized for the present moment by a discount rate which reflects the risk associated with the business.**

$$\text{Net Present Value Approach}^{1} = \sum_{t=1}^{t=n} \frac{\text{Cash flow (t)}}{(1 + \text{Discount rate})^{(t)}}$$

What differs between models is the stream of cash flows and the discount factor.

Moreover, on the next sub-sections the inputs for this formula will be discussed. Firstly the discount factor and all its drivers are presented on a journey to ultimately estimate the weighted average cost of capital and secondly the cash flow streams for each model are identified.

2.2.1.1. The discount factor

"The opportunity cost is the return a company (or its owners) could expect to earn on an alternative investment entailing the same risk" Luehrman 1997

The discount factor is the denominator on the models formulae and represents the opportunity cost of the investment. This section will deeply analyze its components including the cost of equity, the cost of debt and the capital structure.

2.2.1.1.1. Cost of equity

"Opportunity cost consists partly of time value – the return on a nominally risk-free investment. This is the return you earn for being patient without bearing any risk. Opportunity cost also includes a risk premium – the extra return you can expect commensurate with the risk you are willing to bear." Luehrman 1997

[1] In all equations in this article the letter "t" corresponds to one period, when it appears "t-1" it means "previous period".

The cost of equity is the rate of return required by the equity holders of a company. Although there are several risk and return models, they are all based on the fact that**: for higher risk investors will demand higher returns; and investors should only be rewarded for non diversifiable risk**.

However criticized by many (Fernandez 2014), the most used model is Capital Asset Pricing Model (CAPM)[2].

> *"The CAPM reveals the return that investors require for bearing the risk of holding a company's share."* Steiger 2008

$$\text{Cost of Equity} = \text{Risk free rate} + \text{Beta} \times \text{Market Risk Premium}$$

On the next sub-sections the inputs for the CAPM formula will be discussed and analyzed.

2.2.1.1.1.1. Risk free rate

> *"Risk in finance is viewed in terms of the variance in actual returns around the expected return. For an investment to be risk free in this environment, then, the actual returns should always be equal to the expected return"* Damodaran 2008

In short, risk free is something which provides an expected cash flow with a **100%** probability.

Furthermore, to be risk free, the asset must fulfill two conditions:

- **No default risk**: only government securities can potentially accomplish this condition, once they can print money to meet their promises[3], while "Even the largest and safest firms have some measure of default risk." (Damodaran 2008);
- **No reinvestment risk**, this condition makes only zero coupon securities suited for risk free, once otherwise it would not be possible to predict the reinvestment rates of the coupons.

Furthermore, according with Damodoran (2008) "A risk free investment should have returns that are uncorrelated with risky investments in a market".

Moreover, the **security must be denominated in the same currency as the company's cash flows** in order to handle inflation consistently. Regarding the maturity of the risk free asset it should be equal to the length of the cash flows. As we assume that the firm will continue operating in the long run it might be arguable to use the longest maturity. However, since the

[2] Other alternatives are the use of multi-factor models such as Fama and French model and the Arbitrage Pricing Theory.
[3] However history tells us that governments might not honor their agreements.

30 year bonds usually have liquidity problems, the 10 year government bonds in generally used (Koller, Goedhart & Wessels 2010 and Damodaran 2008).

Finally, in the Euro zone none of the members have full control of the Euro currency supply and consequently all have some default risk. In this case it is usually used the 10 year German Bund which is highly liquid and has the lowest credit risk among the European countries. To conclude, as DIA's cash flows are in Euros, **the risk free rate used in this paper will be the 10 year German Bund.** Therefore it was used a **risk free rate of 0,7%**[4].

2.2.1.1.1.2. Beta

> *"Beta represents a stock's incremental risk to a diversified Investor"* Koller, Goedhart & Wessels 2010

Beta is the firm specific risk input of the CAPM model. As Koller, Goedhart & Wessels (2010) defend, beta measures the undiversified risk of adding the stock to a diversified portfolio.

Although there are no consensus on how to compute this parameter, for instance Fernandez (2013) suggest that beta equal to 1 outperforms calculated betas, the standard procedure is to regress stock returns against market returns. In this way beta is be the slop of the regression (Damodaran 1996). This implies that a 1% change in the market should reflect a beta % change on the stock. Consequently, it is expected that firms with higher betas will be more volatile and riskier than lower beta companies.[5]

There are some practical issues and decisions that must be made regarding beta computation:

- **The market index:** the standard procedure is to use the index where the stock is traded, as long as it has considerable size and liquidity, while for international cross border investors it may be better to consider an international index such as the MSCI world Index or the MSCI Europe Index;
- **The length of estimation period**: it is standard to use 5 years or 2 years of data;
- **The return interval**: there are annual, monthly, weekly, daily or even intra-day returns; the shortest intervals provide more observations, however are likely to have a significant bias due to non-trading problem[6], and as such it is standard to use weekly or monthly intervals;

[4] Yield from the 10 year German euro bund on October 27, 2014.
[5] The market beta should be equal to 1 and the risk free asset's beta equal to 0.
[6] Non-trading problem: happens when the returns in non-trading periods are zero, even though the market may have moved during those periods.

- **Adjusted betas**: Bloomberg estimates betas by adjusting them towards one[7], in accordance to studies which defend that there is a tendency for betas to move that way (Damodaran 1996).

Alternatively, one can use comparables to compute company's beta, using similar companies from the same industry, or with similar fundamentals, like growth, profitability, and leverage. The rationale behind this is that similar companies should have similar firm specific risk, and consequently similar betas (Koller, Goedhart & Wessels 2010).

As far as this analysis is concerned it will be used the MSCI Europe Index as benchmark, because it is an international index[8] whose currency is the same as DIA's. Furthermore, it will be used the adjusted beta from Bloomberg with the length of 5 years[9] in order to mitigate the sharp decrease of the food retail market during the last year[10] and a weekly return interval. **The beta computed this way was 1,1**.

As a final remark, the beta referred until now was the levered beta, however to compute the adjusted present value approach the unlevered beta[11] must be computed. In accordance to Damodaran (2003), the relationship between the levered and unlevered beta is:

$$\text{Levered Beta} = \text{Unlevered Beta} \times (1 + (1\text{-Tax}) \left({}^{\text{Dept}}/_{\text{Equity}} \right)$$ [12]

2.2.1.1.1.3. Market risk premium

"The risk premium used in the CAPM is generally based upon historical data, and the premium is defined to be the difference between average returns on stocks and average return s on risk free securities" Damodaran 1996

There are three approaches to compute the market risk premium:

- **Historical premiums:** use the historical difference between de stock market and the risk free rate;
- **Survey investors or managers:** in order to access their risk premiums relative to the risk free rate, and;
- **Forward-looking premiums:** implied from today's market prices (Domodaran 2012).

[7] $\text{Adjusted Beta} = \text{Regression Beta} \times {}^{2}/_{3} + 1 \times {}^{1}/_{3}$

[8] The author assumed that DIA has diversified investors for which an international index would be a better benchmark than the local index

[9] Which in practice is corresponds to three and half years since DIA started to trade on the stock market on July 2011

[10] The decrease is partially explained by the low inflation registered in Europe during 2014 and is expected to be temporarily.

[11] Unlevered beta is the beta as if the company would be 100% financed by equity.

[12] Assuming that the beta of debt is zero

$$\text{Market Risk Premium} = \text{Expected Return of the Market} - \text{Risk Free Rate}$$

Moreover, historical premiums can be computed by arithmetic or geometric average. On one hand, the first one generally outputs higher premiums and is considered as a better predictor for next year premiums[13]. On the other hand, the latter is considered as a better predictor for long term premiums once it takes into account the compounding factor (Damodaran 2012).

For what valuation is concerned, as the cash flows analyzed are over a long period of time, the geometric average might be a best predictor. Additionally, accordingly to Koller, Goedhart & Wessels (2010) it should be used the longest period possible to estimate the market risk premium since short term periods are extremely "noisy".

"Globally diversified investors will demand lower discount rates." Sabal 2003

Another important issue is whether investors are diversified or not. From surveys, individual investors require higher risk premiums than institutional (more diversified) investors (Damodaran 2012). According to Koller, Goedhart & Wessels (2010) market risk premiums for a diversified investor should range between 4,5% and 5,5%.

As DIA's ownership consists of global diversified investors (20%) **(See appendix I)** and free float[14] (80%), it is reasonable to assume that DIA's shareholders are diversified and for this reason a **market risk premium of 5,5%** will be used.

2.2.1.1.1.4. Country risk premium

"In effect, should we demand one global equity risk premium that we use for investments all over the world or should we use higher equity risk premiums in some markets than in others?" Damoradan 2012

The country risk premium concept surges as some countries are exposed to additional risks comparing to others. A typical example is that emergent markets are riskier than developed markets. Some examples of additional risks are high levels of inflation, macroeconomic volatility, capital controls, political instability, war or civil unrest, regulatory changes, poorly defined or enforced contract and investor's rights, lax accounting controls and corruption (James & Koller 2000).

There are two main opinions regarding how to measure the country risk. Some argue that **a country risk factor should be added to the discount rate** on the "business as usual" scenario (Damodaran 2012 and 2009). While others defend that risk should be **incorporated**

[13] Koller, Goedhart & Wessels (2010) suggest the use of the arithmetic average with 10 year dated intervals
[14] According to the company, DIA has a widely disperse international base of investors.

on the cash flows[15] (James & Koller 2000, Goedhart & Haden 2003 and Koller, Goedhart & Wessels 2010).

Both approaches are supported by strong arguments. Damodaran (2012 and 2009) uses empirical evidence showing that the correlation between markets is increasing, which makes diversification unlikely. On the opposite side, the main arguments are: the correlation between markets is low and consequently the risks can be diversified; a probability-weighted scenario provides a better understanding of what is creating (or destroying) value and have a more solid analytical basis; many risks are idiosyncratic and don't apply equally for all the industries and companies of the country being analyzed[16].

After deep consideration, the method used in the present paper is the probability-weighted scenario once the author believes that this approach provides a better understanding about how different risks impact the value of the company and that country risks do not impact equally all firms for which it seems too simplistic to merely use an additional risk premium to the discount rate.

Furthermore, another valuation issue of operating in emerging markets is how to treat inflation. **Inflation leads to lower value creation and must be handled consistently in the construction of the discount rate and the projection of the cash flows** (Damodaran 2009 and Koller, Goedhart & Wessels 2010). As DIA publishes all items in Euros the discount rate used in this paper will be in Euros and the inflation will be handling accordingly to the purchasing power parity[17] for which it will be assumed that the inflation is adjusted by the exchange rate.

2.2.1.1.2. Cost of debt

> *"The cost of debt should be the rate at which a company could refinance its existing debt in the current market conditions."* Bancel, Lathuille & Lhuissier 2013

The cost of debt is the rate of return required by the debt holders of a company. Accordingly to Koller, Goedhart & Wessels (2010) and Bancel, Lathuille & Lhuissier (2013):

$$\text{Cost of Debt} = (\text{Risk Free Rate} + \text{Default Spread})$$

Taxes must be taken into account.

$$\text{After tax Cost of Debt} = (\text{Cost of Debt}) \times (1 - \text{Tax Rate})$$

[15] The discount rate should only reflect non diversifiable risk
[16] It is important to note that both approaches cannot be used together once this would mean double counting of the risk and deeply undervalue the company.
[17] The purchasing power party theory defends that exchange rates should adjust in order to the prices in different countries to be similar, which is the same to say that exchange rates should adjust to the inflation, at least on the long run.

Where the bond rating and the collateral establish the default spread.

Furthermore, it is usually used the company's **yield to maturity,** using the promised yield on newly issued long term debt[18] or the company's debt rating as an estimative[19].

For what this valuation is concerned, the credit rating of Baa3 and BBB- attributed by Moody's and Standard & Poor's respectively, will be used to compute DIA's spread. Therefore the spread of 1,6% **(See appendix II)** was computed. Then, by adding the risk free rate, outputs a **cost of debt of 2,3%.**

2.2.1.1.2.1. Tax

"According to the AFP survey, only 29% of practitioners use the marginal corporate tax rate of the country in which the company pays its taxes (considered the best approach by most experts). One of the reasons might be the difficulty to estimate this rate on a consolidated basis across countries for MNCs." Bancel, Lathuille & Lhuissier 2013

Debt is generally a cheaper way of financing than equity because it is tax deductable (Gruninger & kind 2013 and Steiger 2008) and has more senior claims regarding company's cash flows. However it is important to point that firms only benefit from tax benefits if they are profitable or it are expected to be profitable in the future.

There are three ways of estimating the tax rate:

- **The statutory tax rate**, which is the legal imposed corporate tax: has the advantage of being simple and straight forward but it might overstate the tax effect;
- **The effective tax rate,** which corresponds to the taxes incurred divided by the taxable income: it is a simple way and takes into account the firm's tax history, however does not handle well one-off items;
- T**he marginal tax rate**, which is the rate at which the last dollar of income is taxed: although is considered to be the best proxy, is generally harder to estimate[20] (Franck, Quentin & Alban 2013, Steiger 2008 and Koller, Goedhart & Wessels 2010).

Regarding DIA's valuation, the Spanish expected statutory tax will be used, accordingly with the projection of the company, corresponding to 30%, 28% and 25% for 2014, 2015 and 2016 onwards, respectively.

[18] This method is not a good proxy for firms with low credit rating and high default risk once it is expected that the promising cash flows don't represent the actual cash flows.
[19] There are other less used methods to compute the cost of equity such as the CAPM (Oded, Michel and Feinstein 2011) or simply assume the risk free rate (Gruninger and Kind 2013).
[20] Once it requires the existence of a reconciliation table in order to manage tax consolidation across countries.

2.2.1.1.3. Capital structure

"The financial structure of the firm, including the dividend policy, does not affect the computed free cash flow. The financial structure does affect the valuation of free cash flow, though, through the WACC computation." Jennergren 2011

The last ingredient to estimate the weighted average cost of capital are the weights, defined by the capital structure, which corresponds to the proportion of debt and equity in regard to enterprise value (Koller, Goedhart & Wessels 2010).

To compute this ratio **market values** and not book values should be used. The intuition behind this is that if the company issues either new debt or equity, it will be at market prices (Damodaran 1996 and Koller, Goedhart & Wessels 2010). Additionally, it should correspond to the company's strategic **target ratio**[21].

Accordingly to DIA's investor relations department, the company as the target net debt[22] ratio to range between 0,9 and 1,1 times EBITDA. Therefore it is expected that DIA will adjust its debt accordingly and maintain a stable debt ratio.

2.2.1.1.4. Weighted average cost of capital (WACC)

"The WACC represents the opportunity cost that investors face for investing their funds in one particular business instead of others with similar risk." Koller, Goedhart & Wessels 2010

All the building blocks presented and explained before are used to compute the weighted average cost of capital. WACC includes the required rate of return of all investors, namely equity, debt and hybrid securities[23] owners, weighted by their market values.

$$\text{WACC} = {}^{\text{Debt}}/_{\text{EV}}{}^{24} \times \text{Cost of Debt} \times (1 - \text{Tax}) + {}^{\text{Equity}}/_{\text{EV}} \times \text{Cost of Equity}$$

Moreover the WACC includes the value from interests tax shield, by the use of the **after-tax** cost of debt, and implicitly captures the expected bankruptcy costs (Damodaran 2006).

An important note is that WACC only works if the company has its capital structure fixed. Otherwise the APV model (presented on the next section) should be used.

Finally the author came up with **a WACC for DIA of 5,8%** reflecting all investors' required rate of returns.

[21] In case that the capital structure is very volatile it should be used the APV model rather than the WACC.
[22] $Net\ Debt = Gross\ Debt - Cash\ and\ Cash\ Equivalents$
[23] As hybrid securities do not apply to DIA's valuation I simplified the formula in order to contain only equity and debt.
[24] Note: EV = Enterprise Value.

2.2.1.1.5. Explicit period *vs* Terminal value

"Since you cannot estimate cash flows forever, you generally impose closure in discounted cash flow valuation by stopping your estimation of cash flows sometime in the future and then computing a terminal value that reflects the value of the firm at that point". Damodaran 2006

Before analyzing each discount cash flow model, the concepts of explicit period and terminal value will be presented once they are transversal.

If the company is not on the "steady sate"[25] it is expected to change its fundamentals namely growth, margins and capital structure in the short/medium term. Therefore the **explicit period** is used to capture these changes until the firm reaches maturity. Finally, the length of this stage will depend on the firm but is usually used an explicit period between 5 and 10 years[26].

The terminal value is the perpetuity calculated when the firm reaches maturity. It is important to note that the perpetual growth cannot exceed the long term economy growth, because it would be greater than the economy in the long run, nor be negative, because it would disappear in the long run (Damodaran 2006).

$$\text{Explicit Period} = \sum_{t=1}^{t=n} \frac{\text{Cash Flow (t)}}{(1 + \text{Discount Rate})^t}$$

$$\text{Terminal Value} = \frac{\dfrac{\text{Cash Flow (t + 1)}}{\text{Discount Rate} - \text{Perpetual Growth Rate}}}{(1 + \text{Discount Rate})^t}$$

Furthermore, some methods will output the value of the equity and others the value of the firm. In order to get the equity value from the firm value it must be added the non-operational assets such as cash and marketable securities and subtracted the non-equity claims namely debt, capitalized leases, provisions, unfunded pension plan obligations, minority interests and off balance sheet items[27] (Steiger 2008).

$$\text{Equity Value} = \text{Firm Value} + \text{Cash and Marketable securities} - \text{Debt} - \text{Other Non Equity Claims}$$

Finally, to get the price per share the following formula is used:

$$\text{Price per Share} = \frac{\text{Equity Value}}{\text{Number of Outstanding Shares}}$$

[25] "Steady state" refers to the period when the company is mature and is expected to grow at the same rate forever

[26] Use less than 5 years only in almost mature firms and more than 10 years is very difficult to estimate in a reasonable way all the inputs the models need.

[27] Market values should be used.

2.2.1.2. Dividend discount model (DDM)

"A stock is worth the present value of all the dividends ever to be paid upon it, no more, no less." The Theory of Investment Value by John Burr Williams (1938)

There are two possible cash flows from buying a stock: dividends, during the period that the investor holds the stock, and the price from the sale of the asset. The discount dividend model intuitively values the equity of the company by discounting the future dividends by the cost of equity (Damodaran 2006).

$$\text{Equity value} = \sum_{t=1}^{t=n} \frac{\text{Dividend (t)}}{(1 + \text{ Cost of Equity})^{(t)}}$$

The Gordon Model uses the perpetuity formula and assumes a perpetual growth of dividends:

$$\text{Equity value} = \frac{\text{Dividend}}{\text{Cost of Equity} - \text{Perpetual Growth Rate}}$$

To conclude the dividend model is simple and very intuitive, however it has some limitations. It typically undervalues companies[28], its use is limited to stable companies and, as dividends are "sticky", they may not represent the true performance of the company (Brav et al. 2004 and Damodaran 2006). Finally, given the limitations mentioned the dividend discount model was not considered for the purpose of valuating DIA.

2.2.1.3. Free cash flow to the equity (FCFE)

"The FCFE model treats the stockholder in a publicly traded firm as the equivalent of the owner in a private business. The latter can lay claim on all cash flows left over in the business after taxes, debt payments and reinvestment needs have been met." Damodaran 2006

The free cash flow to the equity discounts the cash left from the business, after paying taxes, debt and reinvestment needs, by the cost of equity, in order to get the company's equity value.

To compute the free cash flow to the equity the following formula is used:

$$\text{FCFE} = \text{Net Income} + \text{Depreciation} - \text{Capital Expenditures} - \text{Change in Working Capital} - \text{Principal Repayments} + \text{New Debt Issued}$$

$$\text{Equity value} = \sum_{t=1}^{t=n} \frac{\text{FCFE (t)}}{(1 + \text{Cost of Equity})^{(t)}}$$

[28] The dividend discount model usually undervalues the company unless the dividend payment is higher than the free cash flow to the equity which in this case it might overvalue the company.

The dividend discount model and the free cash flow to the equity model output different results when companies choose not to distribute all its excess cash to shareholders (Damodaran 2006).[29]

The free cash flow cash flow to the equity has the advantage of taking into account the claims on the non-distributed earnings, however it comes with the cost of having to estimate a lot more factors, including capital expenditures, working capital and financing cash flows.

2.2.1.4. Free cash flow for the firm (FCFF)

"The free cash flows to the firm are the sum of the cash flows to all claimholders in the firm, including stockholders, bondholders and preferred stockholders" Damodaran 1996

In contrast with the dividend discount and free cash flow to the equity models the free cash flow to the firm values the enterprise value instead of the equity value. The intuition behind this approach is the idea that ultimately equity and bond investors are partners (Damodaran 2006) and that value must come from the operations regardless the financing structure.

To compute the free cash flow to the firm the following formula is used:

$$\text{FCFF} = \text{Operating Income} \times (1 - \text{Tax}) + \text{Depreciation} - \text{Capital Expenditures} - \text{Change in Working Capital}$$

$$\text{Firm value} = \sum_{t=1}^{t=n} \frac{\text{FCFF (t)}}{(1 + \text{WACC})^{(t)}}$$

As the author considers the intuition behind the free cash flow model valid and it does not require to estimate the debt cash flow explicitly this method will be used on DIA's valuation.

2.2.1.4.1. Sum of parts

"On many occasions, the company's value is calculated as the sum of the values of its different divisions or business units" Fernandez 2013

The sum of parts valuation approach consists in valuing different business divisions of the company separately. It is very useful to value multi-business or multi-national companies (Damodaran 2009) and access which business units or geographies are adding or destroying value. This way, managers can make valuation based investment decisions, allocating capital on high growth and added value branches and divest in underperforming segments. The

[29] If companies decide to distribute all its excess cash to shareholders both model will output the same result.

author believes that this approach is very informative and will be used to evaluate DIA's business separately in Iberia and emerging markets.

2.2.1.5. Adjusted present value (APV)

> *"In the adjusted present value (APV) approach, we separate the effects on value of debt financing from the value of the assets of a business."* Damodaran 2006

It can be said that The APV model relies on the principal of "value additivity" (Luehrman 1997). First the unlevered value of firm is computed, then the present value of the tax shields are added, and finally the expected bankruptcy costs are subtracted (Damodaran 2006).

$$\text{Firm Value} = \text{Unlevered Value of the Firm} + \text{Present Value of Tax Benefits} - \text{Expected Banruptcy Cots}$$

Unlevered value of the firm

The unlevered value of the firm is calculated the same as valuing a company without debt (100% equity financed). Consequently, the operating cash flows[30] should be discounted at the unlevered cost of equity (Jennergren 2011).

$$\text{Unlevered Firm Value} = \sum_{t=1}^{t=n} \frac{\text{FCFF (t)}}{(1 + \text{Unlevered Cost of Equity})^{(t)}}$$

Present Value of Tax Shields

As debt interests are usually tax deductable there is a benefit from holding debt instead of equity on the form of tax shields. The latter is comprised by the futures interests times the tax rate, discounted back to the present at a discount rate.

$$\text{Present Value of Tax Shields} = \sum_{t=1}^{t=n} \frac{\text{Debt} \times \text{Cost of Debt} \times \text{Tax Rate}}{(1 + \text{Discount Factor})^{(t)}}$$

There is no consensus about the discount factor that should be used to discount tax shields. Myers, together with Luehrman (1997), defend that the tax shields should be discounted using the cost of debt, Harris and Pringle, on the other side, say that it should be used the unlevered cost of equity. More recently Fernandez (2006) argues that it should be the difference between the present value of taxes for the unleveraged company, and the present value of taxes for the leveraged company.

[30] The operating cash flow is the same as the free cash flow for the firm already described on the previous section.

If we assume the first hypothesis then, in perpetuity we have:

$$\text{Present Value of Tax Shields} = \frac{\text{Debt} \times \text{Cost of Debt} \times \text{Tax Rate}}{\text{Cost of Debt}} = \text{Debt} \times \text{Tax Shield}$$

Bankruptcy Costs

The benefits of debt come with a cost: **increasing probability of default and consequently expected bankruptcy costs**. The costs can be either direct, such as lawyer fees, or indirect, such as loss of clients or reduced bargaining power with suppliers, before the company goes officially bankrupt. The indirect bankruptcy costs are estimated to be much higher than direct costs (Pindado & Rodrigues 2005). To access the probability of default it is generally used company's bond rating.

$$\text{Bankruptcy Costs} = \text{Present Value of Bankruptcy Costs} \times \text{Probability of Default}$$

2.2.1.6. FCFF vs APV

"WACC can only be applied if the leverage ratio of the company is deterministic and known at time t = 0. APV can be used to evaluate the firm if the amount of future debt is deterministic and known today" Kruschwitz & Loffer

Both the WACC and the APV have their advantages and disadvantages. On one hand, the WACC does not properly work in companies which are expected to change their capital structure significantly. In these situations is advisable to use the APV method since it provides flexibility to change debt in every period, and take its effects into account (Koller, Goedhart & Wessels 2010).

On the other hand, on the APV bankruptcy costs are very hard to estimate, especially the indirect costs. To avoid these estimations, most practitioners ignore bankruptcy costs, which is not reasonable and will overestimate the value of the firm, especially if it is high levered and therefore with high the bankruptcy costs (Damodaran 2006).

To conclude, although the APV model is considered as superior by many (Luehrman 1997), the bankruptcy costs are very hard to estimate properly and for constant capital ratio firms both models will output similar results. The great advantage of the APV is when valuing leverage buyouts or debt restructuring projects because in these situations capital structure is very volatile. Once DIA as a target net debt to EBITDA between 0,9x and 1,1x the author decided to use the WACC model in this paper.

2.2.2. Value creation

"Value is created by generating excess returns on investments" Damodaran 2006

Value creation models have their roots in capital budgeting and are based on the assumption that value is created by the excess returns generated by the firm[31]. This assumption is consistent with the net present value approach once to get a positive NPV the return of the project should be higher than its cost of capital.

The inputs for the economic value added are: the return on capital invested; the cost of capital; and the capital invested. This way, the return on capital invested must be higher than the cost of capital, in order to create value.

$$\text{EVA} = (\text{Return on Capital Invested} - \text{Cost of Capital}) \times (\text{Capital Invested})$$

Or

$$\text{EVA} = \text{EBIT}\,(1 - \text{Tax}) - \text{Cost of Capital} \times \text{Capital Invested}$$

Furthermore the value of the firm can be computed as:

$$\text{Firm Value} = \text{Capital Invested} + \sum_{t=1}^{t=n} \frac{\text{EVA (t)}}{(1 + \text{Cost of Capital})^{(t)}}$$

Finally, in accordance with Fernandez (2013), EVA should be equivalent to the WACC method if consistent assumption are taken, however the invested capital is very hard to compute[32], and "the typical EVA calculation involves 19 adjustments from a menu of between 9 and 34 adjustments" (Damodaran 2006). For this reason the author decided to use the WACC instead of the EVA.

2.2.3. Relative valuation

"Industry multiples are used often in practice, both to provide stand-alone "quick and dirty" valuations and to anchor more-complex discounted cash flow valuations." Liu, Nissim & Thomas 2007

The relative valuation assumes that the market is efficient and uses comparable stock prices and fundamentals to establish a price for the target company. The first step is to find the comparable peer group. Then, one needs to choose which multiples to apply. The final step is

[31] Excess returns are returns above or below the considered normal returns.
[32] Both the market and book values are not good proxies because, the first includes growth expectations and the latter is deeply affected by the accounting policies namely the depreciation approach the firm uses.

to apply the multiples to the peer group and multiply them by the company's indicators (Damodaran 2006).

Peer group

The peer group consists on **comparable firms**. It is usually chosen by using firms operating in the **same sector**, with the assumption that they are exposed to the same industry risk, with **same geographical presence** and with **similar fundamentals** of expected growth rate, margins and returns on invested capital, leverage ratios and capital investment (Steiger 2008).

Taking this into account, firms in the same industry (Food retail), with similar store concept (Proximity and price), operating in similar geographies (mixed between developed and emerging countries) and similar fundamentals, were used to build DIA's peer group.

Multiples

Multiples are ratios between enterprise value or share price[33] with company's indicators namely earnings, EBIT[34], EBITDA[35] and sales. This paper will focus on four multiples:

Multiples			
Price-to-Earnings (P/E)	Enterprise value-to-EBIT (EV/EBIT)	Enterprise value-to-EBITDA (EV/EBITDA	Enterprise value-to-Sales (EV/Sales)

Exhibit 2: Multiples

Each multiple has its advantages and disadvantages and "different multiples are meaningful in different contexts" (Goedhart, Koller & Wessels 2005). For instance, price to earnings multiple is widely used but is impacted by leverage and cannot be used for loss making companies; EBIT based multiples are impacted by amortizations and depreciations which can be manipulated, and sales multiples disregard profitability but can be used for all companies[36].

Moreover, there is no consensus in which multiple to use. Goedhart, Koller & Wessels (2005) argue that the Enterprise value-to-EBITA[37] multiple is the most appropriate, as it is not impacted by the capital structure and one-offs[38], in contrast Liu, Nissim & Thomas (2001) defend that price-to-earnings perform better.

In contrast, academics and practitioners agree that **forward multiples** should be used instead of current multiples, because they incorporate market growth and return expectations and, as

[33] Share price multiples will output the price per share directly while enterprise multiples output firm value.
[34] EBIT=Earnings before interests and taxes.
[35] EBITDA =Earnings before interests, taxes, depreciations and amortizations.
[36] All companies must have sales.
[37] EBITA = Earnings before interests, taxes and amortizations.
[38] One-offs are onetime non-recurrent extraordinary events.

they use analysts' consensus, they usually exclude one-off items (Liu, Nissim & Thomas 2001 and Goedhart, Koller & Wessels 2005).

Furthermore, in order to compute the peer's multiple, the harmonic average was used, since according to Baker, Ruback & Draft (1999) is the most precise approach to estimate multiples.

To conclude, although multiples are simple to compute, market related, and widely used, **it is very difficult to get a "perfect" peer group**, some are easy to manipulate and they don't require the use of assumptions. Taking into account the advantages and disadvantages, the author believes that multiples should not be used as a standalone method but are a good tool to complement a more complex valuation approach, namely the discount cash flow model (Goedhart, Koller & Wessels 2005 and Steiger 2008).

Finally, in the author's opinion, the best multiples to use to evaluate food retailers would be forward EV- to- EBITDAR[39] or forward EV-to-EBITA because both are capital structure and property ownership neutral. As the previous mentioned multiples are not widely available and easy to estimate the EV-to-EBITDA and EV-to-EBIT multiples will be used as substitutes. The price earnings multiple will also be used because it is widely used by the industry and some academics consider it as the most reliable one.

2.2.4. Contingent claim valuation

"With an option, you have the right (not the obligation) to buy or sell something at a specific price on or before some future date." Leuhrman 1997

The option pricing models are useful to complement a discounted cash flow valuation since it handles both opportunities (Leuhrman 1997) and flexibility (Koller, Goedhart & Wessels 2010) better than the DCF models. The latter models usually underestimate assets whose payoffs are contingent on the occurrence of a specific event (Damodaran 2005).

This method can be used to value assets with option characteristics[40], namely commodity based businesses, such as mining and oil projects in which the production output can be linked to the market prices[41], patents[42], or ultimately new product development, expansion plans or exit strategies (Fernandez 2013).

[39] EBITDAR = Earnings before interests, taxes, depreciations, amortizations and rents.
[40] For this the asset should has its payoffs linked to an underlying asset.
[41] For example, if the price of a mineral is low there is the choice between producing and wait until the prices increase.
[42] "A patent can be analyzed as a call option on a product, with the investment outlay needed to get the project going representing the strike price and the patent life being the time to expiration of the option." Damodaran (2005).

Moreover there are two different option models: the binomial model and the Black-Scholes[43]. Both models are based on the same variables: current value and the volatility of the underlying asset, the strike price[44], the risk free rate and the time to maturity.

To conclude, although the option models can successfully handle complex situation, its parameters are very hard to estimate, especially if the underlying asset is not publicly traded. For this reason the method was never widely used and it will not be used in this valuation.

2.2.5. Asset-based valuation

"Liquidation valuation is likely to yield more realistic estimates of value for firms that are distressed" Damodaran 2006

Asset-based models are based on the assumptions that value comes from the company's balance sheet.

The book value model assumes that the balance sheet's book value of equity is a proxy for the shareholders' equity, is useful to value small subsidiaries of a consolidated group; and **the liquidation value** uses the value as if the company would be liquidated, in which its assets are sold and debt is paid. The latter represents the company's minimum value and is useful to evaluate distress firms.

To conclude, asset-base models are useful and reasonable for some specific companies and circumstances, however they are generally too conservative once they take into account a static point of view and disregard the value of future growth (Fernandez 2013 and Damodaran 2006).

2.3. Conclusion

"Valuation is always a function of three fundamental factors: cash, timing and risk" Luehrman 1997

The literature review provides some insights about valuation. Firstly, cash, timing and risk are drivers of value and are transversal to all valuation methods.

"A valuation has little to do with science. A valuation is always an opinion." Fernandez 2004

Secondly, there is no consensus regarding which method outputs the best approximation for the "true" value and the models used depend on the firm specific characteristics and analysts

[43] The difference between both models is that the binomial takes into account discrete variation while the Black-Scholes uses continuous variations.
[44] The strike price is a fixed value at which the owner can buy or sell the underlying asset.

personal preferences. Additionally, it might be agreeable that combined methods might output a more robust valuation.

"Any analysis, however, is only as accurate as the forecasts it relies on." Goedhart, Koller & Wessels 2005

Thirdly, valuation highly depends on the assumption the analyst makes, therefore it is very important to carefully analyze the company, the industry and the macroeconomic environment. Additionally, it is essential to stress test the main inputs in order to analyze their sensitivity on the output result.

Finally, the present valuation will use the flowing methods: **the discount cash flow model, using the free cash flow to the firm and the WACC as the discount rate; and the EV/EBITDA, EV/EBIT and P/E multiples**.

3. Food Retail Business and Macroeconomic Outlook

Prior to enter on the valuation itself it is crucial to understand the industry and its macroeconomic drivers in order to access reasonable trends.

3.1. Food retail business

The food retail business is characterized by **high volume of sales, low margins, and workforce and capital intensive.** Therefore, albeit firm specific efficiencies and performance, food retail companies might be influenced by the macroeconomic environment, namely private consumption and GDP growth, unemployment, inflation, population, and interest rates.

Furthermore, to have a successful food retail business it is essential to **reach critical mass**. This way the company will be able to dilute its fixed costs and to gain bargaining power over suppliers. It is also important to have **efficient operations,** namely in logistics and inventory management. In sum, **the goal of the food retail business is to put the products on the shelves at the lowest possible cost and have the highest rotation possible.**

Moreover, there are several store formats, each one with its characteristics and primarily focus. The table below summarizes the main distinct formats: **Hypermarkets**, large superficies with focus on assortment; **Discount**, with focus on prices and private label products; **Convenience/Neighborhood**, small stores which value proximity; **Gourmet**, stores focused on quality and shopping experience; and **Traditional**, mainly family owned businesses whose best advantage is to have a personalized service.

Type\Focus	Size	Price	Assortent	Service Personalization	Proximity	Private Label
Hypermarkets	Big	High	High	Low	Low	Medium/Low
Discount	Medium	Very High	Low	Low	Medium	High
Convinence	Small	Medium High	Medium	Medium	High	Medium
Gourmet	Small/Medium	Low	High	High	Low	Low
Traditional	Small/Medium	Medium	Medium	High	Medium/High	Low

Exhibit 3: Store formats

Finally, the food retail business is highly cyclical intra-year since sales hike during the Christmas period and then eases on the first months of the year. For valuation proposes, as the forecasts are made annually the cyclicality effect is absorbed and no further adjustments have to be made.

3.2. International trends

The 2008 crisis dragged developed countries to recession and austerity, and emerging countries to slower growth. Furthermore, the peripheral European countries were further impacted by the sovereign debt crisis, which brought more austerity, and some countries had to be bailed out[45] by the IMF. Additionally, some financial institutions had to be intervened, and capital became scarcer and more expensive, even though the European Central Bank established the reference rate at historical minimums, 0,05% **(See appendix III)**.

With the difficult macroeconomic environment several international retailers had to optimize their capital and portfolio and were forced to abandon unprofitable projects to focus on core markets. For instance, DIA exited from Turkey, Beijing and France; Carrefour exited from Colombia, Indonesia, Malaysia, Greece, among others; and Tesco sold its operations in Japan and USA.

Trends		
Western Europe	**Emerging markets**	**World**
- Ageing Population	- Increase of urban population	- Price and Proximity stores
- Less persons per household	- Rise of middle class	- Health concerns
- Reduced storage space	- Higher personnal costs	- More demanding in fresh products
- Reduced income	- Decrease of poverty	- Franchisinig
- More woman on workforce	- Modernising lifestyles	- Innovative channels

Exhibit 4: World trends

Moreover, **consumer habits are constantly changing**. In Western Europe, the population is ageing, there are fewer people per household and reduced storage space, people have less income to spend and there are more women in the workforce; and in Emerging markets, the

[45] Including Greece, Portugal and Ireland.

urban population and middle class are increasing, and personal costs are higher. **These new trends favor the price and proximity focused formats** in deterioration of larger formats.

Additionally, **franchising is gaining share** due to synergies gained between the know-how and purchasing power of a big retail chain, with the day to day management of an entrepreneur. The franchise system benefits both the franchisee, who opens a business and has the support of an establish retailer, and the company, by reducing the capital requirements of opening a store and saving some operational costs charged to the franchisee.

Furthermore, generally speaking, people are increasingly more concerned about health issues, and clients became more demanding regarding fresh products. In response, **retailers have been adapting its store concepts towards fresh and perishables** such as fruit, vegetables, meat, fish and bakery. It is important to point out that these products bear extra costs once they usually have shorter expiration dates and demand special care regarding transportation and storage. At the same time, retailers have been investing in \ **products** in order to offer "quality at affordable prices" and "value for money" products.

Finally, technology evolves, and with it, new and **innovative distribution channels** arise. Two examples are the "click and collect" system, which consists on ordering the shopping cart online and picking up the order at the store, and e-commerce, which consists in buying online and receiving the products at home. It is important to point out that although the online channel is increasing its share in the market, the majority of food products are still bought in store.

3.3. Macroeconomics

DIA is present in five countries divided in two broad groups: **Iberia**, which includes Portugal and Spain; and **emerging countries**, including Argentina, Brazil and China.

In the very important **appendix IV** the macroeconomic environment is deeply studied, including the competition, in each country where DIA operates.

To summarize, after years of downsizing its portfolios and focus on their core businesses, European retailers face another threat: **Deflation**. To face this adversity and diversify its portfolio, retailers are searching for new growth opportunities and investing in emerging markets. Nevertheless, they also have increasing risks namely hyperinflation and exchange rate volatility. Furthermore, accordingly to the new trends in the market **discount and convenience are the most attractive formats**. Moreover, franchising is gaining share, as well as private labels which are used as a way to differentiate and retain customers. Finally,

innovative distribution channels such as e-commerce and click and collect are gaining share since people are becoming more technological.

4. The Company

"DIA's mission is to offer shoppers quality at unbeatable prices, to which end the company is inspired and abides by the following core business principles: efficiency, initiative, respect, teamwork and customer focus." **Source: Company data**

4.1. Overview

DIA is an international food retailer listed on the main Spanish stock exchange, IBEX 35, since January 2012 after the spinoff from Carrefour on July, 2011. DIA employ more than 40 thousand people and operates 6.707 stores[46] located in five countries: Spain, Portugal, Brazil, Argentina and China. Its stores can be considered as **convenient discount** and **value proximity and price**. Moreover, the EBIT margin growth of 140bp since 2010 shows how profit driven the management team is. Additionally, DIA is expected to have sustainable growth opportunities since it is an active player on the consolidation of the Spanish market and has an increasing presence in emerging markets.

Exhibit 5: DIA geographical presence. Source: Company data

4.2. History

DIA opened its first store in Madrid, in 1979, introducing the discount format in the Spanish market. Six years later, the first own branded product was introduced, followed by the inauguration of the first franchise store in 1989. At the end of 1992, DIA became nationwide,

[46] As of September 2014.

operating 1,000 stores in Spain, after the acquisition of Dirsa, Mercadopopular and Ahorro Diario. The following year marked the start of the international expansion with the opening of first store in Portugal. The next couple years were of international expansion adding Greece and Argentina to DIA's portfolio.

In 1998, the loyalty card "ClubDia" was introduced. The new international expansion phase occurred in 1999, 2001 and 2003, entering in Turkey, Brazil and China, respectively. In the meanwhile DIA merged with the giant Carrefour, which was the Europe's largest player and the second worldwide, and entered in France. In July 2011, DIA achieved some very important milestones: the spin off from Carrefour, the IPO, and consequent entry in Madrid's stock exchange for a share price of €3,5. On the next, six months DIA entered in IBEX 35.

In 2007 the company reinforced its position in Spain by acquiring Plus' 251 stores. In contrast, DIA's network in Greece was rebranded after Carrefour in 2010. DIA's observation of the consumer habits resulted on adding DIA Maxi and DIA Market formats in 2006/2007 and the DIA fresh in order to reinforce its fresh produce and perishables focus, in 2012.

The last two years were very busy for DIA's management team: firstly, it successfully exited Turkey and Beijing loss making operations in 2013 and, more recently, sold DIA France for an enterprise value of 600 million Euros to Carrefour; secondly, on the acquisitions side, DIA bought Schlecker's Iberian operations, a proximity home and personal care (HPC) retailer with 1130 stores, diversifying its portfolio and improving its HPC offer. More recently the company closed two more deals in the fragmented Spanish market: El Árbol, a fresh product specialist; and 160 Eroski stores; lastly, the company issued its first five year maturity Euro Bond in July 2014.

To summarize, these last transactions indicate a strategy of:

- Focus in core markets: Iberia and Latin America;
- Reinforcement product assortment especially in fresh produce and HPC;
- Strong financing muscle.

4.3. Highlights

The transactions made in the last two years have significant impact in DIA's operations. Therefore, in the next sub-section, these transactions will be closely analyzed.

DIA Market III

DIA is currently updating its DIA Market stores, which account for around 60% of total sales, from DIA Market II to DIA Market III. This way DIA is reinforcing its focus on fresh food

and perishables by adding in-store bakeries and improving its offer. The refurbishment costs around 50 thousand Euros per store and is expected to be complete in 2017. Until now the remodeling program has been successful with store sales increasing, on average, by 6%.

Shlecker/Clarel:

Schlecker's operations were bought for 70,5 million Euros and closed in the beginning of 2013. This way DIA added a new store concept for its portfolio and improved its home and personnel care offer. The more than 1.130 stores around Spain and Portugal with an average selling are of 150 square meters are currently being rebranded to Clarel. The process includes the refurbishment of the stores, to get a more modern look; the increase of SKU's[47] number offered in store and the maximization of the portfolio mix to better meet clients' expectations. The remodeling process costs between 30 thousand and 40 thousand Euros per store and have been implemented successfully with stores remodeled increasing its sales by 8%, on average. Furthermore, the company expects to open 100 stores in 2014 and 150 per year from 2015 onwards and increase its private label penetration from 19% to 30%. This acquisition enables DIA to diversify its portfolio and is consistent with its strategy of focus in proximity and price. Finally, a new Clarel store cost between 45 thousand and 60 thousand Euros and the first numbers are showing that this format has a higher return on investment (ROI) than traditional DIA's stores.

DIA France

Due to DIA France poor performance with declining sales, extremely negative like-for-like and EBIT margin deterioration **(See appendix V)**, DIA decided to sell its French operation to Carrefour for an enterprise value of 600 million Euros. The transaction was accepted by the anti-trust authorities in November 2014 and closed in the beginning of the following month. DIA received 283,2 million Euros for the sale of the entire capital plus 361,5 million Euros for repaying intra-group debt. This way the company showed, once more, its focus on profitable growth.

El Árbol

El Árbol's acquisition by DIA was accepted by the anti-trust authorities and closed last October. This way DIA acquired 100% of the equity stake for one euro plus €26 million for a participative loan owned by some of El Árbol shareholders. Moreover, DIA will also take over El Árbol net financial debt of 99 million Euros. The total investment amounts €125 million **(See appendix VI)**.

[47] SKU=Stock keeping unit. It corresponds to the number of references/products the store offers.

In 2013, El Árbol had a network of 451 stores, generating €825 million in sales and EBIT margin of minus 2,4% . El Árbol stores are mainly located in rural areas where DIA's store network is less concentrated and therefore it seems a good complement of the company's network. DIA expects significant synergies arising from this transaction on the logistics, administrative and purchasing power levels. On one hand, the El Árbol's negative condition could be reversed with implementation of DIA's efficient processes. On the other hand, DIA can take advantage from El Árbol's know how in fresh produce.

Finally, the antitrust authorities accepted the transaction with the condition of DIA to divest in 7 stores accounting 1,02% of 2013 total sales.

El Arbol P&L	2011	2012	2013
Sales	836	849	825
EBITDA	22	22	-5
% of sales	*2,6%*	*2,6%*	*-0,6%*
EBIT	5	5	-20
% of sales	*0,6%*	*0,6%*	*-2,4%*

Exhibit 6: El Árbol historical financials. Source: Company data

Eroski

DIA disclosed last November the acquisition of 160 Eroski stores for a maximum price of €146 million[48] **(See appendix VI)**. The transition is still subject of clearance from the Spanish competition authorities but is expected to be accepted. The stores have on average a selling area of 800 square meters, are mainly located in Madrid and generated 487 million Euros in gross sales[49] in 2013. With this transaction DIA would increase its market share in Madrid to 9,8%, and it nationwide market share to 9,5%[50]. In contrast with El Árbol, in the Eroski deal DIA is not buying any central departments and logistics centers and stores are already profitable. Finally, Eroski stores will be converted to DIA Maxi, DIA Market or El Árbol depending on their size and location.

REGION	STORES
MADRID	108
ANDALUCÍA	24
EXTREMADURA	6
CASTILLA LEÓN	20
CASTILLA LA MANCHA	2
TOTAL	**160**

Exhibit 7: Eroski stores. Source: Company data

Notes Issue

Last July, 2014, DIA issued €500 Euros note, under the Euro Medium Term Note Program, approved by the Central Bank of Ireland. The issue matures after 5 years, pays an annual

[48] The final price is still subject to adjustments depending on the final number of stores.
[49] Gross sales, in contrast with net sales, include VAT.
[50] Source: company data.

fixed coupon of 1,5% and had an issue price of 99,419% and a yield to maturity (YTM) of 1,622%. Furthermore the company also secured a syndicated revolving credit facility with several financial institutions amounting 400 million Euros and for a term of 5 years. The amount will be used to partially cancel the current facility agreement and to provide funds for the Company's operations and working capital.

4.4. Organizational chart

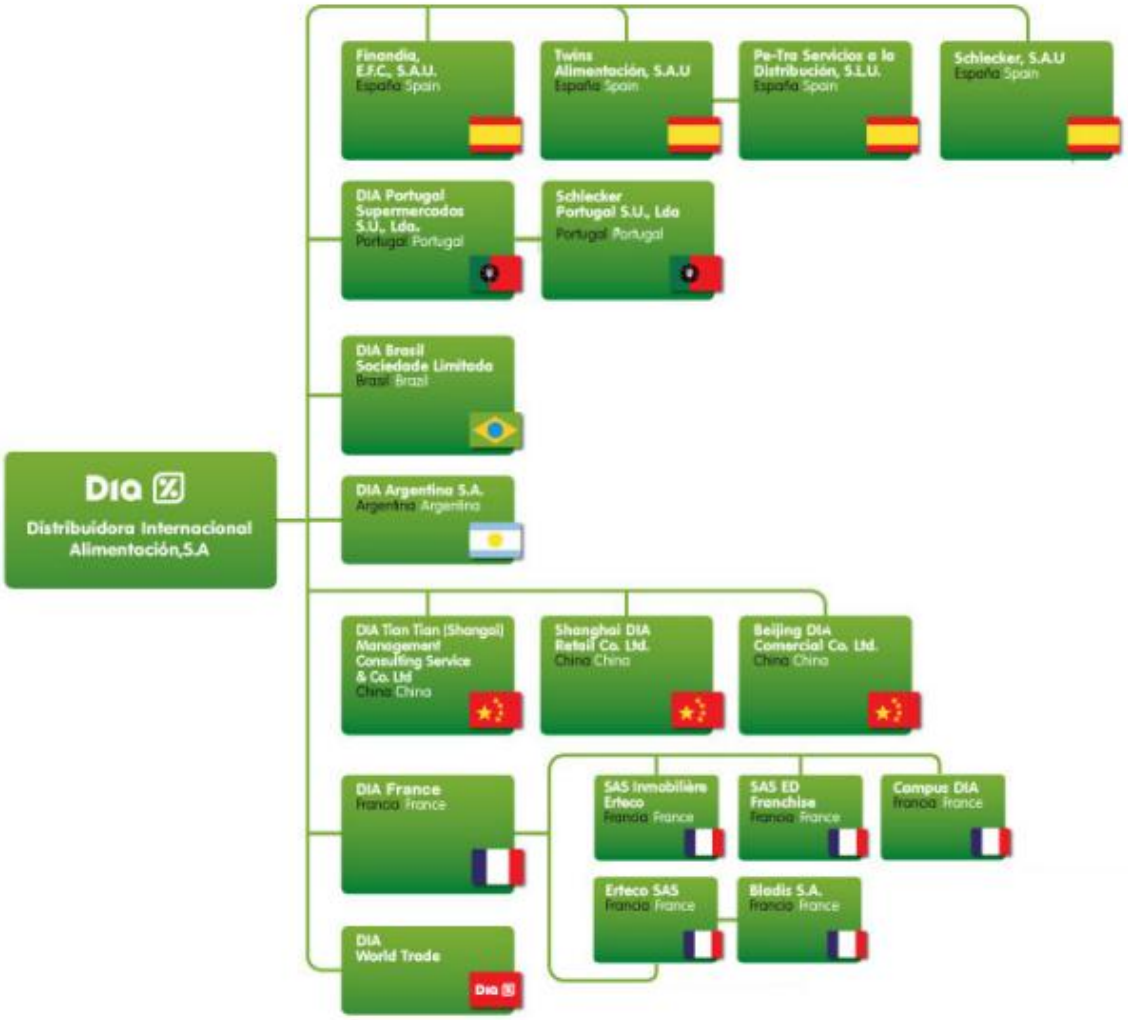


Exhibit 8: Organizational chart. Source: Company data

It is important to note that the Turkish and French are already discontinued and no longer belong to DIA.

4.5. The concept

The company operates several store banners: **DIA market** is the neighborhood store model: the stores range between 400 and 700 square meters of selling area with special attention to perishables; the **DIA fresh** and **fresh by DIA** concepts are in the testing phase: the stores average 150 square meters of selling area and the idea is to turn DIA as a true specialist in

fruit and vegetables; **DIA Maxi** is the largest store format with a floor are of up to 1.000 square meters: they are mainly located in city outskirts, have some parking lots and offer a broader assortment; **Clarel** is the new home and personal care banner, which substitute the former Shlecker; DIA decided to maintain the **El Árbol** brand after its acquisition; **Cada DIA** is the retail format in small towns, particularly in rural areas, and stores are managed by a local entrepreneur; **Mini-Preço** and **Mais Perto** are the brands DIA operates in Portugal. Finally, DIA is developing a "click and collect" system with the use of a shopping website, a mobile phone app and more than 4.150 picking points.

Exhibit 9: DIA banners. Source: Company data

Price and proximity

DIA aims to be leader in both the **neighborhood segment**, offering its clients everyday groceries without having to travel by car, saving money and time in the process, and in **price**, offering quality at the best price in the market. Accordingly to DIA's 2013 annual report, the company has the best price image in Spain, Portugal, Brazil and Argentina.

Fresh Focus

DIA adapted to the new costumers demand and became more focused on fresh and perishable products.

Quality private label

DIA uses its own brand to achieve a good price image, to gain differentiated advantage and increase customer loyalty. The company aims to offer the same or better quality as the leader product with a lower price. On average more than 50% of sales are own brand products. Furthermore, in order to meet the requirements of a broad customer DIA's private label catalogue has around 7.500 SKU's.

Exhibit 10: DIA private label brands. Source: Company data

Loyalty program

DIA implements its "ClubDia" loyalty card, in all countries except for Brazil, in order to offer immediate discount and consequently achieve a better price image. This way the company is able to better understand its clients' consumer patterns and elaborate efficient and profitable sales plans.

Low cost operator

DIA is constantly trying to improve its processes and increase efficiency both in supply chain[51]; and in-store[52]. The result is an efficient operation which is able to further invest in prices.

The franchise

DIA divide its stores in three categories: COCO, which means company owned, company operated; COFO, meaning company owned, franchise operated; and FOFO, franchise owned, franchise operated. The weight of franchise stores in total stores increased from 30% in 2010 to more than 50% in 2014, which shows a clear strategy of increasing the franchise network.

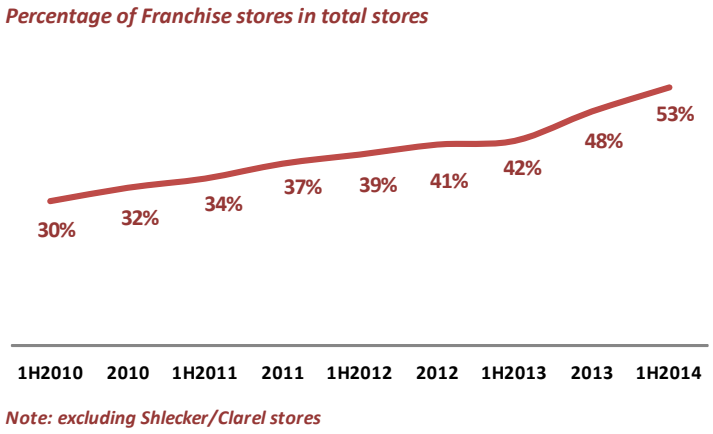


Exhibit 11: Franchise store evolution. Source: Company data

DIA's franchise model consists on a cost/profit sharing between the company and the franchisee, resulting in a "win win" situation. On one hand, DIA supplies all the franchisee's products, **transferring to the latter part of the gross margin**. On the other hand, the **franchisee supports some of the operational costs**. Moreover, the logistics are managed by the company and the franchisee pays the products "in cash"[53] **(See appendix VII)**.

Furthermore the franchise stores are generally located in more rural areas and suburbs[54] and the entrepreneur is usually a local residence working with his/her family in the store.

[51] DIA uses an integrated and optimized logistic system; multi temperature trucks and "voice-picking" technology.
[52] For instance, the packaging and conditioning make products allocation easier; and, the use of bioptic scanner, the fact that the bar-code is in several places of the product and the optimized key board **makes price reading faster and easier.**
[53] This way, DIA keeps its strong working capital surplus. However in the beginning of the franchisee operations DIA provides some credit to the entrepreneur.
[54] Rural stores usually have less competition than stores located in the center of large cities and consequently higher margins.

DIA believes that a local entrepreneur is able to reduce costs, namely personal costs and "unexplained"[55] costs by working in-store with his/her family, and increase sales by being flexible[56].

This way DIA's franchise system allies the bargaining power and the know-how of an international retailer with the flexibility and entrepreneurial spirit of the franchisee. The main benefit for DIA is the increase EBITDA margin and for the franchisee is the opportunity to manage its own competitive and profitable business.

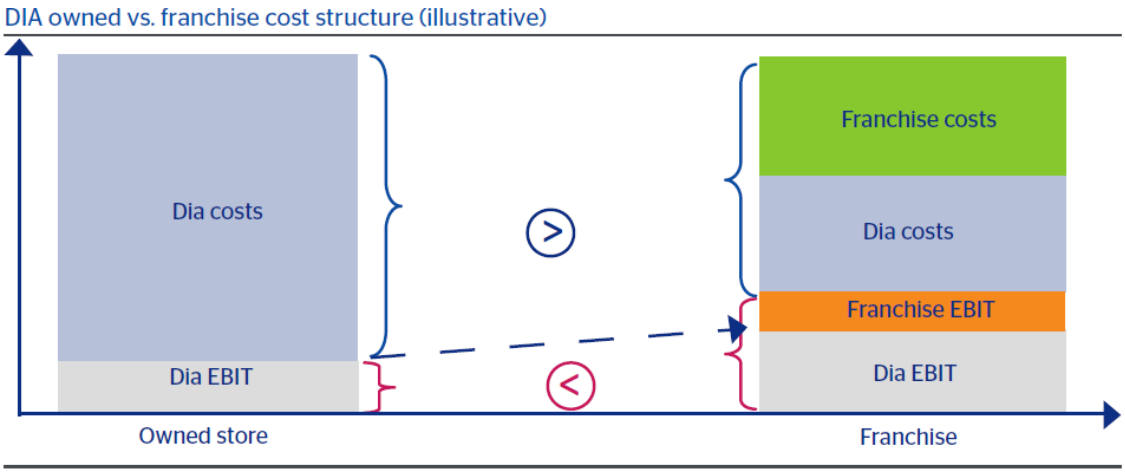


Exhibit 12: Franchise margin accretive. Source: Company data

Profitable Growth

Finally, DIA has been steadily growing since its inception in 1975, however it does not search growth at any cost, which may imply closing unprofitable businesses, as it happened in Beijing and Turkey in 2013 and more recently with DIA France.

4.6. SWOT

Swot	
Strenghts	**Weaknesses**
- Attractive format: Price, Proximity & Franchise; - Price leadership perception; - Strong private label penetration; - High margins;	- Dependence on the Iberia market; - Negative "Like-for-Like" in Iberia; - Dependence on the convenience discount format;
Opportunities	**Threats**
- Emerging markets growth prospects; - Consolidation in the Spanish market; - Clarel as a source of differentiation and growth in new segment;	- Deflationary environment in Iberia; - Hyperinflation and decelerating growth in emerging countries; - Very hostile competitive environment in Portugal; - Exchange rate volatility; - Loss of control over the franchisees

Exhibit 13: SWOT analysis. Source: Own estimations

[55] "Unexplained" costs are for instance some inventory losses and utilities waste which as the manager is also the owner and the employees are usually relatives they tend to be reduced.
[56] For example: extended opening and closing hours.

To summarize, DIA has an attractive store format, suitable for the world market trends; is present in emerging countries, which might provide good sources for growth; has been able to increase its margins, even in a deflationary environment; and its offer is well perceived by the customers. In contrast, DIA is highly depended on its Iberia operations, which are currently facing a competitive and deflationary environment; its emerging operations might face macroeconomic headwinds and with the increase share of franchise DIA might lose some control over operations and unhappy franchisees can deeply affect the company's performance[57].

4.7. The share

DIA is currently trading on IBEX 35, the main Spanish stock exchange comprising the 35 largest companies, and has 651.070.558 shares outstanding.

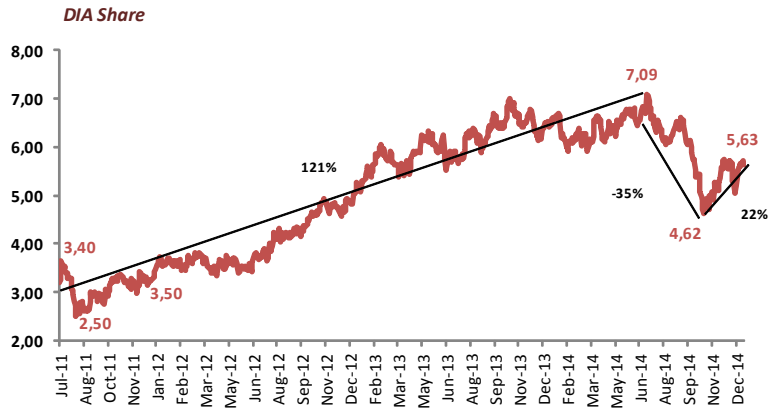


Exhibit 14: DIA Share evolution. Source: Company data

DIA started to be traded on Madrid's stock exchange on fifth July 2011 at €3,4 per share. One month later the stock reached its historical minimum of €2,5. Moreover, the share became to be traded on IBEX 35 in 2012 at a share price of €3,5. On July 2, 2014, fueled by the company's good performance including the successful divestment in loss making operations, DIA's share reached its historical maximum of €7,1 during the day. This price implies a 121,2% valorization since it was first traded. During the same period IBEX 35 grew 6,6% and the food retail index slightly decreased (-0,5%).

[57] There were already some situations where franchisees publicly accused DIA of enforcing them to sell products below cost and to have actions "less transparent". This risk is higher in periods of difficult macroeconomic environment where the company needs to invest in prices but the franchisees are not willing to sacrifice its margins.

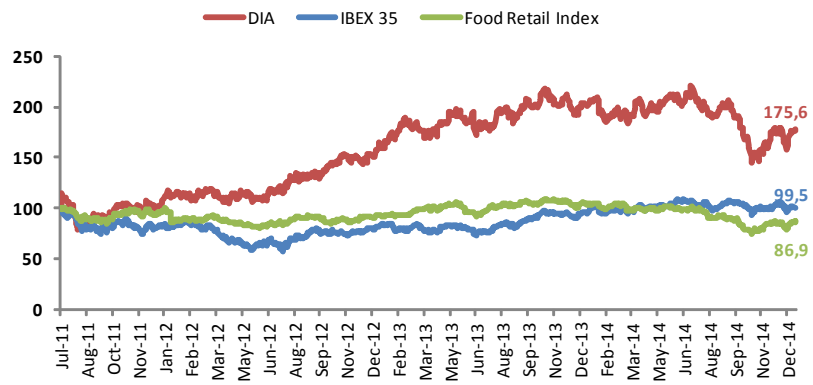


Exhibit 15: DIA performance *vs* IBEX 35 and Food retail index. Source: Company data

Since the historical maximum, the share decreased by 35% to a minimum of €4,6, in 16 of October. During the same period the food retail index slipped by 25%. This was probably due to general deterioration of the macroeconomic environment both in Europe, with risk of further deflation, and in some emerging markets, countries highly dependent on crude production that suffered from the sharp decrease in oil prices and in Eastern Europe, countries continuing to face headwinds from the Russian turmoil. Regarding DIA, it registered historical negative like-for-like in Iberia, of -5,6% during the second quarter and -7,1% in the second quarter, albeit margin increase, and, Brazil and Argentina face macroeconomic uncertainty, which was reflected in devaluation of their currencies pressuring its performance in Euros. These effects supported the negative performance of DIA's Share during this period.

Furthermore, its performance until the end of the year was positive with a valuation of 22% since the minimum in October.

Performance	2012	2013	2014
DIA	37,6%	35,1%	-13,4%
IBEX 35	-4,7%	21,4%	3,7%
Food retail index	-7,1%	15,6%	-17,1%

Exhibit 16: DIA performance per year *vs* IBEX 35 and Food retail index. Source: Company data

Furthermore, DIA deeply outperformed the Spanish market and Food Retail index in 2012 and in 2013. During 2014, the IBEX 35 had a positive performance growing 3,7% showing further signs of recovery while the food retail index and DIA were deeply in red, performing -17,1% and -13,4%, respectively. This was mainly due to macroeconomic conditions of low inflation in Europe and macroeconomic volatility in emerging markets.

Payment Year	2012	2013	2014
Dividend per share	0,11	0,13	0,16
% growth		***18,2%***	***23,1%***

Exhibit 17: DIA dividend distribution. Source: Company data

Finally, since the spin off, DIA distributed increasing dividends every year, and a share redemption of 4,16% of its capital in September 2013.

5. The Assumptions

During the literature review on the second section the valuation methods were analyzed and the author decided to use the discount cash flow as the major valuation method and the multiples models to increase the robustness of the results. In this section the main assumptions will be explained followed by the final results and conclusions on the sixth section.

5.1. Sales

Food retail is a volume business in which **product rotation is essential in order to dilute the high fixed costs**. Hence, understanding sales' drivers is crucial for a good interpretation of the retailer's value.

Higher sales volume can be reached by **positive "like-for-like"** (LFL), corresponding to the year on year growth of the same stores; and **expansion**, which corresponds to the current year openings **(See appendix VIII).**

On one hand, LFL is used to evaluate the performance of the current store network and is vital to maintain sustainable growth. This KPI[58] is mainly driven by food inflation, GDP growth and competitive environment. It is also influenced by the investment in remodeling plans which are expected to increase sales. On the other hand, expansion factor is strictly dependent on investment in new stores.

Iberia's retail environment, including food retail, has been suffering due to the financial crisis of 2008 and the sovereign debt crisis in 2011. Furthermore, the 2014 year confirmed the increasingly DIA's negative trend in sales like-for-like registered since the first quarter of 2013. This decrease is greatly explained by the very low inflation, including deflation in some DIA's key categories. Moreover, the situation in Portugal is poorer since it became a promotional driven market and highly competitive. The first two players, Sonae and Jerónimo Martins, are strongly investing in prices and gaining market share. In terms of expansion, the company opened around 221 DIA stores in the last two years corresponding to a 3,1% annual average growth.

[58] KPI = Key performance indicator

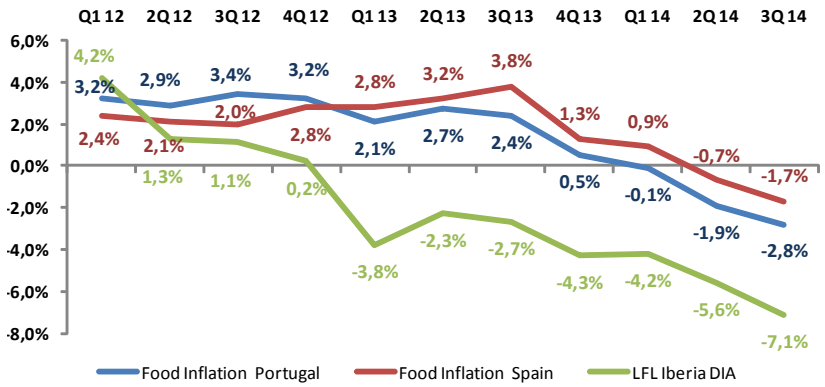


Exhibit 18: DIA Iberia LFl *vs* Food inflation. Source: OECD iLibrary and Company data

Regarding competition, in Spain, Carrefour managed to improve its LFL from deeply negative to around zero. Altough Carrefour' LFL may have been positively affected by a lower denominator[59], the negative LFL trend is a "red flag" for DIA and must be the main reason why investors have been bearish on DIA's stock during 2014. Moreover it is also important to note that, according to the company, DIA has been consistently gaining market share on the spanish market despite negative LFL. In Portugal, the two main players have consistently overpass DIA in LFL terms since the first quarter of 2013.

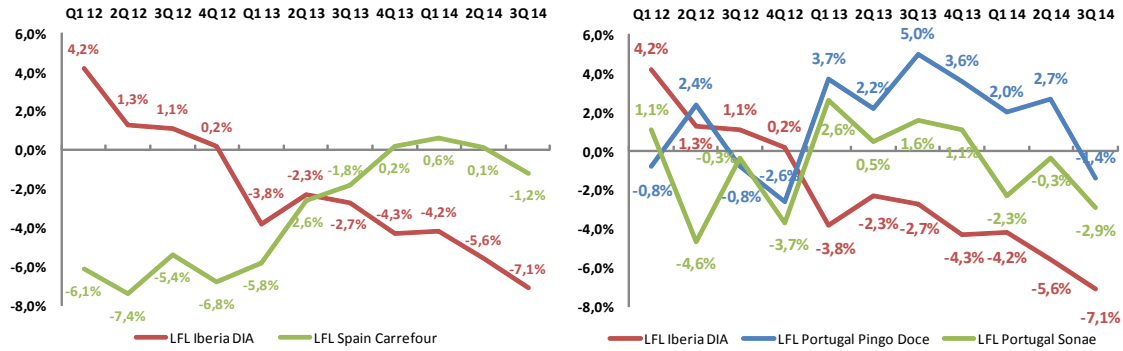


Exhibit 19: DIA Iberia LFl *vs* Competitors.

For the future it is foreseen LFL to improve gradually as a result from the economical environment recovery. GDP is expected to grow in Spain and Portugal, by 1,3% and 1,0%, respectively, in 2014, and there are signs of food inflation to return to positive values. Moreover, in Portugal it is expected the levels of competition to stay high and DIA will probably be forced to invest more in prices to recover clients.

Regarding expansion, DIA's network in Iberia is already somehow crowded and the company estimates cannibalization to have a negative impact of 1% in Spain[60]. Therefore, after the acquisitions of El Árbol and Eroski stores, it is expected the company to ease store openings.

[59] Carrefour LFL has been decreasing during the last years which makes the denominator (sales from the year before, smaller which may have a positive effect on this year's LFL.
[60] According to DIA's third quarter conference call

Moreover the two acquisition recently made are expected to impact DIA's consolidate accounts in 2015 with an increase in sales of around €1.150 million.

Regarding Clarel, it is expected sales to increase substantially from the positive impact of stores remodeling and expansion. Furthermore Clarel is less vulnerable to food inflation which might be positive for its growth.

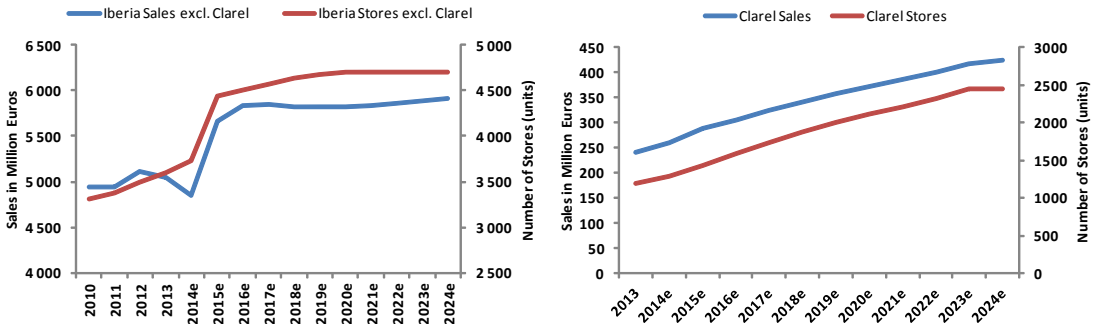


Exhibit 20: DIA Iberia - Sales and Store evolution. Source: Company data and Own estimations

In emerging countries the picture is substantially different with strong positive LFL growth[61] and expansion rates. The headwind in emerging countries has been the negative effect of the exchange rates, especially in 2014 and more particularly in Argentina. Regarding how to manage the exchange effect, the author made two important assumptions: first, in the long run, accordingly to the **purchasing power parity**, the currency effect should only reflect differences between local inflation and the German inflation, used as the European benchmark; secondly, **periods of hyperinflation or deep recession have a negative impact on the currency**, due to higher uncertainty about the future of the country.

As the three countries are significantly different among them, they should be analyzed separately.

Accordingly to the uncertainty environment lived in Argentina it is expected high inflation, low or even negative GDP real growth and negative exchange rate effect. The result is: high LFL evolution and low growth in Euro terms. After the period of high inflation and devaluation of the Argentinean peso it is expected the levels of inflation to ease to historical values, and sales in Euro terms to increase. It is also important to note that DIA is currently growing its sales above inflation levels[62], demonstrating a solid operation despite the macroeconomic environment.

[61] LFL in emerging countries is calculated using local currency
[62] According to DIA's investor relation

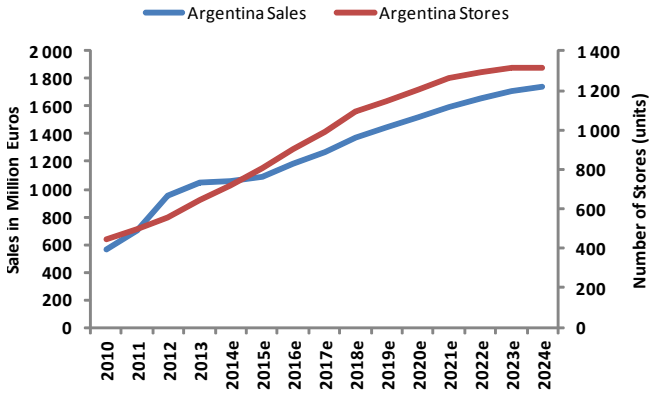


Exhibit 21: DIA Argentina - Sales and Store evolution. Source: Company data and Own estimations

In Brazil, inflation is above the 4,5% government's target including food inflation which is constantly higher then overall inflation. If inflation is good news for food retailers because it should help like-for-like growth, at the same time, the economy is stagnating and the Brazilian Real has been devaluating against the Euro, negatively affecting DIA's sales in 2014. For the future it is estimated the economy to recover to levels around 3% of GDP growth and a gradual declining of inflation levels to government's target. This way prices might decelerate but sales should be helped by an increase of volumes due to higher disposable income. Moreover the exchange effect should be softer in the future.

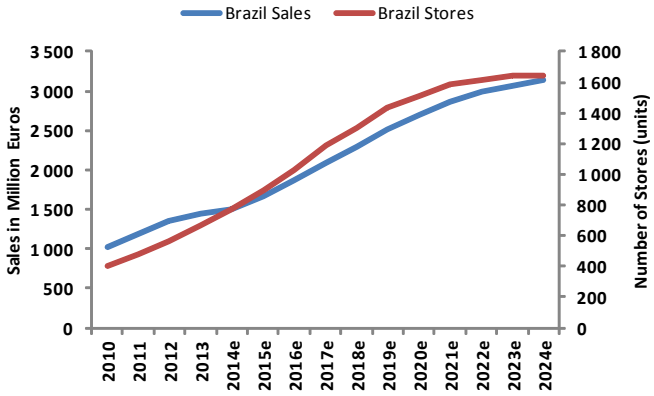


Exhibit 22: DIA Brazil - Sales and Store evolution. Source: Company data and Own estimations

The operation in China is residual for the total group but both sales and store expansion have been witnessing double digit growth which suggests that the company is investing on this market. Although the recent deceleration of the economy, China is still forecasted to grow at levels above 7% for the next two years and above 6% in the medium term which should result in increasing disposal household income and consequently benefiting the retail market. Moreover inflation has been stable around 2,5% and food inflation has been above the overall inflation which should help both like-for-like growth and margins.

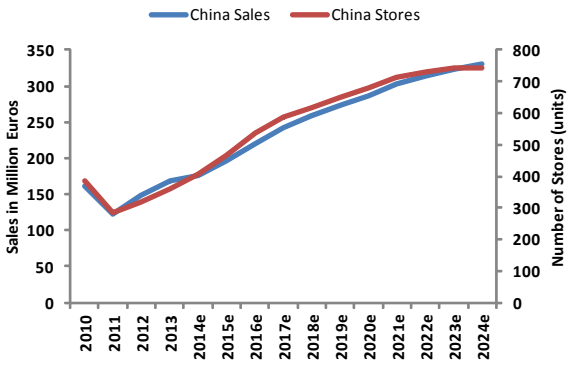


Exhibit 23: DIA China - Sales and Store evolution. Source: Company data and Own estimations

Furthermore, using Carrefour and Casino[63] operations in Latin America to benchmark DIA's performance, it suggests DIA is outperforming its competitors, reinforcing the idea that the company operates a solid store network in emerging countries.

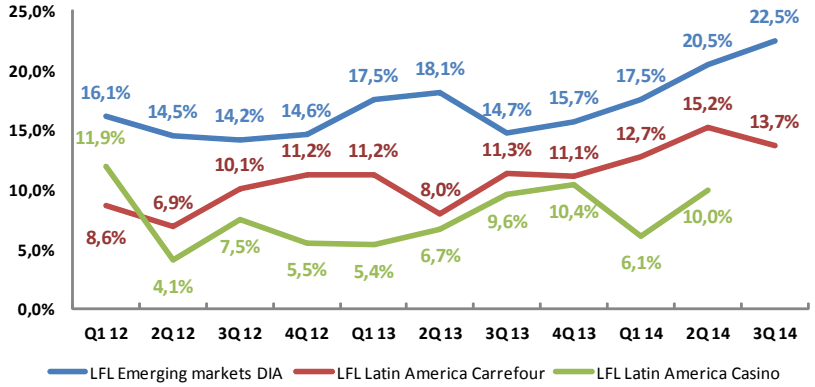


Exhibit 24: DIA emerging markets LFL *vs* Competitors.

To summarize, emerging markets are without doubt a source of growth and DIA has been showing very healthy sales like-for-like and double digit expansion growth. Despite temporary macroeconomic challenges it is expected DIA to continue investing on these markets.

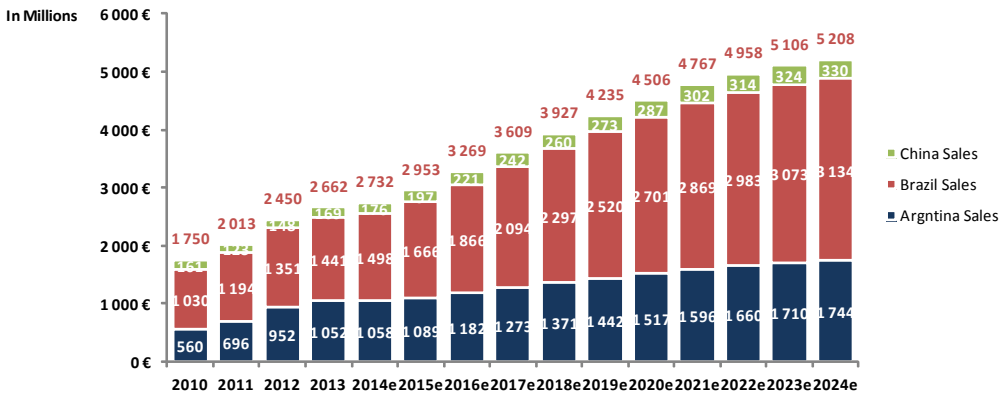


Exhibit 25: DIA emerging markets sales evolution. Source: Company data and own estimations

[63] Casino's operations include Argentina, Brazil, Colombia and Uruguay while Carrefour includes Argentina and Brazil.

5.2. Cost of goods sold

The cost of goods sold (COGS) is the largest expense in the food retail business and is one of the reasons why critical mass is so important: to gain bargaining power with suppliers. There are three main drivers for the COGS: the above mention, **bargaining power**; **investment on prices**; and **franchises**. The first one is closely linked to the economies of scale concept, "the more you buy, the cheaper it gets". With the sale of the French operations, DIA will lose sales volume and consequently bargaining power, however, this should be recovered with the acquisition of El Árbol and Eroski stores. Regarding investment in price, DIA is already recognized as the price leader in most of its markets, which suggest that the current gross profit margin has already this investment incorporated. Furthermore, franchising growth should have a negative impact over the gross profit since DIA "share" part of the margin with the franchisees; however DIA has been able to maintain or even grow the margin, with the exception of 2014, suggesting that the impact should be marginal. To conclude, the author estimated the gross margin to decrease (20bp) in 2014, reflecting the trend verified on the third quarter and a second decrease of another 20bp in the long run due to the increased weighted of franchisees.

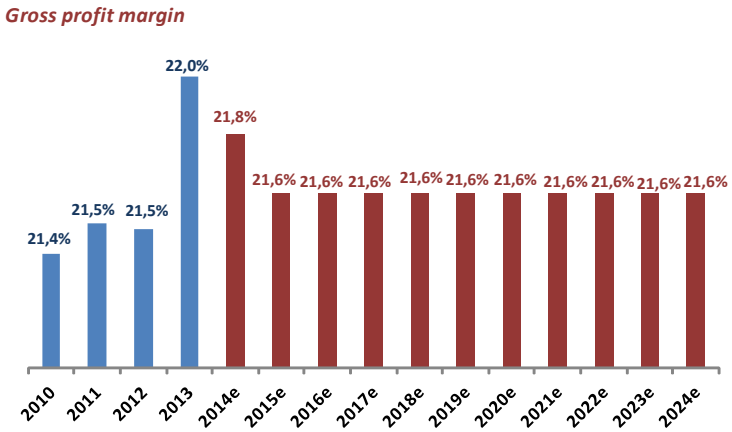


Exhibit 26: Gross profit margin evolution. Source: Company data and own estimations

Furthermore, there is no information decomposing Iberia's and emerging markets gross profit for which it was assumed to be equal in both regions.

5.3. Operating expenses (Opex)

As a low cost operator, DIA is constantly looking to "cut fat" out of the company. As result operating expenses decreased 100bp from 2010 to 2012. Although in 2013 the operating expenses, as percentage of sales, increased from 15,1% to 15,5%, this was due to lower sales per store and per square meter, not from an increase in costs. Moreover, it is important to take into account that the main operating costs are **personnel costs**, **rents**, **logistics** and **utilities**,

which are, at least in the short term, fixed assets. This way it is very important to generate sales and dilute these high fixed costs.

Furthermore, the cost improvement DIA has been able to attain was not only due to efficiency improvements but also from the highest share of franchise operation which, as it was exemplified in section 4.5., reduces DIA's costs and result in higher EBIT margins. DIA has been able to reduce other operating costs, including utilities and logistics which are included on the item "other operating expenses". Moreover, during the first nine months of 2014, operating costs decreased from 15,8% to 14,7% mainly due to DIA France operation considered as discontinued **(See appendix IX).**

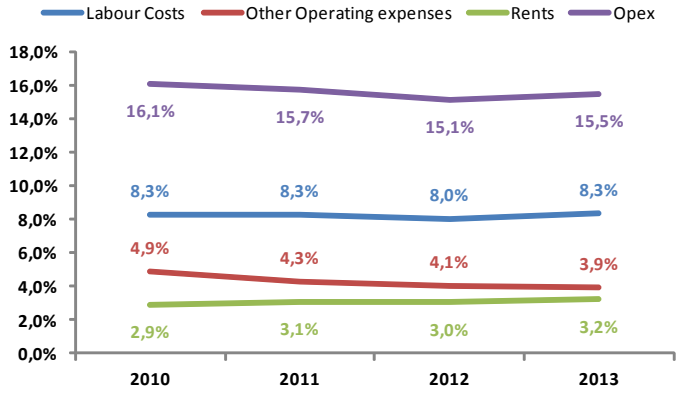


Exhibit 27: Opex evolution. Source: Company data and own estimations

In Iberia EBITDA margins have been increasing consistently from 7,6% in 2010 to 9,6% in 2013. This was due to the above mentioned aspects: increasing contribution of franchise stores and operating efficiencies. For the future, the margin is expected to maintain since both franchise expansion and efficiencies are getting to a limit[64].

In contrast, it is expected slow margin expansion in emerging markets, hence stores get to maturity and DIA reaches critical volumes on those countries, as a contrary effect the fast rate of expansion might slowdown the margin expansion[65].

Regarding the new businesses, Clarel is expected to have a margin of 10% in the long run. El Árbol is expected to have a negative impact on 2015 EBITDA of -2%, reach breakeven in 2017 and gradually improve until the reaches DIA's original stores margin. Finally Eroski, in contrast with El Árbol, is expected to have an accretive impact of 3% in 2015 and gradually converge to original Iberia's store margin.

[64] The company cannot have only franchise stores because it would risk losing control over the operations. In addition, stores located in large cities will strategically be owned by the company since typically, franchise synergies in these locations are lower.
[65] Expansion deteriorates the margin since stores have lower margins during the first years of operation.

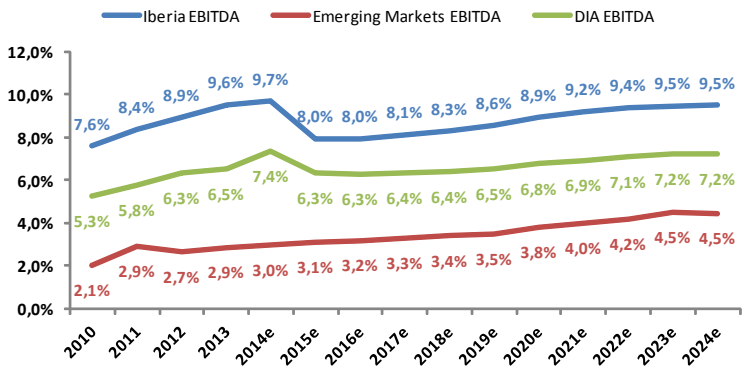


Exhibit 28: EBITDA evolution. Source: Company data and own estimations

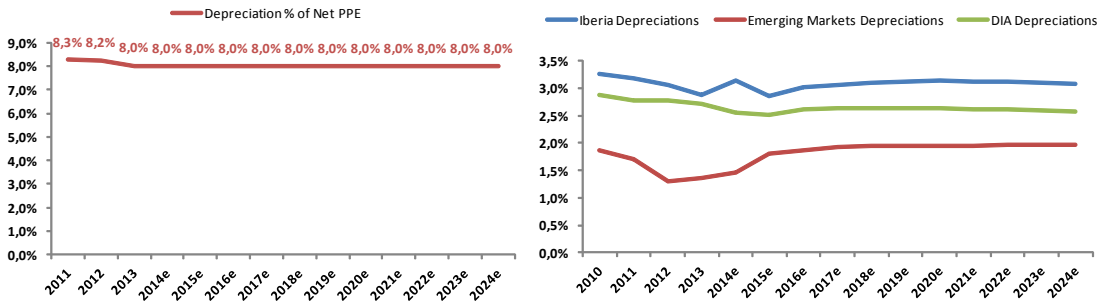
5.4. Capital expenditures (Capex) and depreciations

Food retail is a capital intensive business hence capital expenditures are indispensable for growth and are a function of **acquisitions**, **store opening** and **remodeling programs**.

Regarding acquisitions, DIA closed two deals: one of €125 million to be paid in 2014, related to El Árbol's acquisition, and another of €146 million in 2015, related to Eroski stores acquisition. Moreover, DIA has an aggressive expansion plan for Clarel and in emerging countries with double digit growth rates during the next years which are then expected to ease.

In Iberia the majority of the CAPEX is estimated to be allocated for remodeling as the market becomes saturated and stores need refurbishment to maintain company's standards. Furthermore, remodeling is essential to adapt stores to new purchasing habits and consequently maintain or even increase sales in the future. According to the company, the annual capex for the next years should be around €350 million.

Depreciations are computed as a percentage of previous year gross property plant and equipment (PPE) using the depreciation rate of 2013 (8%).



Exhibits 29 and 30: Depreciations evolution. Source: Company data and own estimations

Furthermore, the PPE is computed using the following formula:

$$PPE\ (t) = PPE\ (t-1) + Capex\ (t) - Depreciations(t)$$[66]

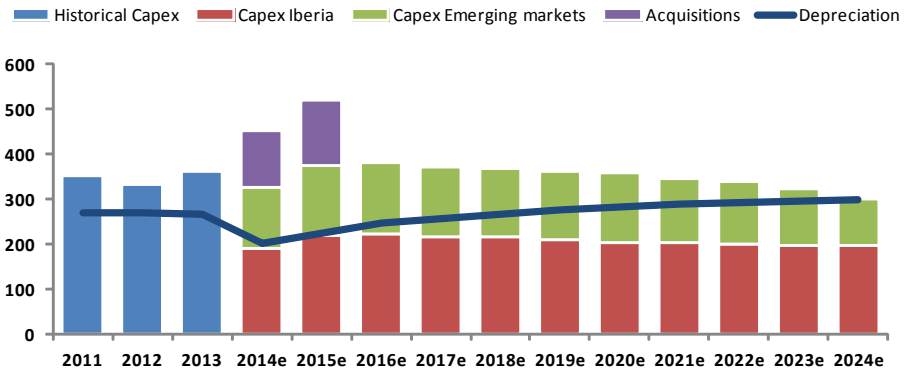


Exhibit 31: Capital expenditures evolution. Source: Company data and own estimations

The exponential increase in Iberia's capex in 2014 and 2015 is due to the acquisition of El Árbol and Eroski stores **(See appendix X)**. It is also important to note that the investment needed in Emerging markets per square meter is lower than in Iberia which results in a high growth of stores with a relatively low investment.

In the long run the CAPEX should be used as replacement investment on assets in order to keep store's minimum standards. For this reason in the long run capex will be equal to the level of depreciations and growth should be driven only by same stores sales.

5.4. Goodwill

The author assumed that the above mentioned transactions will not generate any goodwill and the value paid is equal to the book value of the property plant and equipment. Furthermore the Goodwill is expected to decrease by €146 million due to the sale of DIA France and to be stable thereafter.

5.5. Net Working Capital

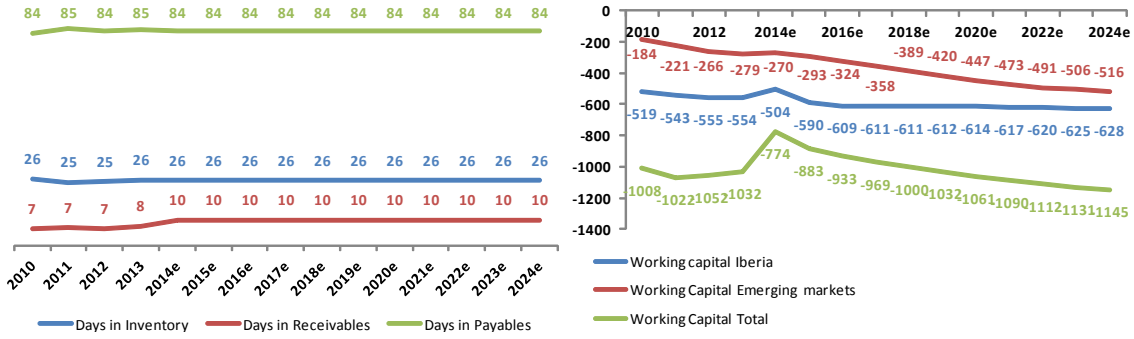
The net working capital is function of three variables: the days in payables (DPO)[67], the days in receivables (DSO)[68] and the days in inventory (DIO)[69]. In contrast with the majority of the other industries, net working capital has a positive effect on the food retail business. This is due to the industry's main characteristics: long payable conditions and sales in cash. This way the retailer is usually able to receive the money from the sale of a product before it pays the supplier's bill.

[66] It was assumed that the company sells totally depreciated assets every year on the amount of current year's depreciation.
[67] Trade Payables/Cost of Goods Sold ×365
[68] Trade Receivables/Net Sales ×365
[69] Inventory/Cost of Goods Sold ×365

Moreover, with the abovementioned variables constant, the net working capital becomes a **function of the level of sales**. This way sales growth will have a positive impact in net working capital, increasing the value of the company, and vice versa. Therefore, the sale of the DIA France will have a negative impact on working capital needs while the acquisition of El Árbol and Eroski will generate the opposite effect.

Furthermore, despite of cash sales both from the end user and the franchisees DIA gives credit for the franchisee's start up costs, and that is way receivables are small but positive.

DIA has been able to keep its trading conditions virtually stable and the days in payables and days in inventory were calculated as an average from the last four years of operation. Since receivables are a function of franchise stores this item was adjusted to DIA France exit with data from DIA's third quarter release, which explains the increase of the DIO from8 to 10 days. In the long run, it is expected the franchise sales to follow the same pattern as the groups sales and therefore the DIO ratio will be stable.



Exhibits 32 and 33: Working capital evolution. Source: Company data and own estimations

Due to the lack of information the author assumed that the working capital conditions are the same for both segments.

5.6. Debt, cash and interest payments

Regarding debt, DIA issued a €500 million Euro bond last July with a fixed coupon of 1,5% and a maturity of five years. Moreover, it raised a syndicate loan amounting €400 million for a term of five years. These two funding sources were used to repay old debt and finance DIA's operations. Moreover, Moody's and Standard & Poor's have assigned to DIA a long-term corporate rating of Baa3 and BBB-, respectively, with a stable outlook. The credit ratings were used in order to calculate DIA's spread over the risk free, resulting in an interest rate of 2,3%.

Debt was computed using the cash flows generated by the company. Furthermore, the company has a target net debt[70] to EBITDA ratio between 0,9 times to 1,1 times. However, in 2014 it is expected net debt to be temporarily below the lower target because of the proceeds from DIA France, and temporally above target in 2015 due to the payment of Eroski's acquisition.

Moreover, as DIA becomes a "cash cow" and generates substantial operating cash flow, it will accumulate cash and according to the model the net debt will be below target in 2019 onwards. However, since cash excess cash accumulated on the balance sheet don't create value and the company as a target net debt to EBITDA it might be expected that DIA will adjust its debt level. Consequently the author believes that the company might return its excess cash to shareholders in form of extraordinary dividends or share buyback. Moreover the company has on its historical accounts the distribution of extraordinary dividends in 2010 and 2011 amounting €369 million and €532 million, respectively.

Furthermore interests are compute using the following formula

$$\text{Interests (t)} = \text{Gross Debt (t} - 1) \times \text{Interest Rate}^{71}$$

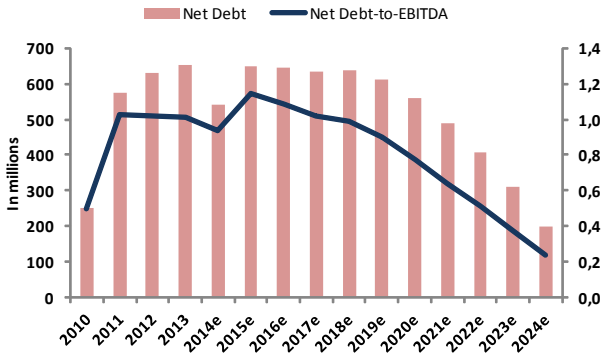


Exhibit 34: Net debt. Source: Company data and own estimations

Note: it was assumed that the company will use debt sources to repay the current debt.

5.7. Equity

Equity was calculated using the following formula:

$$\text{Equity (period t)} = \text{Equity (period t} - 1) + \text{Net Profit (period t)} - \text{Dividends paid(period t)}$$

DIA distributes, by policy, between 45% and 50% of its underlying net profit. Moreover, as the company is expected to generate substantial amount of operating cash, the author assumed

[70] Net Debt = Gross Debt – Cash and Cash Equivalents

[71] It was assumed that, since the company as a target net debt to EBITDA, the risk of the company to cover its obligations won't change significantly and the interest rate would be constant.

that the company will distribute 75% of its underlying net profit as dividends from 2017 onwards.

$$\text{Underlying Net Profit} = \text{Net Profit} - \text{Non recurring items} - \text{Other financials} - \text{Discontinued Operations}$$

5.8. Other items

"Associated companies" were related with DIA France and are estimated to be zero after its disposal.

"Discontinued operations" are related to DIA France and are expected to be zero from 2015 onwards.

"Minority interests" were related with DIA Turkey which as the transaction is complete this item it is expected to be zero.

5.9. Scenarios

In order to incorporate additional macroeconomic risks, several scenarios were idealized and the impact was estimated. This way the author not only incorporated macroeconomic risks in the valuation but also provides valuable information on how the firm might be affected to external factors.

5.9.1. Deflation in Iberia

In 2014, Iberia witnessed deflation, particularly in food items, reaching -1,7% in Spain and -2,8% in Portugal, on the third quarter. The expected economical recovery might have a positive impact on consumption, and inflation is anticipated to gradually recover to target levels, around 1,5%. However, Europe is expected to witness low levels of growth and projections have been revised downwards by analysts and government institutions. This way, it is possible that Europe, and Iberia in particular, would take more than expected to recover and deflation could be a reality on the coming years.

To summarize, in this scenario sales would decrease substantially, pressuring margins down, capex is the same, since openings are reduced and the remodeling and substitution investment is still necessary, and working capital will be negatively affected by diminished sales.

Finally, after two years of deep deflation the scenario foresees a gradual convergence to the base scenario in the long run. The author considered the probability of a deflationary scenario of 25% which is in line with the international authorities estimates **(See appendix XI).**

5.9.2. Hyperinflation and recession in emerging markets

Emerging countries are good sources of growth and opportunities however they also carry substantially more uncertainty and risk. In this environment the economy is very volatile and the risk of a slowdown is always present.

Currently, inflation in Argentina is very high and risk of hyperinflation[72] is present, in Brazil inflation is higher than the government's target, but relatively low comparing to Argentina. In contrast, China has low sustainable inflation. Furthermore, Brazil faced negative GDP growth on the first two quarters of 2014. Regarding Argentina, the IMF alerted that data published by the government may not be reliable and private institutions estimate real GDP growth to be negative in the short run.

Taking into account this adverse macroeconomic environment the scenario projects a deterioration of the economic indicators. Consequently, it is estimated a similar trend for the Argentinean economy as it happened during the 2002 crisis. This way inflation would increase above 40% during the next 18 months. Moreover GDP would decrease and the Argentinean Peso would sharply devaluate. Furthermore the impact on the other geographies is expected to be softer as risks are lower. Brazil would expect inflation around 15% and slightly negative GDP and china around 7% with decelerated growth.

The effects would be: **very high LFL** due to hyperinflation, **negative real growth** and **exponential devaluation of the currency** as the risk of the countries sharply increase and its financial health deteriorates. Moreover, **margins would decrease** because the company would not be able to completely charge the inflation to clients and the company would **delay some of its investment** resulting in lower capex and openings.

Finally, the author considered a probability of 50% for this scenario since the macroeconomic context in the countries analyzed is blurred and volatile and the risks of hyperinflation and recession are present in the current environment.

Scenario	Deflation	Hyperinflation and Recession
LFL	--	++
Expansion	=	-
Exchange rate	n.a.	--
Sales	-	-
EBITDA	-	-
Capex	=	-
Working Capital	-	-
Sales per store	-	-

Exhibit 35: Summary of the alternative scenarios. Source: Own estimations

[72] Hyperinflation corresponds to periods of extremely high inflation levels

6. The Valuation

In this section, the results from the valuation approaches are presented and a sensitivity analysis is performed.

6.1. Discount cash flow model

The author decided to use the sum of parts approach dividing DIA's operations in two segments: **Iberia**, comprising Portugal and Spain; and **Emerging markets**, including Argentina, Brazil and China. Furthermore, weighed scenarios where used to incorporate additional risk.

6.1.1. The discount factor

The discount factor used was based on the current market conditions, the return demanded by an international investor, DIA's historical capital ratio and tax expectations. This way the return on equity computed was 6,9%, the cost of debt 2,3% and the equity ratio assumed to be 80% resulting in a **weighted average cost of capital of 5,8% (See appendix XII)**.

6.1.2. The model

Taking into account all the operational assumptions and the macroeconomic scenarios, Iberia is estimated to value €4.521 million while Emerging markets have an enterprise value of €1.086 million for a total value of €5.607 million.

Furthermore, it was used an **explicit period of 10 years** in order to provide detailed forecasts until DIA's operations reach maturity. To compute the terminal value a growth rate of 0,6% was used for Iberia and 2,0% for emerging markets, both reflecting the expected long term like-for-like growth **(See the estimated balance sheet, income statement and cash flow statement in XIII and the impact of DIA France in appendix XIV).**

Base Scenario											
				Probability:	75%						
Iberia	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	Prepertuity
EBIT*(1-Tax)	219	227	235	241	253	269	283	294	301	305	
Less: Capex	366	221	216	216	210	204	202	200	195	196	
Plus: D&A	170	186	188	191	193	194	195	195	196	196	
Less: NWC	-86	-19	-2	0	-1	-2	-3	-3	-4	-4	
FCFF	108	211	210	216	237	260	279	293	306	309	5 947
Discount factor	1,06	1,12	1,19	1,25	1,33	1,40	1,49	1,57	1,66	1,76	1,76
Disounted cash flow	102	188	178	172	178	185	188	186	184	175	3 377

Exhibit 36: Iberia base scenario forecasts. Source: Own estimations

Deflationary Scenario											
				Probability:		25%					
Iberia	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	Prepertuity
EBIT*(1-Tax)	122	85	86	89	108	133	145	169	181	186	
Less: Capex	366	221	216	216	210	204	202	200	195	196	
Plus: D&A	170	186	188	191	193	194	195	195	196	196	
Less: NWC	-77	29	16	8	3	1	0	-1	-2	-3	
FCFF	3	21	43	56	87	122	138	166	184	189	3 648
Discount factor	1,06	1,12	1,19	1,25	1,33	1,40	1,49	1,57	1,66	1,76	1,76
Disounted cash flow	3	19	36	44	66	87	93	105	110	108	2 071

Exhibit 37: Iberia deflationary scenario forecasts. Source: Own estimations

Base Scenario											
				Probability:		50%					
Emerging Markets	2015e	2016e	2017e	2018e	2019e	2020e	2020e	2020e	2020e	2020e	Prepertuity
EBIT*(1-Tax)	26	29	33	38	44	56	65	74	87	87	
Less: Capex	154	160	155	153	152	153	143	139	128	103	
Plus: D&A	53	61	69	76	82	88	93	97	100	103	
Less: NWC	-23	-31	-34	-32	-30	-27	-26	-19	-15	-10	
FCFF	-52	-39	-19	-7	4	17	41	52	74	97	2 589
Discount factor	1,06	1,12	1,19	1,25	1,33	1,40	1,49	1,57	1,66	1,76	1,76
Disounted cash flow	-49	-34	-16	-6	3	12	28	33	45	55	1 470

Exhibit 38: Emerging markets base scenario forecasts. Source: Own estimations

Hyperinflation and Recession Scenario											
					Probability:	50%					
Emerging Markets	2015e	2016e	2017e	2018e	2019e	2020e	2020e	2020e	2020e	2020e	Prepertuity
EBIT*(1-Tax)	7	4	8	13	18	20	26	32	41	47	
Less: Capex	125	125	137	152	156	141	130	124	120	96	
Plus: D&A	53	59	64	70	77	83	88	91	94	96	
Less: NWC	6	5	-12	-24	-27	-20	-17	-13	-11	-8	
FCFF	-71	-67	-52	-45	-34	-18	0	13	26	54	1 447
Discount factor	1,06	1,12	1,19	1,25	1,33	1,40	1,49	1,57	1,66	1,76	1,76
Disounted cash flow	-67	-60	-44	-36	-26	-13	0	8	16	31	822

Exhibit 39: Emerging markets hyperinflation scenario forecasts. Source: Own estimations

Iberia	
Perpetual Growth	0,6%
Wacc	5,8%
100% Enterprise Value	**4 521**
75% Base Scenario	5 114
25% Deflationary Scenario	2 742
# Shares	645
100% Price	**7,00**
75% Base Scenario	7,92
25% Deflationary Scenario	4,25

Emerging Markets	
Perpetual Growth	2,0%
Wacc	5,8%
100% Enterprise Value	**1 086**
50% Base Scenario	1 541
50% Hyperinflation Scenario	631
# Shares	645
100% Price	**1,68**
50% Base Scenario	2,39
50% Hyperinflation Scenario	0,98

Exhibits 40 and 41: Summary of the valuation output. Source: Own estimations

Non equity claims and adjustments

As explained during the literature review to get the equity value the non equity claims must be subtracted from the enterprise value. This way the net debt amounts €543 million and provisions[73] €61 million.

Furthermore, the company considers some costs related to the remodeling processes[74] as non-recurring. However, since it is related to operations and the costs are predicted to be incurred

[73] "Provisions" are related with the employee long term benefit plan and tax contingencies.
[74] For example, costs of closing the store while the remodeling process takes place.

while remodeling processes are in place, the author considered these costs on the valuation until 2017, when current remodeling programs are expected to be finalized. Moreover, although it is expected remodeling programs after 2017[75], since the benefits from those operations are not incorporated on the valuation, these costs are considered to be as zero from 2018 onwards. Finally, these costs are expected to have a €99 million impact on the valuation.

Share price

Finally to get the price per share the equity value was divided by 645 million shares outstanding. **The final share price of €7,60 Euros** implies a 36% potential upside and consequently a **Buy recommendation**.

Enterprise Value Iberia	4 521
Enterprise Value Emerging Markets	1 086
Total Enterprise Value	5 607
Non-recurring Items	-99
Net Debt	-543
Provisions	-61
Equity	4 904
# Shares	645
Target Price	7,60

Price at December 31, 2014	5,6
Potential Upside	36%
Rating	Buy

Exhibit 42: Summary of the valuation output. Source: Own estimations

6.2. Sensitivity analysis

In order to stress test the model three sensitivity analyses were made.

Firstly, the WACC was stress tested and the author concluded that the model is extremely sensitive to changes in this variable. A 100bp reduction on the discount rate would lead to an increase on the share price of 37% while a decrease on the same amount would make the share price drop by 22% to €5,89. Moreover, the value of the company is more sensitive with declining discount rate than with increases.

	WACC						
Wacc	**4,3%**	**4,8%**	**5,3%**	**5,8%**	**6,3%**	**6,8%**	**7,3%**
Price (€)	12,44	10,38	8,85	7,60	6,69	5,89	5,23
Impact	64%	37%	16%	0,0%	-12%	-22%	-31%

Exhibit 43: Sensitivity test - WACC. Source: Own estimations

Secondly, since the terminal value accounts for 74,8% of the total enterprise value it is important to run a sensitivity analysis on the terminal growth. For this purpose, a double entry

[75] During the third quarter conference call, the company stated that is studying a remodeling program regarding the Maxi stores.

table was built to analyze the impact of both the emerging market and Iberia segments. It can be concluded that, as it was expected, Iberia has a greater impact than emerging market. Furthermore, although the impact of the terminal growth is smoother than the impact of WACC, a decrease of 60bp on Iberia's growth combined with a decrease of 100bp in emerging markets would make the share price drop 11,7% to €6,71.

		Terminal growth Iberia			
Terminal growth EM	1,0%	6,71	7,21	7,63	8,25
	1,5%	6,87	7,38	7,80	8,42
	2,0%	7,08	7,60	8,01	8,63
	2,5%	7,36	7,88	8,29	8,91
	3,0%	7,74	8,25	8,66	9,29

Exhibit 44: Sensitivity test – terminal growth. Source: Own estimations

Thirdly, a sensitivity test on the margins was also made and it can be concluded that the valuation is significantly affected by this variable. Therefore, it is extremely important to be able to manage an efficient store network.

EBITDA Margins					
EBITDA margin change	-1,0 pp	-0,5 pp	0,0 pp	0,5 pp	1,0 pp
Price (€)	5,32	6,46	7,60	8,74	9,88
Impact	-30%	-15%	0%	15%	30%

Exhibit 45: Sensitivity test – EBITDA margins. Source: Own estimations[76]

To conclude, the model is sensible to discount rate, terminal value growth and margin changes. Therefore, it is extremely important to understand the market and its involving variables in order to make accurate estimations. A small change in the assumptions have a exponential impact on the valuation.

6.3. Multiples

To build the peer group Bloomberg's food retail players were used as a starting point from which three filters were taken into account: **geographical presence** in both, developed countries and emerging markets, particularly in Latin America; **store format** focused on convenience discount; and **similar fundamentals** such as EBITDA margins, return on invested capital (ROIC), long term earnings per share growth, capital structure, and historical growth rates. This way the author benchmarked food retailers with seven indicators in order to find a reasonable peer group **(See appendix XV).**

A peer group of 9 companies was then constructed from which 5 companies were excluded: Magnit and O'key because they only operate in Russia; Tesco because of the recently accounting fraud; and Casino Group and Companhia Brasileira de Distribuição because

[76] pp = percentage points.

almost 50% of their operations are related to other activities rather than food retail. At the end, a final peer group of 4 companies was used to benchmark DIA.

	Market Cap (€ Million)	P/E 2014	P/E 2015	EV/EBITDA 2014	EV/EBITDA 2015	EV/EBIT 2014	EV/EBIT 2015
Ahold	13 107	16,5	14,5	7,1	6,8	12,0	11,4
Jerónimo Martins	5 185	15,6	15,3	8,0	7,7	12,7	12,6
Colruyt	6 020	17,0	16,5	8,3	8,2	11,6	11,7
Carrefour	18 428	16,4	14,2	6,9	6,4	11,0	10,2
Harmonic Average	8 171	16,3	15,1	7,5	7,2	11,8	11,4
DIA	3 724	14,8	14,5	8,0	7,9	12,3	12,6
DIA's implied share price (€)		6,27	5,65	5,84	5,44	5,99	5,17
Average (€)				5,73			

Exhibit 46: Peer group. Source: Own estimations

The following conclusions can be taken from the multiple analyses: firstly, price earnings multiples, suggest that DIA is trading at a small discount over its peers while EV/EBIT and EV/EBITDA multiples suggest the contrary; secondly, it would be normal that, in a growing company, the 2015 multiples to be lower than the 2014[77], however DIA's 2014 and 2015 multiples are quite similar which suggest that the profitability margins, in absolute values, won't increase in 2015. This is due to the acquisition of both the Eroski stores, which are expected to have lower margins in the short term, and El Árbol which is expected to have a negative impact on the EBITDA. Since this impact is temporary, and margins from the stores acquired are expected to improve with the implementation of DIA's efficient model, the author considers that 2015 multiples may be distorted and should not be taken into account for valuation purposes; thirdly, the multiples suggest that DIA is fairly priced in the market since the average share price is €5,73 and the company was traded at €5,68 in December 30, 2014. However, if only 2014 multiples were taken into account, multiples may suggest that DIA is slightly undervalued, €6,06 *vs* €5,68.

Furthermore, the DCF model outputs a significantly higher valuation than the multiple analyses. This suggests that the market may be bearish on the stock or bearish in the food retail market as a whole. By analyzing the food retail index[78] performance since January 2008, it reached a seven year minimum on October 24, 2014[79] **(See appendix XVI)**. Moreover, the author is more optimistic than the market, regarding the food retail market and expects the recovery of the European economy and inflation levels to fuel retailers. Regarding DIA, the author believes it should be traded at a premium comparing to its European peers based on its impeccable margin's track record and efficient operation. In accordance, the

[77] In a growing company it is expected that the denominator (earnings, EBIT and EBITDA) to increase year on year which, by having the same nominator, the future multiples should be considerably smaller than current ones.
[78] Bloomberg ticket: BEFOODR.
[79] Note: the author used weekly frequency.

analysts' consensus suggests an appreciation of DIA's stock and rates it as a buy opportunity, above its European peers **(See appendix XVII)**.

Valuation drawbacks

It is important to note that **there is no perfect peer group** and from the initial group of 22 companies only four were chosen as similar. Furthermore, from the seven indicators the author used to benchmark the peer group, only one company had more than four similar characteristics.

7. Comparison with Morgan Stanley

In order to compare this paper's results with a leading investment bank report, a research note from Morgan Stanley published on November 12, 2014, was chosen.

This report was chosen because: firstly, Morgan Stanley is a **global leader in the investment banking** industry; secondly, as it was published on November 12, it i**ncludes the third quarter results and the acquisition of 160 Eroski stores**; thirdly, the research note has an **explicit period of nine years** (*vs* ten years on the thesis); lastly it provides **detailed information regarding the forecasts** including the discrimination between Iberia and emerging markets.

Furthermore, Morgan Stanley established a target price per share of €5,6 and a consequent **equal-weight recommendation**[80]. The share price on November 11,2014, was €5,21.

7.1. Valuation methodology

The first significant difference between the two research notes rise from the methodology used. Although, both used the discount cash flow and the weighted average cost of capital as the discount factor, the author incorporated the risk on the cash flows, with weighted scenarios, while Morgan Stanley's analyst used the discount factor. Therefore, the discount rates are significantly different. The main difference is the risk free rate estimation (0,7% *vs* 5%). The author found no reason why Morgan Stanley's risk free rate estimation is so high once the currency used is Euros, the 10 year German Bund is below 1% and the 10 year Spanish government bonds are around 2%.

[80] An equal-weight recommendation corresponds to an Hold recommendation and suggests the price in the market is close to the fair value of the company taking into account current information and macroeconomic environment expectations.

	Thesis	Morgan Stanley	Variation
Cost of equity	6,9%	8,6%	***-1,7 pp***
Risk Free	0,7%	5,0%	***-4,3 pp***
Beta	1,1	0,9	***0,2***
Market risk premium	5,5%	4,0%	***1,5 pp***
Wacc	5,8%	8,0%	***-2,2 pp***

Exhibit 47: WACC comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

7.2. Main assumptions

The main cash flow assumptions differ significantly between the investment bank and the thesis.

	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e
Sales									
Thesis	8 718	8 909	9 120	9 379	9 666	9 913	10 153	10 344	10 514
Morgan Stanley	8 939	9 465	9 982	10 584	11 193	11 804	12 414	13 021	13 620
Variation	***-2,5%***	***-5,9%***	***-8,6%***	***-11,4%***	***-13,6%***	***-16,0%***	***-18,2%***	***-20,6%***	***-22,8%***
EBIT									
Thesis	295	280	295	309	336	370	400	430	456
Margin	**3,4%**	**3,1%**	**3,2%**	**3,3%**	**3,5%**	**3,7%**	**3,9%**	**4,2%**	**4,3%**
Morgan Stanley	383	399	406	401	420	438	456	474	490
Margin	**4,3%**	**4,2%**	**4,1%**	**3,8%**	**3,8%**	**3,7%**	**3,7%**	**3,6%**	**3,6%**
Variation	***-0,9 pp***	***-1,1 pp***	***-0,8 pp***	***-0,5 pp***	***-0,3 pp***	***0,0 pp***	***0,3 pp***	***0,5 pp***	***0,7 pp***
Depreciation									
Thesis	223	246	255	264	272	279	285	289	293
Morgan Stanley	204	216	228	242	268	300	334	372	412
Variation	***9,4%***	***13,8%***	***11,9%***	***9,0%***	***1,5%***	***-6,9%***	***-14,6%***	***-22,2%***	***-28,9%***
Change in WC									
Thesis	92	20	21	26	28	24	24	19	17
Morgan Stanley	57	40	38	48	50	53	56	59	61
Variation	***60,9%***	***-50,3%***	***-45,2%***	***-46,5%***	***-43,0%***	***-53,9%***	***-57,4%***	***-68,0%***	***-72,3%***
CAPEX									
Thesis	360	364	362	368	364	352	339	331	319
Morgan Stanley	380	410	443	479	474	468	461	453	444
Variation	***-5,4%***	***-11,3%***	***-18,4%***	***-23,1%***	***-23,2%***	***-24,9%***	***-26,5%***	***-26,8%***	***-28,1%***
Asset Disposals/Acquisitions									
Thesis	-146								
Morgan Stanley	-160								
Variation									
Free cash flow									
Thesis	20	110	133	150	185	226	265	293	325
Morgan Stanley	-7	129	111	111	157	209	263	321	383
Variation	***-392,5%***	***-14,5%***	***20,1%***	***35,0%***	***17,5%***	***7,9%***	***0,6%***	***-8,7%***	***-15,0%***
Free cash flow discounted									
Thesis	19	98	112	119	139	161	178	186	196
Morgan Stanley	-6	110	88	82	107	132	154	174	192
Variation	***-422,6%***	***-10,5%***	***27,8%***	***45,7%***	***29,9%***	***21,7%***	***15,6%***	***7,1%***	***1,9%***

Exhibit 48: Main assumptions comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report[81]

Regarding sales, thesis' assumptions were considerably more conservative than the investment banker, especially in Iberia. In the author's view, DIA's operations in Iberia are reaching maturity and the store network is already extremely dense. Therefore it estimated that, after the integration of El Árbol and Eroski stores, the company will ease store openings

[81] The numbers presented on the thesis line correspond to the weighted scenario.

and grow at the LFL levels. Therefore the author did not find any reason for sales in Iberia to grow at around 4%.

	2015e	2016e	2017e	2018e
Sales Iberia				
Thesis	5 953	6 142	6 166	6 165
Morgan Stanley	6 075	6 396	6 642	6 901
Variation	***-2,0%***	***-4,0%***	***-7,2%***	***-10,7%***

Exhibit 49: Sales Iberia comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

In emerging markets, although sales forecasts are similar, the analyst foresees a greater amount of openings which result in a sharp decrease in sales per square meter[82]**.** In the author's opinion lower sales per square meter are understandable hence the macroeconomic environment is not favorable, however it considers the values to be undervalued by the investment bank.

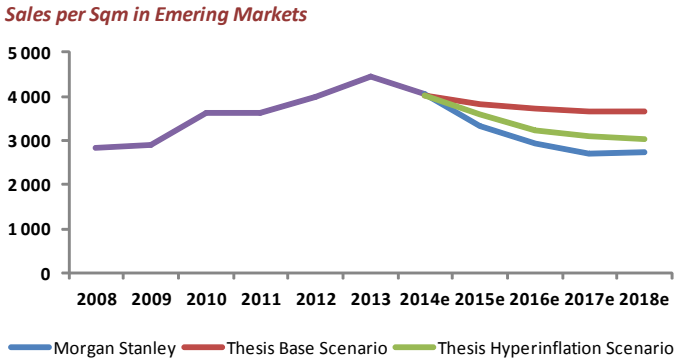


Exhibit 50: Emerging markets sales per sqm comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

In order to support the sales increase, Morgan Stanley analyst estimated significantly **higher capital expenditures**. However, according with the company capex is expect to stand around €350 million. Therefore the author did not agree with the extremely high investment forecasted by the investment bank.

	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e
CAPEX									
Thesis	360	364	362	368	364	352	339	331	319
Morgan Stanley	380	410	443	479	474	468	461	453	444
Variation	***-5,4%***	***-11,3%***	***-18,4%***	***-23,1%***	***-23,2%***	***-24,9%***	***-26,5%***	***-26,8%***	***-28,1%***

Exhibit 51: Capex comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

Moreover, despite of higher capex, **depreciations are lower** on the analyst model during the first 6 years of the explicit period. After which depreciations become exponentially higher. This is due to a lower depreciation rate, which delays depreciations from the new investments.

[82] The author was not able to compute Morgan Stanley's Iberia sales per square meter due to lack of information.

The author could not find any reason for this, since the depreciation rate has been quite stable around 8% of gross property plant and equipment.

	2014e	2015e	2016e	2017e	2018e
Thesis base scenario PPE	2 789	3 086	3 220	3 334	3 436
Depreciation	200	223	247	258	267
% Depreciation/PPE(T-1)		**8,0%**	**8,0%**	**8,0%**	**8,0%**
Thesis weighted scenario PPE	2 789	3 072	3 190	3 296	3 401
Depreciation	200	223	246	255	264
% Depreciation/PPE(T-1)		**8,0%**	**8,0%**	**8,0%**	**8,0%**
Morgan Stanley PPE	3 310	3 850	4 260	4 703	5 182
Depreciation	187	204	216	228	242
% Depreciation/PPE(T-1)		**6,2%**	**5,6%**	**5,4%**	**5,1%**

Exhibit 52: Depreciations comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

Regarding **EBITDA margin evolution**, Morgan Stanley analyst forecasts a 230bp decrease in Iberia's margin while the thesis' base scenario assumes a slightly decrease (20bp) from 9,8% to 9,6% on DIA's original stores in Spain[83]. On the deflationary scenario the author forecasted a margin decrease of 280bp in 2016 and a gradual recovery until it reaches the long term margin. Therefore the weighted scenario incorporates only a slight decrease in margin.

DIA has been able to increase its margins despite the deflationary pressure. The analyst's argument to support the sharp decrease in margins is based on the fact that DIA's current margin increase with negative "like-for-like" evolution is not sustainable. However, the company explains the margin increase with its historical success in reducing their cost base through efficiency gains and the increasing share of franchise. In addition, it is important to note that DIA has little exposure to typically margin dilutive categories such as fuel and tobacco, for which the current margins might not be as high as some analysts argue. To conclude, the author believes that the deflationary pressure will ease with the economical recovery and therefore the company will be able to maintain current margins in the future.

Moreover, both reports estimate a gradual increase on the emerging markets margin. It is also important to note that Iberia margins will be negatively impacted by the acquisitions of El Árbol and Eroski which fully explains thesis' 2015 margin decrease.

	2015e	2016e	2017e	2018e
EBITDA Iberia	**2015e**	**2016e**	**2017e**	**2018e**
Thesis (Base Scenario)	474	489	502	512
Margin	**8,0%**	**8,0%**	**8,1%**	**8,3%**
Thesis (weighted Scenario)	440	441	453	461
Margin	**7,5%**	**7,4%**	**7,6%**	**7,8%**
Morgan Stanley	496	511	514	503
Margin	**8,2%**	**8,0%**	**7,7%**	**7,3%**
Variation	***-0,2 pp***	***0,0 pp***	***0,4 pp***	***1,0 pp***

Exhibit 53: EBITDA margin comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

[83] DIA's original stores in Iberia excludes El Árbol and Eroski acquisitions

Furthermore, fueled by the sales boost, the net working capital is expected to have a greater positive effect on the investment bank valuations.

Additionally, the analyst considered an outflow of €160 million due to acquisitions in 2015 while the master student assumed a smaller amount, €146 million.

To summarize, Morgan Stanley's analyst's reduced margins, delayed deprecations and higher investment rate result in a smaller free cash flow from 2017 until 2021 comparing to the thesis. Thereafter the continued increase of sales and the consequent positive affect from the working capital makes the analyst's terminal cash flow significantly higher than the thesis'. Surprisingly, the sum of the explicit period cash flows is similar (Morgan Santley €1.677 *vs* thesis €1.707).

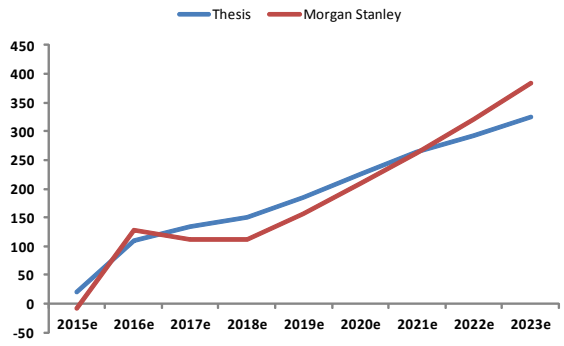


Exhibit 54: Free cash flow comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

Moreover, the implied weighted average cost of capital on the weighted scenario model[84] is 6,5% for Iberia and 7,0% for the emerging markets which is considerably below the 8% considered by the investment bank. In conclusion, Morgan Stanley assumed a higher rate of sales growth in Iberia, a margin decrease in Iberia, a significantly higher investment in capex, on average 20% higher, and a higher discount factor. These factors counterbalanced the higher EV adjustments and the lower terminal growth assumed by the master student. Therefore, the valuation of the investment banker is 35% below from the presented on this report.

€ million	Thesis	Morgan Stanley	Variation
Terminal Value (%)	0,9%	1,8%	*-0,9 pp*
Enterprise Value	5 607	4 230	*32,6%*
EV adjustments	703	614	*14,5%*
Equity Value	4 904	3 616	*35,6%*
Price per Share (€)	7,6	5,6	*35,7%*
Terminal Value	4 196	3153	*33,1%*

Exhibit 63: Share price comparison with Morgan Stanley. Source: Own estimations and Morgan Stanley report

[84] To compute the implied WACC the author used excel's goal seek on the base scenario to access which discount factor would generate the same enterprise value as the weighted scenario.

8. Conclusions

The aim of this dissertation was to establish a fair price for Distribuidora Internacional de Alimentación share and consequently provide an investment recommendation. Taking the goal in consideration, the first step was to carefully study the most important valuation methods and its variables.

The discount cash flow model and the relative valuation were the methods chosen to estimate DIA's value. Furthermore, the sum of parts approach were used to evaluate the company's business segments separately and alternative scenarios were constructed to incorporate macroeconomic risk.

Furthermore, a deep understanding about the food retail market and its macroeconomic drivers was essential to set accurate forecasts.

Taking everything in account, the author came up with a share price of €7,6 which implies a potential upside of 36% from the closing date on December 31, 2014. Therefore a buy recommendation was released.

In addition, the author has the opinion that the market may be bearish regarding food retailers since its index is trading at seven year minimums and inflation in Europe is expected to start recovering in 2015.

Finally, DIA seems to be undervalued in comparison with the market. Its multiples are trading at a small discount. Moreover, the author defends that DIA should be traded at a premium, based on the fact that historically the company has very resilient margins and has a good strategy to keep them in the future. In accordance, the market consensus rate DIA as "buy" stock, above its European competitors.

Appendix

Appendix I: DIA top shareholders

Company	Ownership	Description
Baillie Gifford & CO	8,06%	Global Asset Management
Cervinia Europe	5,01%	Owned by Groupe Arnault - Holding with diversified investments owned by Bernard Arnault
Blue Partners	3,99%	Owned by Colony Capital - Global real estate investment firm
Blackrock	3,01%	Global Asset Management

Note: Data from the end of June 2014

Source: DIA's report

Appendix II: Spread

To compute DIA's spread the author made an average from the two tables below. It was used the credit rating of BBB- and the maturity of five years in accordance with the Euro bond issued by the company.

Corporate bond spreads: basis points over Treasury curve

Rating	1year	2year	3year	5year	7year	10year	30year	Typical Interest Coverage Ratios
Aaa/AAA	40	45	50	60	74	85	96	>8.50
Aa1/AA+	45	55	60	70	84	95	106	6.50-8.50
Aa2/AA	55	60	65	75	89	105	116	6.50-8.50
Aa3/AA-	60	65	70	85	99	117	136	6.50-8.50
A1/A+	70	80	90	105	119	142	159	5.50-6.50
A2/A	80	90	105	120	140	157	179	4.25-5.50
A3/A-	90	100	110	130	150	176	196	3.00-4.25
Baa1/BBB+	105	115	128	145	165	186	208	2.50-3.00
Baa2/BBB	120	130	140	160	180	201	221	2.50-3.00
Baa3/BBB-	140	145	155	172	193	210	232	2.50-3.00
Ba1/BB+	225	250	275	300	325	350	440	2.00-2.50
Ba2/BB	250	275	300	325	350	385	540	2.00-2.50
Ba3/BB-	300	350	375	425	445	460	665	2.00-2.50
B1/B+	375	400	425	500	550	610	765	1.75-2.00
B2/B	450	500	550	625	670	710	890	1.50-1.75
B3/B-	500	550	650	750	875	975	1075	1.25-1.50
Caa/CCC	600	650	800	900	1025	1150	1300	0.80-1.25

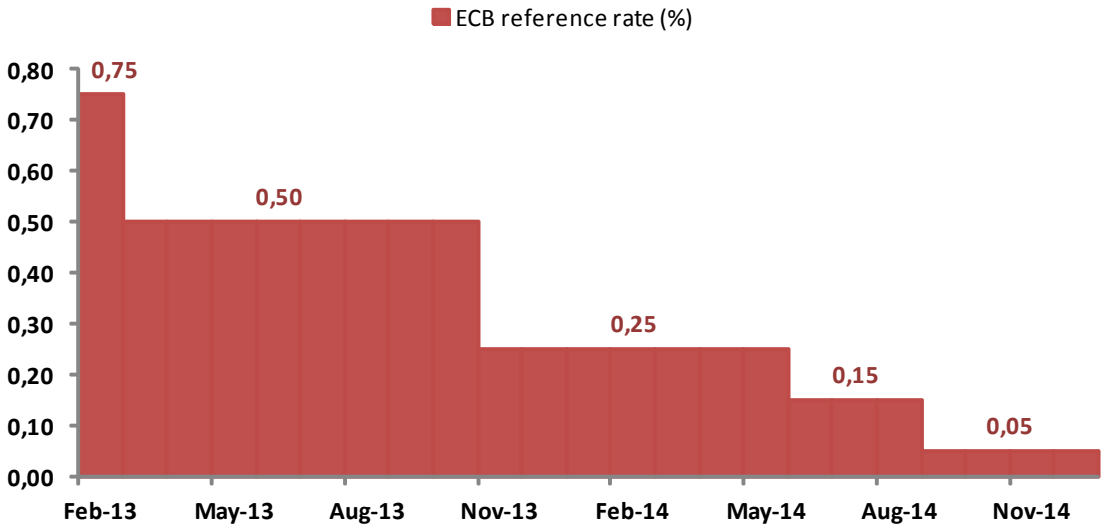
Source: http://giddy.org/db/corpspreads.htm

Reuters Corporate Spreads for Industrials
03/28/2014

Rating	1 yr	2 yr	3 yr	5 yr	7 yr	10 yr	30 yr
Aaa/AAA	5	8	12	18	28	42	65
Aa1/AA+	10	18	25	34	42	54	77
Aa2/AA	14	29	38	50	57	65	89
Aa3/AA-	19	34	43	54	61	69	92
A1/A+	23	39	47	58	65	72	95
A2/A	24	39	49	61	69	77	103
A3/A-	32	49	59	72	80	89	117
Baa1/BBB+	38	61	75	92	103	115	151
Baa2/BBB	47	75	89	107	119	132	170
Baa3/BBB-	83	108	122	140	152	165	204
Ba1/BB+	157	182	198	217	232	248	286
Ba2/BB	231	256	274	295	312	330	367
Ba3/BB-	305	330	350	372	392	413	449
B1/B+	378	404	426	450	472	495	530
B2/B	452	478	502	527	552	578	612
B3/B-	526	552	578	604	632	660	693
Caa/CCC+	600	626	653	682	712	743	775
US Treasury Yield	0.13	0.45	0.93	1.74	2.31	2.73	3.55

Source: http://www.bondsonline.com/Todays_Market/Corporate_Bond_Spreads.php

Appendix III: European Central Bank – Reference rate for interest rates



Source: Global rates

Appendix IV: Macroeconomics

DIA is present in five countries divided in two broad groups: **Iberia**, which includes Portugal and Spain; and **emerging countries**, including Argentina, Brazil and China. Therefore, the aim of this section is to analyze the macroeconomic environment, including the competition, in each country where DIA operates.

Iberia

Iberia is the most important segment for DIA's operations, accounting for 66% of total sales and 86% of EBITDA during the first nine months of 2014. Moreover, Iberia is also the most profitable segment with an EBITDA margin close to 10%.

Spain

Spain is DIA's home and major market. During the first nine months of 2014, the Spanish operation accounted for 86% of Iberia's sales. Therefore, understanding the macroeconomic environment of Spain is essential for DIA's valuation.

Spain is the 5th most populous country in the European Union with around 46,5 million[85] people in 2013. It is also the 5th largest economy in terms of GDP[86], being one of the most important European Union countries.

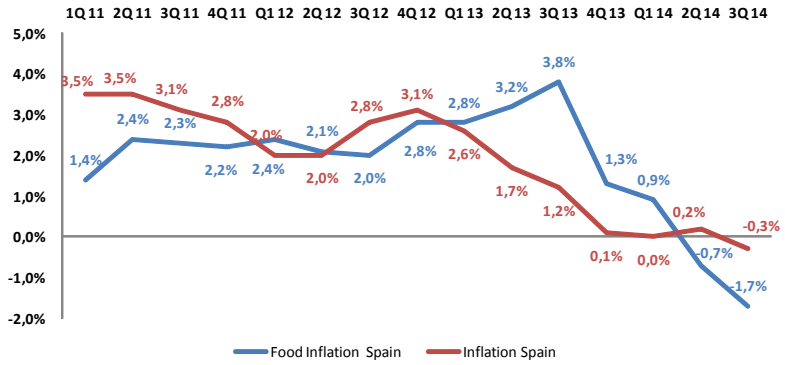
After 2008, Spain suffered the longest recession in decades with its GDP contracting 3,8% in 2009 and unemployment rising from 8,2%, before crisis, to 26,1% in 2013. The austerity measures, including the increase in VAT of basic food products[87], together with the lower income, made clients **become more price sensitive**, pressing retailer's prices down and **avoiding buying large baskets in "one-stop" shopping therefore favoring proximity stores** to buy the weekly or daily groceries. In consequence retail sales growth has been negative since 2009.

	2009	2010	2011	2012	2013
Retail Sales (%)	-5,6	-1,8	-5,8	-7,0	-4,0

Source: Focus economics

Moreover with the reforms regarding labor flexibility, the restructure of the financial sector and the deleveraging of the private sector, the consumer confidence index improved and the GDP and employment started recover in 2013. However, Spain registered very low inflation, including deflation on the food prices index, particularly on fruits and vegetables which have a significance weight on DIA's basket, negatively affecting the food retailer's performance.

[85] Estimations from the IMF, 2013.
[86] GDP = Gross Domestic Product.
[87] The average basket of products VAT increased 25% from 8% to 10% and, in an attempt to maintain volumes, retailers tend assumed the tax burden at the expense of profit margins.



Source: OECD iLibrary

It is also important to note that the GDP growth is driven by a recovery of the private consumption and a positive impact of exports which are dependent on the performance of Europe.

Economic indicators	2007	2008	2009	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e
GDP Real (%)	3,5	0,9	-3,8	-0,2	0,1	-1,6	-1,2	1,3	1,7	1,8	1,8	1,9	2,0
GDP Nominal (%)	6,9	3,3	-3,8	-0,1	0,1	-1,6	-0,6	1,1	2,3	2,8	3,0	3,3	3,4
Inflation (%)	2,8	4,1	-0,2	2,0	3,1	2,4	1,5	0,0	0,6	0,9	1,0	1,3	1,3
Unemployment rate (%)	8,2	11,3	17,9	19,9	21,4	24,8	26,1	24,6	23,5	22,4	21,2	19,9	18,5
Population Growth (%)	2,0	1,7	0,8	0,4	0,4	0,1	-0,3	-0,2	-0,2	-0,2	-0,2	-0,3	-0,3
Government Debt (% of GDP)	36,3	40,2	54,0	61,7	70,5	85,9	93,9	98,6	101,1	102,1	102,1	101,1	99,6

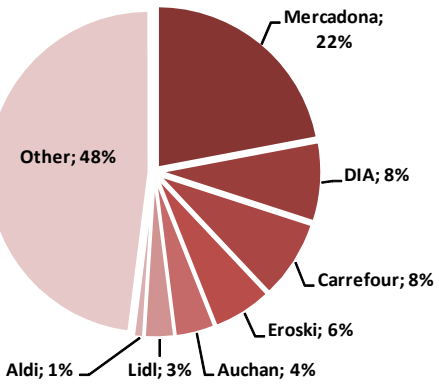
Source: IMF forecasts

Despite the positive outlook for the next years, with increasing GDP and improving employment rates, government debt is still at alarming levels, corresponding to 98,6% of GDP, and as such, a scenario of deeper food deflation and further austerity measures is still possible. This event would drag the economy, and consequently retailers, for more years of struggle.

Regarding competition, **the Spanish food retail market is widely dispersed** and the top 5 retailers account for 45% of the market. Mercadona is the market leader with €18.033[88] million sales, more than 1.500 stores and 22% market share, followed by Carrefour and DIA with market share around 8% each. However taking the acquisitions of El Árbol and Eroski stores into account, DIA becomes standalone on the second place. Furthermore the financial crisis was devastating for many small retailers and less profitable companies turning the food retail market a perfect place for consolidation.

[88] Mercadona's 2013 annual report.

Spain 2013 - Food Retail Market Share

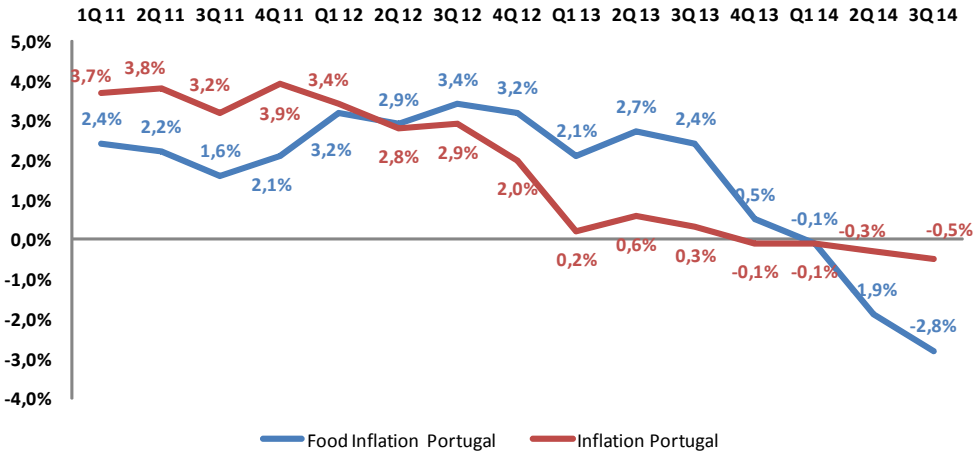


Source: BPI Equity Research October 23, 2014

Portugal

Portugal is substantially smaller comparing with Spain, both in terms of GDP (243,3 *vs* 1.389 billion dollars[89]) and population (10,5 *vs* 46,5 million people[90]). Regarding its contribution to DIA, its 600 stores account for around 14% of Iberia's sales.

Similarly to what happened in Spain, Portugal also suffered a lot with the 2008 crisis. However Portugal felt deeper in recession and had to be bailed out by the IFM in 2011 due to the sovereign debt crisis.



Source: OECD ILibrary

Comparing to before crisis the government debt rose substantially to 131,1% of GDP in 2014, unemployment increased 860bp[91] to 16,2% in 2013 and GDP decreased by -2,9% in 2009 and -3,2% in 2012. In order to reduce government spending and increase revenue, austerity

[89] Estimations from the CIA factbook, 2013.
[90] Estimations from the IMF, 2013.
[91] Bp=basis points; 100bp=1%.

measures were taken causing taxes to increase and pensions to decrease, making pressure to the household budget.

With these adverse macroeconomic conditions Portuguese retail market as well as consumer confidence sharply decreased, and consumer habits changed. Similarly to what happened in Spain, clients started to **favor proximity formats** and became more **price sensitive**. In response, retailers invested substantially in private label products and **aggressive promotion initiatives**. These trends intensified following the 1st of May 2012 when Pingo Doce, made a 50% direct discount in all baskets above €100, changing its value proposition from EDLP[92] to promotion driven.

	2009	2010	2011	2012	2013
Retail Sales (%)	-1,9	-1,2	-8,1	-5,8	-1,5

Source: Focus economics

Portugal successfully got out of the IMF program on May 2014 and future projections imply a recovery of the Portuguese economy. The government interest rates have been decreasing, GDP is expected to increase due to internal demand, unemployment is expected to decrease and consumer confidence is increasing. However, Government's debt is still at alarming levels and there is the risk of further deflation on consumer prices. Furthermore economic growth is highly dependent on the other European countries performance, particularly Spain which accounts for 23% of total exports.

Economic indicators	2007	2008	2009	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e
GDP Real (%)	2,4	0,0	-2,9	1,9	-1,3	-3,2	-1,4	1,0	1,5	1,7	1,8	1,8	1,8
GDP Nominal (%)	5,3	1,6	-2,0	2,6	-1,0	-3,5	0,4	1,7	2,5	3,5	3,6	3,7	3,7
Inflation (%)	2,4	2,7	-0,9	1,4	3,6	2,8	0,4	0,0	1,1	1,5	1,5	1,5	1,5
Unemployment rate (%)	8,0	7,6	9,4	10,8	12,7	15,5	16,2	14,2	13,5	13,0	12,4	11,9	11,3
Population growth (%)	0,2	0,1	0,1	0,0	-0,1	-0,4	-0,9	0,1	0,1	0,1	0,1	0,1	0,1
Government Debt (% of GDP)	68,4	71,7	83,7	94,0	108,2	124,1	128,9	131,3	128,7	126,5	124,1	121,8	119,3

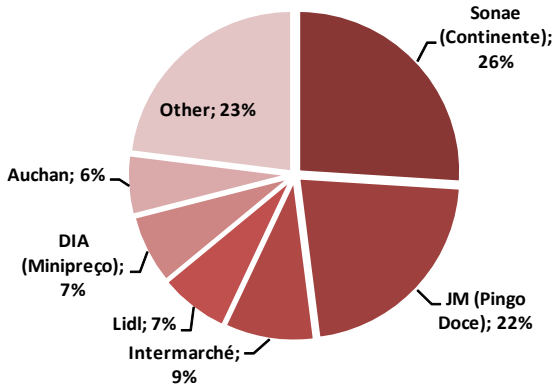
Source: IMF forecasts

Moreover, in contrast with Spain, the **Portuguese food retail market is highly concentrated** with the top 5 retailers controlling 75% market share. However, the market is promotion driven and very competitive with the two main players, Sonae and Pingo Doce, detached from the others with more than 20% market share each, "fighting" for market share. DIA was negatively affected by tough market environment, facing competitors in price and proximity (Pingo Doce, Lidl and more recently Meu Super[93] and Amanhecer[94]). It is expected weak

[92] EDLP = Everyday low price. It is a pricing strategy where the company offers low prices everyday and disregards promotions.
[93] Meu Super is a Sonae's franchise banner
[94] Amanhecer is a partnership between Jeronimo Martins' Cash&Carry, Recheio, and traditional stores

sales evolution until 1H2015 and an ease on promotions since it has not been generating volumes[95].

Portugal 2013 - Food Retail Market Share



Source: BPI Equity Research October 23, 2014

Emerging markets

The second segment is the Emerging markets which correspond for 34% of total sales and has an EBITDA margin close to 3,0%. This segment has been growing exponentially albeit negative exchange rate effect in 2014.

Emerging countries exposure carry additional risks but also new growth opportunities that developed countries lack.

Moreover, it is important to note that emerging markets' macroeconomic environment is much more volatile than Iberia's and precise forecasts are difficult or impossible to access.

Emerging countries, in general, experienced faster recovery from the financial crisis than developed countries. However current macroeconomic environment, namely declining commodity prices and the Chinese slowdown, is negatively affecting emerging countries exports, depreciating their currencies and threatening their growth.

Moreover, in a market where traditional stores still dominate, the top five players account for approximately 25% of the market. Additionally, demographics and purchasing habits have been evolving as young and urban consumers move away from the traditional channel to favor convenience store formats in city centers. Furthermore, average disposal income has been increasing and second tier[96] cities are growing leaving profitable opportunities for retailers.

[95] Source: BPI research report
[96] Considered smaller and less important and usually have lower competition.

Finally joint ventures and franchising allow international players to have access the local market, namely to the local expertise and geographic particularities.

Argentina

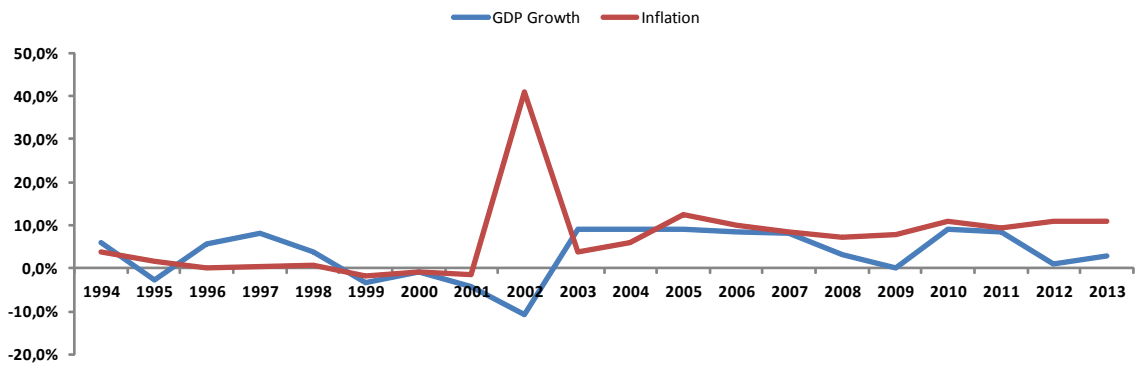
Argentina is the third largest country in South America with a population of 41,5 million people[97] and a GDP of 771 billion dollars[98].

In the first nine months of 2014, DIA's operations in Argentina reached 765 million Euros in sales, accounting for 38,2% of emerging markets sales. Comparing with the first nine months of 2013 sales decreased by -1,7% due to negative exchange rate effect (growth of 54% in constant exchange rates). Nevertheless, Argentina represents DIA's fastest growing segment with a CAGR of 17,1% between 2010 and 2013[99].

	2009	2010	2011	2012	2013
Retail Sales (%)	10,8	16,4	17,1	14,7	18,8

Source: Focus economics

Historically, **Argentina's economic performance has been very volatile**, suffering from recurring economic crisis and hyperinflation in some years and growing closely to double digit in others. A severe crisis hit Argentina in 2002 after the end of the peso's 1-1 fixed exchange rate with the US dollar, with GDP falling at a double digit rate, inflation surpassing 40% and almost 60% of Argentines were below the poverty line. After this crisis the GDP grew at an average of 8,5% per year and inflation ranged between 5% and 11% until the 2008 financial crisis. Argentina had a fast recovery from the financial crisis growing 9,1% and 8,6% in 2010 and 2011, respectively.



Source: IMF forecasts

Nowadays, despite of the Argentinean Peso's devaluation by 20% and tightened monetary and fiscal policies, in the early 2014, Argentina is witnessing hyperinflation and negative growth.

[97] Estimations from the IMF, 2013.
[98] Estimations from the CIA factbook, 2013.
[99] In Euro values.

Furthermore, the Argentinean government has restrictive currency exchanges controls which create a black market with deeply unfavorable rates. The cash restrictions should have a negative impact on DIA's valuation, however, according to the company, all the money generated by the operations today is reinvested back in the business and it is expected this will continue so during the next years since DIA has an ambitious expansion plan in Argentina.

Additionally, **the IMF alerted for the possibility of the statistics provided by local institutions to be unreliable** since private entities forecast high inflation and negative GDP evolution while government estimate positive GDP growth and smother levels of inflation.

Economic indicators	2007	2008	2009	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e
GDP Real (%)	8,0	3,1	0,1	9,1	8,6	0,9	2,9	-1,7	-1,5	n.a.	n.a.	n.a.	n.a.
GDP Nominal (%)	27,1	25,0	9,9	28,2	27,2	19,2	21,8	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Inflation (%)	8,8	8,6	6,3	10,5	9,8	10,0	10,6	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Unemployment rate (%)	8,5	7,9	8,7	7,8	7,2	7,2	7,1	8,8	9,0	9,2	9,4	10,0	10,3
Population growth (%)	1,1	1,1	1,1	1,1	1,1	1,1	1,1	1,1	1,1	1,1	1,1	1,1	1,1

Note: "n.a." Means that the information is not available

Source: IMF forecasts

Although, the retail environment is still dominated by traditional stores, big international players such as Carrefour, Casino, Walmart and DIA are opening stores and grabbing market share.

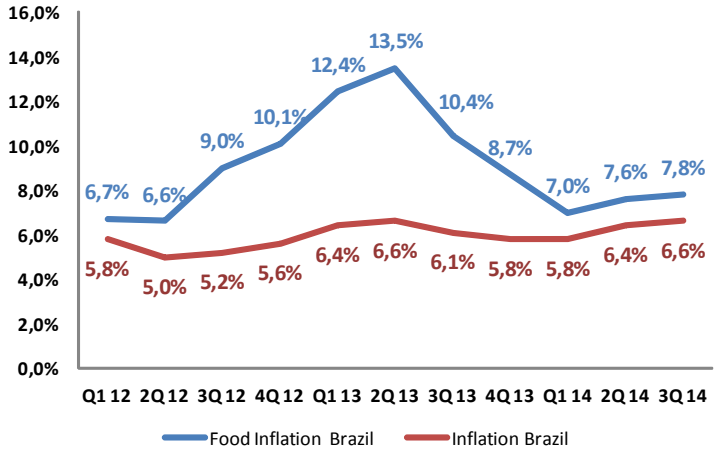
To summarize, the short term perspective is negative with hyperinflation, negative GDP growth and low business sentiment. The long perspective is blurred and the IMF doesn't provide forecasts. To conclude, the risks of hyperinflation and depression will be properly incorporated on the cash flows of the business scenarios.

Brazil

Brazil is the largest country in South America in terms of population (201 million people[100]), area (8,5 million square km[101]) and GDP (2.416 trillion dollars[102]). Moreover, it is the main emerging country for DIA's operations, accounting 55% of the segment's total sales with a 9% CAGR since 2010[103].

Brazil was one of the fastest countries to recover from the 2008 crisis with its real GDP growing at 7,5% in 2010. In contrast, the economy have been slowing down in the last years and, albeit historical minimum levels of unemployment, Brazil is currently facing weak GDP growth, including two quarters of recession in 2014, and high inflation (6,5%), above the 4,5% government's target.

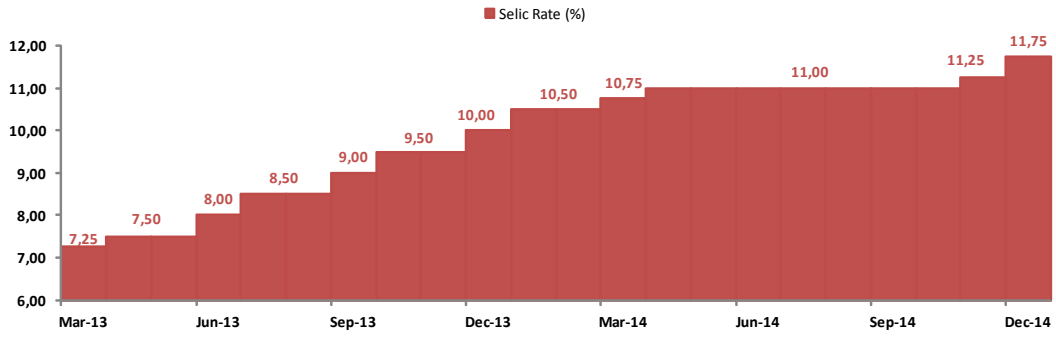
[100] Estimation from the IMF, 2013.
[101] Estimation from the CIA factbook, 2013.
[102] Estimation from the CIA factbook, 2013.
[103] In Euro values.



Source: OECD iLibrary

In addition, on the last October 26, Dilma Rousself, from the workers' party, was re-elected by the narrowest margin[104], from her opponent, Aécio Neves. Markets were favoring a change of strategy and reacted negatively. The Bovespa index, Brazil's main stock exchange, decreased by 2,8% and the Real, Brazilian currency, sank to its lowest value in nine years (2,52 against the U.S. dollar).

Moreover, in order to ease the current inflation level the Brazilian central bank has been tighten the monetary policy by increasing the interest rate reference, SELIC, from 7,25% in April 2013 to 11,75% on the last update, 3rd December of 2014.



Source: Banco Central do Brazil

In the long run, it is expected GDP to gradually increase to 3%, inflation to converge to the 4,5% target and unemployment to stay at low levels (5,5%).

Economic indicators	2007	2008	2009	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e
GDP Real (%)	6,1	5,2	-0,3	7,5	2,7	1,0	2,5	0,3	1,4	2,2	2,7	2,9	3,0
GDP Nominal (%)	12,3	13,9	6,8	16,4	9,9	6,0	10,3	5,7	6,6	7,3	7,8	8,0	8,2
Inflation (%)	3,6	5,7	4,9	5,0	6,6	5,4	6,2	6,3	5,9	5,6	5,0	4,6	4,5
Unemployment rate (%)	9,3	7,9	8,1	6,7	6,0	5,5	5,4	5,5	6,1	5,9	5,7	5,5	5,5
Population growth (%)	1,1	1,1	1,1	1,0	1,0	0,9	0,9	0,9	0,8	0,8	0,8	0,7	0,7

Source: IMF forecasts

[104] Only 3% of the votes separated the candidates.

Regarding the food retail market, DIA is the 5th supermarket player with 1,4 billion Euros in sales in 2013, below the market leader Grupo Pão de Açucar with around 11 Billion Euros, its former "parent company" Carrefour, Walmart Brazil and Chilean Cencosud[105].

Moreover, Brazil has a large labor pool and it is expected that the growth of the middle class with higher disposable income will fuel convenient and discount formats. Furthermore most Brazilians are brand-oriented and therefore there is open space for private label penetration.

	2009	2010	2011	2012	2013
Retail Sales (%)	5,9	10,9	6,6	8,4	4,3

Source: Focus economics

Brazil is the 6th most populous country in the world and each region can have the same size as a European country and has its particularities. Therefore a deep local analysis is essential for the success of the operations. In response, DIA has been adopting a cautions and sustainable growth strategy by entering in a new region with intervals of 18 months.

To summarize, Brazil is facing headwinds in terms of exports, dependent on the Chinese economy (17% of total exports), GDP growth and inflation. Nevertheless, the tighter credit conditions are expected to ease inflation, and the historical minimum unemployment rate should have a positive impact on the medium to long term growth.

China

DIA's operation in China are the smallest segment accounting for 6,3% of emerging markets sales and only 2,1% of total group's sales, during the first nine months of 2014.

China is the most populous country in the world with over one billion people and has been witnessing consistently double digit growth. It is the world's largest manufacturer and exporter and it is estimated that every perceptual point of lower growth to have a significant impact on the world's economy. Additionally, China has been gradually transforming itself into a market-based economy.

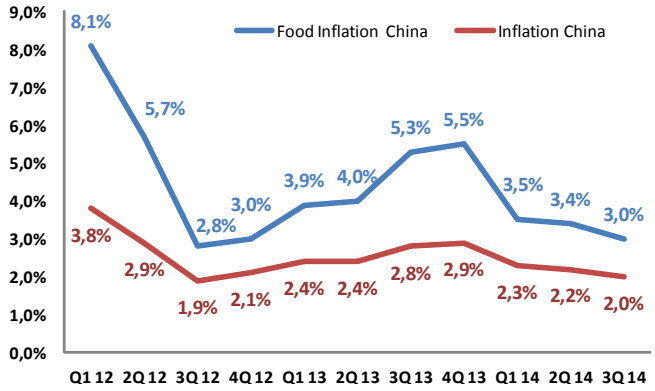
Economic indicators	2007	2008	2009	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e
GDP Real (%)	14,2	9,6	9,2	10,4	9,3	7,7	7,7	7,4	7,1	6,8	6,6	6,4	6,3
GDP Nominal (%)	19,7	18,5	10,4	15,5	17,3	12,0	10,8	9,9	9,5	9,2	9,3	9,1	9,0
Inflation (%)	4,8	5,9	-0,7	3,3	5,4	2,6	2,6	2,3	2,5	3,0	3,0	3,0	3,0
Unemployment rate (%)	4,0	4,2	4,3	4,1	4,1	4,1	4,1	4,1	4,1	4,1	4,1	4,1	4,1
Population growth (%)	0,5	0,5	0,5	0,5	0,5	0,5	0,5	0,5	0,5	0,5	0,5	0,5	0,5

Source: IMF forecasts

For the future it is expected a gradual deceleration of the economy to sustainable levels, a stable inflation level at around 3% and unemployment rate constant at 4,1%. Furthermore, China is relatively dependent on Hong Kong and USA economies since together correspond

[105] According to the Brazilian magazine: Supermercado Moderno.

for 34,1% of its exports. The main economic risks are the over reliance on investment, especially on the property sector, and the highly indebted local governments.



Source: OECD iLibrary

The retail market in China has been growing at double digit rates due to increase in disposable income despite China's slowdown. Moreover, Chinese are technology fans hence the online shopping is well developed.

	2009	2010	2011	2012	2013
Retail Sales (%)	15,5	18,4	17,1	14,3	13,1

Source: Focus economics

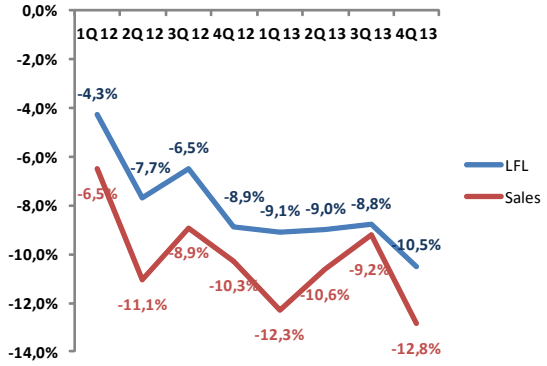
Furthermore it is expected healthy growth in grocery retailing driven by purchasing power evolution and further expansion of modern channels.

The main international players are present in China namely Walmart, Carrefour, Tesco and Auchan, seeking growth opportunities, in a market where the top five retailers have a combined market share of only 5%.

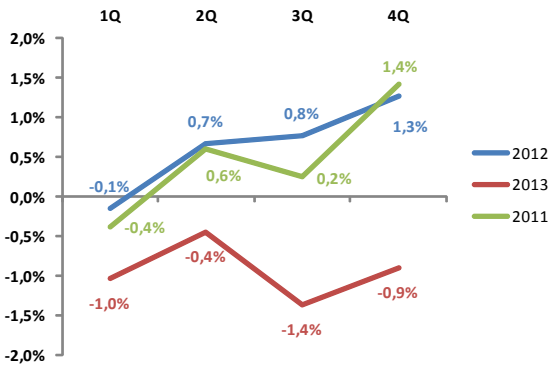
Finally, the main trends are: private label and convenience format penetration, more on-the-go meal services and partnership with online retailers to adapt the click and collect system.

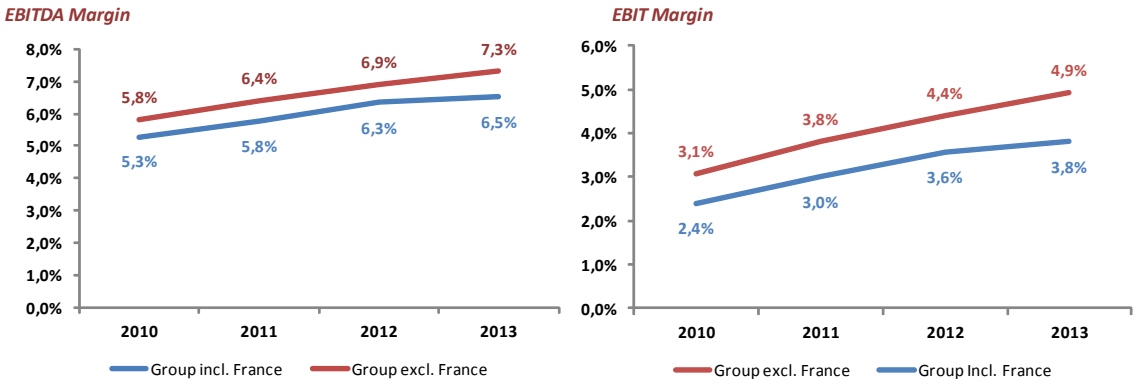
Appendix V: DIA France

DIA France Sales evolution



DIA France EBIT evolution





Source: Company data

Appendix VI: Eroski and El Árbol

	El Árbol	Eroski
Amount invested (1)	125	146
Number of stores (2)	444	160
Net sales in 2013 (1)	825	443
EBITDA margin in 2013 (3)	-0,6%	3,0%
Average selling area (Sqm)	700	800
Total area (Sqm)	310 800	128 000
Sales per Sqm	2 654	3 459
EV/Sales multiple	0,15	0,33

(1) In Million Euros
(2) Eroski stores are subject of adjustments
(3) Estimatimations
Sqm = Square meters

Source: Company data and own estimations

Appendix VII: Franchise

	Investment	Gross margin	Operating costs (e.g. shrinkage, personnel costs, utilities)	Logistics
COCO	DIA	DIA	DIA	DIA
COFO	DIA	Shared	Franchise	DIA
FOFO	Franchise	Shared	Franchise	DIA

Advantages	
Franchisee	Support of an international retailer and opportunity to manage its own business;
DIA	Lower cost base and operational flexibility;

Disadvantages & Risks	
Franchisee	Contractual obligation to buy from DIA;
DIA	Loss of control and risk of unhappy franchisees;

Source: Own estimations

Appendix VIII: Sales estimation tables

The "estimation tables" were used to estimate sales. As both segments have different characteristics, different tables were used for Iberia and Emerging Markets. The Iberia estimation table includes two main drivers: Like-for-Like and Expansion. The first is the sum

of four variables: food inflation; cannibalization effect, forecasted to be equal to one third of openings; discount effect, since DIA aims to be the price leader company's internal inflation should be lower than food inflation; and remodeling effect which corresponds to the increase in sales expected after a refurbishing process. Additionally, the remodeling effect is multiplied by a factor corresponding to the percentage of stores remodeled during the previous year. The expansion effect corresponds to the perceptual increment of new stores and it is multiplied by the factor of 50%, assuming that the stores are opened uniformly during the year. It was assumed the same growth for Eroski and El Árbol new stores and DIA's original store network in Spain (Base Spain) with the exception of 2014 in which it is expected the two banners to perform worse than DIA established portfolio before being integrated. It is also important to note that in Portugal the macroeconomic environment is expected to be tougher mainly due to higher levels of competition and lower competitive advantage (compared to DIA's position in Spain). This effect is reflected on the item "discount" once the company will have to invest a lot in prices to recover sales.

Regarding Emerging Market the estimation table has three main variables: Like-for-Like; Expansion; and Exchange rate. The Like-for-Like performance is the sum of two variables: food inflation; and quantities which indicate if the company is growing faster than inflation; the GDP evolution and individual performance of the company were used to estimate this variable.

Finally, all estimations were based on the IMF estimations and observation of the current market.

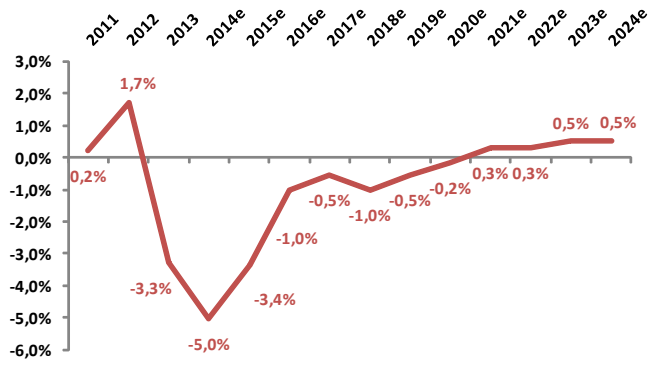
Base Scenario											
Projections	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Base Spain											
Food inflation	-4,0%	-2,5%	-0,5%	0,0%	0,5%	0,8%	1,0%	1,3%	1,3%	1,5%	1,5%
Canibalization	-1,0%	-0,8%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	6,0%	6,0%	6,0%	6,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	16,0%	16,0%	16,0%	16,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***1,0%***	***1,0%***	***1,0%***	***1,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-5,0%***	***-3,4%***	***-1,0%***	***-0,5%***	***-1,0%***	***-0,5%***	***-0,2%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
Expansion	3,5%	2,5%	1,5%	1,5%	1,5%	1,0%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***1,8%***	***1,3%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-3,3%***	***-2,1%***	***-0,3%***	***0,2%***	***-0,3%***	***0,0%***	***0,1%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
El Arbol											
Food inflation	-4,0%	-2,5%	-0,5%	0,0%	0,5%	0,8%	1,0%	1,3%	1,3%	1,5%	1,5%
Canibalization	0,0%	-0,8%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-3,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	0,0%	6,0%	6,0%	6,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	0,0%	33,0%	33,0%	33,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***0,0%***	***1,0%***	***1,0%***	***1,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-7,0%***	***-3,4%***	***-1,0%***	***-0,5%***	***-1,0%***	***-0,5%***	***-0,2%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
Expansion	-1,0%	2,5%	1,5%	1,5%	1,5%	1,0%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	100,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***-1,0%***	***1,3%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-8,0%***	***-2,1%***	***-0,3%***	***0,2%***	***-0,3%***	***0,0%***	***0,1%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
Eroski											
Food inflation	-4,0%	-2,5%	-0,5%	0,0%	0,5%	0,8%	1,0%	1,3%	1,3%	1,5%	1,5%
Canibalization	0,0%	-0,8%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-3,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	0,0%	6,0%	6,0%	6,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	0,0%	33,0%	33,0%	33,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***0,0%***	***1,0%***	***1,0%***	***1,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-7,0%***	***-3,4%***	***-1,0%***	***-0,5%***	***-1,0%***	***-0,5%***	***-0,2%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
Expansion	0,0%	2,5%	1,5%	1,5%	1,5%	1,0%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***0,0%***	***1,3%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-7,0%***	***-2,1%***	***-0,3%***	***0,2%***	***-0,3%***	***0,0%***	***0,1%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
Clarel											
Inflation	0,0%	0,6%	0,9%	1,0%	1,3%	1,3%	1,3%	1,5%	1,5%	1,5%	1,5%
Canibalization	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Extra	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	8,0%	8,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***4,0%***	***4,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***4,0%***	***4,6%***	***0,9%***	***1,0%***	***1,3%***	***1,3%***	***1,3%***	***1,5%***	***1,5%***	***1,5%***	***1,5%***
Expansion	8,5%	11,5%	10,5%	9,5%	8,0%	7,0%	5,0%	5,0%	5,0%	5,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***4,3%***	***5,8%***	***5,3%***	***4,8%***	***4,0%***	***3,5%***	***2,5%***	***2,5%***	***2,5%***	***2,5%***	***0,0%***
Total Sales	***8,3%***	***10,4%***	***6,2%***	***5,8%***	***5,3%***	***4,8%***	***3,8%***	***4,0%***	***4,0%***	***4,0%***	***1,5%***
Portugal											
Food inflation	-4,0%	-2,5%	-0,5%	0,0%	0,5%	0,8%	1,0%	1,3%	1,3%	1,5%	1,5%
Canibalization	-1,0%	-0,7%	-0,5%	-0,5%	-0,3%	-0,2%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-5,0%	-4,0%	-3,0%	-2,0%	-1,5%	-1,5%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	6,0%	6,0%	6,0%	6,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	16,0%	16,0%	16,0%	16,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***1,0%***	***1,0%***	***1,0%***	***1,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-9,0%***	***-6,2%***	***-3,0%***	***-1,5%***	***-1,3%***	***-0,9%***	***-0,2%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***
Expansion	3,0%	2,0%	1,5%	1,5%	1,0%	0,5%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***1,5%***	***1,0%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-7,5%***	***-5,2%***	***-2,3%***	***-0,8%***	***-0,8%***	***-0,6%***	***0,1%***	***0,3%***	***0,3%***	***0,5%***	***0,5%***

					Deflationary Scenario						
Projections	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Base Spain											
Food inflation	-4,0%	-5,0%	-4,0%	-3,0%	-1,0%	0,0%	0,5%	0,8%	1,0%	1,2%	1,5%
Canibalization	-1,0%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-1,0%	-3,0%	-3,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	6,0%	3,0%	3,0%	3,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	16,0%	16,0%	16,0%	16,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***1,0%***	***0,5%***	***0,5%***	***0,5%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-5,0%***	***-8,0%***	***-7,0%***	***-4,0%***	***-2,3%***	***-1,2%***	***-0,7%***	***-0,2%***	***0,0%***	***0,2%***	***0,5%***
Expansion	2,5%	1,5%	1,5%	1,5%	1,0%	0,5%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***1,3%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-3,8%***	***-7,3%***	***-6,3%***	***-3,3%***	***-1,8%***	***-0,9%***	***-0,4%***	***-0,2%***	***0,0%***	***0,2%***	***0,5%***
El Arbol											
Food inflation	-4,0%	-5,0%	-4,0%	-3,0%	-1,0%	0,0%	0,5%	0,8%	1,0%	1,2%	1,5%
Canibalization	0,0%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-3,0%	-3,0%	-3,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	0,0%	3,0%	3,0%	3,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	0,0%	33,0%	33,0%	33,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***0,0%***	***1,0%***	***1,0%***	***1,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-7,0%***	***-8,5%***	***-7,5%***	***-4,5%***	***-2,3%***	***-1,2%***	***-0,7%***	***-0,2%***	***0,0%***	***0,2%***	***0,5%***
Expansion	-1,0%	1,5%	1,5%	1,5%	1,0%	0,5%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	100,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***-1,0%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-8,0%***	***-6,8%***	***-5,8%***	***-2,8%***	***-1,8%***	***-0,9%***	***-0,4%***	***-0,2%***	***0,0%***	***0,2%***	***0,5%***
Eroski											
Food inflation	-4,0%	-5,0%	-4,0%	-3,0%	-1,0%	0,0%	0,5%	0,8%	1,0%	1,2%	1,5%
Canibalization	0,0%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-3,0%	-3,0%	-3,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	0,0%	3,0%	3,0%	3,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	0,0%	33,0%	33,0%	33,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***0,0%***	***1,0%***	***1,0%***	***1,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-7,0%***	***-8,5%***	***-7,5%***	***-4,5%***	***-2,3%***	***-1,2%***	***-0,7%***	***-0,2%***	***0,0%***	***0,2%***	***0,5%***
Expansion	0,0%	1,5%	1,5%	1,5%	1,0%	0,5%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***0,0%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-7,0%***	***-6,8%***	***-5,8%***	***-2,8%***	***-1,8%***	***-0,9%***	***-0,4%***	***-0,2%***	***0,0%***	***0,2%***	***0,5%***
Clarel											
Inflation	0,0%	0,0%	0,5%	0,5%	0,7%	1,0%	1,0%	1,0%	1,0%	1,2%	1,5%
Canibalization	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Extra	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	8,0%	5,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***4,0%***	***2,5%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***4,0%***	***2,5%***	***0,5%***	***0,5%***	***0,7%***	***1,0%***	***1,0%***	***1,0%***	***1,0%***	***1,2%***	***1,5%***
Expansion	8,5%	11,5%	10,5%	9,5%	8,0%	7,0%	5,0%	5,0%	5,0%	5,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***4,3%***	***5,8%***	***5,3%***	***4,8%***	***4,0%***	***3,5%***	***2,5%***	***2,5%***	***2,5%***	***2,5%***	***0,0%***
Total Sales	***8,3%***	***8,3%***	***5,8%***	***5,3%***	***4,7%***	***4,5%***	***3,5%***	***3,5%***	***3,5%***	***3,7%***	***1,5%***
Portugal											
Food inflation	-4,0%	-5,0%	-4,0%	-3,0%	-1,0%	0,5%	1,0%	1,0%	1,0%	1,2%	1,5%
Canibalization	-0,8%	-0,5%	-0,5%	-0,5%	-0,3%	-0,2%	-0,2%	0,0%	0,0%	0,0%	0,0%
Discount	-5,0%	-7,0%	-4,0%	-3,0%	-2,0%	-2,0%	-1,0%	-1,0%	-1,0%	-1,0%	-1,0%
Remodelling	6,0%	3,0%	3,0%	3,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Factor	16,0%	16,0%	16,0%	16,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%	0,0%
Remodelling	***1,0%***	***0,5%***	***0,5%***	***0,5%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
LFL	***-8,9%***	***-12,0%***	***-8,0%***	***-6,0%***	***-3,3%***	***-1,7%***	***-0,2%***	***0,0%***	***0,0%***	***0,2%***	***0,5%***
Expansion	2,5%	1,5%	1,5%	1,5%	1,0%	0,5%	0,5%	0,0%	0,0%	0,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***1,3%***	***0,8%***	***0,8%***	***0,8%***	***0,5%***	***0,3%***	***0,3%***	***0,0%***	***0,0%***	***0,0%***	***0,0%***
Total Sales	***-7,6%***	***-11,3%***	***-7,3%***	***-5,3%***	***-2,8%***	***-1,4%***	***0,1%***	***0,0%***	***0,0%***	***0,2%***	***0,5%***

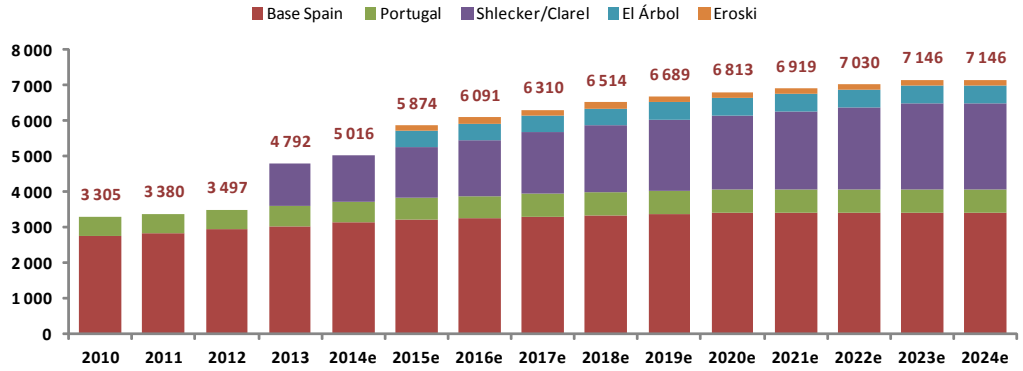
Base Scenario											
Projections	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Argentina											
Food inflation	30,0%	20,0%	10,0%	10,0%	10,0%	10,0%	8,0%	8,0%	8,0%	8,0%	8,0%
Extra	1,0%	1,0%	1,0%	1,0%	1,0%	1,0%	1,0%	1,0%	1,0%	0,0%	0,0%
LFL	***31,0%***	***21,0%***	***11,0%***	***11,0%***	***11,0%***	***11,0%***	***9,0%***	***9,0%***	***9,0%***	***8,0%***	***8,0%***
Expansion	12,0%	12,0%	12,0%	10,0%	10,0%	5,0%	5,0%	5,0%	2,0%	2,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***6,0%***	***6,0%***	***6,0%***	***5,0%***	***5,0%***	***2,5%***	***2,5%***	***2,5%***	***1,0%***	***1,0%***	***0,0%***
Germany's inflation	0,9%	1,2%	1,5%	1,7%	1,7%	1,7%	1,7%	1,7%	2,0%	2,0%	2,0%
Exchange rate	***-36,5%***	***-24,0%***	***-8,5%***	***-8,3%***	***-8,3%***	***-8,3%***	***-6,3%***	***-6,3%***	***-6,0%***	***-6,0%***	***-6,0%***
Total Sales	***0,5%***	***3,0%***	***8,5%***	***7,7%***	***7,7%***	***5,2%***	***5,2%***	***5,2%***	***4,0%***	***3,0%***	***2,0%***
Brazil											
Food inflation	8,0%	7,5%	7,0%	6,5%	6,0%	5,5%	5,5%	5,5%	5,5%	5,0%	5,0%
Extra	0,0%	2,0%	3,0%	3,0%	3,0%	3,0%	3,0%	2,0%	1,0%	0,0%	0,0%
LFL	***8,0%***	***9,5%***	***10,0%***	***9,5%***	***9,0%***	***8,5%***	***8,5%***	***7,5%***	***6,5%***	***5,0%***	***5,0%***
Expansion	16,0%	16,0%	15,0%	15,0%	10,0%	10,0%	5,0%	5,0%	2,0%	2,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***8,0%***	***8,0%***	***7,5%***	***7,5%***	***5,0%***	***5,0%***	***2,5%***	***2,5%***	***1,0%***	***1,0%***	***0,0%***
Germany's inflation	0,9%	1,2%	1,5%	1,7%	1,7%	1,7%	1,7%	1,7%	2,0%	2,0%	2,0%
Exchange rate	***-12,0%***	***-6,3%***	***-5,5%***	***-4,8%***	***-4,3%***	***-3,8%***	***-3,8%***	***-3,8%***	***-3,5%***	***-3,0%***	***-3,0%***
Total Sales	***4,0%***	***11,2%***	***12,0%***	***12,2%***	***9,7%***	***9,7%***	***7,2%***	***6,2%***	***4,0%***	***3,0%***	***2,0%***
China											
Food inflation	3,5%	3,5%	3,0%	3,0%	3,0%	3,0%	3,0%	3,0%	3,0%	3,0%	3,0%
Extra	0,0%	3,0%	3,0%	3,0%	3,0%	1,0%	1,0%	1,0%	1,0%	0,0%	0,0%
LFL	***3,5%***	***6,5%***	***6,0%***	***6,0%***	***6,0%***	***4,0%***	***4,0%***	***4,0%***	***4,0%***	***3,0%***	***3,0%***
Expansion	12,0%	15,0%	15,0%	10,0%	5,0%	5,0%	5,0%	5,0%	2,0%	2,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***6,0%***	***7,5%***	***7,5%***	***5,0%***	***2,5%***	***2,5%***	***2,5%***	***2,5%***	***1,0%***	***1,0%***	***0,0%***
Germany's inflation	0,9%	1,2%	1,5%	1,7%	1,7%	1,7%	1,7%	1,7%	2,0%	2,0%	2,0%
Exchange rate	***-5,0%***	***-2,3%***	***-1,5%***	***-1,3%***	***-1,3%***	***-1,3%***	***-1,3%***	***-1,3%***	***-1,0%***	***-1,0%***	***-1,0%***
Total Sales	***4,5%***	***11,7%***	***12,0%***	***9,7%***	***7,2%***	***5,2%***	***5,2%***	***5,2%***	***4,0%***	***3,0%***	***2,0%***

Hyperinflation and Recession Scenario											
Projections	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Argentina											
Food inflation	30,0%	35,0%	35,0%	20,0%	10,0%	10,0%	10,0%	10,0%	8,0%	8,0%	8,0%
Extra	1,0%	-2,0%	-2,0%	-1,0%	0,0%	1,0%	1,0%	1,0%	1,0%	0,0%	0,0%
LFL	***31,0%***	***33,0%***	***33,0%***	***19,0%***	***10,0%***	***11,0%***	***11,0%***	***11,0%***	***9,0%***	***8,0%***	***8,0%***
Expansion	12,0%	10,0%	10,0%	10,0%	15,0%	15,0%	10,0%	5,0%	2,0%	2,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***6,0%***	***5,0%***	***5,0%***	***5,0%***	***7,5%***	***7,5%***	***5,0%***	***2,5%***	***1,0%***	***1,0%***	***0,0%***
Germany's inflation	0,9%	1,2%	1,5%	1,7%	1,7%	1,7%	1,7%	1,7%	2,0%	2,0%	2,0%
Exchange rate	***-36,5%***	***-42,0%***	***-42,0%***	***-24,0%***	***-8,3%***	***-8,3%***	***-8,3%***	***-8,3%***	***-6,0%***	***-6,0%***	***-6,0%***
Total Sales	***0,5%***	***-4,0%***	***-4,0%***	***0,0%***	***9,2%***	***10,2%***	***7,7%***	***5,2%***	***4,0%***	***3,0%***	***2,0%***
Brazil											
Food inflation	8,0%	25,0%	25,0%	10,0%	6,0%	5,5%	5,5%	5,5%	5,5%	5,5%	5,0%
Extra	0,0%	-2,0%	-1,0%	1,0%	2,0%	2,0%	1,0%	0,5%	0,5%	0,0%	0,0%
LFL	***8,0%***	***23,0%***	***24,0%***	***11,0%***	***8,0%***	***7,5%***	***6,5%***	***6,0%***	***6,0%***	***5,5%***	***5,0%***
Expansion	16,0%	10,0%	10,0%	10,0%	10,0%	10,0%	5,0%	5,0%	2,0%	2,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***8,0%***	***5,0%***	***5,0%***	***5,0%***	***5,0%***	***5,0%***	***2,5%***	***2,5%***	***1,0%***	***1,0%***	***0,0%***
Germany's inflation	0,9%	1,2%	1,5%	1,7%	1,7%	1,7%	1,7%	1,7%	2,0%	2,0%	2,0%
Exchange rate	***-12,0%***	***-30,0%***	***-30,0%***	***-8,3%***	***-4,3%***	***-3,8%***	***-3,8%***	***-3,8%***	***-3,5%***	***-3,5%***	***-3,0%***
Total Sales	***4,0%***	***-2,0%***	***-1,0%***	***7,7%***	***8,7%***	***8,7%***	***5,2%***	***4,7%***	***3,5%***	***3,0%***	***2,0%***
China											
Food inflation	3,5%	16,0%	16,0%	5,0%	3,0%	3,0%	3,0%	3,0%	3,0%	3,0%	3,0%
Extra	0,0%	0,0%	0,0%	1,0%	2,0%	1,0%	1,0%	1,0%	1,0%	0,0%	0,0%
LFL	***3,5%***	***16,0%***	***16,0%***	***6,0%***	***5,0%***	***4,0%***	***4,0%***	***4,0%***	***4,0%***	***3,0%***	***3,0%***
Expansion	12,0%	7,5%	7,5%	10,0%	10,0%	5,0%	5,0%	5,0%	2,0%	2,0%	0,0%
Factor	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%	50,0%
Expansion	***6,0%***	***3,8%***	***3,8%***	***5,0%***	***5,0%***	***2,5%***	***2,5%***	***2,5%***	***1,0%***	***1,0%***	***0,0%***
Germany's inflation	0,9%	1,2%	1,5%	1,7%	1,7%	1,7%	1,7%	1,7%	2,0%	2,0%	2,0%
Exchange rate	***-5,0%***	***-19,2%***	***-19,2%***	***-3,3%***	***-1,3%***	***-1,3%***	***-1,3%***	***-1,3%***	***-1,0%***	***-1,0%***	***-1,0%***
Total Sales	***4,5%***	***0,6%***	***0,6%***	***7,7%***	***8,7%***	***5,2%***	***5,2%***	***5,2%***	***4,0%***	***3,0%***	***2,0%***

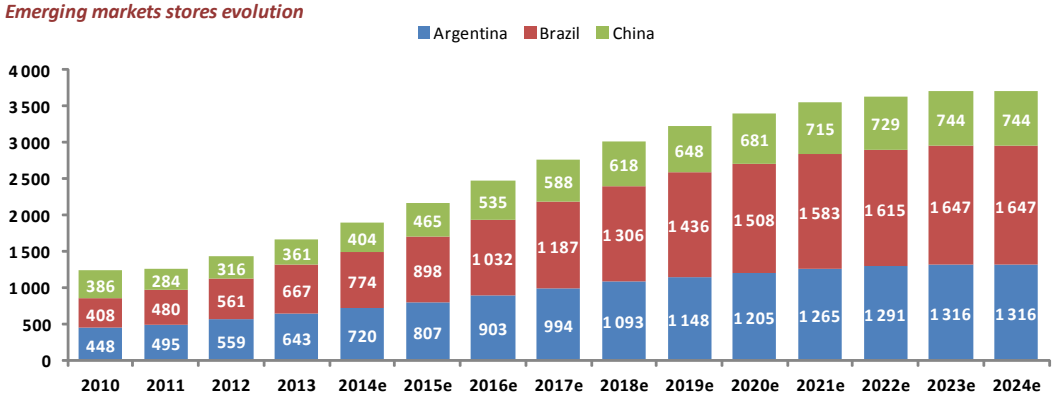
Iberia LFL



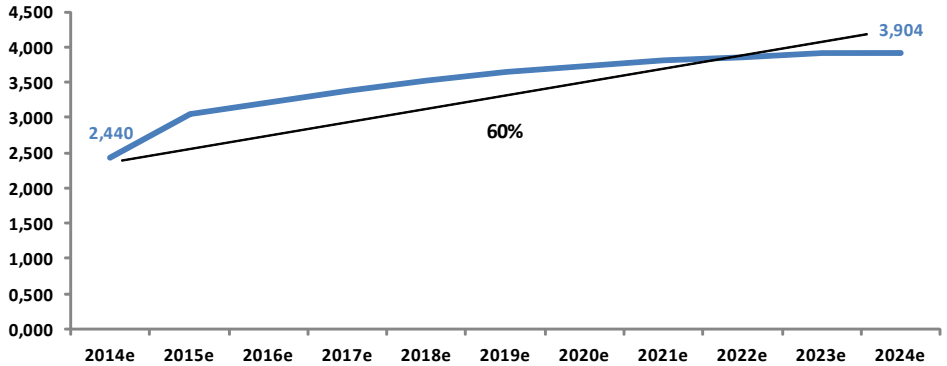
Iberia stores evolution



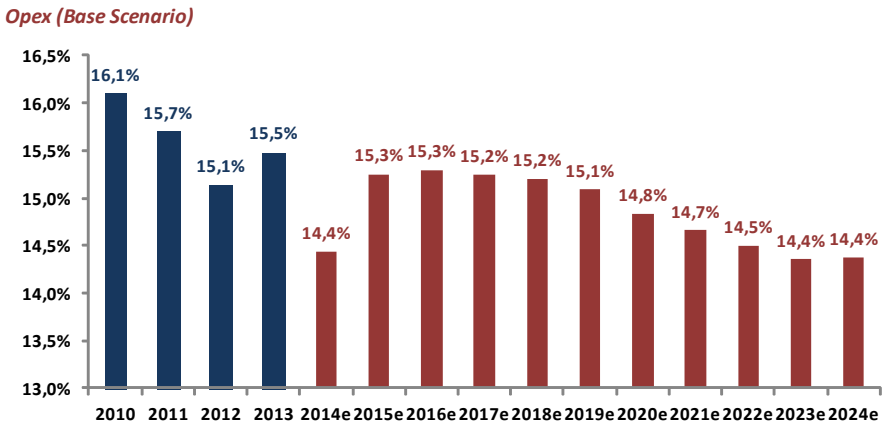
Emerging markets stores evolution



Total sales area in million sqm

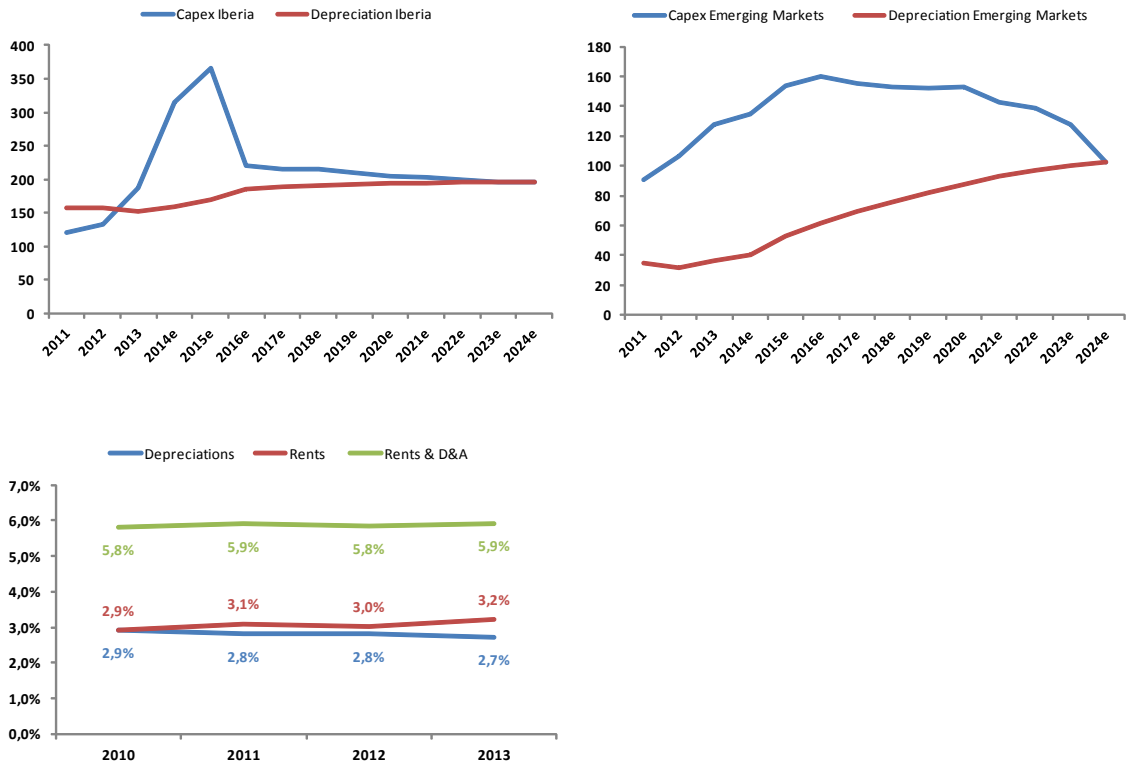


Appendix IX: Opex



Source: Company data and own estimations

Appendix X: Capex and depreciations



Source: Company data and own estimations

Appendix XI: Deflation news

EUROPE NEWS

IMF sees 25% chance of euro zone deflation by 2015

Wednesday, 14 May 2014 | 10:21 AM ET

REUTERS

The International Monetary Fund sees a 25 percent chance of the euro zone slipping into deflation by the end of next year, the fund's chief economist said on Wednesday

Getty Images

Christine Lagarde

For now, the IMF is predicting low inflation in the euro zone, Olivier Blanchard told a forum in New York. But "we think that there is a 25 percent probability that we see deflation in the euro zone by the end of 2015".

Appendix XII: Discount rate

		Comments
Rd	**2,3%**	Risk free + Spread
Rf	0,7%	German 10 years bond 27 Oct 2014
Beta	1,1	5 anos weekly MSCI Europe index
Market risk premium	5,5%	
Re	**6,9%**	
Tax	30,0%	
E/EV	80,0%	
D/EV	20,0%	
Wacc	**5,8%**	

Beta			
Benchmark	**Period (years)**	**Frequency**	**Beta**
IBEX 35	2	Weekly	0,9
IBEX 35	5	Weekly	0,8
IBEX 35	2	Monthly	1,0
IBEX 35	5	Monthly	0,6
MSCI World Index	2	Weekly	1,3
MSCI World Index	5	Weekly	1,1
MSCI World Index	2	Monthly	1,4
MSCI World Index	5	Monthly	0,8
MSCI Europe Index	2	Weekly	1,2
MSCI Europe Index	5	Weekly	1,1
MSCI Europe Index	2	Monthly	1,5
MSCI Europe Index	5	Monthly	0,9

Source: Bloomberg

Appendix XIII: Balance sheet, income statement and cash flow statement

Base Scenario															
€ million	2010	2011	2012	2013	2014e	2015e	2016e	2017	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Goodwill	414	417	423	454	308	308	308	308	308	308	308	308	308	308	308
Net property plant and equipment	1 597	1 626	1 619	1 602	1 357	1 653	1 788	1 901	2 003	2 091	2 167	2 224	2 271	2 297	2 297
Cash & cash equivalents	317	290	350	262	370	263	264	276	270	298	348	421	500	600	711
Inventory	539	522	527	545	429	489	516	536	554	571	587	603	616	626	634
Trade receivables	179	191	180	210	215	244	258	268	276	285	293	301	307	313	316
Other assets	206	264	306	298	378	378	378	378	378	378	378	378	378	378	378
Assets available for sale	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Assets	**3 253**	**3 310**	**3 405**	**3 371**	**3 057**	**3 336**	**3 512**	**3 668**	**3 790**	**3 931**	**4 082**	**4 236**	**4 380**	**4 523**	**4 645**
Financial dept	569	866	980	913	913	913	913	913	913	913	913	913	913	913	913
Trade payables	1 726	1 780	1 759	1 787	1 418	1 616	1 707	1 773	1 831	1 889	1 941	1 994	2 035	2 070	2 095
Provisions	184	169	101	81	61	61	61	61	61	61	61	61	61	61	61
Other liabilities	352	390	418	406	309	309	309	309	309	309	309	309	309	309	309
Liabilities associated with asset held for sale	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Liabilities	**2 831**	**3 205**	**3 257**	**3 187**	**2 701**	**2 899**	**2 990**	**3 056**	**3 114**	**3 172**	**3 224**	**3 277**	**3 318**	**3 353**	**3 378**
Total Equity	**423**	**105**	**148**	**184**	**356**	**437**	**522**	**612**	**676**	**760**	**858**	**959**	**1 063**	**1 170**	**1 267**
Retained earnings					184	356	437	522	612	676	760	858	959	1 063	1 170
Net profit					276	194	203	216	264	282	309	333	353	372	377
Dividends					-103	-112	-118	-127	-199	-198	-211	-232	-250	-265	-279
Total Liabilities & Shareholders Funds	**3 253**	**3 310**	**3 405**	**3 371**	**3 057**	**3 336**	**3 513**	**3 668**	**3 790**	**3 932**	**4 082**	**4 237**	**4 381**	**4 523**	**4 646**

Base Scenario															
€ million	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	9 588	9 729	9 708	9 844	7 838	8 906	9 411	9 775	10 092	10 411	10 700	10 993	11 217	11 411	11 549
% gowth		*1,5%*	*-0,2%*	*1,4%*	*-20,4%*	*13,6%*	*5,7%*	*3,9%*	*3,2%*	*3,2%*	*2,8%*	*2,7%*	*2,0%*	*1,7%*	*1,2%*
p.m. Iberia	4 938	4 947	5 117	5 284	5 106	5 953	6 142	6 166	6 165	6 176	6 194	6 226	6 259	6 305	6 340
% gowth		*0,2%*	*3,4%*	*3,3%*	*-3,4%*	*16,6%*	*3,2%*	*0,4%*	*0,0%*	*0,2%*	*0,3%*	*0,5%*	*0,5%*	*0,7%*	*0,6%*
p.m. Emerging markets	1 750	2 013	2 450	2 662	2 732	2 953	3 269	3 609	3 927	4 235	4 506	4 767	4 958	5 106	5 208
% gowth		*15,0%*	*21,8%*	*8,6%*	*2,6%*	*8,1%*	*10,7%*	*10,4%*	*8,8%*	*7,8%*	*6,4%*	*5,8%*	*4,0%*	*3,0%*	*2,0%*
Gross Profit	2 051	2 091	2 085	2 166	1 709	1 924	2 033	2 111	2 180	2 249	2 311	2 375	2 423	2 465	2 495
% of Sales	*21,4%*	*21,5%*	*21,5%*	*22,0%*	*21,8%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*
EBITDA	507	561	615	642	577	566	593	621	646	678	724	763	796	827	835
% of Sales	*5,3%*	*5,8%*	*6,3%*	*6,5%*	*7,4%*	*6,3%*	*6,3%*	*6,4%*	*6,4%*	*6,5%*	*6,8%*	*6,9%*	*7,1%*	*7,2%*	*7,2%*
p.m. Iberia	375	414	457	505	495	474	489	502	512	530	553	573	588	597	603
% of Sales	*7,6%*	*8,4%*	*8,9%*	*9,6%*	*9,7%*	*8,0%*	*8,0%*	*8,1%*	*8,3%*	*8,6%*	*8,9%*	*9,2%*	*9,4%*	*9,5%*	*9,5%*
p.m. Emerging markets	36	59	65	77	82	92	105	119	134	148	171	191	208	230	232
% of Sales	*2,1%*	*2,9%*	*2,7%*	*2,9%*	*3,0%*	*3,1%*	*3,2%*	*3,3%*	*3,4%*	*3,5%*	*3,8%*	*4,0%*	*4,2%*	*4,5%*	*4,5%*
EBIT	231	292	347	375	377	342	346	364	379	403	442	475	504	531	537
% of Sales	*2,4%*	*3,0%*	*3,6%*	*3,8%*	*4,8%*	*3,8%*	*3,7%*	*3,7%*	*3,8%*	*3,9%*	*4,1%*	*4,3%*	*4,5%*	*4,7%*	*4,6%*
p.m. Iberia	214	256	300	352	335	304	303	314	321	337	359	378	393	402	407
% of Sales	*4,3%*	*5,2%*	*5,9%*	*6,7%*	*6,6%*	*5,1%*	*4,9%*	*5,1%*	*5,2%*	*5,5%*	*5,8%*	*6,1%*	*6,3%*	*6,4%*	*6,4%*
p.m. Emerging markets	3	24	33	40	42	38	43	50	57	66	83	98	111	129	130
% of Sales	*0,2%*	*1,2%*	*1,4%*	*1,5%*	*1,5%*	*1,3%*	*1,3%*	*1,4%*	*1,5%*	*1,6%*	*1,8%*	*2,0%*	*2,2%*	*2,5%*	*2,5%*
Associated companies	-1	1	1	1	0	0	0	0	0	0	0	0	0	0	0
Financial results	-13	-35	-26	-40	-40	-21	-21	-21	-21	-21	-21	-21	-21	-21	-21
Non-recurring items	-93	-75	-38	-49	-50	-50	-50	-50	0	0	0	0	0	0	0
EBT	**125**	**182**	**283**	**286**	**287**	**272**	**276**	**293**	**358**	**383**	**421**	**455**	**483**	**510**	**516**
Taxes	-87	-83	-102	-96	-87	-78	-72	-77	-94	-101	-112	-121	-130	-138	-139
Net Profit (from continuing operations)	**38**	**99**	**182**	**191**	**200**	**194**	**203**	**216**	**264**	**282**	**309**	**333**	**353**	**372**	**377**
Income from discontinued operations		-5	-35	5	76	0	0	0	0	0	0	0	0	0	0
Minority interest		4	12	13	0	0	0	0	0	0	0	0	0	0	0
Net Profit Attributable to the Company	**38**	**99**	**158**	**209**	**276**	**194**	**203**	**216**	**264**	**282**	**309**	**333**	**353**	**372**	**377**
Underlying Net Profit	**137**	**159**	**204**	**228**	**250**	**244**	**253**	**266**	**264**	**282**	**309**	**333**	**353**	**372**	**377**
Underlying EPS					0,387	0,378	0,393	0,412	0,409	0,436	0,479	0,516	0,548	0,577	0,583
% growth						*-2,4%*	*4,0%*	*4,9%*	*-0,7%*	*6,7%*	*9,8%*	*7,7%*	*6,1%*	*5,3%*	*1,2%*
Dividend payout ratio		46%	41%	45%	45%	49%	50%	75%	75%	75%	75%	75%	75%	75%	75%
Dividend		72,5	83,9	103,4	112,4	118,2	126,7	199,4	198,0	211,3	232,0	249,9	265,1	279,3	282,5
Dividend per share		0,11	0,13	0,16	0,17	0,18	0,20	0,31	0,31	0,33	0,36	0,39	0,41	0,43	0,44
% growth			*15,7%*	*23,2%*	*8,7%*	*5,2%*	*7,2%*	*57,4%*	*-0,7%*	*6,7%*	*9,8%*	*7,7%*	*6,1%*	*5,3%*	*1,2%*

Base Scenario											
€ million	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
EBT	287	272	276	293	358	383	421	455	483	510	516
Capex	-325	-374	-381	-371	-369	-362	-358	-345	-339	-323	-298
Depreciations	200	223	247	258	267	275	282	288	293	296	298
Working capital	-258	108	50	36	31	32	29	29	22	19	14
Tax	-87	-78	-72	-77	-94	-101	-112	-121	-130	-138	-139
Dividend	-103	-112	-118	-127	-199	-198	-211	-232	-250	-265	-279
Acquisition El Arbol	-125										
Acquisition Eroski		-146									
Cash from DIA France	645										
Others	-125										
Financing needs / surplus	108	-107	1	12	-6	28	51	73	79	100	111
Cash T-1	262	370	263	264	276	270	298	348	421	500	600
Cash T	370	263	264	276	270	298	348	421	500	600	711

Weigthed Scenario															
€ million	2010	2011	2012	2013	2014e	2015e	2016e	2017	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Goodwill	414	417	423	454	308	308	308	308	308	308	308	308	308	308	308
Net property plant and equipment	1 597	1 626	1 619	1 602	1 357	1 639	1 757	1 864	1 968	2 060	2 132	2 186	2 228	2 254	2 254
Cash & cash equivalents	317	290	350	262	370	259	264	264	294	309	352	418	492	581	683
Inventory	539	522	527	545	429	479	490	502	516	531	545	558	569	578	585
Trade receivables	179	191	180	210	215	239	244	250	257	265	272	278	283	288	291
Other assets	206	264	306	298	378	378	378	378	378	378	378	378	378	378	378
Assets available for sale	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Assets	**3 253**	**3 310**	**3 405**	**3 371**	**3 057**	**3 302**	**3 442**	**3 565**	**3 721**	**3 852**	**3 987**	**4 126**	**4 258**	**4 387**	**4 500**
Financial dept	569	866	980	913	913	913	913	913	913	913	913	913	913	913	913
Trade payables	1 726	1 780	1 759	1 787	1 418	1 616	1 707	1 773	1 831	1 889	1 941	1 994	2 035	2 070	2 095
Provisions	184	169	101	81	61	61	61	61	61	61	61	61	61	61	61
Other liabilities	352	390	418	406	309	309	309	309	309	309	309	309	309	309	309
Liabilities associated with asset held for sale	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Liabilities	**2 831**	**3 205**	**3 257**	**3 187**	**2 701**	**2 899**	**2 990**	**3 056**	**3 114**	**3 172**	**3 224**	**3 277**	**3 318**	**3 353**	**3 378**
Total Equity	**423**	**105**	**148**	**184**	**355**	**404**	**452**	**509**	**608**	**680**	**764**	**849**	**941**	**1 034**	**1 122**
Retained earnings					184	355	404	452	509	608	680	764	849	941	1 034
Net profit					275	160	155	166	213	233	258	279	301	319	327
Dividends					-103	-112	-107	-109	-115	-160	-174	-193	-209	-226	-239
Total Liabilities & Shareholders Funds	**3 253**	**3 310**	**3 405**	**3 371**	**3 057**	**3 302**	**3 442**	**3 565**	**3 722**	**3 852**	**3 988**	**4 127**	**4 259**	**4 388**	**4 500**

Weigthed Scenario															
€ million	2010	2011	2012	2013	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
Sales	9 588	9 729	9 708	9 844	7 833	8 718	8 909	9 120	9 379	9 666	9 913	10 153	10 344	10 514	10 638
% gowth		*1,5%*	*-0,2%*	*1,4%*	*-20,4%*	*11,3%*	*2,2%*	*2,4%*	*2,8%*	*3,1%*	*2,6%*	*2,4%*	*1,9%*	*1,6%*	*1,2%*
p.m. Iberia	4 938	4 947	5 117	5 284	5 100	5 912	5 971	5 949	5 928	5 928	5 940	5 965	5 993	6 033	6 067
% gowth		*0,2%*	*3,4%*	*3,3%*	*-3,5%*	*15,9%*	*1,0%*	*-0,4%*	*-0,4%*	*0,0%*	*0,2%*	*0,4%*	*0,5%*	*0,7%*	*0,6%*
p.m. Emerging markets	1 750	2 013	2 450	2 662	2 732	2 807	2 938	3 171	3 451	3 739	3 973	4 188	4 351	4 481	4 571
% gowth		*15,0%*	*21,8%*	*8,6%*	*2,6%*	*2,7%*	*4,7%*	*7,9%*	*8,8%*	*8,3%*	*6,3%*	*5,4%*	*3,9%*	*3,0%*	*2,0%*
Gross Profit	2 051	2 091	2 085	2 166	1 708	1 883	1 924	1 970	2 026	2 088	2 141	2 193	2 234	2 271	2 298
% of Sales	*21,4%*	*21,5%*	*21,5%*	*22,0%*	*21,8%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*	*21,6%*
EBITDA	507	561	615	642	576	518	526	551	573	608	650	685	720	749	762
% of Sales	*5,3%*	*5,8%*	*6,3%*	*6,5%*	*7,4%*	*5,9%*	*5,9%*	*6,0%*	*6,1%*	*6,3%*	*6,6%*	*6,7%*	*7,0%*	*7,1%*	*7,2%*
p.m. Iberia	375	414	457	505	494	440	441	453	461	482	507	526	546	557	563
% of Sales	*7,6%*	*8,4%*	*8,9%*	*9,6%*	*9,7%*	*7,5%*	*7,4%*	*7,6%*	*7,8%*	*8,1%*	*8,5%*	*8,8%*	*9,1%*	*9,2%*	*9,3%*
p.m. Emerging markets	36	59	65	77	82	78	85	98	111	126	142	159	173	192	199
% of Sales	*2,1%*	*2,9%*	*2,7%*	*2,9%*	*3,0%*	*2,8%*	*2,9%*	*3,1%*	*3,2%*	*3,4%*	*3,6%*	*3,8%*	*4,0%*	*4,3%*	*4,3%*
EBIT	231	292	347	375	376	295	280	295	309	336	370	400	430	456	467
% of Sales	*2,4%*	*3,0%*	*3,6%*	*3,8%*	*4,8%*	*3,4%*	*3,1%*	*3,2%*	*3,3%*	*3,5%*	*3,7%*	*3,9%*	*4,2%*	*4,3%*	*4,4%*
p.m. Iberia	214	256	300	352	334	271	256	264	271	289	313	332	351	361	367
% of Sales	*4,3%*	*5,2%*	*5,9%*	*6,7%*	*6,6%*	*4,6%*	*4,3%*	*4,4%*	*4,6%*	*4,9%*	*5,3%*	*5,6%*	*5,9%*	*6,0%*	*6,1%*
p.m. Emerging markets	3	24	33	40	42	24	25	31	38	47	57	68	79	95	100
% of Sales	*0,2%*	*1,2%*	*1,4%*	*1,5%*	*1,5%*	*0,9%*	*0,8%*	*1,0%*	*1,1%*	*1,2%*	*1,4%*	*1,6%*	*1,8%*	*2,1%*	*2,2%*
Associated companies	-1	1	1	1	0	0	0	0	0	0	0	0	0	0	0
Financial results	-13	-35	-26	-40	-40	-21	-21	-21	-21	-21	-21	-21	-21	-21	-21
Non-recurring items	-93	-75	-38	-49	-50	-50	-50	-50	0	0	0	0	0	0	0
EBT	**125**	**182**	**283**	**286**	**286**	**224**	**210**	**225**	**288**	**315**	**350**	**379**	**410**	**436**	**446**
Taxes	-87	-83	-102	-96	-87	-64	-54	-59	-75	-82	-92	-100	-109	-117	-120
Net Profit (from continuing operations)	**38**	**99**	**182**	**191**	**199**	**160**	**155**	**166**	**213**	**233**	**258**	**279**	**301**	**319**	**327**
Income from discontinued operations		-5	-35	5	76	0	0	0	0	0	0	0	0	0	0
Minority interest		4	12	13	0	0	0	0	0	0	0	0	0	0	0
Net Profit Attributable to the Company	**38**	**99**	**158**	**209**	**275**	**160**	**155**	**166**	**213**	**233**	**258**	**279**	**301**	**319**	**327**
Underlying Net Profit	**137**	**159**	**204**	**228**	**249**	**210**	**205**	**216**	**213**	**233**	**258**	**279**	**301**	**319**	**327**

Weigthed Scenario											
€ million	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e
EBT	286	224	210	225	288	315	350	379	410	436	446
Capex	-325	-360	-364	-362	-368	-364	-352	-339	-331	-319	-295
Depreciations	200	223	246	255	264	272	279	285	289	293	295
Working Capital	-257	123	76	49	36	34	32	33	25	21	15
Tax	-87	-64	-54	-59	-75	-82	-92	-100	-109	-117	-120
Dividend	-103	-112	-107	-109	-115	-160	-174	-193	-209	-226	-239
Acquisition El Arbol	-125										
Acquisition Eroski		-146									
Cash from DIA France	645										
Others	-125										
Financing needs / Surplus	108	-112	6	-1	30	15	43	65	75	89	102
Cash T-1	262	370	259	264	264	294	309	352	418	492	581
Cash T	370	259	264	264	294	309	352	418	492	581	683

Appendix XIV: DIA France impact

Thousands of Euros	30/06/2014
Assets	
Tangible fixed assets	494,486
Goodwill	146,395
Other Intangible assets	14,793
Investments in companies consolidated by equity method	1,027
Other non-current financial assets	9,317
Inventories	113,832
Trade and other receivables	31,764
Current tax assets	29,636
Other current financial assets	4,891
Other assets	6,476
Non-current assets held for sale	**852,617**
Liabilities	
Non-current borrowings	274,544
Provisions	19,578
Deferred tax liabilities	11,287
Current borrowings	38,391
Trade and other payables	194,095
Current income tax liabilities	41,592
Taxes payable to the Tax Office due to Income Tax	52
Other financial liabilities	43,555
Liabilities directly associated with non-current assets held for sale	**623,094**

Source: DIA France balance sheet - DIA's first semester report

The above DIA France **balance sheet** was used in order to adjust the 2014 consolidate balance sheet (excluding DIA France). For this purpose the amount of tangible assets, €494 million, was subtracted on the property plant and equipment, the amount of Goodwill, €146 million, was subtracted to goodwill and the following items: "other intangible assets", "investment in companies consolidate by equity method", "other non-current financial assets", "current assets", "other current financial assets" and "other assets"; were subtracted on "other assets" in the model. Furthermore, provisions amounting €20 million, were subtracted on group provisions, and the following items were subtracted on "other liabilities": "deferred tax liabilities", "current income tax liabilities", "taxes payable to the tax office due to income tax" and "other financial liabilities".

Details of tax assets and liabilities at 30 June 2014 and 31 December 2013 are as follows:

Thousands of Euros	30-jun-2014	31-dec-2013
Deferred tax assets	201,811	57,667
Taxation authorities, VAT	21,804	30,580
Taxation authorities	23,305	24,618
Current income tax assets	-	22,453
Total tax assets	**246,920**	**135,318**
Deferred tax liabilities	753	57,978
Taxation authorities, VAT	23,491	36,780
Taxation authorities	29,552	105,057
Current income tax liabilities	39,408	18,702
Total tax liabilities	**93,204**	**218,517**

The increase in deferred tax assets at 30 June 2014 is mainly due to the tax effect of the temporary difference arising from DIA France's imminent exit from the consolidated Group (see note 11).

Source: Deferred tax assets - DIA's first semester report

Furthermore a deferred tax asset amounting €145 million, due to DIA France, was added to "other assets".

Cash flow statement: in order to match assets with liabilities plus equity, €125 million had to be added, on "others" in 2014, due to lack of information regarding the complete impact of DIA France.

Income statement: the value of €76 million was imputed in the line "income from discontinued operations" due to DIA France sale. Due to lack of information, the value from the nine months report was used as an approximation for the year end.

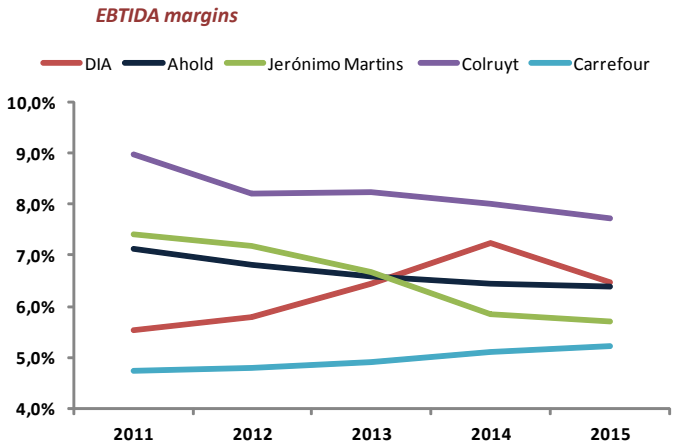
Appendix XV: Multiples

Name	CAGR Sales 3 years (%)		LTG EPS (%)		Roic 2014 (%)		Debt to EV (%)		EBITDA (%)		Store Format: Convenience/Discount	Geography: Europe + Emerging markets	Number of: Yes	Peer?
DIA	0,9		12,0		17,5		25,7		7,2					
Ahold	3,4	Yes	10,9	Yes	11,8	Yes	24,6	Yes	6,4	Yes	No	No	5	Yes
Casino Group	18,7	No	6,4	Yes	6,8	No	48,3	No	6,7	Yes	No	Yes	3	No (1)
Jerónimo Martins	10,8	No	-0,9	No	17,9	Yes	12,6	No	5,9	No	Yes	Yes	3	Yes
Sonae	1,0	Yes	0,0	No	0,0	No	52,3	No	7,9	Yes	No	No	2	No
X5	15,2	No	19,3	No	9,9	No	38,2	No	7,5	Yes	No	No	1	No
Delhaize	0,4	Yes	7,0	Yes	4,3	No	36,0	No	6,1	No	No	No	2	No
Kesko	2,1	Yes	0,0	No	8,4	No	15,4	No	4,2	No	No	No	1	No
Colruyt	5,9	No	4,2	No	17,8	Yes	0,7	No	8,0	Yes	Yes	No	3	Yes
WM Morrisson	2,4	Yes	-3,9	No	0,0	No	40,0	No	6,6	Yes	No	No	2	No
Sainsbury	4,3	Yes	-11,7	No	9,0	No	47,8	No	5,9	No	No	No	1	No
AxFood	3,1	Yes	0,0	No	28,3	No	2,3	No	5,6	No	No	No	1	No
Dixy	41,5	No	29,9	No	10,2	No	39,8	No	7,3	Yes	Yes	No	2	No
Magnit	33,1	No	17,5	Yes	20,3	Yes	7,0	No	11,4	No	Yes	No	3	No (2)
Carrefour	-2,3	Yes	14,8	Yes	5,9	No	55,6	No	5,1	No	No	Yes	3	Yes
Tesco	1,7	Yes	5,3	No	9,1	No	57,4	No	7,5	Yes	No	Yes	3	No (3)
Metro Ag	-1,5	Yes	0,0	No	3,1	No	54,7	No	4,4	No	No	Yes	2	No
CIA Brasileira	22,6	No	19,6	No	11,0	Yes	29,1	Yes	7,9	Yes	No	No	3	No (1)
BIM	21,7	No	0,0	No	0,0	No	0,1	No	4,6	No	Yes	No	1	No
O'key Group	19,2	No	9,4	Yes	16,5	Yes	30,4	Yes	7,8	Yes	No	No	4	No (2)
Pick n Pay	7,2	No	0,0	No	25,7	No	4,3	No	3,1	No	No	No	0	No
Organizacion Soriana	3,9	Yes	4,1	No	6,1	No	4,5	No	7,0	Yes	No	No	2	No
Cencosud	18,7	No	24,0	No	6,0	No	43,0	No	6,9	Yes	No	No	1	No

Note: The indicators were extracted from Bloomberg on the 2nd of January 2015, using the fiscal years of 2014 and 2015 and Bloomberg's analyst panel consensus.

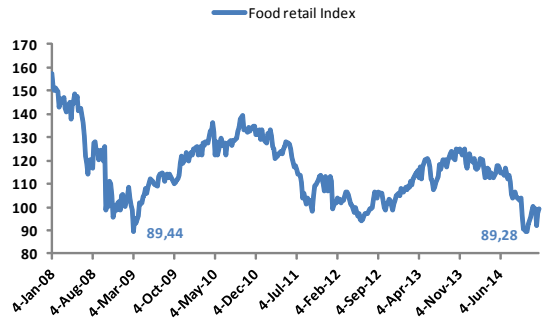
Note: LTG EPS mean long term earnings per share forecasted by Bloomberg for the next business cycle (between 3 and 5 years)

(1) Casino group and CIA (Companhia Brasileira de Distribuição) were excluded because almost 50% of their sales don't correspond to food retail business.
(2) Magnit and O'key group were excluded because they only operate in Russia.
(3) Tesco was excluded because of the recent accounting fraud.



Source: Bloomberg

Appendix XVI: Food retail index



Source: Bloomberg

Appendix XVII: Analysts recommendations

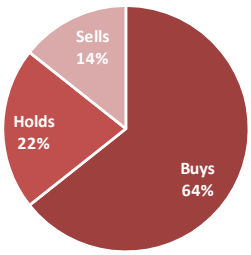
Analysts recommendations		
	% of Buy / Total	Recommendation Consensus
DIA	64,3%	4,0
Ahold	33,3%	3,3
Casino Group	30,4%	3,4
Jerónimo Martins	28,6%	3,2
Sonae	57,1%	3,9
X5	76,2%	4,4
Delhaize	46,4%	3,6
Kesko	50,0%	3,6
Colruyt	4,0%	2,3
WM Morrisson	26,1%	2,6
Sainsbury	20,8%	2,5
AxFood	25,0%	2,6
Dixy	78,3%	4,5
Magnit	78,6%	4,4
Carrefour	44,7%	3,7
Tesco	15,4%	2,8
Metro Ag	41,7%	3,6
CIA Brasileira	64,7%	4,3
BIM	16,7%	2,8
O'key Group	23,8%	2,9
Pick n Pay	37,5%	2,9
Organizacion Soriana	14,3%	2,1
Cencosud	19,0%	2,9

Source: Bloomberg

Note: the recommendation consensus is a Bloomberg scale which ranges between 1 and 5 being "1" = Sell and "5" = Buy. As it can be seen in the table above DIA has the fifth highest recommendation level among the 23 players, with a recommendation of 4.

Market consensus: €6,41 | Potential upside: 13,1%

Anaysts recommendations



Source: Bloomberg

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