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Value Investor INSIGHT

The Leading Authority on Value Investing

Sacré Bleu

Political upheaval appears to be the norm rather than the exception in countries around the world, including the United States. That can spell incremental investment risk, or opportunity. Which is more likely the case for France's Vinci S.A.?

For a timely reminder that political risk for investors is alive and well, look no further than France's Vinci S.A. When Jacopo Di Nardo of Latitude Investment Management detailed the investment case for the concessions and construction company just over a year ago [*VII*, November 30, 2023], the key driver of his optimism was the company's large global contracting business. With long-established engineering expertise and a track record of on-time and on-budget project delivery, he expected the company to benefit as infrastructure spending in the U.S. and elsewhere advanced, particularly involving energy-transition initiatives. The valuation on the stock, then trading at around €112 per share, was at a 15-year low that he thought significantly undervalued the company's earnings power.

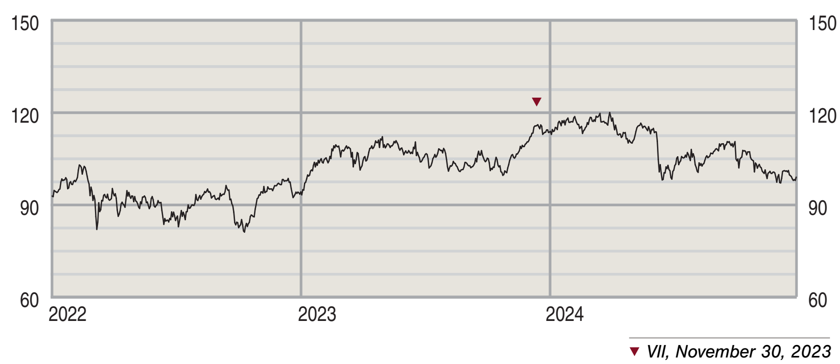
From a business perspective, the thesis is intact. Vinci's France-focused toll-roads business is fine, with modest growth from inflation passthroughs in pricing. The global airport-concessions division – it owns and operates airports in France and around the world, including Gatwick in London and Kansai International in Japan – has benefitted from increased air travel and has added two airports, in Scotland and Hungary, through acquisition in the past year. Energy contracting and construction remains the most exciting business, says Di Nardo, winning high-profile contracts to build what is now a record-high €67 billion order backlog. The company' energy division has also been buying up competitors in the space, closing on some 30 deals this year – all financed with current cash flow – that add more than €900 million of annual revenues.

What has most impacted Vinci's stock, however, are the machinations of French politicians. After large increases in fiscal spending in 2022 and 2023, to comply with European Union limits on deficits as a percentage of GDP the French government has enacted a number of tax increases. These include for companies like Vinci with more than €1 billion in annual French turnover an 8%-of-revenue corporate-tax surcharge for 2024 and 4% for 2025. The government has also imposed special taxes of 4% of revenues on French motorway and airport operators for the period 2024 to 2030. Assuming all the new taxes are imposed as planned – some are being challenged in court – Di Nardo says they reduce his discounted-cash-flow

INVESTMENT SNAPSHOT

Vinci S.A.
(Paris: DG)

DG PRICE HISTORY



Share Information (@12/30/24):

Price	**€98.72**
52-Week Range	€96.26 – €120.62

Valuation Metrics (@12/30/24):

	DG	S&P 500
P/E (TTM)	12.4	25.2
Forward P/E (Est.)	11.4	21.9

ORIGINAL BOTTOM LINE – November 30, 2023

While it has rock-solid toll road and airport concession businesses, the company's stock is often influenced by its construction arm, says Jacopo Di Nardo. He thinks that business is structurally improving and a valuation re-rating could add to the otherwise low-double-digit annualized shareholder return he expects to earn from profit growth and the dividend.

NEW BOTTOM LINE

New corporate taxes imposed by the French government in the past year have obscured the company's operating success in its large global contracting business, says Jacopo Di Nardo. He values the company's shares at nearly 70% above the current share price.

Sources: S&P Capital IQ, company reports, other publicly available information derived estimate of Vinci's intrinsic value by about €4 per share.

Frustrating as that is, he still considers the stock significantly undervalued. On a sum-of-the-parts basis, using different costs of capital for each division, he pegs Vinci's net asset value today at approximately €165 per share, a nearly 70% premium to the current price. "The energy business here is one of the very few high-quality industrial businesses in the world benefitting from a number of key secular trends – electrification, spending on computing infrastructure, energy transition – that isn't earning a high valuation," he says. "If that persists, they could spin it off and that would likely be a real kicker to unlocking value." VII