

9 February 2007

SGS

Reuters: **SGSN.VX** Bloomberg: **SGSN VX** Exchange: **VTX** Ticker: **SGSN**

Time to revisit SGS

Ken Kagerer

Research Analyst
(41) 44 227 3378
ken.kagerer@db.com

David Cerdan

Research Analyst
(33) 1 4495 6624
david.cerdan@db.com

Upside from M&A not factored in

SGS is a well-positioned growth company that is characterized by high visibility of earnings. The strong management team should be able to achieve the announced set of ambitious targets. While we carry the organic targets in our model, the targeted growth via acquisitions would potentially add more upside to our share price target.

Secular trends drive growth

As the global market leader in inspection, verification and certification services, SGS is well positioned to meet the continuously growing market demand that is driven by secular trends such as globalization, outsourcing and increased quality needs. High entry barriers like brand, reputation and a global network support SGS's dominant position.

Top-line and margin growth

Management should be able to achieve the announced set of ambitious targets, i.e. top-line growth of 15% p.a. (10% organic and 5% from acquisitions). The EBIT margin should reach the targeted 17% by 2008 (2006: 16.3%, DB fc 2008E: 17%) and the company's 2008 EPS target stands at a realistic CHF80 (DB fc 2008E: CHF75). Margins should be supported by increased exposure to the high-margin Asian markets, introduction of higher-margin non-trade related service offerings and further focus on efficiency measurements and cost reductions.

Valuation and risks

Our price target of CHF1570 is DCF-based assuming a WACC of 8.0% and long-term growth of 2.5% that should be mainly inflation driven (see pp. 15-16). Downside risks to our investment case include a slowdown in global trade or inherent risks involved when executing the targeted acquisition strategy of the group.

Forecasts and ratios

Year End Dec 31	2005A	2006A	2007E	2008E	2009E
Revenue (CHFm)	3,308	3,821	4,247	4,689	5,148
EBITA (CHFm)	502	624	702	796	896
DB EPS (CHF)	49.46	60.82	66.23	75.02	84.11
DB EPS growth (%)	26.4	23.0	8.9	13.3	12.1
P/E (DB EPS) (x)	18.7	19.9	21.5	18.9	16.9
EV/EBITDA (x)	10.1	11.3	11.5	9.9	8.5
DPS (CHF)	50.00	20.00	22.00	25.00	28.00
Yield (%)	5.4	1.7	1.5	1.8	2.0

Source: Deutsche Bank estimates, company data

Deutsche Bank AG/London

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DISCLOSURES AND ANALYST CERTIFICATIONS ARE LOCATED IN APPENDIX 1

Momentum

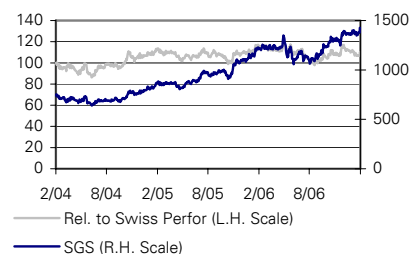
Buy

Price at 8 Feb 2007 (CHF)	1,421.00
Price Target (CHF)	1,570.00
52-week range (CHF)	1,425.00 - 1,057.00

Key changes

Target Price	1,530.00 to 1,570.00	↑	2.6%
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Price/price relative



Performance (%)	1m	3m	12m
Absolute	4.6	9.2	17.6
Swiss Performance Index	4.9	6.8	23.1

Stock data

Market cap (CHF)(m)	10,794.0
Shares outstanding (m)	8
Free float (%)	63
Swiss Performance Index	7,323.8

Key indicators

ROE (%)	29.0
Net debt/equity (%)	-24.2
EBIT margin (%)	16.5

Model updated: 09 February 2007

Running the Numbers

Europe

Switzerland

Outsourcers

SGS

Reuters:SGSN.VX Bloomberg:SGSN.VX

Buy

Price as of 08 February CHF 1421.00

Target price CHF 1570.00

Company website

http://www.sgs.com

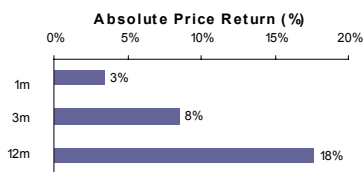
Company description

SGS provides industrial inspection, analysis, testing, and verification services worldwide. The Company inspects, samples, analyzes, and monitors raw materials, petroleum, food, crops, chemicals, consumer goods, and production machinery for compliance with industrial standards and local regulatory requirements, including tax and duty.

Research Team

Ken Kagerer
+41 11 227 3378 ken.kagerer@db.com

David Cerdan
+33 144 95 6624 david.cerdan@db.com



52-week Range: CHF 1057.00 - 1425.00
Market Cap (m) CHF 10,794 USD 8,665

Company identifiers
Cusip NA
SEDOL 4824778

Year Ending 31December 2003 2004 2005 2006 2007E 2008E 2009E

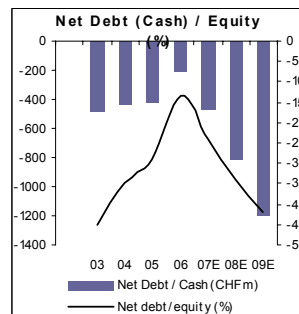
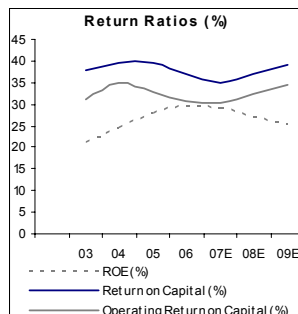
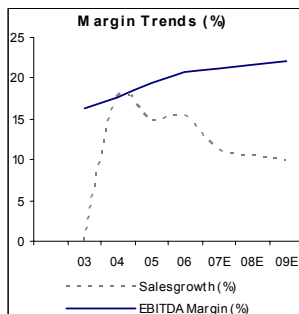
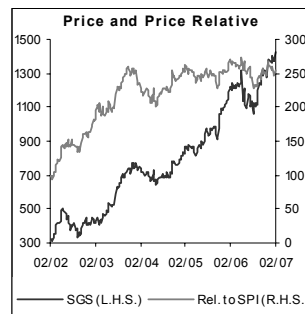
	2003	2004	2005	2006	2007E	2008E	2009E
SUMMARY							
DB EPS (CHF)	30.22	39.13	49.46	60.82	66.23	75.02	84.11
P/E (x)	19.0	18.3	18.7	19.9	2.15	18.9	16.9
DB EPS growth (%)	na	29.5	26.4	23.0	8.9	13.3	12.1
EPS FD (CHF)	29.18	37.25	49.46	58.32	66.23	75.02	84.11
P/E FD (x)	19.7	19.2	18.7	20.8	2.15	18.9	16.9
CFPS (CHF)	43.20	57.82	57.99	80.57	87.38	98.39	109.78
P/CFPS (x)	13.3	12.4	16.0	15.0	16.3	14.4	12.9
Free CFPS (CHF)	25.33	32.58	31.60	44.63	54.47	65.48	76.87
DPS (CHF)	9.00	12.00	50.00	20.00	22.00	25.00	28.00
Dividend Yield (%)	1.6	1.7	5.4	1.7	1.5	1.8	2.0
BV/Share (CHF)	137.81	164.11	191.84	205.63	251.86	304.88	363.99
Price/BV (x)	5.56	4.85	5.78	6.60	5.64	4.66	3.90
Weighted average shares (m)	7.8	7.5	7.5	7.6	7.6	7.6	7.6
Average market cap (CHF m)	4,466	5,356	6,947	9,194	10,794	10,794	10,794
Enterprise value (CHF m)	4,047	5,030	6,515	8,977	10,315	9,985	9,591
EV/Sales	1.65	1.74	1.97	2.35	2.43	2.13	1.86
EV/EBITDA	10.1	9.9	10.1	11.3	11.5	9.9	8.5
EV/EBIT	13.8	13.3	13.0	14.4	14.7	12.5	10.7
EV/Operating Capital	5.5	5.4	4.6	5.4	5.8	5.3	4.9

	2003	2004	2005	2006	2007E	2008E	2009E
INCOME STATEMENT (CHF m)							
Sales revenue	2,454	2,885	3,308	3,821	4,247	4,689	5,148
Operating EBITDA	399	509	642	796	897	1,012	1,132
Depreciation	96	115	140	172	195	216	237
Amortisation	10	16	0	0	0	0	0
EBIT	293	378	502	624	702	796	896
Net interest income(expense)	1	0	2	-4	5	5	5
Associates/affiliates	0	0	0	0	0	0	0
Investment/other income(expense)	9	6	3	3	0	0	0
Exceptionals/extraordinaries	0	0	0	0	0	0	0
Income tax expense	68	90	119	155	179	207	238
Minorities/preference dividends	8	15	17	25	24	24	24
Net income	227	279	371	443	503	570	639

	2003	2004	2005	2006	2007E	2008E	2009E
CASHFLOW (CHF m)							
Cash flow from operations	336	433	435	612	664	747	834
Movement in net working capital	-31	11	-80	-31	-59	-62	-66
Capex	-171	-201	-205	-248	-250	-250	-250
Free cash flow	197	244	237	339	414	497	584
Other investing activities	48	-144	-82	-201	0	0	0
Equity raised(bought back)	0	0	-52	42	0	0	0
Dividends paid	-56	-69	-97	-393	-152	-167	-190
Net inc(dec) in borrowings	0	0	0	0	0	0	0
Other financing cash flows	-2	-2	-59	-27	0	0	0
Total cash flows from financing	-58	-71	-208	-378	-152	-167	-190
Net cash flow	155	17	-60	-215	262	330	394
Movement in net debt(cash)	-155	-17	60	215	-262	-330	-394

	2003	2004	2005	2006	2007E	2008E	2009E
BALANCE SHEET (CHF m)							
Cash and other liquid assets	526	456	531	239	501	831	1,225
Tangible fixed assets	415	493	586	656	711	745	758
Goodwill	117	242	329	503	503	503	503
Other intangible assets	30	62	100	141	141	141	141
Associates/investments	2	2	2	2	2	2	2
Other assets	932	957	1,217	1,311	1,423	1,538	1,657
Total assets	2,022	2,212	2,765	2,852	3,280	3,760	4,286
Interest bearing debt	33	18	101	24	24	24	24
Other liabilities	899	939	1,189	1,236	1,289	1,342	1,395
Total liabilities	932	957	1,290	1,260	1,313	1,366	1,419
Shareholders' equity	1,072	1,229	1,439	1,562	1,933	2,336	2,765
Minorities	18	26	36	30	54	78	102
Total shareholders' equity	1,090	1,255	1,475	1,592	1,967	2,394	2,867
Net working capital	196	139	223	220	279	341	407
Net debt(cash)	-493	-438	-430	-215	-477	-807	-1,201
Capital	597	817	1,045	1,377	1,490	1,587	1,666

	2003	2004	2005	2006	2007E	2008E	2009E
RATIO ANALYSIS							
Sales growth (%)	na	17.6	14.7	15.5	11.2	10.4	9.8
EBITDA Margin (%)	16.3	17.6	19.4	20.8	2.11	2.16	2.20
EBIT Margin (%)	11.9	13.1	15.2	16.3	16.5	17.0	17.4
Payout ratio (%)	30.8	32.2	10.1	34.3	33.2	33.3	33.3
ROE (%)	2.12	24.3	27.8	29.5	29.0	26.9	25.1
Return on Capital (%)	37.9	39.5	39.7	36.8	34.8	36.8	39.1
Operating Return on Capital (%)	31.1	34.8	32.8	30.5	30.5	32.4	34.5
Capex/sales (%)	7.0	7.0	6.2	6.5	5.9	5.3	4.9
Capex/depreciation (x)	1.8	1.7	1.5	1.4	1.3	1.2	1.1
Net debt/equity (%)	-45.2	-34.9	-29.2	-13.5	-24.2	-33.7	-41.9
Net interest cover (x)	nm	nm	nm	156.0	nm	nm	nm



Source: Company data, Deutsche Bank estimates

Investment thesis

Outlook

Market leader in inspection, verification and certification industry

SGS is the market leader in the inspection, verification and certification industry with over 48,000 employees and more than 1,000 offices across the globe. SGS, with its global network, strong management and high barriers to entry would be in a better position than competitors to absorb most of the demand growth. SGS currently enjoys leadership in the commodity-linked services like agriculture, minerals or oil and gas services.

Strong management team

SGS is a high quality growth company characterized by good earnings visibility. The strong management team around the new CEO Chris Kirk, the former EVP of mineral services, should be able to achieve the announced set of targets, i.e. top-line growth of 15% p.a. (10% organic and 5% from acquisitions). We are forecasting SGS to reach the targeted EBIT margin of 17% by 2008. The company's 2008 EPS target stands at a realistic CHF80 (DBE 2008E: CHF75, excluding acquisitions).

High barriers to entry

The company's business (inspection, testing and certification) is characterized by high entry barriers (mainly due to brand, reputation and global network) and the stock offers good exposure to powerful secular trends like globalization, outsourcing and increased quality needs.

Valuation

Our price target of CHF1570 is DCF based assuming a WACC of 8.0% and long-term growth of 2.5% that should be mainly inflation driven.

We believe that the full potential of the group is currently not reflected in the stock's valuation. We reiterate our Buy rating.

Risks

Downside risks to our investment case include a slowdown in global trade or inherent risks involved when executing the targeted acquisition strategy of the group. Please also consult the chapter on investment risks at the end of the report.

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Introduction

History and overview

Founded in 1878 as a French grain shipment inspection house, SGS now operates a network of c1000 offices and laboratories around the world, employing about 48000 employees, providing industrial inspection, testing, verification, and certification services. SGS was registered in Geneva as Société Générale de Surveillance in 1919. SGS shares were first listed on the Swiss Exchange (SWX) in 1985.

Fragmented client base, strong customer loyalty and predictable sales pattern

SGS's customer base is relatively fragmented, i.e. the group's top three clients together account for less than 5% of group sales. The contract scope is wide, ranging from basic quantity checks to very sophisticated tailor-made services involving laboratory testing. Revenue patterns are quite predictable since a big portion is generated from recurring contracts. Customer loyalty is high as it is expensive and time consuming to change from one company to another. Most services are specialized and only delivered by certain certification companies. Acquiring and processing the first certification cycle is costlier than subsequent recurring testing and certification processes.

Key entry barriers are reputation, network and brand

French Bureau Veritas and UK-based Intertek are the major global competitors to SGS. Due to significant entry barriers like a global network that seems very difficult to replicate, reputation, and a recognized brand, it is difficult to imagine the emergence of a completely new global player in the industry.

1) Globalization, 2) outsourcing, and 3) increased quality needs drive growth

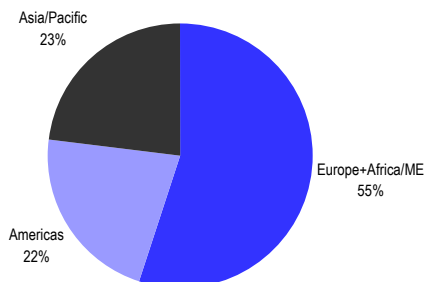
SGS benefits from global trends that can be summarized under the three key areas: 1) globalization, 2) outsourcing and 3) increased quality needs. Outsourcing and global sourcing put an increasing emphasis on the monitoring of process quality, which has to be developed, implemented and checked for compliance.

SGS operates globally across 10 different business lines in three main areas:

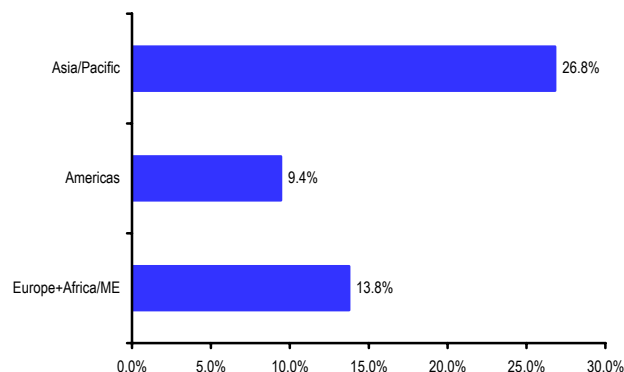
- **Inspection Services:** SGS inspects and verifies the quantity, weight and quality of traded goods. Inspection takes place prior to shipment at the manufacturer's or supplier's premises.
- **Testing Services:** This service tests product quality and performance against various health, safety and regulatory standards. It is done by SGS in state-of-the-art laboratories close to the customer's premises.
- **Certification Services:** SGS certifies whether products, systems or services meet the requirements of standards set by governments, standardization bodies (e.g. ISO 9000) or by SGS customers. SGS also develops and certifies its own standards.

Growth in Asia means better margins

In Figure 1 we highlight the geographical sales distribution of SGS. Europe, Africa and Middle East contribute 55%, America contributes 22% and Asia Pacific contributes 23% of sales. SGS continuously tries to strengthen its footprint in the Americas as well as in the Asia Pacific markets through organic growth initiatives and acquisitions. Figure 2 shows the EBIT margin of the three main areas of geographic activity of the group. A continuous shift toward the more profitable Asian business should have healthy effects on the overall group profitability.

Figure 1: Sales by geography, 2006

Source: Company data

Figure 2: Geographical EBIT margin, 2006

Source: Company data

Outsourcing trend drives growth for SGS

We estimate that roughly two-thirds of the inspection and testing market is still directly managed in house by companies, while the rest of the market is operated by a plethora of specialized agencies. We believe that a continuing trend for global corporations to focus on their core competencies should lead to more outsourcing. SGS is well positioned to benefit from this trend.

If a company decides to outsource, it benefits from outsourcing advantages discussed below:

- Focus on core business: Involving delegation of non-core operations to an external subcontractor.
- Generation of cost savings:
 - Labor costs (wages, training, recruitment) and investments (laboratories) managed by specialists who can amortize on a larger base of clients (i.e. generation of economies of scale).
 - Technology, new practices: specialists are early adopters and have expertise in using technologies and assimilating the latest regulatory rules to deliver best practices.
- Higher flexibility and reactivity: Specialists can provide greater flexibility by enabling companies to migrate from a fixed to a variable cost model. Outsourcers can more rapidly and efficiently dedicate a number of employees according to clients' needs without affecting profitability and quality of service. Outsourcers can manage seasonality more efficiently (peaks and troughs).
- Global network: The larger outsourcers have developed a global network of offices throughout the world to meet clients' needs at an affordable price.

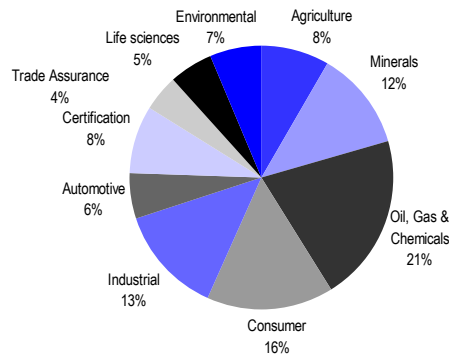
The points above should support our theory that outsourcing penetration in the industry should rise from its current level of roughly only one third.

Divisional overview

SGS is serving a very diverse client base. Each division is concentrating on serving major industries exposed to global trade. The ten divisions are: Agricultural Services, Automotive services, Consumer Testing Services, Environmental Services, Trade Assurance Services,

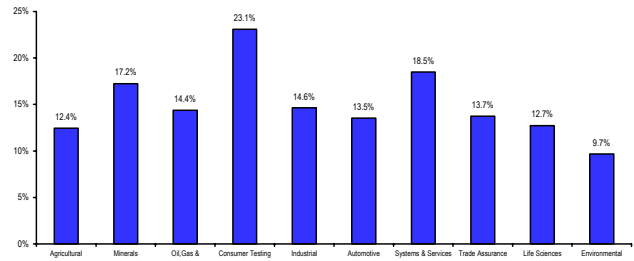
Industrial Services, Life Sciences Services, Minerals Services, Oil, Gas & Chemicals Services, and Systems & Services Certification.

Figure 3: Divisional sales split, 2006



Source: Company data

Figure 4: Divisional EBIT margins, 2006



Source: Company data

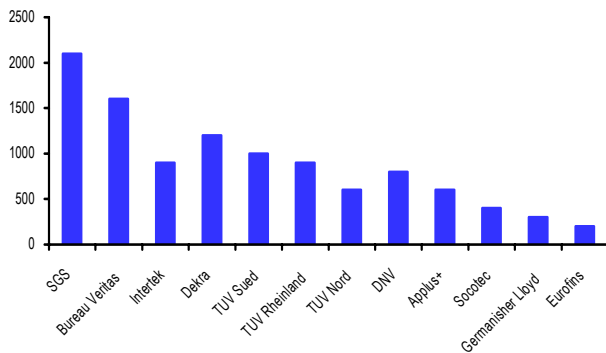
As shown in Figure 3, the major contributor to sales in 2006 is forecasted to be Oil, Gas and chemicals with 21% of sales, followed by Consumer Testing with 16% of sales, Industrial Services accounting for 13% of sales and Minerals with 12% of sales.

Figure 4 illustrates SGS’s divisional profitability. Consumer Testing Services along with System & Service Certification have been the most profitable for SGS.

Global market structure

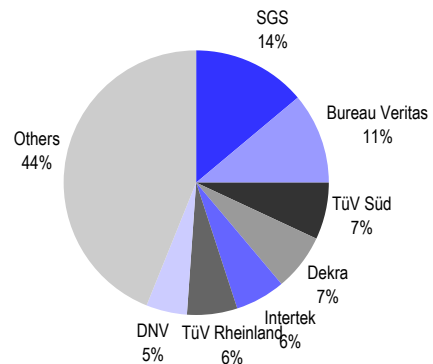
We estimate the global inspection, certification and testing industry to serve a cEUR40-50bn market. Out of this market c30-35% is served by specialized and independent agencies such as SGS, Bureau Veritas and Intertek while the rest is not yet outsourced. Figures 5 and 6 highlight the competitive landscape of the industry.

Figure 5: Main players, 2005 (sales in Euro m)



Source: Deutsche Bank estimates

Figure 6: Market shares, 2005



Source: Deutsche Bank estimates

The industry covers all sectors (primary, secondary and tertiary), companies of various scales of operation (from small to large), and all regions. A large portfolio of services is offered, ranging from very basic (commodities quantity control) to tailored and sophisticated services (tests in laboratories, critical products / building conformity assessment). The market is still highly fragmented with only a few global players operating in multiple sectors (SGS, BV and

Intertek) while the rest of the market (DNV, Dekra, TÜV and others) comprises mid-size organizations that often focus only on one region or on a limited number of sectors and areas of expertise.

SGS is #1 in agriculture, mineral, oil, gas and chemicals

- SGS (Switzerland, sales of EUR2.1bn): SGS is the worldwide leader with the most diversified business / service portfolio (10 business lines). With 48000 employees and over 1000 offices around the world, SGS has key global positions in several sub-segments: #1 in agriculture, mineral, oil, gas and chemicals, #1 in certification, #2 in consumer goods, top 3 in assurance trade and top 5 in automotive services.
- Bureau Veritas (France, sales of EUR1.6bn): BV is the world's second largest player with leadership in industry (oil / gas and chemicals, construction) and in certification, #2 in maritime services, and #3 in consumer products (#1 for toys, #2 for textiles). The group operates through a network of 700 offices in 140 countries and has 23700 staff members.
- Intertek (UK, sales of EUR0.9bn) is the world's fifth largest player with leading positions in oil, gas and chemicals (#2), leader in consumer goods (textiles, toys, electrical and electronic equipment) as well as trade insurance and government services.
- Other competitors are less diversified than the three leaders of the industry. The long list of significant players includes TÜV (Germany, consumer testing, industry), Dekra (Germany, automotive and industry), and DNV (Norway, maritime, certification), which can compete with the three market leaders.
- In Figure 7 we highlight the most important industry players and their positioning in various subsections.

Figure 7: Competitive landscape (Sales and positions in 2005)

	SGS	Bureau Veritas	Intertek	Dekra	TÜV*	DNV	Applus+ (Candover)	Socotec	Germanisher Lloyd
Nationality	Swiss	French	UK	German	German	Norwegian	Spanish	French	German
Sales in 2005 (EUR bn)	2.1	1.6	0.9	1.2	2.6	0.8	0.6 (in 06E)	0.4	0.3
Industry	Top 5	# 1	X	X	# 2	X		X	X
Consumer Testing	# 2	# 3	# 1		X				
Certification	# 1	# 1	X			# 5	X		
Maritime		# 2				# 1			Top 5
Oil/Gas/Chemicals	# 1	X	# 2						
Automotive	Top 5			Top 5	X		X		
Environment	X						X	X	
Agriculture	# 1	X	X						
Mineral	# 1								
Life Sciences	X								
Trade Assurance	Top 3	Top 3	X						

Source: Deutsche Bank estimates, company data; TÜV include several independent entities such as TÜV Sued (sales of E1.1bn), TÜV Rheinland (0.9bn) and TÜV Nord (E0.6bn)

Barriers to entry

The industry's services range from basic quantity checks to highly sophisticated laboratory testing. Barriers to entry vary depending on the service provided and the country, with various specific local regulatory environments. Main barriers to entry into the industry are summarized below:

- Establishment of a certification and inspection franchise that is recognized by government authorities, international standards organizations and customers. Companies entering the certification market have to be accredited, which requires solid internal

management systems. Thus, agencies invest regularly in new norms, the training of their staff, in the development of innovative services in order to value their competencies and their brand names.

- Development of a global network that is capable of serving an international client base. Being global enables agencies to leverage their experience across borders and attract global clients. Size is also a key advantage to capture the largest or the most complex contracts and take advantage of economies of scale.
- Focus on staff utilization rate, personnel turnover, recruitment and training are key for strong performance and large players are best positioned to deliver on these criteria. Furthermore, customers look for service providers with appropriate financial strength and the ability to mobilize large teams to perform short-duration projects. Hence, large specialists can deliver better proposals than comparable in-house solutions and other third party offers.

Growth drivers

While each end market is characterized by specific dynamics, we believe the following growth drivers seem to positively impact almost all divisions of SGS:

Global trade

- Global trade: We believe that globalization resulting in increased global trade flows is a major driver of growth for SGS, generating among other things the desire to trace the origin of goods. Historical evidence shows that global trade seems to grow at roughly double the speed of underlying global GDP growth. Furthermore, we believe in the increasing importance of intra-regional trade (within China for example).

More regulations and standards

- Increasing regulations and standards: Increasing and tougher regulations and standards environment and international harmonization positively drive testing and certification activities in all of SGS's sub-segments. Standards have been applied with growing intensity over the past decades. Well-defined standards are important to guarantee the smooth functioning of markets. Standards are necessary to ensure the protection of human health and/or the environment. Even though there may be differences regarding the degree of protection (e.g. Genetically Modified Organisms (GMO)) among or within societies, there is a general trend toward increasing the complexity of standards.

Health and safety issues

- Health and safety issues: Companies are increasingly aware of health and safety issues, and environmental and liability risks of their products and services, with regard to employees and their commercial partners. This is positive for certification and standard activities (e.g. ISO norms, sustainable development).

Increased quality requirements

- Increasing quality requirements: Consumer awareness of quality and safety encourage companies to increasingly ensure the quality of their products and services through verification, standards and testing services. Quality seems to have become an increasingly important differentiation argument for producers, since it can have a cooling effect on price competition. While minimum standards are identical in most cases, companies tend to differentiate their products through higher quality requirements.

Increased product variety and shorter product life cycles

- Product variety and shorter product life cycles: There seems to be a general trend of increasing product variety in various sectors (e.g. automotive or clothing industry). We believe that companies generally try to increase product variety in recessionary environments to compensate for a lack of growth with potential market share gains. Such industry behavior cushions the effects of GDP weakness for SGS and peers in our opinion, since the number of goods to be tested increases. Shorter product life and enlargement of the product range tend to increase the intensity of conformity assessment services.

Increased outsourcing

- Increased outsourcing: Companies tend to outsource those tasks to specialists who are able to meet their needs at higher quality and lower cost.

New innovative services**Additional growth drivers for SGS**

- Additional services: SGS plans to expand its existing customer base with additional services. New services can be bundled together, thereby enabling SGS to offer favorable prices.
- Market share gains: We believe SGS has the potential to gain market share from smaller local players due to its global reach and the fact that global companies tend to seek global partners.

Market share gains**Management guidance**

As the market leader in most of its activities, SGS is the single largest operator in the testing, verification and certification market, which puts it in a position to outperform the industry's growth over time; hence we believe that SGS's targets for 2008E are realistic. The main cornerstones of SGS's 2008E targets are:

- Revenue target of CHF5bn, implying an annual organic growth of 10% and 5% growth via acquisitions;
- Increased operating margin of 17%; and
- EPS of CHF80.

Upside to our numbers might result from targeted acquisitions

In our view, SGS's CHF5bn sales target is realistic; however, we do not forecast future acquisitions in our numbers, which results in our sales forecast of CHF4.7bn for 2008E. While the group's operating margin stood at 15.8% in 2005, we are forecasting an expansion towards 17% by 2008E, in line with the group's target. Our EPS forecast for 2008E stands at CHF75 (as we do not include the targeted future acquisitions). Keeping our view on forecasting with potential future questions in mind, acquisitions would mean upside to our numbers.

Acquisitions could mean upside for EPS forecasts and price target**Acquisitions**

SGS has always believed in growth via acquisitions and has acquired a number of companies across various segments over the past few years in order to reinforce or penetrate new sectors. SGS still believes that it could expand its business segments through major acquisitions. We expect the group to continue to make smaller bolt-on acquisitions in the normal course of its business. However, we also think that SGS is actively looking for larger acquisition targets. The strategic growth plan of SGS targets external growth of 5% per annum.

In our view, SGS could take on 3x EBITDA (2007E: CHF897m) or CHF2.7bn in debt. Hence, CHF3.2bn could be acquired (adding our forecasted net cash position of CHF477m for 2007E). Should SGS spend CHF500m on acquisitions at a 15x PE multiple, the EPS impact in 2007E would be 5.3%. As mentioned above, we do not forecast any future acquisition in our model; hence any deal could offer potential upside to our EPS forecasts.

Figure 8: Estimated impact of potential acquisitions on group earnings, 2007E

		P/E			
		10x	15x	17.5x	20x
Cash used (CHF m)	300	5.2%	3.2%	2.6%	2.2%
	500	8.6%	5.3%	4.3%	3.6%
	1000	17.2%	10.5%	8.6%	7.2%
	1500	25.8%	15.8%	12.9%	10.8%
	2000	34.4%	21.1%	17.3%	14.4%

Source: Deutsche Bank estimates

Directors and management

Board of Directors

Sergio Marchionne (1952, Canadian/Italian, Chairman)

Sergio Marchionne was appointed the CEO of Alusuisse Lonza Group Limited, Zurich, in 1997. He was then the Managing Director and CEO of Lonza Group Ltd. (spun off from Alusuisse Lonza), of which he is now the Chairman. He is also a Board Member of Serono and Fiat. In February 2002, he was appointed the CEO and Managing Director of SGS. On June 1st, 2004, he was appointed the Managing Director and CEO of Fiat SpA. Sergio Marchionne holds a bachelor's degree in law and a master's in business administration.

Tiberto Ruy Brandolini d'Adda (1948, Italian, Board Member)

Mr. Brandolini has been on the SGS Board since March 2005. He is also the Chairman at Sequana Capital SA, Antalis International SAS, Antonin Rodet SAS, Mercurey and ArjoWiggins SAS, Issy les Moulineaux. He is the Vice Chairman of Exor Group, Luxembourg and the CEO of Exint, Paris. He is on the boards of Spirito Santo, Fiat SpA, IFIL S.p.A. and Vittoria Assicurazioni SpA. Mr. Brandolini d'Adda is a Knight of the Legion of Honour.

Pascal Lebard (1962, French, Board Member)

Pascal Lebard began his career in 1986 with Crédit Commercial de France, where he worked in London and Paris, before joining the UK private equity group, 3i group plc, in 1988, working first in London and then Paris as an Account Manager. He was appointed the Investment Director in 1989 and Associate Director in the Paris office in 1990. In 1991, he joined IFINT (now Exor Group, part of the Agnelli Group) where he was in charge of investments. He was the Chairman of Club Méditerranée from 2002 to 2004. Pascal Lebard is a graduate from EDHEC Business School.

August Von Finck (1930, Swiss, Board Member)

Mr. Von Finck descends from the banking family von Finck. His grandfather, Wilhelm von Finck, founded "Merck, Finck & Co." in 1870, the private bank which was at the origin of companies including Munich Re, Allianz insurance and the Löwenbräu breweries, among others. Based in Munich, the member of the third generation of the von Finck family belongs to several boards of directors and holds interests in a number of German, Swiss, Austrian companies as well as in groups from other countries. In Switzerland, August von Finck's participations include Mövenpick and Von Roll.

François Von Finck (1968, German, Board Member)

Mr. Von Finck has a banking background and is currently the Managing Director of Carlton Holding in Basel. Mr. Von Finck holds an MBA from Georgetown University.

Hans Peter Keitel (1947, German, Board Member)

Dr. Ing. Hans-Peter Keitel holds degrees in construction engineering, and in labor and economic sciences from Stuttgart and Munich Universities respectively, and a doctorate from the Technical University in Munich. He joined Hochtief AG, in 1988 and was appointed the CEO in 1992.

Shelby R. du Pasquier (1960, Swiss, Board Member)

Mr. Shelby R. du Pasquier holds degrees from Geneva University Business School and School of Law as well as from Columbia University School of Law (LLM). He was admitted to the Geneva Bar in 1984 and to the New York Bar in 1989. He became a partner of Lenz & Staehelin in 1994.

Management

SGS' management has gone through numerous changes in the past five years. On 29th November, 2006, the new CEO Chris Kirk (EVP of both Minerals and Environmental Services) was promoted to the former position of previous CEO Dan Kerpelman.

SGS's CEO history

- Antony M. Czura: August 1998 – January 2002
- Sergio Marchionne: February 2002 – May 2004; Mr. Marchionne left to become the CEO of Fiat SpA, but stayed on SGS's Board of Directors.
- Werner Pluss: May 2004 – November 2004, Mr. Pluss resigned for health reasons.
- Johan Allegaert: November 2004 – April 2005, Mr. Allegaert was serving as the interim CEO until a permanent appointment was made.
- Dan Kerpelman: April 2005 – November 2006.
- Chris Kirk: From November 2006

Functional managers

- Chris Kirk (1956, British, CEO)

Chris Kirk was appointed CEO from November 2006 from Executive Vice President, Minerals and Environmental Services, which he was serving since 2003. Mr. Kirk joined SGS in 1981 as GM of New Zealand. He was then appointed to the operations council in 2002, as COO of the South East Asia/Pacific region. He was also responsible for the cross-sectoral Collateral Management business. He has held a number of senior positions in Thailand, Ghana, Singapore and Australia.

- Richard Tobin (1963, American, CFO)

Richard Tobin joined SGS in 2002. He was an officer in the US Army from 1985 to 1989 and started his professional career as an International Marketing Executive at GTE Corp. (1989-1996). In 1996, Mr. Tobin joined Alu-Suisse-Lonza in Zurich as a Business General Manager. He was then appointed Business General Manager at Alcan Aluminum in Montreal, Canada in 2000.

- Jean-Luc de Buman (1953, Swiss, IR)

Jean-Luc de Buman spent the first part of his career in the financial industry. He joined SGS in 1998 and is responsible for all aspects of internal and external communication as well as the relationship between the company and the investor community.

- Hugh Markey (1950, Canadian, Senior Vice President, Corporate Development)
- Jean-Pierre Mean (1944, Swiss, Senior Vice President, Legal & Compliance)

Business managers

- Agricultural Services: Francis Lacroze (1953, French)
- Oil, Gas and Chemical Services: Jan Milio (1948, Belgian)
- Minerals Services: Michael Belton (1960, British)
- Industrial Services: Friedrich Hecker (1962, German)
- Automotive Services and Trade Assurance Services: Fred Herren (1955, Swiss)
- Life Science Services: Helge Bastian (1960, German)
- Systems and Services Certification: Jeffrey McDonald (1964, Australian)
- Consumer Testing Services: Frankie Ng (1966, Swiss)

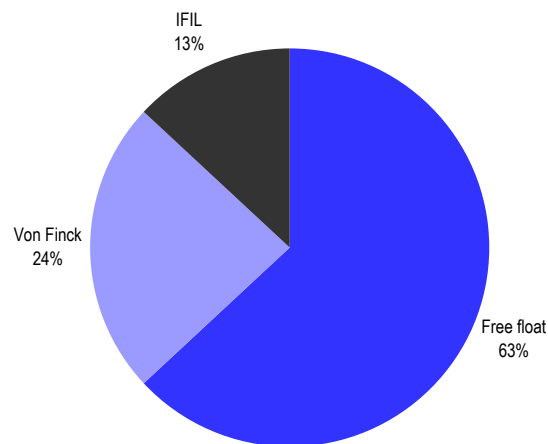
Regional managers

- COO Western Europe: Fernando Basabe (1959, Spanish)
- COO Africa: Robert Markus (1956, Dutch)
- COO South Eastern Europe: Duilio Giacomelli (1950, Italian)
- COO China and Hong Kong: Helmut Chik (1966, Hong Kong Chinese)
- COO South America: Alejandro Gomez de la Torre (1959, Peruvian)
- COO Central Europe and Scandinavia: Dirk Hellemans (1958, Belgian)
- COO North America: Christian Jilch (1957, Austrian)
- COO South Eastern Asia and Pacific: Claude Lanouhe (1950, French)
- COO Eastern Europe and Middle East: Alim Saidov (1964, Azerbaijani)
- COO Eastern Asia: Dennis Yang (1949, Taiwanese)

Shareholder structure

SGS's free float is currently at 63%, following Sequana Capital's strategic review that resulted in Sequana Capital becoming a pure play focused on its paper assets and pulling out of its SGS investment. This led to a distribution of SGS shares to Sequana Capital shareholders via a share exchange offer. Following the unwinding of Sequana Capital's investment in SGS, IFIL is left with only 13% stake in SGS compared to the past IFIL when had a de-facto control of 24% through its majority stake in Sequana Capital. Hence a certain shift of power occurred in favor of the von Finck family.

Figure 9: SGS's shareholder structure, 2007



Source: SGS

Valuation

Figure 10: Valuation summary, 2004-09E

Valuations	2004	2005	2006	2007E	2008E	2009E
Market capitalization	5372.9	6828.7	10794.0	10794.0	10794.0	10794.0
Net debt	(438.0)	(430.0)	(215.0)	(476.8)	(807.1)	(1201.1)
Minorities	26.0	36.0	30.0	54.0	78.0	102.0
Enterprise value	4908.9	6362.7	10549.0	10263.2	9908.9	9490.9
EBITDA	506.0	642.0	777.0	896.9	1012.1	1132.4
EBIT	391.0	502.0	605.0	701.5	796.4	895.6
EPS	37.3	49.5	58.3	66.2	75.0	84.1
	9.7	9.9	13.6	11.4	9.8	8.4
EV / EBITDA (x)	12.6	12.7	17.4	14.6	12.4	10.6
EV / EBIT (x)	19.3	18.4	24.4	21.5	18.9	16.9
PE (x)	5372.9	6828.7	10794.0	10794.0	10794.0	10794.0

Source: Deutsche Bank estimates; Priced on Feb 8th @CHF1421

Discounted cash flow analysis

Our price target is based on DCF valuation, which yields a fair value per share of CHF1570. We are applying a weighted average cost of capital (WACC) of 8%, in line with the Swiss mid-cap universe. Our long-term growth assumption after 2014 is 2.5% (mainly driven by the global inflation rate).

We believe our assumptions are not aggressive, but provide a sensitivity analysis of various WACC and long-term growth assumptions in Figure 11.

Figure 11: DCF Sensitivity analysis (CHF per share)

		WACC				
		6%	7%	8%	9%	10%
LTG	1.0%	2,005	1,639	1,381	1,191	1,045
	1.5%	2,142	1,722	1,435	1,227	1,070
	2.0%	2,313	1,821	1,497	1,268	1,098
	2.5%	2,533	1,942	1,570	1,315	1,130
	3.0%	2,826	2,094	1,658	1,370	1,166
	3.5%	3,237	2,289	1,766	1,435	1,208
	4.0%	3,853	2,549	1,900	1,513	1,257

Source: Deutsche Bank estimates

Figure 12 highlights our assumptions and the cash flows per annum during 2006-2014. The calculation of our estimated fair value of CHF1570 for the group is also outlined in the said figure.

Figure 12: DCF valuation

(CHF m)	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2017E	2018E	2019E	FCF t+1
Sales growth (%)	11.2%	10.4%	9.8%	7.0%	6.8%	6.6%	6.4%	6.2%	6.0%	6.0%	6.0%	5.7%	
Depreciation as a % of sales	4.6%	4.6%	4.6%	4.5%	4.2%	4.0%	3.7%	3.5%	3.3%	3.1%	3.2%	3.1%	
Operating margin (%)	16.5%	17.0%	17.4%	17.5%	17.5%	17.5%	17.5%	17.5%	17.5%	17.5%	17.6%	17.6%	
Effective tax rate (%)	25.4%	25.9%	26.4%	26.4%	26.4%	26.4%	26.4%	26.4%	26.4%	26.4%	26.4%	26.4%	
Capex as a percentage of sales	5.9%	5.3%	4.9%	4.5%	4.2%	4.0%	3.7%	3.5%	3.3%	3.1%	3.2%	3.1%	
WC as a % of sales	1.4%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	1.3%	
Free cash flow	360.6	438.0	517.9	573.1	616.6	661.6	708.2	756.2	805.5	857.8	914.2	968.0	992.2
													18,040.2
Discount factor	0.9	1.9	2.9	3.9	4.9	5.9	6.9	7.9	8.9	9.9	10.9	11.9	12.9
Discounted free cash flow (DCF)	336.6	378.6	414.5	424.7	423.1	420.3	416.6	411.9	406.3	400.6	395.3	387.5	6687.5
WACC:	8.0%												
Assumed terminal growth rate:	2.5%												
Enterprise value	11503.3												
Net Cash	476.8												
+ Participations-Minorities	(54.0)												
Net shareholder value	11926.1												
Shares in issue (m)	7.6												
DCF value per share	1570.0												

Source: Deutsche Bank estimates

Financials

Management should be able to achieve the announced set of ambitious targets, i.e. top-line growth of 15% p.a. (10% organic and 5% from acquisitions). We forecast a top-line growth of 11.2%, 10.4% and 9.8% for 2007E, 2008E and 2009E respectively. Our forecasts do not consider any acquisitions; however, we do believe that there is a high likelihood of SGS making acquisitions in the future. Such deals should be EPS-enhancing.

Figure 13: Summary of group P&L, 2003-2009E

Year end Dec (CHF m)	2003	2004	2005	2006	2007E	2008E	2009E
Turnover	2454.0	2885.0	3308.0	3821.0	4247.4	4689.3	5148.5
Growth (%)	2.6%	17.6%	14.7%	15.5%	11.2%	10.4%	9.8%
Salaries and wages	(1240.0)	(1434.0)	(1615.0)	(1818.0)	(2038.7)	(2250.8)	(2471.3)
Subcontractor's expenses	(155.0)	(181.0)	(217.0)	(263.0)	(293.1)	(323.6)	(355.2)
Other operating expenses	(663.0)	(764.0)	(834.0)	(963.0)	(1018.6)	(1102.7)	(1189.5)
EBITDA	396.0	506.0	642.0	777.0	896.9	1012.1	1132.4
EBITDA margin (%)	16.1%	17.5%	19.4%	20.3%	21.1%	21.6%	22.0%
EBITDA growth (%)	27.4%	27.8%	26.9%	21.0%	15.4%	12.8%	11.9%
Depreciation & amortization	(96.0)	(115.0)	(140.0)	(172.0)	(195.4)	(215.7)	(236.8)
EBIT	293.0	378.0	502.0	624.0	701.5	796.4	895.6
EBIT margin (%)	11.9%	13.1%	15.2%	16.3%	16.5%	17.0%	17.4%
EBIT growth (%)	130.2%	29.0%	32.8%	24.3%	12.4%	13.5%	12.5%
Net financial	10.0	6.0	5.0	(1.0)	4.8	4.8	4.8
Profit before taxes	303.0	384.0	507.0	623.0	706.3	801.2	900.4
Taxes	(68.0)	(90.0)	(119.0)	(155.0)	(179.3)	(207.3)	(237.5)
Tax rate (%)	-22.4%	-23.4%	-23.5%	-24.9%	-25.4%	-25.9%	-26.4%
Minority interests	(8.0)	(15.0)	(17.0)	(25.0)	(24.0)	(24.0)	(24.0)
Net profit	227.0	279.0	371.0	443.0	503.1	569.9	638.9
Net margin (%)	9.3%	9.7%	11.2%	11.6%	11.8%	12.2%	12.4%
Net growth (%)	108.0%	22.9%	33.0%	19.4%	13.6%	13.3%	12.1%
EPS (CHF)	29.2	37.3	49.5	58.3	66.2	75.0	84.1

Source: Deutsche Bank estimates and company data

Figure 14: Cash flow analysis, 2003-2009E

Year end Dec (CHF m)	2003	2004	2005	2006	2007E	2008E	2009E
Net income	227.0	279.0	371.0	443.0	503.1	569.9	638.9
Depreciation	96.0	115.0	117.0	141.0	195.4	215.7	236.8
Amortization of goodwill	10.0	16.0	23.0	35.0	0.0	0.0	0.0
Change in other provision	(2.0)	(21.0)	(44.0)	(37.0)	0.0	0.0	0.0
Minorities	8.0	15.0	17.0	25.0	24.0	24.0	24.0
Reintegration of taxes, interest income	67.0	90.0	0.0	0.0	0.0	0.0	0.0
Actual cash tax paid	(39.0)	(72.0)	12.0	11.0	0.0	0.0	0.0
Other adjustments	0.0	0.0	19.0	25.0	0.0	0.0	0.0
Cash flow	367.0	422.0	515.0	643.0	722.5	809.6	899.7
Net change in working capital	(31.0)	11.0	(80.0)	(31.0)	(58.7)	(62.2)	(65.8)
Cash flow from operating activities	336.0	433.0	435.0	612.0	663.7	747.4	833.9
Capital expenditure	(171.0)	(201.0)	(205.0)	(248.0)	(250.0)	(250.0)	(250.0)
Investment	(38.0)	(208.0)	(90.0)	(178.0)	0.0	0.0	0.0
Disposal of assets	32.0	12.0	7.0	(25.0)	0.0	0.0	0.0
Change in financial assets	54.0	52.0	1.0	2.0	0.0	0.0	0.0
Net cash investing activities	(123.0)	(345.0)	(287.0)	(449.0)	(250.0)	(250.0)	(250.0)
Dividend & capital reductions	(56.0)	(69.0)	(97.0)	(393.0)	(151.9)	(167.1)	(189.9)
Purchase / sale treasury shares	0.0	(15.0)	(1.0)	43.0	0.0	0.0	0.0
Actual net interest paid	(2.0)	0.0	(11.0)	(12.0)	0.0	0.0	0.0
Increase in capital	0.0	0.0	(52.0)	42.0	0.0	0.0	0.0
Other	0.0	(2.0)	(48.0)	(15.0)	0.0	0.0	0.0
Net cash financing activities	(58.0)	(71.0)	(209.0)	(335.0)	(151.9)	(167.1)	(189.9)
Net (debt) / cash at beginning of year	401.6	493.0	438.0	430.0	215.0	476.8	807.1
Change in net cash / (debt)	155.0	17.0	(61.0)	(172.0)	261.8	330.3	394.0
Other	(63.6)	(72.0)	53.0	(43.0)	0.0	0.0	0.0
Net (debt) / cash at end of year	493.0	438.0	430.0	215.0	476.8	807.1	1201.1

Source: Deutsche Bank estimates and company data

We are forecasting SGS to be in a net cash position of CHF477m by 2007E, which would allow the company to conduct a serious re-leverage of its balance sheet. Furthermore, we believe that SGS can take on net debt of 3 x EBITDA. Hence SGS should be able to spend c.CHF3.2bn on acquisitions, share buybacks or dividend increases.

Figure 15: Balance sheet analysis, 2003-2009E

Year end Dec (CHF m)	2003	2004	2005	2006	2007E	2008E	2009E
Inventories	108.0	118.0	147.0	180.0	193.4	206.8	220.3
Trade receivables	571.0	579.0	713.0	762.0	847.0	935.2	1026.7
Other receivables	135.0	132.0	134.0	182.0	195.5	209.1	222.8
Marketable Securities	55.0	10.0	10.0	9.0	9.0	9.0	9.0
Cash	471.0	446.0	521.0	230.0	491.8	822.1	1216.1
Current assets	1340.0	1285.0	1525.0	1363.0	1736.8	2182.1	2694.9
Land, buildings, equipment	415.0	493.0	586.0	656.0	710.6	744.9	758.1
Investments in associates	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Other non-current assets	23.0	21.0	62.0	38.0	38.0	38.0	38.0
Deferred tax	95.0	107.0	161.0	149.0	149.0	149.0	149.0
Goodwill	117.0	242.0	329.0	503.0	503.0	503.0	503.0
Other intangibles	30.0	62.0	100.0	141.0	141.0	141.0	141.0
Fixed assets	682.0	927.0	1240.0	1489.0	1543.6	1577.9	1591.1
Total	2022.0	2212.0	2765.0	2852.0	3280.4	3760.1	4286.0
Loans	22.0	10.0	94.0	17.0	17.0	17.0	17.0
Trade payables	299.0	329.0	329.0	402.0	424.4	446.5	468.4
Current tax liabilities	36.0	45.0	58.0	88.0	88.0	88.0	88.0
Other creditor	283.0	316.0	384.0	414.0	444.8	475.6	506.7
Current liabilities	640.0	700.0	865.0	921.0	974.2	1027.2	1080.1
Other loans	11.0	8.0	7.0	7.0	7.0	7.0	7.0
Deferred and other tax liabilities	72.0	64.0	51.0	46.0	46.0	46.0	46.0
Provisions for liabilities	209.0	185.0	367.0	286.0	286.0	286.0	286.0
Long-term liabilities	292.0	257.0	425.0	339.0	339.0	339.0	339.0
Total liabilities	932.0	957.0	1290.0	1260.0	1313.2	1366.2	1419.1
Share capital	156.0	156.0	156.0	8.0	8.0	8.0	8.0
Reserves	916.0	1073.0	1283.0	1554.0	1905.2	2307.9	2756.9
Shareholders' equity	1072.0	1229.0	1439.0	1562.0	1913.2	2315.9	2764.9
Minority interests	18.0	26.0	36.0	30.0	54.0	78.0	102.0
Total	2022.0	2212.0	2765.0	2852.0	3280.4	3760.1	4286.0

Source: Deutsche Bank estimates and company data

Free cash flow

According to the company, the business is becoming more capital intensive and capex will pick up in the coming years. SGS expects the capex to be 5-7% of sales. Currently growth capex forms circa 65% of total capex and versus maintenance capex making up for the remainder.

Figure 16: Free cash flow, 2004-09E

Year end Dec (CHF m)	2004	2005	2006	2007E	2008E	2009E
EBITDA	506.0	642.0	777.0	896.9	1012.1	1132.4
Change in NWC	11.0	(80.0)	(31.0)	(58.7)	(62.2)	(65.8)
Capex	(201.0)	(205.0)	(248.0)	(250.0)	(250.0)	(250.0)
Tax	(90.0)	(119.0)	(155.0)	(179.3)	(207.3)	(237.5)
Net financials	6.0	5.0	(1.0)	4.8	4.8	4.8
FCF	232.0	243.0	342.0	413.7	497.4	583.9
As a % of market cap	4.3%	3.6%	3.2%	3.8%	4.6%	5.4%
As a % of EV	4.6%	3.7%	3.3%	4.0%	5.0%	6.1%

Source: Deutsche Bank estimates; Priced on Feb 8th @CHF1421

Agricultural Services

Demand from new crop formulation and GMO food certification

Continuing high demand for Agricultural services

Laboratories continue their quest for high-yield crop formulation to feed the increasing global population. Growth in the agricultural sector has worked to increase demand for SGS's Agricultural services division.

Global leadership

SGS believes in an underlying market growth of 7% pa. SGS' main market is in Europe, Africa and Asia with little presence in the US market. SGS is the clear global leader in this sector, controlling approximately 70-80% of its current operating market. Competitors include government-related organizations (e.g. FGIS in the US, CGC in Canada, AWB in Australia and CIQ in China).

Agricultural services' clients are involved in the agricultural product supply chain and include traders, shippers, buyers, food manufacturers and local agricultural producers. SGS enable clients to minimize the risk involved in business transactions through a large variety of services using its global expertise located within its network. Agricultural services inspects tons of commodities shipped worldwide each year. SGS performs a variety of tasks such as cleanliness inspection, supervision, sampling, analysis, fumigation and denaturing, risk management, quality risk protection, guarantee of rejection, collateral management services, supply chain monitoring IPP (identity preservation program) or traceability. Over 100 specialized laboratories are located in key agricultural countries worldwide.

Focus on growing high margin add-on services

SGS is constantly expanding its service offerings (e.g. supply chain management (SCM)) and complementing basic inspection services with processing, trading and compliance services. Value-added services include lab, quality control and storage management outsourcing for primary processors, trade execution outsourcing for traders or regulatory compliance assurance. The add-on services that SGS seems to focus on tend to have higher margins and should have a positive impact on the profitability; furthermore, these services tend to reduce the division's trade dependency.

High growth in the GMO inspection and certification sector

Demand on GMO food certification

SGS certifies non-GMO food items. Using expertise located in key countries, Agricultural services set up dedicated processes including the testing of goods at critical points from farms to storage, transport and shipment. With non-GMO certificates, clients are able to prove that every precaution has been taken to deliver genuine and unadulterated goods. Further, SGS continuously maintains a transparent relationship with environmental pressure groups concerned with the origin of food products.

Financials

We expect these sales to grow by 5% p.a. over 2007-09E, respectively. This is slightly behind of SGS's forecast for underlying market growth of 7% p.a.; these growth rates should be driven by a combination of geographic network expansion, product mix, integrated SCM and positioning into in-land and commodity logistics services.

Figure 17: Agricultural Services sales and EBIT analysis, 2002-2009E

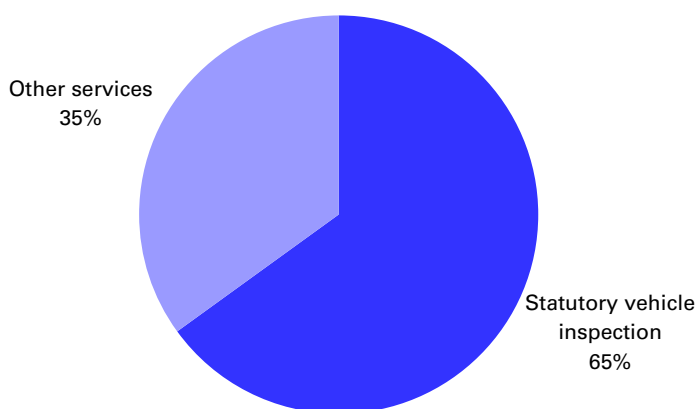
(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	250.4	241.8	257.1	294.8	316.9	332.7	349.4	366.9
CHF growth (%)	15.3%	-3.4%	6.3%	14.7%	7.5%	5.0%	5.0%	5.0%
EBIT	24.5	24.3	23.6	33.5	39.4	43.9	48.9	53.2
Margin (%)	9.8%	10.0%	9.2%	11.4%	12.4%	13.2%	14.0%	14.5%

Source: Deutsche Bank estimates and company data

Automotive Services

For governmental regulatory agencies, SGS is a long-term trusted partner operating comprehensive statutory emission and safety vehicle inspection programs. SGS delivers independent, impartial and timely information about the condition of vehicles. Commencing from the time of departure from the plant, throughout transportation, and till the approval of a lease agreement, SGS facilitates remarketing or even the disposal of vehicles. SGS delivers its services across four continents. Statutory vehicle inspections comprise the majority of sales to divisional sales; this is positive due to the stable sales pattern of this business.

Figure 18: Business split – automotive services, 2007E



Source: Deutsche Bank estimates and company data

Automotive services for governments

SGS is a preferred partner with governments for the design and operation of efficient statutory vehicle inspection programs. Statutory vehicle inspection involves intermittent checking of the general condition of vehicles in accordance with the legislation in force. The government's objective is to increase road safety and reduce vehicle emissions, which are a significant contributor to air pollution.

There are two business models for statutory vehicle inspection. The first is a decentralized structure where the tests are conducted by any garage. In that case, there is a need for information flow between the garages and the authority. SGS has an IT platform that allows it to process the information efficiently. The second is a centralized structure where inspection centers perform the tests so there is no conflict of interest, which is sometimes not the case with garages. In both cases SGS charges a fee per test, but the former generally incurs no incremental costs. In both cases, contracts tend to be long term.

Automotive services for the industry

Motor vehicle manufacturers and distributors, marine insurance companies and ocean carriers use SGS as an independent inspector of vehicles during their lengthy distribution cycles. SGS' Inspection Management System enables the transmission of detailed reports about a vehicle's condition, while moving along the supply chain and converting that data into meaningful information to identify damage trends.

SGS inspects around 12m new cars per year on behalf of the car manufacturer, transporter or insurer. The fee per car is relatively low (<CHF10 per car) and the inspection is basic. SGS's global network represents a significant advantage as cars can be manufactured in South Africa, transported to Rotterdam and then delivered to the UK. The company is the market leader in the US with a market share of circa 50% and has activities in other regions such as Europe, Korea and China.

Financials

While SGS believes in an underlying market growth of 5% p.a. of this business the company's initiatives to accelerate growth in its statutory inspection business and manufacturing services should support slightly stronger-than-underlying market growth rates. The company aims to focus and reap benefits from the several new opportunities from privatization and establishment of statutory vehicle inspection programs. It also plans to expand the client range for off-lease inspection services in Europe as well as other regions.

Figure 19: Automotive Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	211.3	211.0	187.7	200.2	220.3	231.3	242.9	255.0
CHF growth (%)	0.0%	-0.1%	-11.0%	6.7%	10.0%	5.0%	5.0%	5.0%
EBIT	13.1	20.8	20.0	25.2	29.8	31.2	32.8	34.4
Margin (%)	6.2%	9.9%	10.7%	12.6%	13.5%	13.5%	13.5%	13.5%

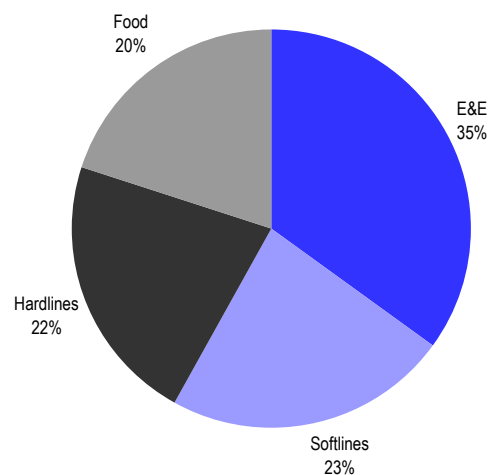
Source: Deutsche Bank estimates and company data

Consumer Testing Services

Consumer testing services have expertise in laboratory testing, product consultancy, process assessment and statistical product verification. These services are available for manufacturers, importers, exporters and retailers of consumer products on a global basis for most consumer products such as textiles, toys, footwear, hardware, homeware, electrical and electronic goods and food.

Consumer testing services cover the entire food production chain from primary production through food processing, transportation and distribution networks to the final consumer, including services for hotels and restaurants, under the food sector. Figure 21 gives the segment break-up of CTS showing that E&E is the major contributor in 2007E.

Figure 20: SGS Consumer testing sales split, 2007E



Source: Deutsche Bank estimates and company data

SGS offers comprehensive services in the following major sectors:

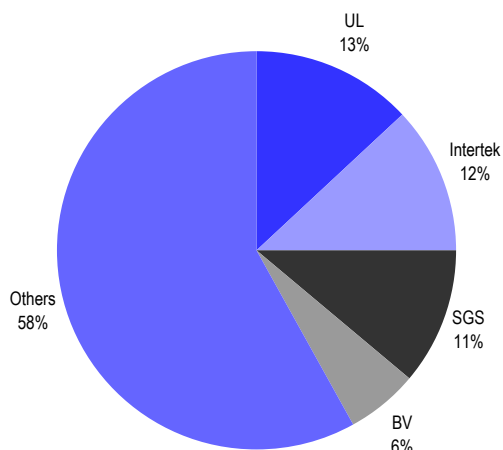
- Soft lines (estimated market size: CHF1bn): Comprises textiles and apparel, home textiles, footwear, leather and latex products.
- Food (estimated market size: CHF1bn): Includes food of animal and plant origin, beverages and bakery products.
- Hard lines (estimated market size: CHF1bn): Including toys, premiums/gifts, homeware and hardware. The latter includes DIY, hand and power tools, fasteners, lawn and garden products, automotive parts, furniture, sporting goods, and home improvement products.
- Electrical and electronics (E&E) (estimated market size: CHF2.5bn): Luminaries, audio, video and automotive E&E, household and industrial products, IT, telecommunications and components.

Market

The consumer testing market is estimated at c.EUR4bn and is very fragmented as the Top 4 has a combined share of only c.40%. The largest player is Underwriter Laboratories (UL), an independent US not-for-profit product-safety testing and certification organization which tests products for public safety (5,800 staff, 62 laboratories) ahead of lucrative entities, Intertek

(market share of 12%), SGS (11%) and BV (6%). The rest of the market includes small boutiques which are potential targets for the main players. Over the next two years, SGS estimates that the consumer testing services sector should grow at 15% CAGR due to favourable drivers: 1) Growing trade flows between Western economies and low-cost production regions, 2) Increased safety/environmental consciousness of distributors and consumers, 3) Shorter life of products and 4) Tougher and more standards/regulations.

Figure 21: Consumer testing market, 2007E



Source: Deutsche Bank estimates

Barriers to entry

The barriers to entry are very high for several reasons:

- Players in this market deliver a critical service to its clientele who wants to ensure the quality of the products they buy. A large retailer ordering shirts from Asia cannot afford to have quality or delivery issues. The retailer is therefore reluctant to switch service provider.
- Players need a global footprint in order to meet international clientele's needs
- The service providers spend considerable time with the retailer to define quality and then with the manufacturer (often before manufacturing begins) to ensure that the manufacturer will meet the required standards.

SGS offers the following testing and inspection within its Consumer testing division.

Consumer testing services

Testing involves: 1) materials testing to confirm the suitability of the raw materials and components involved in production, 2) performance testing to establish conformity to contractual requirements, 3) safety testing to reduce liability exposure against regulations, 4) eco-testing to determine restricted or hazardous substances, 5) comparative testing to benchmark one product against similar products in the market and 6) product certification to certify products against industry standards.

Consumer inspection services

Inspection includes: 1) Pre-production, initial and ongoing production checks to inspect materials and compare production samples for conformity against specification. Corrective actions can be taken before the completion of the entire consignment. 2) Final random inspection to ensure all criteria specified in the service instructions are met. 3) Retail store check to evaluate product presentation and shelf life, including sample selection for testing.

Technical assistance

Technical assistance involves: 1) code of conduct assessment to evaluate working conditions and social compliance, 2) factory quality assessment to evaluate the capabilities of a manufacturer to deliver the product quality and quantities within a specified time frame, 3) food, safety & health assessment to evaluate safety and quality issues during food production and processing, 4) regulatory advisory services to provide information on regulations, standards and quality specifications for specific products and markets, 5) training to educate client staff on quality assurance principles and other relevant topics and 6) private label support to assist retailers to launch their own product lines

Financials

The consumer testing market is expected to growth by 15% annually according to SGS; especially the environmental and social responsibility component of the business seems to show a solid growth momentum. We forecast a sales growth of 17% for the next three years based on the accelerating momentum in automotive parts testing and services, new development opportunities in emerging countries including India and Eastern Europe. In consumer testing, SGS is the second largest player globally; while Intertek is number 1 and Bureau Veritas is number 3. SGS targets to become the market leader by 2008.

Figure 22: Consumer Testing Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	283.3	272.3	360.6	476.2	592.7	699.4	818.3	957.4
CHF growth (%)	0.2%	-3.9%	32.4%	32.1%	24.5%	18.0%	17.0%	17.0%
EBIT	29.5	39.4	65.2	102.1	136.8	164.4	196.4	234.6
Margin (%)	10.4%	14.5%	18.1%	21.4%	23.1%	23.5%	24.0%	24.5%

Source: Deutsche Bank estimates and company data

Environmental Services

Environmental services meet the needs of companies relating to environmental regulatory compliance issues and reduce the risk of environmental liabilities. Due to increasing issues related to environmental pollution there is increasing demand for these services. To support government and international organizations' operations, SGS' Environmental services provide laboratory services, testing and field-based measurement and sampling as well as a range of specialty environmental services.

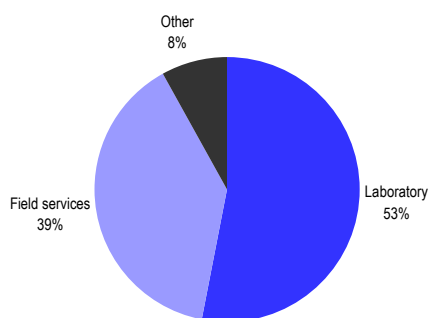
Growth drivers

Main growth for the division is expected from increased regulations and awareness of environmental issues. Furthermore, not only in developed markets the need for environmental services is increasing, but also in emerging markets environment issues have become an important issue. With the extension of the EU, the environmental regulations will become applicable also for new member states. SGS is in a good position to attract rising demand because of global reach and breadths of its service offering.

SGS service offerings include:

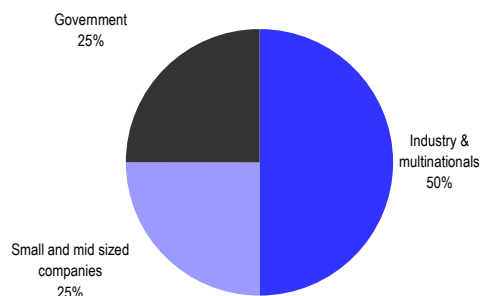
- **Laboratory analytical services:** Laboratory services focus on analyzing substances such as soils, sediments, sludge, minerals, water, wastes (hazardous and solid), air and oils.
- **Field-based services:** Field-based services are carried out by high level multi-disciplinary expertise. By this SGS ensures the continuous development of new, innovative and standardized global services while focusing on delivering the highest level of customer service. Field-based service applications cover sampling, monitoring and certification of air, water, waste, noise and vibration, indoor environmental quality and occupational health and safety monitoring. Further, under Environmental services, SGS undertakes outsourced laboratory management, environmental data management, environmental drilling, geo-technical services and training.

Figure 23: Business mix, 2006E



Source: Deutsche Bank estimates and company data

Figure 24: Client mix, 2006E



Source: Deutsche Bank estimates and company data

Strategy

SGS plans to leverage its network to enter markets with emerging regulations, develop comprehensive analytic solutions for existing mining and oil & gas clients, expand data management services to provide higher value and continue networking laboratories for efficiency.

Financials

SGS has a regional leadership in this segment and as a result of increased global environmental regulation leading to higher volumes, stable pricing in lab services and growing opportunities in the developing markets, SGS believes this market to grow by 4% pa in 2007E. In 2006, SGS entered new market regions like Gulf peninsula and Ghana and is continuing its successful expansion in emerging markets like Ghana, India, Pakistan, China, Korea, South Africa and Greece, which shows SGS' capabilities to grab the growing opportunities in these developing countries.

Figure 25: Environmental Services sales and EBIT analysis, 2003-2009E

(CHF m)	2003	2004	2005	2006	2007E	2008E	2009E
Sales	172.0	208.6	235.0	249.2	264.2	280.0	296.8
CHF growth (%)	-4.2%	21.3%	12.7%	6.0%	6.0%	6.0%	6.0%
EBIT	11.2	16.8	26.0	24.1	27.7	30.8	35.6
Margin (%)	6.5%	8.1%	11.1%	9.7%	10.5%	11.0%	12.0%

Source: Deutsche Bank estimates and company data

Industrial Services

The industrial service division provides all kinds of services related to quality and safety covering site inspection, expediting, material testing, asset management, risk management, vendor pre-qualification surveys, design reviews, commissioning, statutory inspections and certification, QA/QC services, training and technical consultancy to the industrial clients focusing on power generation & transmission, process industry, construction, transportation and logistics. The company is benefiting from the large infrastructure development in Asia which is being supported by the construction materials testing and site supervision services. BV is the leader in the industrial services market.

These services are provided during new construction or when upgrading assets as well as to support maintenance, reliability and integrity during operations. The actual service offerings can be summarized as:

- **Material testing and non-destructive examination:** This service tests whether the quality of a product matches the relevant requirements and standards. SGS has laboratories and field testing inspectors located around the world.
- **Reliability services and integrity management:** These services assess the installation, analyze the condition of assets and provide interpretation of inspection results to ensure plant integrity, safety and reliability to all plant operators. Emphasis is placed on reducing downtime and controlling maintenance cost.
- **Supply chain services:** SGS provides a broad range of supply chain services, helping customers control the input of their processes. Demand for supply chain services is mainly due to the increasing outsourcing activities carried out in the commercial world.
- **Product and import certification:** SGS can certify its customer's product against all major certification schemes in order to launch a product in a specific market. Many countries require such products to conform to national, regional or international safety standards.
- **Technical consultancy and training services:** Skills needed in an industry keep changing continuously and evolve over time due to new technical developments, new regulations and new product developments.

Financials

The industrial services division, like the oil & gas division, has benefited from rising energy prices over the past. At the same time higher construction growth in emerging economies in Asia and Eastern Europe has also boosted results. SGS believes the market to grow by 7% annually in 2007-08E. Organic growth momentum should be fueled by construction markets in China, India and Middle East, further geographical expansion in Africa, Eastern Europe and Asia, strengthening of asset integrity management in power generation. We forecast growth rates of 11%, 10% and 9% for 2007E, 2008E and 2009E respectively.

Figure 26: Industrial Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	325.4	330.1	379.8	444.8	510.4	566.5	623.2	679.3
CHF growth (%)	1.4%	1.4%	15.1%	17.1%	14.7%	11.0%	10.0%	9.0%
EBIT	39.1	34.9	46.1	58.6	74.7	87.8	96.6	105.3
Margin (%)	12.0%	10.6%	12.1%	13.2%	14.6%	15.5%	15.5%	15.5%

Source: Deutsche Bank estimates and company data

Life Science Services

Life science services are considered to be a leading contract service provider for the drug development industry for Phase I to IV clinical trials, bio-statistical management services, regulatory affairs services and bio-analytical laboratory services, as well as comprehensive testing capabilities in microbiology, analytical chemistry, biocompatibility, toxicology, microbiology, sterility, method development and stability testing to pharmaceuticals, biotechnology, medical devices and cosmetics companies worldwide. SGS serves a wide variety of life science companies including pharmaceutical, biopharmaceutical, biotechnology, and medical devices and cosmetics companies. It operates more than 30 labs and three clinical research units in Europe, Asia and America.

Quality control testing

Laboratory testing services focuses on product characterization, identification of potential contaminants and in-vitro and in-vivo toxicology studies to support clients in the qualification of materials used in the supply chain and the quality control testing of finished goods.

Agrochemical product registration services

The know-how around the registration requirements is the key success factor of SGS' comprehensive range of services for the global pesticide, fertilizer, biocide, chemical and plant production industries. SGS' services include GLP (Good Laboratory Practice) study-related services and consultancy on risk assessment and regulatory affairs.

Clinical research services

SGS runs the clinical research process enabling clinical researchers to focus on their areas of strength and expertise.

- Early stage: SGS operates its own Phase I centers. These centers have a qualified database of healthy volunteers who can be rapidly assembled for vaccine studies. SGS provides all the necessary safety and medical infrastructure needed to perform Phase I investigations such as "first-administration-to-man-test", special population studies, pharmacokinetics: bioavailability and bioequivalence studies, single ascending dose tolerance studies, multiple-dose tolerance studies, interaction studies, radio-labeled marker studies, pharmacodynamics/dose effect relationship, vaccine studies, QTC prolongation and proof of concept.
- Late stage: SGS offers comprehensive services in Phase II-IV clinical research from study design to clinical study report. SGS manages clinical trials on behalf of pharmaceutical, biotechnology and medical device companies all over Europe, North America and other regions of the world.
- Bioanalytical services: SGS has GLP-certified bio-analytical laboratories with an international reputation for the assay of drugs and metabolites. It also conducts immuno-assays in biological samples.
- Data management and statistics: SGS' Data Management and Statistics Department delivers trial design and consulting, statistical analysis, data management, and report writing services to its customers. SGS manages huge amounts of data and provides value-added information.
- Regulatory affairs: SGS employs a multidisciplinary and multilingual team of experienced regulatory affairs experts who deliver services in all regulatory aspects for customers on marketing authorization applications for both human and veterinary medicinal products.

- Health economics and pharmacovigilance: SGS provides customer services in design and conducts studies that measure and document perceived product value to support the decision making process in drug development strategies, pricing, marketing and evaluations of expected health benefits. Pharmacovigilance is a process which spontaneously reports adverse drug reactions to the authorities. SGS offers this service to its clients which helps them avoid costly setbacks proactively which can threaten both product revenue and company reputation.

Market

SGS is the market leader in France and Germany in this sector, while Life science services have been experiencing expansion in North America and the Asian region. The clinical research services have shown exceptional growth potential in North America and Quality Control Testing showed strong organic growth in Canada, the US and Belgium.

SGS believes this market to grow at an average rate of 11% pa over the next two years with major growth coming from generic market, outsourcing trends due to rising R&D costs and pricing pressure, supply chain and expansion of drug safety standards and guidelines.

Financials

Acquisitions like Medisearch International in December 2003, assets from Fresenius in March 2004 and aster.cephac in 2005. The company plans to further expand its network for QC testing labs early stage clinical research services and resources for clinical trial management. The company plans to increase utilization rates in 5-6 new labs, which were opened in Asia particularly in India, China and Hong Kong in a step to ramp up and start operations in Asian labs. Thus we forecast this division's sales to grow by 15% pa over the next three years ahead of market growth.

Figure 27: Life Science Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	57.1	59.1	106.5	125.3	193.4	222.4	255.8	294.1
CHF growth (%)	-4.2%	3.5%	80.2%	17.7%	54.3%	15.0%	15.0%	15.0%
EBIT	3.7	5.9	12.8	19.1	24.6	31.1	38.4	47.1
Margin (%)	6.5%	10.0%	12.0%	15.2%	12.7%	14.0%	15.0%	16.0%

Source: Deutsche Bank estimates and company data

Mineral Services

SGS offers services to clients engaged in exploration, mineral and coal processing, power generation, risk management and seaborne trade in bulk commodities due to its expertise in mineral services, extensive laboratory network and comprehensive sampling procedures. The mineral services market should show a growth profile of c12% per annum. SGS's mineral services division is considered the market leader with about 45% market share. Second largest player in the segment is BSI with about 15% market share. Largest customers are the major mining houses such as CVRD, BHPB, Peabody or Rio Tinto, as well as the large trading companies such as Glencore and Trafigura.

Services offering

Trade and shipping-related services: SGS offers customer services such as sampling, weight determination, hatch and hold inspection, draft survey, tally, stockpile inventory, visual inspection, laboratory testing and witnessing for custody transfer.

Exploration and mine site services: SGS is the largest global player with more than 50 laboratories around the world. SGS offer a full range of analytical services to its clients. Further, SGS has commercial third-party exploration laboratories which are ideal for off-site testing and independent services which are globally standardized and accredited. SGS also designs, builds, staffs and manages on-site laboratories.

Financing and risk management services: SGS tries to facilitate trading. SGS also speeds the process with e-certificates, which are digitalized versions of the paper certificate that is issued at the point of loading.

Technical consulting – value-chain management: SGS helps clients in mechanical sampling, performance testing, bias testing, mobile and fixed sampling augers, sampling system consultancy, laboratory design and build, value chain monitoring and management.

Technical consulting – metallurgy/mineralogy: SGS' technical experts are leaders in their respective fields and are active members of international and domestic standards bodies such as ISO or ASTM. Internally, SGS operates to define Standard Operating Procedures (SOPs) and these ensure a uniform level of quality across all global affiliates. Services offered are process and flow sheet development for the recovery and purification of metals; HIPAL: pilot plants, test modifications to existing flow sheets without disturbing regular plant production; characterization of pilot-plant products; tailings and waste-rock characterization; geo-technical studies and diamonds: exploration to evaluation services.

Financials

The sector as a whole has achieved long-term (1950-2004) growth of 2.8% pa. SGS sales have been growing at a CAGR of 10.8% over a period of 1998-2006. The globalization of the world economy should continue in the foreseeable future to support a trade growth ahead of total production growth. Further we saw a solid demand in energy minerals, non-ferrous metals and industrial minerals.

Figure 28: Mineral Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	268.3	279.9	319.5	393.7	467.0	518.4	570.2	621.5
CHF growth (%)	30.2%	4.3%	14.1%	23.2%	18.6%	11.0%	10.0%	9.0%
EBIT	27.5	35.5	46.3	63.1	80.5	92.3	103.2	113.1
Margin (%)	10.2%	12.7%	14.5%	16.0%	17.2%	17.8%	18.1%	18.2%

Source: Deutsche Bank estimates and company data

Oil, Gas and Chemical Services

SGS' oil, gas and chemicals services are considered to be the leading provider of trade inspection and testing services, quality assurance, risk management and technical support services to the petroleum and chemical industries involving crude oil, petroleum products, chemicals and gases. SGS's largest division accounts for 21% of total revenues in 2006. The primary services include: quantity and quality control during custody transfer, laboratory testing, automatic sampling, static and dynamic calibration, gas technical services for the conditioning and purging of gas carriers, lubricant predictive maintenance testing, packing and forwarding of samples, tank and container inspection services, offshore support services and logistics, together with contract laboratory and terminal manning and management.

Market and competition

Multinational oil companies typically split their inspection and testing work between two or more suppliers to sustain competition. SGS, together with Caleb Brett – a division of Intertek – are regarded as market leaders in this industry. SGS ranked #1 in this sector with circa one third of the global market share. The market is based on long-term contracts (one to five years) and should grow at an average 5% per annum. Contracts are either rolled-over or tendered at the end of the contract period (long lead time) or are "spot" nominations, which are sales intensive and performance related (short lead time). The breakdown between the two is roughly two thirds/one third.

Services

- Field inspection, laboratory testing and blending: Field inspections are made as products are loaded and discharged from ships, rail and road trucks, containers and pipelines, and at storage tank transfers. Further, services are available to producers before the delivery; these include sample testing for internal quality assurance and end-control purposes.
- Cargo treatment – petroleum: This service reduces the lead time between the change in commercial situation and the client reaction.
- Outsourcing

Financials

SGS has witnessed a strong organic growth since 2003 driven by high and volatile oil prices and production capacity increases in Asia in the Middle East. SGS' clients faced challenges to meet the rising demand particularly in India and China. We expect this division's sales to grow at an average c.10% pa over the next three years ahead of the market growth expected to be 5% pa, driven among other reasons by the diversification of SGS's service portfolio to accommodate the future growth of alternative fuel types (LNG, bio-fuels).

Figure 29: Oil, Gas and Chemical Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	398.8	439.1	574.6	635.3	783.4	877.4	965.1	1042.4
CHF growth (%)	-3.9%	10.1%	30.9%	10.6%	23.3%	12.0%	10.0%	8.0%
EBIT	31.1	47.9	68.6	79.4	112.6	131.6	147.7	160.5
Margin (%)	7.8%	10.9%	11.9%	12.5%	14.4%	15.0%	15.3%	15.4%

Source: Deutsche Bank estimates and company data

Systems and Services Certification

SGS holds #1 position in this segment with 12% market share.

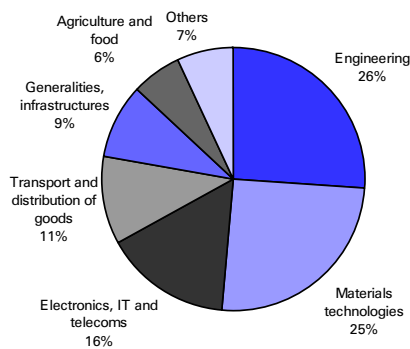
SGS is considered to be the leader in the management systems and services certification market. Services are spread over 70 countries and ISO 9000 accreditation is available in over 30 countries. SGS also offers auditing as well as training in a wide range of management systems.

SGS is the number one player in this market and has a market share of 12%, with Bureau Veritas, a very close competitor is not much behind. The market is fragmented with five global and leading players which have a cumulative market share of over 50%. According to SGS, the segment should grow by 9% over the near term due to: 1) Increasing and tougher specific standards, which are supported by countries, industry organizations and companies. 2) Continued globalization and the necessary mutual trust that goes with it will continue to require certification against international standards.

We estimate that around 25% of revenues are recurring as the life of an ISO standard certification is generally limited to three years. A cycle is composed of a certification audit in year one, followed by surveillance visits in the following years.

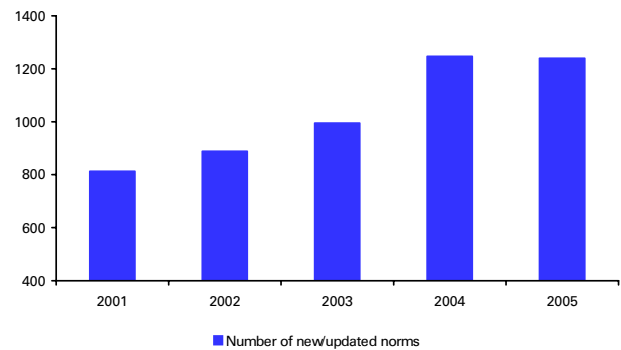
SGS has built a very strong position in the mindset of the clients who are into ISO (International Standard Organization) certification. ISO is the world's largest developer of standards with over 15,000 international norms at end-2005. These standards are developed to enhance quality, safety, reliability, efficiency of the products/services and systems.

Figure 30: World norms breakdown by sector in 2005

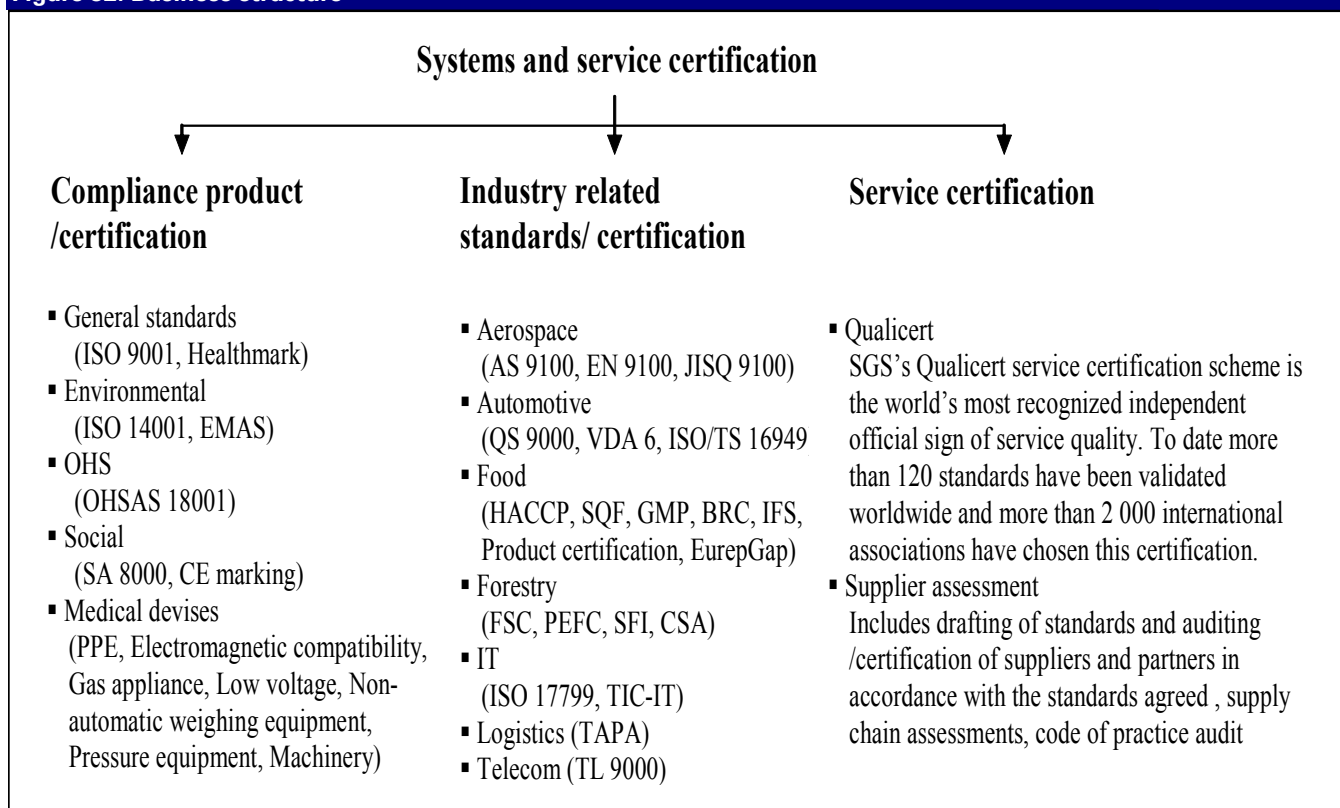


Source: Deutsche Bank estimates

Figure 31: New/updated international norms



Source: Deutsche Bank estimates

Figure 32: Business structure

Source: Company data

Financials

In 2006, the sector was successful in growing revenues from the traditional compliance schemes (ISO 9001, ISO 14001) faster than the overall market as the group was properly positioned in geographies with expanding economies and industrial activity. The company is also focusing on offering customized solutions and launched several new products like Six Sigma benchmarking standard and Six Sigma program certificates. We expect that the effect of the combination of new service line introduction, volume leverage, and reduced back-office administrative costs through internal Six Sigma projects will continue to benefit SGS over the next years. SGS already enjoys a high operating margin in this market as it is a low capacity business and expect it to improve further slightly from 2006E level of 18.5% to 18.7% by 2009E.

Figure 33: System and service certification services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	208.1	229.7	235.4	274.0	318.7	360.1	403.3	447.7
CHF growth (%)	4.9%	10.4%	2.5%	16.4%	16.3%	13.0%	12.0%	11.0%
EBIT	23.8	34.7	30.5	46.5	58.9	67.0	75.4	83.7
Margin (%)	11.4%	15.1%	13.0%	17.0%	18.5%	18.6%	18.7%	18.7%

Source: Deutsche Bank estimates and company data

Trade Assurance Services

Trade services are related to parties involved in the trade as well as regulatory authorities

Globalization drives demand

As world trade expands across geographical boundaries, many economies enter global markets with their own expertise as well as demands. Each player expects an assurance for receiving the correct deal while government authorities satisfy their requirements. Increasing global trade and vigilance of stakeholders have increased the demand for Trade assurance services.

We expect this market to be worth CHF520m in mid-2006. SGS caters to c.50% of the global market share and is ranked #1 in the world. Global rank #2 was held by Intertek with c.30% market share. We expect this market to grow at circa 8% in the future. Barriers to entry are high due to the need for a global inspection network, expertise in a wide range of products and the ability to handle significant volume.

Trade assurance services offer services to governments and international institutions to facilitate international trade, protect national interests, enhance tax and customs revenue collection, and support the sustainable management of natural resources and international assistance programs.

The demand for these trade assurance services is mainly due to the need of governments in emerging countries to secure fiscal revenue from international trade. For the last 35 years, SGS has provided these governments with import verification programs (pre-shipment inspection) and is considered to be the industry leader. Trade liberalization and complex international supply chains have increased demand for more sophisticated and specific trade assurance services.

SGS's business is diversified with a total of 23 contracts and earlier the three largest contracts represented less than 50%. But with the recent loss of Nigerian contract which was the largest followed by Venezuelan and Cameroon, the division's sales were affected. Now no contract represents more than 10% of divisional sales. The company's margin would be lowered due to the loss of high margin contracts and company plans to slowly regain its margins by replacing these contracts by providing more IT specific solutions. The pre-shipment inspection business still represents about 60% of the division's revenue.

The core trade assurance services offered by SGS are:

- **Import verification programs:** These comprehensive programs enable the proper identification of goods prior to shipment with regard to quality, quantity, tariff classification, import eligibility and the provision of valuation information for customs purposes.
- **Risk management services:** SGS' Risk management services enable government agencies to introduce controls based on the actual knowledge of transactions as well as effectively manage modern investigation tools such as cargo scanning equipment. This is done with the help of SGS Profiler™, an automated risk management system comprising trade and revenue risk data collected by the SGS global network and the specialized knowledge of Trade assurance services.

With the use of its ValuNet™ system, SGS enables customs administrators to identify valuation fraud whilst, at the same time, meeting the requirements of the WTO Agreement on Customs Valuation. SGS' ValuNet™ uses the SGS global network to investigate declared customs values and build a client specific valuation reference system.

- **Trade facilitation:** The main function of this service is to build trust between trade institutions and governments. Trade assurance services offer governments and enterprises tailor-made services to ensure compliance with national and international regulations. These services balance the economic policy issues of governments and the commercial responsibility of enterprises with a complete range of services to improve competitiveness and access to international markets. Core services of Trade facilitation:
 1. **Transit monitoring:** Enables governments to maintain effective control of transit trade.
 2. **Trade compliance and security services:** SGS continuously develops these to provide trade participants with modern monitoring and certification tools.
 3. **Cargo scanning systems:** This tracks goods and increases the safety and security of goods while reducing the incidence of duty avoidance.

- **Sustainable development services:** This service concentrates on the sustainable management of natural resources and strengthens international development assistance. The protection of natural resources and the effectiveness of international aid are highly debated global issues. To cater to the above needs, SGS aims to build trust among stakeholders through the development of highly effective monitoring programs. The core Sustainable development services are:
 1. **Sustainable forestry programs:** These include independent verification, monitoring and certification of the entire management and utilization cycle of forest resources.
 2. **Climate change program:** This program certifies the global climate change mitigation process and international greenhouse gas emissions trading. SGS can validate greenhouse gas emission reduction projects and verify/certify actual emissions.
 3. **Aid monitoring services:** This service addresses the need for improved governance, accountability and transparency in the implementation of both public and private economic development programs and projects. Aid monitoring services include the audit of projects and programs, review of procurement processes and decisions, and the benchmarking of non-governmental organizations.

Financials

Trade assurance services have been difficult due to major emerging countries creating their own structures for pre-shipment inspection, resulting in contract losses. In 2006 also division's sales hit two major contract losses (Nigeria and Venezuela). Although this division has witnessed declining sales in the past, EBIT has declined comparatively less due to the company's ability to successfully cover the contract mobilization costs through decisive action, productivity improvements on continuing contracts and new contract wins and renewals. We expect the company to continue to migrate to newer services, with expansion in evolved PSI offerings, as PSI will continue to weigh on the division's results. We have estimated a c.3.5% growth from 2007 onwards as the traditional PSI market is declining and the EBIT margin to revive and reach 15% by 2009E from 13.7% in 2006.

Figure 34: Trade Assurance Services sales and EBIT analysis, 2002-2009E

(CHF m)	2002	2003	2004	2005	2006	2007E	2008E	2009E
Sales	209.7	219.5	255.4	228.6	169.0	174.9	181.0	187.4
CHF growth (%)		4.7%	16.4%	-10.5%	-26.1%	3.5%	3.5%	3.5%
EBIT	23.3	45.1	61.5	48.5	23.2	24.5	26.3	28.1
Margin (%)	11.1%	20.5%	24.1%	21.2%	13.7%	14.0%	14.5%	15.0%

Source: Deutsche Bank estimates and company data

Risks

The main risks to our investment case are:

- Increased protectionism
- Reputation risks
- Currency fluctuations
- Country risks
- General GDP development
- Potential change in the shareholder structure
- Slowdown in international trade

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Appendix 1

Important Disclosures

Additional information available upon request

Disclosure checklist

Company	Ticker	Recent price*	Disclosure
SGS	SGSN.VX	1421.00 (CHF) 8 Feb 07	6,8,14

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

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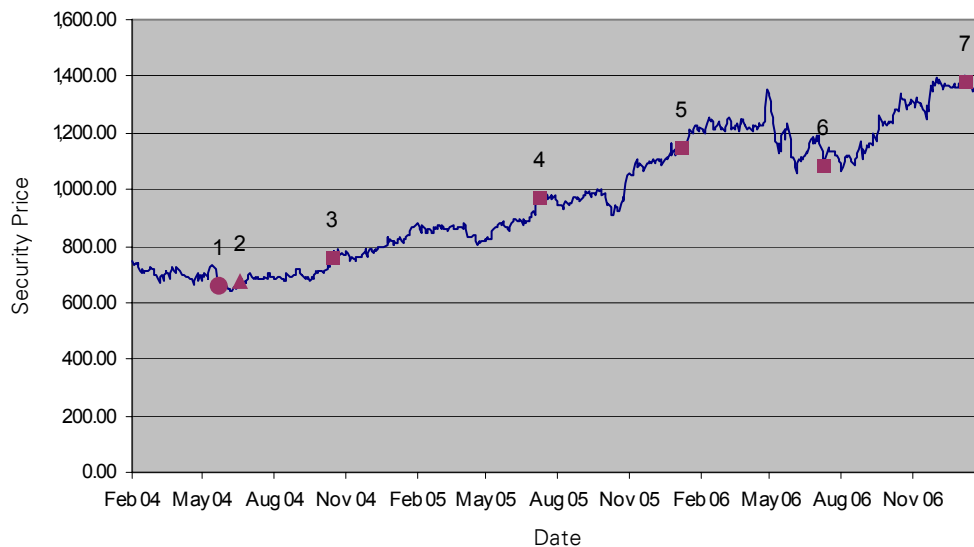
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Historical recommendations and target price: SGS (SGSN.VX)

(as of 2/8/2007)



Previous Recommendations

- Strong Buy
- Buy
- Market Perform
- Underperform
- Not Rated
- Suspended Rating

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- Hold
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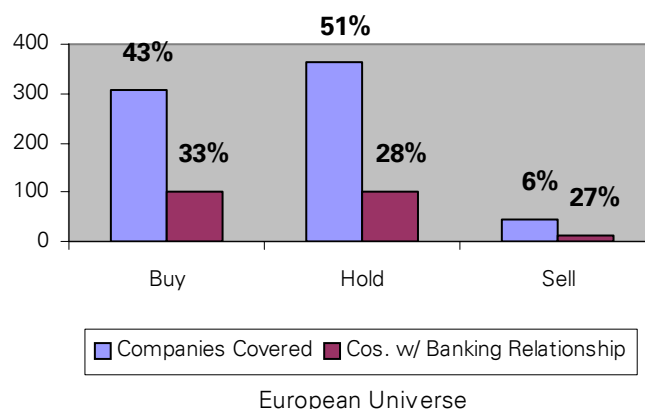
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Deutsche Bank AG/London**European locations****Deutsche Bank AG London**

1 Great Winchester Street
London EC2N 2EQ

Tel: (44) 20 7545 8000
Fax: (44) 20 7545 6155

Deutsche Bank AG

Herengracht 450
1017 CA Amsterdam
Netherlands

Tel: (31) 20 555 4911
Fax: (31) 20 555 4428

Deutsche Bank AG

Uraniastrasse 9
PO Box 7370
8023 Zürich
Switzerland

Tel: (41) 1 224 5000
Fax: (41) 1 227 3100

**Deutsche-Bank AG,
Secoursale de Paris**

3, Avenue de Friedland
75008 Paris Cedex 8
France

Tel: (33) 1 44 95 64 00
Fax: (33) 1 53 75 07 01

**DB Corretora - Sociedade
Corretora de Valores
Mobiliários, SA**

Rua Castilho 20-5
125069 Lisbon
Portugal

Tel: (351) 21 311 1200
Fax: (351) 21 353 5241

Deutsche Bank AG, Helsinki

Kaivokatu 10 A, P.O.Bvox 650
FIN-00101 Helsinki
Finland

Tel: (358) 9 25 25 20 0
Fax: (358) 9 25 25 25 85

**Deutsche Bank AG
Equity Research**

Große Gallusstraße 10-14
60272 Frankfurt am Main
Germany

Tel: (49) 69 910 41339
Fax: (49) 69 910 34225/7

**Deutsche Securities
S.V.B, S.A.**

PO de la Castellana, 42
7th Floor
28046 Madrid
Spain

Tel: (34) 91 782 8400
Fax: (34) 91 782 8465

Deutsche Bank AG

Hohenstaufengasse 4
1010 Vienna
Austria

Tel: (43) 1 5318 10
Fax: (43) 1 5318 1114

Deutsche Bank Sim S.p.a

Via Santa Margherita 4
20123 Milan
Italy

Tel: (39) 0 24 024 1
Fax: (39) 0 24 024 2636

Deutsche Bank AG

Stureplan 4 A, Box 5781
S-114 87 Stockholm
Sweden

Tel: (46) 8 463 5500
Fax: (46) 8 463 5550

Deutsche UFG

10 Povarskaya Street
121069 Moscow
Russia

Tel: (7) 501 967 37 27
Fax: (7) 501 967 37 30

International locations**Deutsche Bank Securities Inc.**

60 Wall Street
New York, NY 10005
United States of America

Tel: (1) 212 250 2500

Deutsche Bank AG London

1 Great Winchester Street
London EC2N 2EQ
United Kingdom

Tel: (44) 20 7545 8000
Fax: (44) 20 7545 6155

Deutsche Bank AG

Große Gallusstraße 10-14
60272 Frankfurt am Main
Germany

Tel: (49) 69 910 41339

Deutsche Bank AG

Deutsche Bank Place
Level 16
Corner of Hunter & Phillip Streets
Sydney, NSW 2000
Australia

Tel: (61) 2 8258 1234
Fax: (61) 2 8258 1400

Deutsche Bank AG

Level 55
Cheung Kong Center
2 Queen's Road Central
Hong Kong

Tel: (852) 2203 8888
Fax: (852) 2203 6921

Deutsche Securities Inc.

Level 20, 2-1-1 Nagatacho
Sanno Park Tower
Chiyoda-ku, Tokyo 100-6171
Japan

Tel: (81) 3 5156 6701
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