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Morgan Stanley double upgrades B&Q owner Kingfisher even though it expects turnaround plan to fail

Morgan Stanley has double upgraded Kingfisher PLC (LON:KGF) despite being convinced that the turnaround strategy implemented by the B&Q and Screwfix owner last year will ultimately fail.

Analysts at the bank expect it to become clear, probably in 2018, that 'One Kingfisher' hasn't worked, at which point it thinks investors will have to look for new ways to value the group.

"It seems to us that, if One Kingfisher fails, then investors will increasingly start valuing the group on its assets, not its earnings," wrote Geoff Ruddell in a note to clients this morning.

READ: Kingfisher drops as first-quarter like-for-like sales fall 0.6%, hit by weak trading in France

The analyst believes that it is "hard to create a credible sum-of-the-parts valuation" that suggests shares are worth much less than 400p.

Ruddell adds: "Kingfisher has £3.4bn of freehold property, £0.6bn of cash and a surplus in its pension scheme.

"If Screwfix is worth, say 15x earnings, the other key operating companies would have to be valued on single digit PE [price-earnings] multiples to be worth less than 400p. The current share price would imply they are almost worthless."

Given that, Ruddell has upped his price target to 380p - the sum-of-the-parts valuation discounted by 10% - and he also reversed his rating to 'overweight' from 'underweight', although he admits that it isn't an exact science.

"We believe that the biggest downside risk to this call is timing - it's hard to identify exactly when investors will start to focus on asset backing.

"Also, if One Kingfisher proves only partially successful, neither driving a shift in focus to asset backing, nor the increase in profitability that management is aiming for, the shares could yet drift down further."

The double upgrade didn't do much for Kingfisher shares today though; they were down 1.3% to 298p in mid-morning trade.

Company Synopsis:
Kingfisher is Europe’s leading home improvement retail group and the third largest in the world, with leading market positions in the UK, France, Poland, Turkey and China.
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