Thursday, 23rd November 2017

Morning Round Up

Fed Minutes - Inflation puzzle continues

The minutes from the last Federal Reserve meeting were released yesterday and continued what has been a pretty consistent theme this year. Fed officials continue to remain confident in the labour market and above-trend economic growth but remain confused about the lack of pick-up in inflation. Several officials even want to see inflation on an upward path again before lifting rate sin 2018. All officials are comfortable with the upcoming December hike but it is the 2018 trajectory that is now the focus. Currently, the Fed is guiding for 3 hikes in 2018. Some major investment houses have published their 2018 outlooks recently and are calling for four hikes. But markets will be watching the December meeting closely to see if any officials will market down their 2018 economic projections, in particular their inflation outlook.

China - Equity investors suffer the jitters

Chinese stocks fell by over 2% last night as recent bond market weakness and concern of state crackdown on financial leverage continues to scare investors. Yield on sovereign debt has spiked recently with the 10 year rate moving about 4%. Similarly on the corporate side, 5 year corporate yield is now at 5.3%, the highest in three years. Investors are quite cautious and are expecting more liquidity tightening from the PBOC and Chinese authorities. Here at Cantor, we had been guiding that the state was likely to resume its crackdown post the Party Congress in October. This appears to be what is happening and Chinese growth should slow into year end. Presently, this volatility in China is not too much of a worry for global markets presently but will require monitoring in the near-term.

UK Budget - Tories try to win back the electorate

Phillip Hammond gave his budget speech to Parliament yesterday, in what many analysts have perceived as the Tory attempt to win back the young vote. Despite sticking to his notion of balancing the books by 2025, Hammond loosened the spending reins a little. Most notably, he abolished stamp-duty for first time buyers of homes worth up to £300,000. At the same time he commissioned a review into the gap between building approvals and number of homes built. UK housebuilders fell on the announcement as markets had been expecting significantly more measures to stimulate the housing market.

UK Homebuilders - Price Chart

Source: Bloomberg, CF Research November 2017

Key Upcoming Events

30/11/2017 OPEC meeting

Market View

Asian markets were down overnight as Chinese worries spread across the region. European equities opened lower on the back of this. EURUSD moved back above €1.185 on the back of relatively dovish Fed minutes. This move is likely to weigh on European exporters. We are sticking with our year end call for EURUSD to be in the $1.18 - $1.20 range. US markets continue to be range bound as markets make up their mind about the likelihood of US tax reform. Market focus today will be on German Q3 GDP, UK preliminary Q3 GDP estimates and Eurozone PMIs. Trading volume is likely to be light as the US moves into Thanksgiving period.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	23526	-64.65	-0.27%	19.04%
S&P	2597	-1.95	-0.08%	16.00%
Nasdaq	6867	4.88	0.07%	27.57%
Nikkei	22,523	106.67	0.48%	17.83%
Hang Seng	29,708	-295.55	-0.99%	35.03%
Brent Oil	63.07	-0.25	-0.39%	11.00%
WTI Oil	57.85	-0.17	-0.29%	7.69%
Gold	1288	-4.14	-0.32%	12.24%
€/$	1.1844	0.0022	0.19%	12.62%
€/£	0.8903	0.0031	0.35%	4.31%
£/$	1.3303	-0.0022	-0.17%	7.80%

	Yield	Change
German 10 Year	0.356	0.007
UK 10 Year	1.261	-0.014
US 10 Year	2.319	0.000
Irish 10 Year	0.578	0.010
Spain 10 Year	1.47	0.018
Italy 10 Year	1.772	0.007

Source: Bloomberg, CF Research November 2017

Vinci - Re-iteration of investment case

Closing Price - €86.60

News

Vinci is up 17% since we included it in our Core Portfolio. It is currently trading at €86.60. From a 12 month perspective we believe €98 represents a fair value target price, implying a further 13.1% upside. The longer term investment case also remains very compelling. Please see below for a reiteration of our investment case.

Intro

Vinci is a very high quality company with an excellent management team and a long historical track record of solid earnings growth and accretive acquisitive activity. The company retains a mixture of defensive assets such as Toll Roads and Airports which are complemented by higher growth activities such as contracting, building and financing infrastructure projects. We have been highlighting our belief that 2017 represents the first true year of recovery for the European economy with strong growth across all countries (excluding Greece) driven by increased confidence on behalf of both consumers and governments. This strong growth should benefit both the established assets through increased traffic but also lead to strong revenue growth on the contracting and financing side.

Company History

Vinci was formed in 1899 as the Societe Generale d'Enterprise. In 2000, the company merged with GTM group to become Vinci. Today it is a global leader in infrastructure and construction employing approx. 180,000 people with operations in 100 countries. France remains its major base of operations with 60% of revenue stemming from there. Overall 77% of revenue is derived from Europe with the remainder a mix of Asia Pac (5.8%), Russia(6%), North America (4%), Africa (3.5%) and South America (3%). As such, Vinci does not represent a high degree of FX exposure. We believe the euro will moved higher against most currencies in H2/17. While we believe this will not be much of a obstacle to European equities due to the strength of the recovery, we believe this removes any potential headwind that may occur. It also makes Vinci a reasonably pure play on the European recovery.

Business Model

The company is structured into two divisions – **Concessions** (17% of Group revenue & 72% of EBITDA) and **Contracting** (83% of Group revenue & 27% of EBITDA). **Concessions** designs, finances, constructs and mange transport infrastructures and public amenities, usually under the auspices of a public private partnership. It operates in areas such as motorways, bridges, tunnels, railways and stadiums. It is the smaller of two divisions but it is a very high margin business (2016 EBITDA margin of 68%) and generates 72% of group EBITDA. The assets in this division are predominantly European based and the group is organised into three further subdivisions; **Autoroutes, Airports and Other Concessions** (including Highways, Railways and Stadium). Autoroutes (86% of Concessions EBITDA) operates the biggest toll motorway network in Europe with 4,422km in total carrying over 2 million drivers a day. Airports (13% of Concessions EBITDA) manages 35 airports worldwide and handles approx. 132.3m passengers. Other Concessions (1% of Concessions EBITDA) is further subdivided into Highways (which has approx. 30 road assets around the world), Railway (which operates high speed rail lines) and Stadium (which owns 5 stadiums in France and the UK). **Contracting** also contains three divisions; **Energies, Eurovia and Construction**. Energies is the industrial contracting division and generates 40% of Contracting EBITDA. Eurovia is responsible for civil contracting in rail & road and management of quarries (26% of Contracting EBITDA). Construction is the division responsible for implementing major contracts (34% of EBITDA)

Investment Case

In terms of reason to buy Vinci there are several which we wish to highlight. Firstly there is the quickening pace of European economic growth. This should ensure **above average traffic growth** for the assets Vinci already owns, most notably roads and airports. These assets form the overwhelming majority of Vinci's EBITDA. As European economic growth comes through traffic through these assets should increase. Rates on these assets, particularly on autoroutes, should **grow above inflation** due to compensation clauses in contracts that Vinci signed. Lastly toll roads represent an asset with **sizeable operational leverage** – any traffic increase automatically means margin enhancement. Secondly, Vinci has recently **won some high profile contracts** including the Grand Paris Express Program which seeks to modernise Paris's urban transport network. It involves the building of an additional 4 metro lines, about 200km and 68 stations, a ring route around Paris and new lines serving outlying suburbs. According to estimates, the project will invest €26bn. Vinci has already been awarded two major contacts within the project for €496m and €926m (10% of its current backlog). Expectations are that contract awards will ramp up in 2018 and we expect Vinci, as the major domestic infrastructure specialist, to benefit.

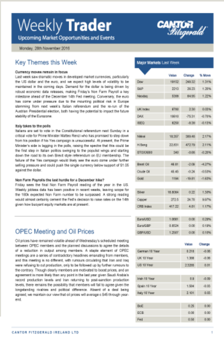
From a capex perspective Vinci is at the latter end of a heavy investment cycle with Capex expected to move from €844m in 2017 to €1.2bn in 2018. However, **after 2018 it is expected to decline** (€800m by 2021)and should be less of a headwind going forward. It is expected its European autoroute capex will halve by 2020 and enter into just maintenance only by 2024. As this occurs **free cash flow should increase dramatically, allowing for potential dividend increases and higher margin growth.** Vinci currently pays a dividend of 3.1% and has a FCF yield of 7.3%. These numbers will improve as capex declines. Vinci currently has €4.5bn in cash on its balance sheet with a net debt/EBITDA position of just under 2x. This is very healthy and Vinci has a long history of accretive acquisitions properly executed by an excellent management. Management recently stated it remains committed to M&A. From a

Vinci - Re-iteration of investment case Closing Price - €86.60

financing perspective it is also quite solid with interest cover of 6.17x. Infrastructure companies tend to have an inverse relationship with yields – when yields rise they do badly as they generally pay decent dividends and investors perceive their financing ability to be impacted. We believe this is less of a factor for Vinci. European yields are moving from such a low base and Vinci's balance sheet is very strong. This was backed up during the recent tick up in yields in which Vinci outperformed the broader European market. Summary Vinci is a very solid company that generates 7-9% EPS growth on a consistent basis. We would expect this to increase, possibly to low double digit, on the back of declining capex, new contracts and the strength of the coming European recovery. Infrastructure companies have outperformed the broader market from a historical perspective. Traditionally, because it is a sector that is not correlated with the overall market, it has outperformed in down markets also. It retains excellent diversification qualities for an investor's portfolio. Vinci has an excellent management team who are committed to earnings accretive acquisitions. It is currently trading at €86.60 which we believe represents a good buy-in point and a further 12-15% potential upside based on 7-9% EPS growth. From a valuation perspective it is trading at an FY17 P/E of 18.29x dropping to 16.7x in 2018. This is a slight premium to its 3 year average but still at a discount to its peers in the sector. FY17 estimated dividend is 3.06%, rising to 3.32% in 2018. We believe Vinci represents the ideal model by which to play a domestic European recovery.

Will Heffernan | Investment Analyst

Cantor Publications & Resources



Weekly Trader

On Mondays, we release our weekly note in which we provide a view on equity markets for the coming days, and highlight a number of equities which we believe provide exposure to the important themes unfolding in the markets. Our in-house Investment Committee meets on a weekly basis to craft this strategy, thereby allowing clients to dynamically position portfolios to take advantage of the most up to date market developments.

[Click Here]

Monthly Investment Journal

Each month our Private Client and Research departments collaborate to issue a publication which highlights the performance of our flagship products, funds and our Core Portfolio, including the Green Effects fund, most recent private equity deals and structured product investment opportunities.

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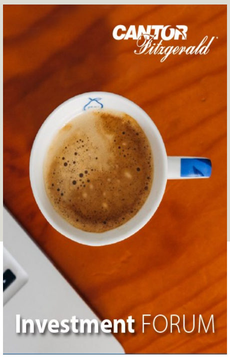

Investment Forum

Through our investment Forum we bring you the latest market news, investment insights and a series of informative articles from our experts.

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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

VINCI SA: VINCI is a global player in concessions and construction with expertise in building, civil, hydraulic, and electrical engineering

Historical Recommendation:

VINCI SA: We initiated coverage of Vinci SA with an Outperform rating, on 25/08/2017.

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