Daily Note

Views, news and topics from today's markets

CANTOR Fitzgerald

Thursday 15th March 2018

Morning Round Up

Kudlow First Words as Trump's new Economic Advisor

Larry Kudlow will be the latest addition to the Trump administration, replacing the recently resigned Garry Cohn as chief economic advisor. Kudlow , an economist and CNBC commentator, has previously worked on Wall Street as an economist with Bear Stearns and in the White House under Ronald Regan. Kudlow, who has been regarded as an advocate for free trade and tax cuts, appeared on the CNBC minutes after the announcement. Here he highlighted his views on the dollar strength , tax cuts and a tougher line with China. Stating "I would buy King Dollar and I would sell Gold", Kudlow spoke at length on the US currency and its current undervaluation while noting that its stability is key. While White House officials generally avoid commenting on monetary policy due to the fear of the potential interference with Federal Reserve independence, Kudlow added his opinions, advising the FED not to "overdo" hikes to the interest rate. He went on to speak on how the Trump administration would pursue a second phase of tax over hall. This would include the lowering of the capital gains rate and ensuring tax cuts for individuals are permanent. Importantly Kudlow was supportive of Trumps trade policies. When speaking on potential tariffs with China, he stated "China needs a comeuppance of trade".

This harder stance on trade is contrary to his previous comments and criticisms of the administrations approach. Earlier this month he voiced the opinion that Trumps trade logic was flawed and would put up to 5 million manufacturing and related jobs at risk. He has however been quite supportive of Trumps tax cutting policy and was one of the few on wall street who forecast the markets positive reaction to election result. It is difficult to see the controversial commentator not fall in behind Trump and his ever changing administration.

Unilever move HQ to Rotterdam

Political commentators are quick to point out the damage caused to Theresa May and post Brexit Britain by the decision taken by the Unilever board to move its primary HQ to Rotterdam. But it's not so clear cut. Number 10 has some retort to its critics citing it as little more than a brass plate move along with the fact that the announcement did not cite Brexit as a reason behind the decision. In the statement released this morning, Unilever confirmed that it was simplifying its legal entities. Currently it operates two, an N.V. and a PLC, with the group moving forward as a N.V. incorporated in Rotterdam. The board sighted the volume of shares in N.V. outweighed the PLC at approx. 55% versus 45% and the N.V. listing trades with greater liquidity. Unilever will remain listed in London, Amsterdam and New York. Further good news for Mrs May, the UK will retain the HQ of two of the three sub divisions of Unilever, the Beauty and Personal Care Division and the Home Care Division while Food and Refreshment Division remains based in Rotterdam. The announcement confirmed the 7,300 people in the UK and 3,100 people in the Netherlands will be unaffected by the changes. While this won't be as big a blow as it could have been to Mays post Brexit Britain, it will undoubtedly be pulled into the political spot light at will by the Brexit opposition irrespective of managements aforementioned reasoning.

Source: Bloomberg, CF Research March 2018

Key Upcoming Events

16/03/2018 Eurozone Inflation

Market View

On news of Trumps latest appointment, Asian market fluctuated overnight before finishing relatively flat. US stocks dropped yesterday evening. European stocks have opened up this morning. The euro weakened relative to the dollar, as the US 10 year rose slightly to 2.81%. The German 10 year is down to 0.59%. The Yen has strengthened while gold has dropped marginally.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	24758	-248.91	-1.00%	0.16%
S&P	2749	-15.83	-0.57%	2.84%
Nasdaq	7497	-14.20	-0.19%	8.60%
Nikkei	21,804	26.66	0.12%	-4.22%
Hang Seng	31,541	106.09	0.34%	5.42%
Brent Oil	64.82	-0.07	-0.11%	-3.07%
WTI Oil	61.06	0.10	0.16%	1.06%
Gold	1323	-1.71	-0.13%	1.56%
€/$	1.2363	0.00	-0.04%	2.98%
€/£	0.8854	0.00	-0.05%	-0.30%
£/$	1.3963	0.00	0.01%	3.33%

	Yield	Change
German 10 Year	0.591	0.00
UK 10 Year	1.439	0.00
US 10 Year	2.8152	0.00
Irish 10 Year	1.036	0.00
Spain 10 Year	1.379	-0.02
Italy 10 Year	1.99	-0.0240

Source: Bloomberg, CF Research Mar 2018

Prudential - Asian footprint drives strong profitability

Closing Price - £19.18

News

Prudential released a strong set of results yesterday that saw the stock trade up 5.81% on the day to £19.31. Markets reacted positively to management's confirmation, of the previously flagged, decision to spin out the UK & European business under the M&G Prudential brand. It is intended to be a leading savings and investment business in the UK and Europe well positioned to target growing customer demand for comprehensive financial solutions. In addition to this news, the core business performed strongly growing operating profits (OP) by 6% to £4.6bn and new business profits by 12% on a constant currency basis as well as net profit up 21% yoy at £2.39bn. Cash remittance to group was up 4% yoy to £1.7bn, with £1.1bn of this paid out to shareholders in a dividend reflecting a yield of 2.60%. The group's capital position was also strong with £13.3bn in estimated surplus representing a coverage ratio of 202%.

Asia

Management are particular keen to stress, not only the performance, but the potential of the Asian business. Operating profits were up 15% to £1.975bn, representing approximately 36% of the group. There was improved performance across all countries in region with 8 territories showing double digit growth. AUM in the Asian asset management business was up 18% at £139bn, delivering a revenue margin of 33bps (FY16 35bps) with a Cost/Income ratio of 56% (FY16 56%). Management are very excited about the structural demand in Asian with internal research showing that 1mln people are entering the work force every month, which will drive growth prospects well into the future. Management are keen to expand Health and Protection products, along with targeting the growing middle class with wealth products.

US

The US produced slower growth in OP than the group at 6% reflecting lower investment returns and a more mature market. OP was split across fee-based (variable annuities) income at £1.8bn and spread-based (fixed annuities) income at £317mln.The fee-based business was up 12% on higher account values due to both inflows and market moves and stable fee income. The spread-based business was down 6% due to decline of 24bps in spread margin. Management addressed the changes to the US tax code. They are expecting a materially lower tax rate for FY18 in the region of 18% versus 28%. Management are looking for continued growth in retirement income segment taking advantage of the aging demographic in the US.

UK & Europe

UK and Europe contributed yoy growth in OP of 10% coming in at £1.4bn. The life insurance business generated core operating profit of £600mln with management noting this as stable yoy. Other income on the Life side was £281mln included ALM management, provisions and mortality assumption changes. The asset management business performed very strong, producing 18% growth in OP bringing it to £500mln. AUM was up 20% to £164bn at year end. The revenue margin was unchanged at 37bps while the C/I ratio was down 1% to 58%.

Comment

Very strong performance from Prudential with profitability up across all markets, the stock traded up 5% on the day. The spinoff of the UK and European business is intended to reduce the capital requirements and allow management to solely focus on that market. From a current shareholder perspective, post demerger, holders can retain the same economic exposure by holding both stocks and management expect the new M&G Prudential to be a FTSE 100 company. Prudential trades at a premium to the rest of the market with a P/E ratio of 13x FY18 earnings compared to a sector multiple of 11x, it pays a lower dividend yield at approx. 2.4% versus 4.3% and a P/B of 2.7x versus the wider insurance sector at 1.2x. At first glance Prudential looks expensive but when you consider a mature insurance business in a developed economy you can expect growth rates in line with GDP. Due to Prudential's large and established footprint in Asia it can expect growth rates much higher than this, justifying the premium in our opinion. Prudential currently has a consensus price target of £21.20, which is under revision. We maintain our outperform rating.

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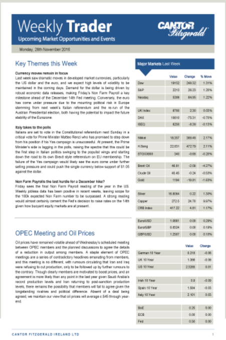

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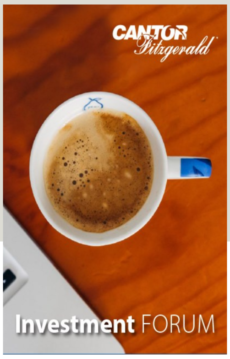

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