Daily Note
Views, news and topics from today's markets
CANTOR Fitzgerald
Wednesday, 9th May 2018

Morning Round Up

Trump Exits Iran Deal

Yesterday evening Donald Trump confirmed the US would withdraw from the 2015 Iran nuclear deal bringing a new wave of uncertainty to the Middle East. The US will reimpose nuclear and economic sanctions on Iran. The sanctions will prohibit US companies entering into new deals involving oil and energy. Over the next six months trade involving various other sectors as well as any transactions involving Iranian government debt and currency will cease. Despite the fact that the deal will still exist between 6 other countries including France, Germany and Britain, European companies will face US sanctions themselves for doing business with Iran. It will therefore face a simple decision, stop doing business with Iran or stop doing business with the US. European leaders, who have campaigned Mr Trump to remain with the agreement, have issued a joint statement emphasising their "continuing commitment" to the accord and urged Iran to show restraint in response to the decision. The worry is Iran will respond by restarting its nuclear program. However this would lead to the end of the accord with the 5 other nations, which Iran has suggested it will continue to honour. With trade tripling since 2015 between the EU and Iran, both stand to be significantly effected with further change.

Oil has risen by about 3% since the decision with Brent reaching over $77 a barrel (WTI moving above $71). Oil sensitive sectors, such as airlines, sold off this morning. Adding to geopolitical unrest in the Middle East, an hour after the US decision, it was reported Israel launched strikes on Syria killing 9 people (with speculation these were members of the Iran's Revolutionary Guard). Israel has strongly supported the US decision, with Benjamin Netanyahu previously referring to the accord as fatally flawed.

The House of Lords Brexit Vote

Yesterday the House of Lords voted in favour of keeping Britain in the European single market, contrary to both the Government's and Labour's approach. This would mean continued membership of the European Economic Area, essentially adopting the Norwegian model. This again adds further uncertainty to the UK's stance on the issue.

One Year Oil (Brent) Price

Source: Bloomberg, CF Research May 2018

Key Upcoming Events

30/06/2018 US Tariff Exemption Deadline

Market View

The major headline overnight has been the US withdrawal from the Iran deal. This has resulted in oil appreciating by circa 3% to $77 (Brent) . European equity markets are up slightly this morning, the US finished flat while Asia was mixed. The US ten year has risen above 3% while the German 10 year is at 0.58%. EUR/USD has weakened to 1.18.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	24360	2.89	0.01%	-1.45%
S&P	2672	-0.71	-0.03%	-0.06%
Nasdaq	7267	1.69	0.02%	5.27%
Nikkei	22,409	-99.81	-0.44%	-1.56%
Hang Seng	30,536	133.33	0.44%	2.06%
Brent Oil	76.95	2.10	2.81%	15.07%
WTI Oil	71.07	2.01	2.91%	17.63%
Gold	1306	-8.47	-0.64%	0.26%
€/$	1.1843	0.00	-0.18%	-1.35%
€/£	0.8748	0.00	-0.12%	-1.50%
£/$	1.3538	0.00	-0.07%	0.19%

	Yield	Change
German 10 Year	0.581	0.02
UK 10 Year	1.474	0.03
US 10 Year	3.0098	0.03
Irish 10 Year	1.003	0.01
Spain 10 Year	1.313	-0.01
Italy 10 Year	1.85	-0.0130

Source: Bloomberg, CF Research May 2018

Vodafone - Acquiring Liberty Global's European Assets

Closing Price - £2.07

News

Vodafone announced a well flagged deal to acquire Liberty Global assets in Germany, Czech Rep, Hungry and Romania at an enterprise value of €18.4bn with consensus estimates greater than €20bn. From a valuation point of view, Vodafone look to have paid a fair price as they have been heavily criticised for overpaying for assets in the past. The deal will require €10.8bn in cash to be paid to Liberty Global as well as the refinancing of a portion of the €7.6bn of debt attached to the deal. Vodafone intend to raise between €5-7bn in equity financing using hybrid debt securities, €3bn of which will be raised using mandatory convertible bonds (MCBs). The MCBs will be accounted for as equity and mature in three years. Management have committed to buying back the shares given enough head room on its net debt/EBITDA target range of 2.5-3x. It has also guided for significant cost and capex synergies, expecting €535mln per year by the fifth year post completion and a net present value (NPV) of €6bn post integration costs. The cross selling opportunity in these markets through packages and bundles is significant and it estimates that upside potential from revenue synergies is equivalent to a net present value of more than €1.5bn. Management have also stressed that the deal does not change its policy to grow the dividend per share annually and it believes the expected accretion to FCF per share from the transaction will support this target.

Comments

This is a positive deal for Vodafone and it further solidifies its position as a leading telecoms provider in European markets. Given the success of the combination of Dutch assets, expectations for both cost and revenue synergies are high as well as organic growth opportunities. This is particularly the case in the German market where the deal will face significant opposition from Deutsche Telecom as it goes through the regulatory approval process. Leverage will be a concern as Vodafone's current level stands at 2.1x (net debt/EBITDA), but the issuance of MCBs should keep this multiple in the 2.5-3.0x range. Overall a positive step for Vodafone and we maintain our Outperform rating.

Pierce Byrne, CFA | Investment Analyst

IFG - Q1 trading update

Closing Price - €1.57

News

IFG released a trading update this morning, updating on new management, FY18 costs and assets under administration/advice (AuA). IFG has had an eventful year thus far, with new management looking to focus attention back on the two businesses. James Hay reported new client wins of 1,400 which is slower growth than previous quarters. AuA was marginally down £100mln to £25.4bn as net inflows were offset by market moves. The statement called out repricing in FY17 along with BoE rate increase in FY17, feeding through to FY18 revenues, as having "significantly improved revenues and profits" compared to the same period in FY17. Marginally lower cash balances, as well as the likelihood that the BoE will not raise rates this week, will hurt full year top and bottom line estimates. Saunderson House reported 77 new clients for the quarter, compared to net 165 new clients in FY17, bring total clients to 2,214. Management have guided that the new client pipeline may be weaker for the remainder of the year due to the sale process but it should also see some increase in AuA from existing clients who were deferring a decision because of the uncertainty. AuA was flat on FY17 balances of £5.1bn as net inflows were offset by market moves. A £3mln retention cost for senior staff at Saunderson House relating to FY18 & FY19 is to be recognised fully in FY18, this will materially reduce full year operating profit expectations. Management are also flagging higher group costs for FY18 due to management changes and a review of the business currently underway, again this will hurt FY18 estimates.

Comment

Reported strong performance at James Hay is welcomed, but the business is facing some revenue pressures due to low interest rates and higher operating expenses. Marginally lower cash balances in JH along with the BoE not increasing the base rate in May will impact the top line by about £1.5mln, it remains to be seen if increased fee income can offset this. Recognition of a £3mln expense in SH will also be a direct hit on the bottom line. Management had expressed a target of maintaining an operating margin above 20% for FY18 which looks unlikely given the increase in costs. There was no significant update on Elysian Fuels as new management gets up to speed on the issue. New management are also reviewing the business, the results of which should provide some clarity on the strategic direction of the business over the coming years. Given recent price action the stock looks undervalued at around 14x FY18 earnings but considering the increase in both Group and underlying business operating expenses this multiple is stretched to closer to 18x-20x FY18 earnings with peers trading around 16x FY18 estimates. The uncertainty caused by legacy and exceptional items remains the primary risk to this stock. IFG is currently under review pending model updates.

Pierce Byrne, CFA | Investment Analyst

Siemens - Very strong quarter

Closing Price - €110.30

News

Siemens released Q2 FY 2017 results that are likely to be well received by the market. Overall revenue was €20.14bn, which was in line with Street estimates. Overall group orders came in at €22.32bn, which was 4% ahead of consensus. Organic revenues were flat yoy but continuing weakness in Power & Gas (-21%) was not as bad as the market was expecting. This weakness was also more than offset by very strong revenue performance in other divisions including Digital Factory (+13%), Mobility (+9%) and Building Technologies (+8%). The profit from the Industrials Businesses came in at €2.254m (+9.5% yoy), 9% ahead of consensus. The underlying margin came in at 11.7%, 10bps down on last year but a full 100bps ahead of consensus. Digital Factory was the standout performer with organic sales up 13% and margin of 20.9% (+290bps yoy and 260bps above consensus). Management raised its FY EPS guidance to €7.70-€8.00 (previous guidance was €7.20-€7.8), mainly driven by one-offs including a €900m gain related to its Atos investment. It also maintained its margin guidance at 11-12%. Lastly, its book-to-bill ratio is a very solid 1.11x.

Comment

Overall these results were very positive and the stock traded up 4.6% in early trading. Even when the positive one-offs are removed, trends in all of the underlying businesses are moving in the right direction. In our preview this week, we highlighted that we expected strong performance in all divisions bar P&G and that we believed the worse of P&G was in the price already (due to previous management downgrades). However, even we are surprised by the underlying performance. The margin numbers across segments was particularly impressive and was well ahead of expectations. The 20.9% margin for Digital Factory was achieved post the Mindsphere investment of 130bps and the Mentor integration costs of 40bps. This would imply the actual margin in Digital Factory is north of 23%, an excellent number. Short cycle growth was very strong also with China growing by above 20%. This release confirms CEO, Joe Kaeser's, transformation story is well under way and current valuations make it one of the cheapest large cap multi-industrials in the world. We maintain our Outperform.

William Heffernan | Investment Analyst

Grafton - March and April weather affect trading

Closing Price - £7.99

News

Grafton Group released a trading update this morning that showed it is not immune to some the recent poor Q1 events that have affected the industry. Like for like (LFL) revenue was up only 1.3% for the period January to April. Despite a positive start in January and February (LFL sales up 3.8%), March and April suffered weaker trading primarily due to poor weather conditions and excessively low temperatures. Group revenue increased by 7% to £907m, (6.2% in constant currency (cc) terms). At a divisional level, the only real change from previous performance trends was Belgium, which had seen the beginnings of a recovery but for this period fell by 4.8%. Ireland Merchanting grew by 4.6% while Retailing (Woodies DIY) grew by a more moderate 4.7%. The Netherlands continued its recent impressive performance with 8% revenue growth. The recently acquired Leyland business has been performing as expected and the Selco store opening plans remain on track.

Comment

Management maintained the same guidance and outlook as outlined in our previous meeting. Ireland and Netherlands will continue growing strongly supported by a robust housing market and consumer demand. In the UK, management expects house building to perform strongly but the RMI market to remain subdued. The overall outlook remains positive. Grafton was down 4% in early trading as investors used this release to take profits after a strong run over recent quarters. Grafton remains the best model in the sector and there is not enough in this release to warrant downgrades to estimates. However, it is likely to be weak in the short term with strong support at the £7.40-£7.71 range.

William Heffernan | Investment Analyst

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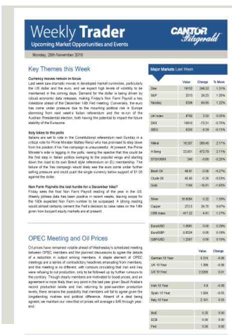

Weekly Trader

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.

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Monthly Investment Journal

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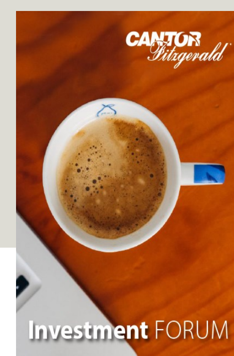

Investment Forum

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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

IFG: IFG Group PLC is a focused financial services company. The Company offers full platform services, pension administration and independent financial advice

Vodafone: is a mobile telecommunications company providing a range of services, including voice and data communications.

Siemens: Siemens AG is an engineering and manufacturing company. The Company focuses on four major business sectors including infrastructure and cities, healthcare, industry and energy. Siemens AG also provides engineering solutions in automation and control, power, transportation, and medical.

Grafton Group: Grafton Group PLC manufactures and retails building supplies.

Historical Recommendation:

IFG: We have been positive on IFG"s outlook since 17/05/14. We are moving our rating to Under Review as of 21/03/2018, Cantor Fitzgerald Ireland clients hold a significant portion of IFG stock.

Vodafone: We have been positive on Vodafone's outlook since 04/02/14 and no changes have been made to this recommendation in the last 12 months

Siemens: We changed our rating to Outperform on the 30/01/02017

Grafton Group: We changed our rating on Grafton from Market Perform to Outperform on the 20th Feb 2018

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