Daily Note
Views, news and topics from today's markets
CANTOR Fitzgerald
Wednesday, 16th May 2018

Morning Round Up

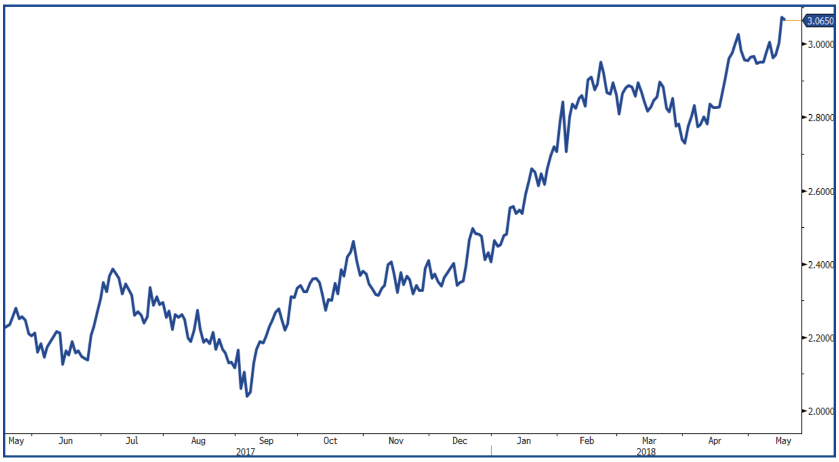
Paddy Power Betfair making waves in the US

Following on from Mondays Supreme Court ruling, overturning the federal ban on US sports betting, it has been reported that Paddy Power Betfair (PPB) are looking to acquire Fan Duel. Fan Duel is New York based fantasy sports gaming company. It, along with Draft Kings, who have already said they will enter the US sports betting industry, are the two largest companies in the daily fantasy sports in the US. Valuations for the private company have been wide ranging, however it looks to be upward of $1bn. PPB, who has roughly $445m in cash, guided at its FY17 results that it would be moving from essentially little or no debt to a net debt to EBITDA of between 1x and 2x. With an FY18 EBITDA of $663m, we can assume PPB can take on debt up to approximately $1.3bn. Overall this is further positive speculation. We will update again once we have spoken to management.

To yield or not to yield

If you have been reading our research over the last few months, you probably grew tired of the amount of time we spent discussing yields. After a month or so where the market moved on from the topic, they remained a key focus for us. Yesterday they came back into focus for the market as the US 10 year yield moved to 3.093%, its largest daily move in three months, past the Jan 2014 intraday peak and its highest level since 2011. As in previous instances of yield spikes this year, equity markets sold off. There was no substantial catalysts yesterday behind the move. US Retail Sales for April came in 4.7% growth, ahead of forecast at 4.1%. However when you strip out auto sales the number was pretty much in line. The NY Empire Manufacturing Index came in at 20.1 vs an estimate of 19 but again this was not a substantial enough beat to warrant the yield movement we seen yesterday. The "prices paid" component of that index rose to its highest level since 2011, perhaps reinvigorating the inflation narrative. However, some things we can be certain off. We are in a rising rate environment which will continue to lead to a decline in equity risk premium, Fed issuance over the next few years is skyrocketing due to White House funding needs and we are late cycle i.e. the Fed needs to get rates higher from here in preparation for any eventuality. We have seen significant tick-up on the short end also with the US 2 year yield now at 2.57%. One further point to note is the concurrent volatility we have seen in equity markets as yields move up. Up until Tuesday, there had been 93 trading days this year. 32 have ended with a 1% move in either direction. That is approx. 36%. The average going back to 1960 is 21%. The same metric in 2017 was 3%. This means that relative to 2017, the number of 1% moves has gone up by a factor of 10.

US Ten Year Yield



Source: Bloomberg, CF Research May 2018

Key Upcoming Events

30/06/2018 US Tariff Exemption Deadline

Market View

Asian markets sold off overnight as they took their lead from US equities who were spooked by yield movements. Oil remained above $71 a barrel, despite a significant beat on US inventory build (+4.854m vs est. -2m) as oil investors hold fire and wait for the outcome of the ongoing US sanctions on Iran and other Middle East volatility. Focus today will be on economic data including EU inflation numbers and US home sales, along with any further developments in yields & US-China trade discussions.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	24706	-193.00	-0.78%	-0.05%
S&P	2711	-18.68	-0.68%	1.42%
Nasdaq	7352	-59.69	-0.81%	6.49%
Nikkei	22,717	-100.79	-0.44%	-0.21%
Hang Seng	31,148	-4.35	-0.01%	4.11%
Brent Oil	78.04	-0.39	-0.50%	16.70%
WTI Oil	71.07	-0.24	-0.34%	17.63%
Gold	1295	4.76	0.37%	-0.58%
€/$	1.1844	0.00	0.05%	-1.34%
€/£	0.8772	0.00	0.08%	-1.23%
£/$	1.3502	0.00	0.00%	-0.08%

	Yield	Change
German 10 Year	0.628	-0.02
UK 10 Year	1.506	-0.01
US 10 Year	3.065	-0.01
Irish 10 Year	1.03	-0.01
Spain 10 Year	1.356	0.00
Italy 10 Year	1.99	0.0350

Source: Bloomberg, CF Research May 2018

Vodafone - Strong results overshadowed by CEO departure Closing Price - 198.38 GBp

News

Vodafone traded down on the back of results yesterday despite posting some very encouraging financials. The news that current CEO, Vittorio Colao, will step down in October of this year drove the majority of the weakness in pricing. While this announcement was not expected by the market, it is not a major surprise as this is a natural end point for Colao given his tenure. However, it is most definitely a loss to Vodafone's leadership team. Fortunately for investors, his successor, current CFO Nick Read, has been working under Colao for 12 years and has been groomed for the role.

Headline revenues fell from €47.6bn to €46.6bn (-2.2% YoY), the main drivers of the decline being FX exposure and the deconsolidation of Vodafone Netherlands. Management highlighted opportunities in total communications (Internet of Things (IoT) and Cloud), looking for opportunities to partner with market leaders like Amazon and Microsoft. EBITDA margins have been expanding year on year since FY15. FY18 adjusted EBITDA margin came in at 30.8% or €14.7bn. Management have been growing EBITDA faster than organic revenues indicating that the business is producing efficiencies above organic growth rates in sales.

Vodafone's primary European markets, which provided approx. 77% of EBITDA, have a mixed outlook in regard to competitive market conditions. Germany and the UK are described as stable. Both markets have high proportions of contracted customers and average revenue per user (ARUP) is weighted more towards contracts. Germany provided significant growth in EBITDA as management eked out efficiencies. Italy is providing a challenging mobile market with broadband growth offsetting some losses. Spain is also experiencing intense competition with some losses in share across broadband and mobile. AMAP, excluding India, is much more stable, providing strong revenue and EBITDA growth.

Vodafone spent €1.1bn on Spectrum auctions in FY18 across Italy, UK, and Germany. Management advised that the average cash spend on spectrum has been €1.2bn per annum and it does not expect this to change in the near term. Vodafone have a number of these auctions coming up and it is encouraging that management are not guiding for a significant increase in average annual costs over the near term.

Comment

The outlook for Vodafone remains positive, while the trading environment in Europe is competitive, its focus on connectivity speed and quality should protect margins and help grow the customer base. Data consumption is expected to continue to grow in European markets, while Vodafone has achieved double digit growth in its AMAP markets. Vodafone's scale adds a competitive advantage on it cost base as management have grown EBITDA faster than top line revenues over the past couple of years. Spectrum costs have spiked lately causing concern for investors but management do not expect its long term average spend on spectrum to change significantly which is positive. The Liberty Global transaction provides a platform to grow the fixed line services by giving Vodafone access to 54mln marketable homes in Europe. Vodafone remains highly cash generative, paying out €3.9bn in FY18. This represents the majority of free cash flow post spectrum cost giving a yield of over 6%. We maintain our Outperform rating.

Pierce Byrne, CFA | Investment Analyst

PTSB - Q1 Trading Update Closing Price - €1.72

News

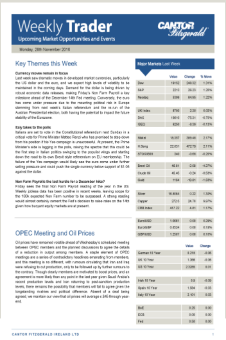
PTSB released a trading statement this morning updating on Q1 performance. The most encouraging news came from new mortgage market share coming in at 14% along with new lending of €300mln a strong start compared to €1bn in new lending for FY17. Gross loans contracted by €0.2bn in the quarter down to €20.4bn as repayments outpaced new lending. There was more disappointing news on NIM as it came in at 176bps, which is 4bps behind FY17 NIM of 180bps. The note flagged the sale of some treasury assets as the driver of the decline and highlighted the gain in non-interest income as "more than compensating". The note confirmed that the most politicized aspect of Project Glas, the split mortgages, will not be included in the loan sale. This reduces the total balance by €0.9bn as well as a further €0.6bn has been removed bringing the total face value of the loan sale to €2.2bn. There was also deterioration in Capital levels with the full loaded CET1 ratio coming in at 13.2% down from 15%. The move was attributed to the impact of TRIM and the change to IFRS9.

Comment

Results this morning will have disappointed on a range of key metrics and further confirm some of the structural issues PTSB management are facing. While gains in market share are welcomed, the continued decline in margin is a concern. The PTSB earning loan book is heavily skewed to tracker products and in conjunction with our outlook on ECB rates, the upside for margins brought by higher ECB rates is still some way off. This is compounded by higher earning treasury assets maturing, with the proceeds not being reinvested at the historic yields. The larger pillar banks are facing the same problem but have the scale in their balance sheets to carry such portfolios. All of this adds up to a weak outlook on NIM over the coming periods. Weakness in the top line is feeding down to the earnings as costs in the bank remain elevated with management guiding costs in line with FY17. Clarity around Project Glas is welcome but the €600mln reduction from FY17 face value was not addressed with any detail. Removal of the split loans should ease the political and media pressures on the loan sale, but will likely cause an increase in provisions recognised in FY18 to cover the full exposure on the warehoused portion of these loans. Overall the reduction in the size of the Project Glas (ex split loans) is disappointing. We maintain our Market Perform rating.

Pierce Byrne, CFA | 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.

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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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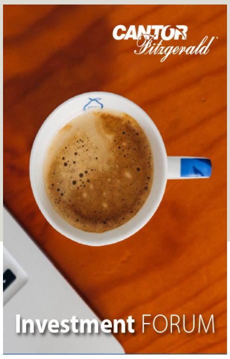

Investment Forum

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)

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

Paddy Power Betfair: Paddy Power Betfair Public Limited Company is a betting and gaming company. The Company provides online betting and gaming products.

PTSB: Permanent TSB Group Holdings Plc provides personal financial services in the Irish market with strong market positions in life and pensions, fund management and retail banking

Historical Recommendation:

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

Paddy Power Betfair: Currently outlook is Under Review

PTSB: We have changed our outlook on PTSB to "Market Perform" from "Outperform" on the 26th of July 2017

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