Daily Note

Views, news and topics from today's markets

CANTOR Fitzgerald

Wednesday, 2nd May 2018

Morning Round Up

Bank of England March data pointing to weakness

Bank of England Money and Credit figures reported yesterday showed a decline in the growth rate of money in the economy and consumer lending. The numbers compound the poor GDP data last week increasing pressure on BoE Governor Mark Carney. Broad money supply figures are trending downward indicating weakness in the UK economy in Q1.

M4, a measure of broad money supply, decreased £0.9bn with YoY growth rates trending down throughout Q1. Mortgage market remained quite robust, with new mortgage lending marginally down on the previous month. Both house purchases and re-mortgaging activity holding firm. Consumer credit on the other hand fell off a cliff. Averaging £1.5bn per month over the past 6 months, came in at £0.3bn. This is one of the sharpest corrections the series has experienced, which has been trending upward since 2009. Lending to non-financial corporates increased £4bn in the month; this was driven by large corporates accounting for £3.5bn as SME made up the remaining £500mln.

These figures further confirm weakness in the UK economy and while undoubtedly some of this can be attributed to the exceptional weather in March, the outlook remains very uncertain. The market expectation of the BoE moving its base rate in May has fallen from a peak probability of 88% to 16.8% currently.

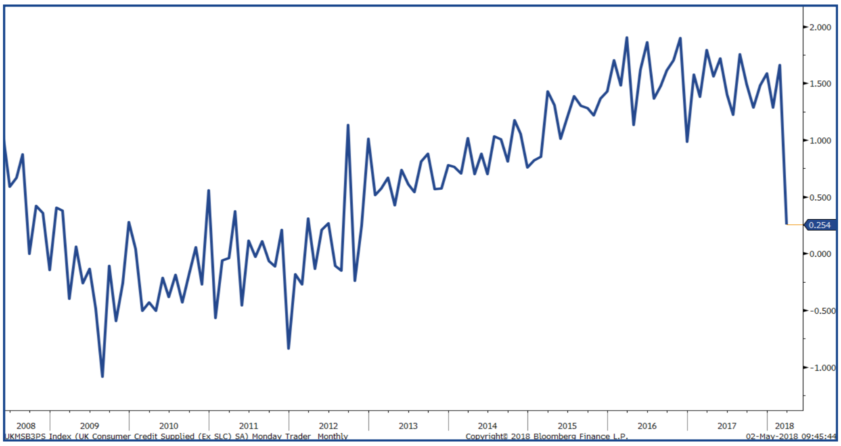
Russia investigation continues

Deputy Attorney General Rod Rosenstein, who is overseeing Robert Mueller's Russia investigation, dismissed those trying to intimidate him after a group of Republicans have drafted a version of articles of impeachment. The draft contains accusations that the Department of Justice (DoJ) failed to hand over documentation to Republicans regarding the Trump investigation and the Hillary Clinton's email investigation. In other news, Mueller warned he could issue a subpoena for President Trump to appear before a grand jury as part of his investigation. This would be an unprecedented move against a sitting US president. The increase in uncertainty would drive market volatility.

CRH commence buyback

CRH management announced its intention to begin the initial phase of its share buyback scheme (€1bn). The initial phased will run from 2nd May to 22nd August 2018 and will be for an initial €350m. This should provide further support to the investment case for CRH in the medium term.

Monthly Change UK Consumer Credit Supply



Source: Bloomberg, CF Research May 2018

Key Upcoming Events

02/05/2018 FED Meeting
30/06/2018 US Tariff Exemption Deadline

Market View

US markets pared early loses in yesterday's session on the back of positive Tech results and a strengthening dollar, with the NASDAQ closing up almost 1%. US 10Y yields advanced to 2.98%. Interest in the Russia investigation has picked up along with attention turning to the Federal Reserve and the Treasury's announcement of its quarterly refunding plan. Asia closed marginally down overnight as trade fears remain elevated and US rate increases look more likely. European markets opened positive this morning on the back of positive US data. WTI oil remains high in the wake of an industry report that showed U.S. crude stockpiles rose by more than expected last week.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	24099	-64.10	-0.27%	-2.51%
S&P	2655	6.75	0.25%	-0.70%
Nasdaq	7131	64.44	0.91%	3.29%
Nikkei	22,473	-35.25	-0.16%	-1.28%
Hang Seng	30,724	-84.57	-0.27%	2.69%
Brent Oil	73.35	0.22	0.30%	9.69%
WTI Oil	67.74	0.49	0.73%	12.12%
Gold	1310	5.99	0.46%	0.54%
€/$	1.2006	0.0013	0.11%	0.01%
€/£	0.8798	-0.0010	-0.11%	-0.94%
£/$	1.3648	0.0034	0.25%	1.00%

	Yield	Change
German 10 Year	0.579	0.020
UK 10 Year	1.448	0.043
US 10 Year	2.993	0.028
Irish 10 Year	0.984	0.016
Spain 10 Year	1.27	-0.006
Italy 10 Year	1.761	-0.024

Source: Bloomberg, CF Research May 2018

Paddy Power Betfair - Q1 trading update

Closing Price - €98.83

News

Paddy Power Betfair (PPB) released an underwhelming Q1 trading update this morning, which led to the stock dropping by 6% at the open. The majority of headline figures were poor and below trend. However management announced a £500m share buyback which will occur over the next 18 months. PPB had a net cash of £330m at the end of the quarter. Revenue was £408m, -2% yoy and flat from a constant currency (cc) perspective. EBITDA was £102m, down 8% yoy and –6%cc. EBITDA margin tightened from 26.6% last year to 24.9%. It noted that this was adversely affected by £5m annualisation of new betting taxes and levies implemented during 2017, while marketing spend was up 4%.

Three of the four main business segments were negative with Online, Australia and Retail underperforming. however the US was more positive . Online revenue, PPB largest source of income, was down 2% to £219m. Within online, Sportsbook revenue was up 3%, this is however below trend. Worryingly in Sportsbook, Paddy Power's underperformance relative to Betfair continued. Exchange and Gaming (the other two sub segments within Online) were negative down -7% and -4% respectively. It highlighted that exchange revenue was effected by lower horse racing commissions and a reduction in other high value customer charges. On a positive note the new integrated platform, which was completed in January, aided in boosting overall gaming revenue, increasing in February and March. Australia, PPB's second largest market, saw revenues increase by 6% in local currency (lc) terms. This marks a slowdown from historical growth trends as adverse sports results effected profits. It highlighted that it sees opportunity in the market as consolidation occurs. Retail, PPB third largest segment, was down 4% to £79m. This was performing well last year however unfavourable weather conditions had a sizeable impact. In the smallest segment, the US, results were positive with revenue increasing by 23% lc.

Management guided for an FY18 EBITDA of between £470m and £495m assuming no new taxes become payable in Australia for the year. This guidance is below analyst estimates for the year of £498m and shows limited growth from £473m achieved in 2017. There was no change to the 50% dividend payout policy.

Comment

Overall these are a poor set of results that should lead to eps downgrades of between 4% and 6% from analysts. This follows on from a less than impressive FY17 results.

Online, growth is slowing and Paddy Powers continued underperformance of Betfair is worrying. Importantly, it reiterated (from FY17 announcement) that customer activity was negatively effected by very strong gross margins in Q4 2017. This adverse recycling impact was then compounded by bookmaker friendly results in January and February. This form of adverse recycling would be more prevalent in Paddy Powers business given its "discretionary" punter base. A standout underperformer was Exchange revenue which turned to negative growth. However platform integration showed positive signs, stemming gaming declines (which had been poor) in February and March. Management highlighted with the platform integration completed, it will focus on curbing Paddy Power's falling market share. This will take time, however we would need to see some improvement in numbers over coming quarters.

The Australian numbers were noteworthy underperforming historic growth trends. This market has become increasingly competitive but PPB should be able to capitalise on consolidation going forward. The £500m share buyback is a positive as management look to follow through on the balance sheet restructuring (bringing debt between 1x and 2x EBITDA) announced in March.

Looking forward regulation is a major headwind for PPB and the sector overall. It looks likely that maximum stakes of £2 will be implemented on fixed odds betting terminals (FOTBs) in the UK. The Competitive Markets Authority (CMA) is showing signs of clamping down on bonus schemes offered and withdrawal conditions. In Australia it is probable that remaining states will introduce the consumption tax. Gambling advertising is also being reviewed. US figures were solid as PPB develops its capabilities to take advantage of any regulatory change. Attention will turn to the US Supreme Court to see if regulated US sports betting gets the go ahead. This would be a huge boost, potentially opening up a whole new market. That not withstanding, these results have highlighted the major headwinds and weaknesses facing the stock. We maintain our Market Perform rating.

David Fahy | Investment Analyst

Apple - Results better than expected

Closing Price - $169.10

News

Apple posted quarterly results last night that were better than we and the market were expecting. The major worry was around the number of handsets sold in the quarter, with estimates being downgraded in advance of this release. Q2 iPhone unit sales came in at 52.2m (+2.9%), ahead of estimates at 52.9m. EPS also beat at $2.73 vs est. $2.64. Revenue was $61.1bn (+15.6%) vs the Street estimate of $60.9bn. Service revenue (App Store, iTunes, Apple Pay, Apple Music) came in at $9.19bn (+31% yoy), a very strong result and well ahead of consensus estimates of $8.5bn. Other Products was also very strong with revenue of $3.9bn, 10% ahead of estimates. Management also guided for Q3 revenue in the range of $51.5 – $53.5bn, which is ahead of Street estimates pre-release. The market expectations for Q3 iPhone sales remains at 39m. Lastly management confirmed a $100bn buyback increase beginning in the June quarter but did not specify the end date. The company spent approx. $23bn in buybacks in this quarter. Management also announced at 16% increase in dividend to 73c per share. We estimate management has $163bn in cash that it could return to shareholders/use to add value and that management has headroom for further dividend increases over time.

There were only two real negatives. Overall gross margin was 20bps behind estimates at 38.35% and Average Selling Price (ASP) came in at $720 vs Street estimate of $740. This was still above the ASP at the same time last year which was $655.

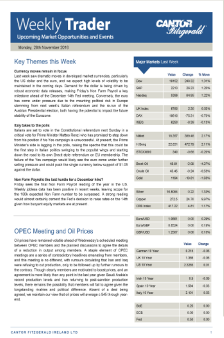
Comment

This was a very good report from Apple, especially in the context of the worries that preceded it. On the call management stated that the iPhone X was its bestselling unit, which should dampen concerns about the high price point ($999). It stated that the iPhone X being the best seller was a pleasant surprise and reaffirms its faith in that pricing level. Management are unlikely to reduce its price point and it is likely ASP forecasts move up post these results. It should be noted that the 2.9% growth rate in unit sales still puts the iPhone X below growth levels of previous iterations of the iPhone. It should also be noted that analysts revising down estimates in advance of results undoubtedly helped. We had feared that these results would lead to a downgrade in Q3 estimates for iPhone sales but there is little risk of that now.

Services and Other Products revenue growth was the other standout trend. Growth in these segments are strategically important as management looks to reduce overreliance on handset sales in the medium-long term. Services revenue had its best growth rate since 2012. Paid subscriptions are now at 270m, up 100m yoy and 30m vs the December 2017 number. There remains significant growth potential in this segment as Apple's install base is 1.3bn users. In Other Products, management on the call stated that Watch, Beats and Airpods all had a really strong quarter. From a regional perspective Greater China stood out with revenue up 21% yoy to $13bn and now accounting for 21% of overall sales. Management noted that the iPhone X was the best-selling model in China also, which again should ease concerns regarding the high price point relative to competitors in this region. Overall, a very strong set of results that should allay investor concerns coupled with buyback program that will continue to provide support to the share price. We maintain our Outperform.

William 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.

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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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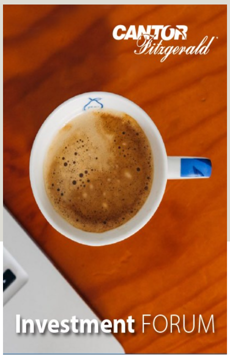

Investment Forum

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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

Apple: Apple Inc. designs, manufactures, and markets personal computers and related personal computing and mobile communication devices along with a variety of related software, services, peripherals, and networking solutions. The Company sells its products worldwide through its online stores, its retail stores, its direct sales force, third-party wholesalers, and resellers

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

CRH: CRH is a global building materials group.

Historical Recommendation:

Apple: We changed our rating on Apple to Outperform from Market Perform, as of 02/08/2017

Paddy Power Betfair: Currently outlook is Market Perform

CRH: We have added CRH to our core portfolio on the 01/01/16, with a recommendation of Outperform

http://www.cantorfitzgerald.ie/research_disclosures.php

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Dublin: 75 St. Stephen's Green, Dublin 2. Tel: +353 1 633 3633.

email : ireland@cantor.com **web :** www.cantorfitzgerald.ie

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