Daily Note
Views, news and topics from today's markets

CANTOR Fitzgerald

Tuesday, 27th November 2018

Morning Round Up

Budget climb-down would be a good start
Italy's governing coalition will meet this evening to discuss cutting its 2019 budget deficit target in a bid to defuse a dispute with the European Commission and calm financial markets. The government is discussing reducing next year's budget deficit target to as low as 2.0% of GDP from the draft Budget target of 2.4% of GDP, a government source told Reuters. Deputy Prime Minister Luigi Di Maio said in a radio interview he was open to cutting the deficit target. The Commission deems the target too high and in violation of the EU's fiscal rules. The difference in the yield between Italian 10 -year government bonds and their German equivalents has narrowed sharply to 288 basis points this morning from 307 basis points on Friday. The FTSE Italian banks index is up over 5%. An Italian Budget climb-down would be a good start. The country's anti-austerity government may trim its 2019 spending plans to defuse a clash with the European Commission that has led to asset outflows and weakened Italian banks.

Coalition partners Matteo Salvini of the League and 5-Star Movement leader Luigi Di Maio are due to meet later today to decide how to deal with the Budget, which the Commission has rejected. The two had vowed to stand firm against pressure from Brussels. But prolonged market turbulence in Italy, the prospect of EU sanctions and a weak auction of government bonds last week appear to be taking a toll. The benefits of trimming next year's budget deficit from the current target of 2.4% of GDP have been immediately apparent this morning. Yields on Italian sovereign bonds fell to two-month lows and bank stocks have rallied as investors anticipate an easing of tensions. That reaction should strengthen the hand of government moderates represented by Economy Minister Giovanni Tria. Reducing the budget deficit target to as low as 2.0% GDP next year would prevent an increase in Italy's public debt, which at around 131% of GDP is the main worry for the Commission, rating agencies and investors. A narrower deficit would have other benefits too.

The Bank of Italy estimates that the sharp rise in market interest rates following the creation of the Eurosceptic coalition will cost the country €5bn in additional debt servicing costs next year, and an extra €9bn in 2020. This undermines any benefit in extra consumer spending that Italy may get from distributing €7bn in welfare hand-outs. Yet while backtracking on the deficit will soothe investors, it will not improve the country's anaemic growth prospects. As things stand, Salvini and Di Maio look minded to change the form but not the substance of their Budget plan. They may delay launching their welfare plans but probably won't overhaul their approach by allocating more money to growth-enhancing public infrastructure. Even a smaller Budget stimulus would still end up in the wrong place.

Allianz making inroads in China
Allianz received approval to set up the first foreign insurance holding company in China, as part of China's effort to open up its financial markets. While the move will have no immediate impact on business in the region, it signals managements long term strategy. Allianz earns c. 6% of revenues in Asia, is underrepresented in the region given its global footprint. A wholly owned Chinese subsidiary will be the focal point for both organic and acquisitive growth in the region going forward.

Investor like GM's cost strategy
GM announced the closure of 5 North American (4 in the US and 1 in Canada) plants and reduce staff levels by c. 15% (c. 25% of executives). The stock finished yesterday up almost 5%. Management cited a change in consumer demand as the company moves away from sedans and focuses investment on electric vehicles and autonomous driving. President Trump warned about the Ohio factory included in the closures, with an expectation that GM will repurpose the facility. Ohio will be a key state in the 2020 Presidential Election.

Source: Bloomberg, CF Research November 2018

Key Upcoming Events

29/11/2018 Fed Minutes
30/11/2018 G20 Summit
11/12/2018 UK Parliament vote on Brexit
13/12/2018 ECB Meeting
13/12/2018 EU Summit

Market View

US Markets had a positive day yesterday, with the NASDAQ finishing up 2.06% as the technology sector posted strong gains. Asia was mixed overnight, with most markets positive, however, Hong Long and Shanghai were both down. The dollar was flat against the Euro at $1.1313 and the pound was weaker at £0.8875. Yields tightened, with the US 10 year trading at 3.05% and the 10 year bund at 33.4bps. The markets focus will be on the Fed this week, with expectations of more dovish tones from speakers, before trade takes centre stage in Buenos Aires with Presidents Trump and Xi are expected to meet.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	24640	354.29	1.46%	-0.32%
S&P	2673	40.89	1.55%	-0.01%
Nasdaq	7082	142.87	2.06%	2.59%
Nikkei	21952	140.40	0.64%	-3.57%
Hang Seng	26332	-44.22	-0.17%	-11.99%
Brent Oil	59.81	-0.67	-1.11%	-10.56%
WTI Oil	51.14	-0.49	-0.95%	-15.36%
Gold	1221	-1.10	-0.09%	-6.26%
€/$	1.1316	0.00	-0.11%	-5.74%
€/£	0.8874	0.00	0.36%	-0.08%
£/$	1.2753	-0.01	-0.58%	-5.62%

	Yield	Change
German 10 Year	0.344	-0.02
UK 10 Year	1.388	-0.02
US 10 Year	3.059	0.01
Irish 10 Year	0.983	-0.02
Spain 10 Year	1.534	-0.03
Italy 10 Year	3.23	-0.0390

Source: Bloomberg, CF Research November 2018

UDG Healthcare - Mixed result leads the stock to drop

Closing Price: £6.20

News

UDG released a mixed set of FY18 results this morning, delivering on double digit profit growth however continued weakness in Ashfield Commercial & Clinical, capital investment next year and questions over cash flow have led to weakness on open. Revenue over the year grew by 6% (constant currency (cc)) to $1.315bn, in line with expectations of $1.351bn. Adjusted operating profit grew by 12% cc to $147.5m, again in line with expectations. This represented 7% growth excluding the investment in Future Fit and the sale of Aquilant. Adjusted EPS grew increased by 22% cc to $0.459, slightly above expectations of $0.444. The balance sheet remains in a strong position with a net debt of $460.8m, 0.34x EBITDA. Adjusted net operating margin increased to 13.1% from 12.6%. It has proposed a 21% increase to the final dividend to $0.1175

Looking at the underlying components of the business. Ashfields (65% of the business) performance was mixed as Communications & Advisory performed well however Commercial & Clinical continued to lag. Headline figures were strong as net revenue grew 17% to $735.9m and operating profit grew by 21% to $98.4m. Ashfield Communications and Advisory saw solid growth with underlying operating profit increasing by 13%. Overall operating profit inclusive of acquisitions grew by 44%. Management has guided that it will grow STEM (acquired in 2016), through and expansion program known as STEM aXcellerate, this will hamper profit growth rates next year. Ashfield Commercial and Clinical continued to underperform with net revenues falling by 5% while underlying profits declined by 10%. Challenges in this market are set to continue into 2019. Sharp (35% of the business) saw improved momentum during the second half of the year in the US, however performance was weaker in Europe. Revenue grew by 3% to $311m and operating profit was up 11% to $45.8m. Sharp US performed well delivering underlying profit growth of 15% for the full year.

Official guidance for 2019 will be provided in January. Management noted that it expects continued profit from Ashfield Communications & Advisory and Sharp however Commercial and Clinical will remain weak. Management will be holding a call at 8.30am this morning.

Comment

Overall very much a mixed set of results leading the stock to fall by 8%. Communications & Advisory was solid and Sharp showed a pick up in the second half of the year however worries regarding the future growth of the Ashfield Commercial & Clinical segment and the investment STEM aXcellerate were not well received. The stock has suffered significantly over recent months as the investors questions its ability to grow in more troubled markets. This has led the valuation to fall to a 25% discount to its 5 year average. We are placing UDG Under Review from not rated.

David Fahy, CFA | Investment Analyst

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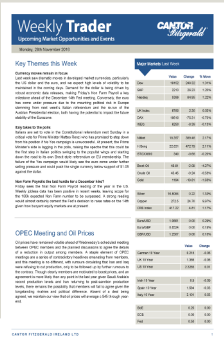

Weekly Trader

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

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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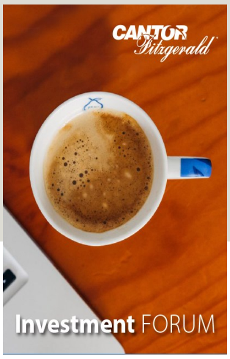

Investment Forum

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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Issuer Descriptions: (Source: Bloomberg)
UDG Healthcare: UDG Healthcare provides commercialisation solutions for health care companies.
General Motors Company: GM designs, builds, and sells cars, trucks, crossovers, and automobile parts.
Allianz: Allianz, through it subsidiaries, provides insurance and financial services.

Historical Recommendation:
UDG Healthcare: UDG Healthcare has been moved to under review from not currently rated.
General Motors Company: We do not currently rate GM
Allianz: We have been positive on Core Portfolio stock, Allianz since 24/04/14 and no changes have been made to the recommendation since then.

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