Daily Note
Views, news and topics from today's markets
CANTOR Fitzgerald
Tuesday, 04th December 2018

Morning Round Up

UK's Mixed Messages to Provide a Volatile Pound
Today will see the start of a five-day parliamentary debate on Theresa May's Brexit deal in Westminster, with lawmakers to vote on the withdrawal agreement next Tuesday the 11th December. The debate was expected to start at 1 p.m. in London with a speech from May promoting the deal, however opposition parties were granted and emergency debate on whether her government is in contempt of parliament for refusing to release legal advice from that the attorney general Geoffrey Cox on the Brexit deal. This question will be the first order of business for parliament today, with May's speech opening the Brexit debate to start later in the afternoon.

Meanwhile the European Court of Justice (ECJ) advocate general will give his opinion on whether the UK can revoke its notice to withdraw from the EU without agreement of the other 27-member states. This is not the final judgement in the case, brought forward by a group of Scottish politicians, but could be an indication of how the court's 27 judges will rule. A favourable ruling would add weight to the building moment for a second referendum.

The increased political uncertainty around the debate, with clear and heightened resistance to May's deal is likely to weigh on the pound in the coming days. The 14-day implied volatility on sterling, a gauge of near term expected swings in the pound, has climbed as investors have started betting on sterling volatility. Tensions will come to a head next Tuesday as the debate is set to close with turbulent market conditions and a volatile Pound being the only certainties for the UK at this point.

GlaxoSmithKline TESARO acquisition leads to sell off
Yesterday GSK confirmed today that it will be purchasing TESARO for $5.1bn (£4bn). This represents $75 per share, a 63% premium to the yesterdays price of $46. TESARO are a commercial stage biopharmaceutical company. Its biggest selling product is Zejula (ovarian cancer), representing c. 90% of sales. Zejula is currently being investigated for use as a treatment in lung, breast and prostate cancer. It will generate sales of about $240 million this year and will reach circa $1 billion in 2023 according to BBG estimates. The stock dropped by 7.5% yesterday knocking £6bn from the market cap. With an acquisition valuation of 19.6x sales the premium paid is excessive however as was the initial negative reaction.

European auto executives to meet with Trump
Ahead of a meeting between BMW, Daimler, VW executives and Donald Trump today, BMW's CFO stated that he expects the group to take a €500m hit to earnings from US/China tariffs in 2019. China has a 40% tariff in place on some auto imports which include BMW SUV's made in South Carolina. €500m compares to FY 2018 EBITDA of €13bn. We assume the headline was intended to put some meat on the bone, ahead of the Trump meeting. BMW continues to guide for 8-10% profit margin which would be ahead of consensus estimates of 7.1% in 2019.

Yield curve inversion
The spread between 3 and 5 year US yields fell to negative 1.4 basis points Monday, dropping below zero for the first time since 2007, and the 2 to 5 year gap soon followed. This could imply that the Fed is closer to the end of its tightening cycle. Some analysts also attribute the short term underperformance due to demand for riskier assets as global trade tensions ease following the tariff truce. Given that there has been an increase in demand for short term US government bonds since the 2019 growth concern began, it is no surprise that demand for "safe asset" has fell away after Trump and Xi's "extraordinary" meeting.

Source: Bloomberg, CF Research December 2018

Key Upcoming Events

11/12/2018 UK Parliament vote on Brexit
13/12/2018 ECB Meeting
13/12/2018 EU Summit

Market View

After a strong start to the week for markets, sentiment turned overnight as Asian markets were weaker on uncertainty regarding the outcome of the Buenos Aires dinner. US and European markets posted strong gains on Monday, but Europe has opened weaker this morning with US futures indicating a similar open in the US this afternoon. The short end of the yield curve inverted, with the 2s5s spread turning negative, while the more closely watched 2s10s spread fell to 13bps this morning. Markets will be looking for clarity on the trade message from Washington and Beijing. In the UK, Mrs May will continue to sell her Brexit package as debate begins in Commons.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	25826	287.97	1.13%	4.48%
S&P	2790	30.20	1.09%	4.37%
Nasdaq	7442	110.98	1.51%	7.80%
Nikkei	22036	-538.71	-2.39%	-3.20%
Hang Seng	27260	78.40	0.29%	-8.89%
Brent Oil	63.08	1.39	2.25%	-5.67%
WTI Oil	54.22	1.27	2.40%	-10.26%
Gold	1241	9.91	0.81%	-4.78%
€/$	1.1408	0.01	0.48%	-4.97%
€/£	0.8909	0.00	-0.16%	0.31%
£/$	1.2806	0.01	0.64%	-5.23%

	Yield	Change
German 10 Year	0.283	-0.02
UK 10 Year	1.299	-0.01
US 10 Year	2.9461	-0.02
Irish 10 Year	0.905	-0.01
Spain 10 Year	1.492	0.00
Italy 10 Year	3.15	0.0020

Source: Bloomberg, CF Research December 2018

IPL Plastic - Management update allay some concerns — Closing Price: C$10.16

News

We meet with IPL Plastic's senior management team this week, where it addressed some of the headwinds the business faced in Q3. IPL's Q3 results met expectations after significant downgrades in expectations as resin costs (c. 49% of cost of sales) increased from 60c/lb to 83c/lb through out 2018. In the Agri component of the Returnable Packaging Solutions (RPS), which does not have a pass through mechanism in its contracts, sold units based on 60c/lb resin costs but manufactured units with prices closer to 83c/lb. The impact saw margins in the unit fall from c. 13% to 10%. Looking forward, measures have been put in place to give management the ability to limit volatility between pricing contracts and manufacturing units. On the input costs side, we also discussed freight and labour costs. Increasing volumes and higher oil prices have also weighed on margins, management are moving to a tender process as part of a refinement of its freight procurement process, improving visibility on costs. Management also noted the impacts of tight labour markets in North America, which are again adding to margin pressures.

The outlook for the whole business remains encouraging, with Automotive demand in the RPS segment particularly strong. The unit is operating at capacity out to 2020, with management looking at expanding capacity for the segment. Expectations for the unit to deliver up to 25% of revenues for the segment in FY18. Organic revenue and EBITDA growth is also encouraging with guidance approx. 6-9% and consensuses expectation marginally higher. While management are also considering and remain open to possible M&A, noting equity capital as a possible source for larger acquisition. However, it did note that private market valuations had not suffered the same price correction as publically quoted names and valuations in that space were still high.

Comment

IPL Plastic is an interesting business, which has suffered since its IPO on the back of sharply higher resin costs. We believe that margin headwinds are mostly priced in and with resin prices stabilising and forecasted to fall in FY19, having declined 12% in November, could generate somewhat of a tailwind as margin outlook is beginning to turn more positive. Contracts are priced in the Agri segment in Q4 and manufactured at a later point offering margin upside on a weaker resin prices. Margins can also stand to benefit from increased automation of its North American plants, which can deliver sustainably high margin by reducing labour costs and increasing productivity. IPL also offers organic growth opportunities on the top line driven by customer demand with particular potential within the RPS segment. The end of the lock up period, on the 28th of December, could also act as a tailwind for the stock as fear of mass selling from existing shareholders is removed. This is an unlikely scenario in our opinion given the nature of the larger legacy shareholders. We don't expect much movement in the stock prior to the end of the lock up period, however, post this date there are a number of catalysts that can generate moment in the name including organic growth, margin improvement, falling resin prices and M&A. We currently have IPL Plastic Under Review.

Pierce Byrne, CFA | Investment Analyst

Ryanair - Makes progress with German Unions — Closing Price: €11.67

News

Ryanair released two statements this morning. Firstly, Ryanair and the German Pilot union have signed a framework agreement, covering a 4 year deal including pay, pension, seniority, annual leave and base transfers with an agreement that the detailed documents to be concluded by Feb 28th 2019. The airline also made progress on agreeing terms with the German cabin crew union last month. In addition, Ryanair released traffic stats for November, reporting an 11% increase in passengers carried to 10.4m passengers which includes 300,000 from Laudamotion. Excluding Laudamotion, Ryanair grew traffic by 8% to 10.1m passengers. This was an improvement in growth momentum relative to October when Ryanair grew traffic by 7%. Ryanair load factor was 96%. Laudamotion reported a load factor of 93% in November, up from 89% in October. Today's news follows a recent announcement that Ryanair intends to invest $1.5bn in Ukraine with the intention of adding 5m passengers in over the next 3-5 years.

Comment

The framework agreement with German Unions is welcome (particularly given the previous disagreements between these two parties) because it should help minimise strike disruption for Ryanair over the busy Christmas period. With a framework agreement now in place for all six of its Ryanair's core geographies, cementing these down prior to Easter will likely be managements focus. We view formal long term agreements to be a key catalyst for an improvement in sentiment toward the stock.

Recent capacity cuts in the sector will help improve industry supply/demand metrics. However while the recent drop in oil prices is positive from a shorter term cost perspective, it will hamper the rate of consolidation in the market. Certainty around Brexit could potentially see the shares trade back up toward €13.50 (+14%) in the short term. In the new year we will look for further guidance for fares (Q1/19 results) into the summer. We maintain our Outperform rating with a 12m price target of €16.

David Fahy, CFA | Investment Analyst

Greencore - Mixed reaction to FY18 results Closing Price: £1.83

News

Greencore released a relatively positive set of results this morning, meeting EPS guidance for the year and changing the capital return from the special dividend (US business sale) to a tender offer. Having consulted with shareholders management has confirmed its intention to return £509m to shareholders via a tender offer. Any proceeds not effected through the tender offer will be returned via a special dividend shortly after. Full details are still to be finalised with the return date expected to be Q2/19 (January - March 2019). FY18 Adj EPS came in at 15.1p (-1.9% yoy), meeting guidance (14.7p - 15.7p) and above consensus expectations of 14.8p. With the US business presented as discounted operations after the disposal, the following is based on the remaining UK/Ireland business. Group revenue grew by 4.2% to £1,498.5m. Excluding the central costs previously allocated to discontinued operations operating profits rose by 3.6% to £110.6m (£104.6m reported). Operating profit margin was flat at 7.4% (7% reported), however, it improved by 30bps yoy in H2/18. Return on Invested Capital (ROIC) was down slightly from 16% to 15.6%. The board is recommending a final dividend of 3.37p per share. Net debt to EBITDA was 2.3x, with this expected to fall to range between 1.5x - 2x post proceeds from the US sale.

Within the underlying segments, the Food to Go (60% of revenue) segment grew by 10.8% (11.1% including acquisitions), accelerating in H2/18 and outperforming category growth of 3%. Ex Food to Go business (40% of revenue) grew by 4.9% on a pro forma basis (falling by 5.5% including disposals).

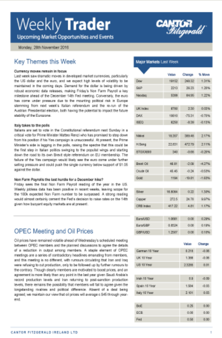
There was little outlook provided in the statement. Management noted that it expects operating profit growth to be driven by a combination of revenue growth and operational efficiency improvements. It also notes that risks from Brexit are manageable in the medium term. A conference call will be held at 9am.

Comment

A relatively positive set of results with figures generally coming in line and the change to the capital return policy making sense. Food to Go drove growth again, a trend which we expect to continue for the medium term. As we have highlighted previously the sale of the US business removes a significant portion of the growth opportunity, however, given the price paid we understand managements rationale. It is now left with a smaller market with lower growth potential, higher concentration risk and possible pricing pressures. Growth above the category rate will have to stem from innovation in the product range and operational efficiencies. However, its current low valuation of c. 7x FY18 EV/EBITDA should be taken into consideration. The stock is currently down 3% following the results having gained earlier in the morning. We expect to be provided more clarity on the outlook for UK/ Ireland at the conference call at 9am. We are holding Greencore as Under Review until after we have reviewed the remaining business fully following the conference call.

David Fahy, CFA | Investment Analyst

Cantor Publications & Resources



Weekly Trader

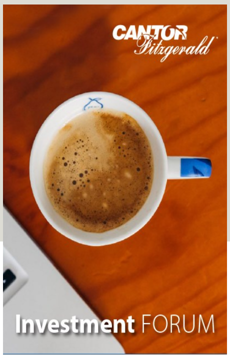
On Mondays, we release our weekly note in which we provide a view on equity markets for the coming days, and highlight a number of equities which we believe provide exposure to the important themes unfolding in the markets. Our in-house Investment Committee meets on a weekly basis to craft this strategy, thereby allowing clients to dynamically position portfolios to take advantage of the most up to date market developments.

[Click Here]

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.

[Click Here]



Investment Forum

Through our investment Forum we bring you the latest market news, investment insights and a series of informative articles from our experts.

[Click here]

Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

IPL Plastics: IPL manufactures specialty packaging products such as film seals, lids, overcaps, resins, and containers used primarily in food and consumer, agricultural, logistics, and environmental end-markets.

Ryanair: Ryanair Holdings plc provides low fare passenger airline services to destinations in Europe.

Greencore: Greencore manufactures and distributes a diverse range of primary foods and related products, food ingredients and prepared foods to the consumer and industrial sectors.

GlaxoSmithKline: GSK is a research based pharmaceutical company.

Historical Recommendation:

IPL Plastics: We have an Outperform on rating on IPL Plastics since 17/7/15 changing to Outperform from Not Rated.

Ryanair: Ryanair was added to the Core Portfolio at inception in and have had an Outperform recommendation since then.

Greencore: We revised our recommendation for Greencore, to Market Perform from Outperform, as of 25/08/2017.

GlaxoSmithKline: We moved our rating from Outperform to Market Perform on the 26/10/2017

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

This material is approved for distribution in Ireland by Cantor Fitzgerald Ireland Ltd. It is intended for Irish retails clients only and is not intended for distribution to, or use by, any person in any country where such distribution or use would be contrary to local law or regulation. Cantor Fitzgerald Ireland Ltd ("CFIL") is regulated by the Central Bank of Ireland. Cantor Fitzgerald Ireland Ltd is a member firm of the Irish Stock Exchange and the London Stock Exchange.

Where CFIL wishes to make this and other Cantor Fitzgerald research available to Retail clients, such information is provided without liability and in accordance with our terms and conditions that are available on the CFIL website.

No report is intended to and does not constitute a personal recommendations or investment advice nor does it provide the sole basis for any evaluation of the securities that may be the subject matter of the report. Specifically, the information contained in this report should not be taken as an offer or solicitation of investment advice, or to encourage the purchased or sale of any particular security. Not all recommendations are necessarily suitable for all investors and CFIL recommend that specific advice should always be sought prior to investment, based on the particular circumstances of the investor either from your CFIL investment adviser or another investment adviser.

CFIL takes all responsibility to ensure that reasonable efforts are made to present accurate information but CFIL gives no warranty or guarantee as to, and do not accept responsibility for, the correctness, completeness, timeliness or accuracy of the information provided or its transmission. This is entirely at the risk of the recipient of the report. Nor shall CFIL, its subsidiaries, affiliates or parent company or any of their employees, directors or agents, be liable to for any losses, damages, costs, claims, demands or expenses of any kind whatsoever, whether direct or indirect, suffered or incurred in consequence of any use of, or reliance upon, the information. Any person acting on the information contained in this report does so entirely at his or her own risk

All estimates, views and opinions included in this research note constitute CANTOR IRELAND's judgment as of the date of the note but may be subject to change without notice. Changes to assumptions may have a material impact on any recommendations made herein.

Unless specifically indicated to the contrary this research note has not been disclosed to the covered issuer(s) in advance of publication.

Past performance is not a reliable guide to future performance. The value of your investment may go down as well as up. Investments denominated in foreign currencies are subject to fluctuations in exchange rates, which may have an adverse affect on the value of the investments, sale proceeds, and on dividend or interest income. The income you get from your investment may go down as well as up. Figures quoted are estimates only; they are not a reliable guide to the future performance of this investment.

Conflicts of Interest & Share Ownership Policy

It is noted that research analysts' compensation is impacted upon by overall firm profitability and accordingly may be affected to some extent by revenues arising other CANTOR IRELAND business units including Fund Management and Stock broking. Revenues in these business units may derive in part from the recommendations or views in this report. Notwithstanding, CANTOR IRELAND is satisfied that the objectivity of views and recommendations contained in this note has not been compromised. Nonetheless CANTOR IRELAND is satisfied that the impartiality of research, views and recommendations remains assured.

Analyst Certification

Each research analyst responsible for the content of this research note, in whole or in part, certifies that: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research note.

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

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

Twitter : @cantorIreland **Linkedin :** Cantor Fitzgerald Ireland