Daily Note

Views, news and topics from today's markets

CANTOR Fitzgerald

Friday, 01st February 2019

Morning Round Up

US jobs growth likely slowed in January

US job growth likely slowed in January after December's weather-related outsized surge, but the pace of hiring probably remains fast enough to support the economy amid a darkening outlook resulting from government policy and cooling global economies. The Labour Department will publish its closely watched monthly employment report on Friday, two days after the Federal Reserve signalled its three-year interest rate hike campaign might be ending because of rising headwinds to the economy. It also comes at the end of the first week back at work for hundreds of thousands of federal workers furloughed during the recent partial government shutdown. The 35-day shutdown, which ended a week ago, may complicate the report but is not expected to have a lasting effect on US employment or the economy. Non-farm payrolls probably increased by 165,000 jobs last month, according market forecasts, after shooting up 312,000 in December - the most in 10 months. The anticipated job gains would be more than the roughly 100,000 per month needed to keep up with growth in the working-age population. In addition to the impact of the shutdown, the report may be muddied by annual revisions to payrolls, hourly earnings and the work week, as well as the incorporation of new population estimates. The shift in population controls means figures on the labour force or number of employed or unemployed would not be directly comparable to December.

GE moves back above $10

GE moved up 17% yesterday in early trading on the back of its Q4 earnings, finishing the day up 11.6%. Operating results were mixed and missed lowered expectations on earnings. Q4 revenue came in at $33.3bn (est. $32.33bn), while earnings per share (EPS) was 17c (est. 22c). Looking across the divisional performance, Power stands out as the worst preforming segment as management attempt to tackle a litany of operational issues. Management commented there was no timeline regarding the IPO of its Healthcare Unit and that GECAS was not for sale. The market took comfort from the amount of cash generated by divesting and asset disposal. Progress on deleveraging and the confirmation of a settlement with the Department of Justice on subprime mortgages saw the spread on its 5 year Credit Default Swap (CDS) fall 13bps. GE is at the beginning of a multi-year restructuring and we would advise clients who have exposure to use this move higher to reduce holdings.

International Paper posts beat on earnings

International Paper, the company that launched a failed bid to acquire Smurfit Kappa, posted earnings yesterday which beat on earnings (EPS $1.65 vs est. $1.59) and in line sales numbers ($5.95bn vs est. $5.96bn). The company reported lower containerboard volume and higher input cost in North America and improved pricing and volumes offset by higher raw materials in Brazil. In Europe, the company reported higher prices and volumes and again it saw higher raw material costs in the region. The read through for Smurfit is positive as the European market looks resilient. We retain an outperform on Smurfit ahead of its earnings on the 13/02/2019.

PaddyPower Betfair expands into Georgia

This morning PPB announced that it was taking a 51% controlling stake in Adjarabet, a Georgian online betting and gaming company. The deal, which will cost an initial £101m, enables PPB to acquire the remaining 49% over the next three years at a valuation equivalent to 7x 2021 EBITDA. The initial 51% works outs out at c.10x FY18 EBITDA (£20M). Adjarabet is leading player in Georgia with a 40% holding in the market. This deal will give access to the fast growing Georgian market, with further expansion into Eastern Europe likely. Due to regulatory, valuation and competition headwinds (particularly in Betfair), we maintain our Market Perform rating on PPB. Should we see these headwinds subside and/or a further realisation of growth in new markets (notably the US) we will likely upgrade our rating. Short term it will likely move upward from the €71 level.

Source: Bloomberg, CF Research February 2019

Key Upcoming Events

01/02/2019 US Jobs Data

Market View

Yesterday saw the end to the strongest start to the year in 30 years with the SPX rising 8% in January. Equity markets are relatively flat this morning as positive news on the trade front was offset by a weak Caixin Manufactoring PMI (48.3) reading in China overnight and underwhelming results from Amazon after close. Investors will turn their attention to non-farm payrolls in the US this afternoon. Average hourly earnings, the participation rate and the payroll numbers themselves will be closely watched. On the earnings front a number of European banks and Oil majors report today.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	25000	-15.19	-0.06%	7.17%
S&P	2704	23.05	0.86%	7.87%
Nasdaq	7282	98.66	1.37%	9.74%
Nikkei	20788	14.90	0.07%	3.87%
Hang Seng	27931	-11.73	-0.04%	8.07%
Brent Oil	60.53	-0.31	-0.51%	12.51%
WTI Oil	53.42	-0.38	-0.71%	17.62%
Gold	1319	-1.75	-0.13%	2.89%
€/$	1.1466	0.0023	0.20%	0.03%
€/£	0.8789	0.0060	-0.68%	2.25%
£/$	1.3046	-0.0062	-0.47%	2.30%

	Yield	Change
German 10 Year	0.161	0.015
UK 10 Year	1.225	0.006
US 10 Year	2.631	0.001
Irish 10 Year	0.885	0.015
Spain 10 Year	1.23	0.032
Italy 10 Year	2.697	0.112

Source: Bloomberg, CF Research February 2019

Amazon - Q4 beats but guidance and investment spend disappoint Closing Price: $1,718.73

News

Amazon released Q4 results yesterday after market, which beat expectations but disappointed on guidance. Fourth quarter revenue came in at $72.38bn (est. $71.92bn) with Amazon Web Services (AWS) revenue of $7.43bn (est. $7.3bn) representing 45% growth. Net sales growth is moderating, with Q4 North American growth at 18%, International segment at 15% and AWS at 45% compared with FY18 growth rates of 33%, 21% and 47% respectively. Full year consolidated sales growth held constant versus FY17 at 31%. Q4 Earnings also beat estimates with operating income reported at $3.79bn (est. $3.65bn) and earnings per share (EPS) of $6.04 (est. $5.56).

Management's Q1 guidance and FY19 investment spend sparked doubt for investors and caused the stock to sell of by c. 4% in after hours trading. Q1 guidance on revenue and earnings both missed market expectations. Q1 net sales is expected to range between $56-$60bn (est. $60.99bn) and operating income is expected to range between $2.3-$3.3bn (est. $2.99bn). Management also guided for higher investment spend in FY19 which will concern investors as lower profitability is less expectable when the business isn't producing the top line growth rates.

Comment

Another record profit for Amazon in Q4, which is the third record quarter in a row. However, moderating growth and higher investment spend are the headlines which has caught investors attention. Growth rates are unquestionably moderating looking at its North American business positing quarterly revenue growth of 18% versus 42% a year earlier. Full year growth rates held up at 33% but as Amazon moves into physical stores in the US its difficult to see how it can develop these lower margin products at the sale growth rates. AWS remains the brightest spot as it continues to invest heavily in data centres and roles out new functionality across its AWS offering. Amazon currently trades at c. 45x blended forward earnings, it hasn't trade below 50x since 2010. We remain positive on Amazon and would advise clients to buy on weakness. We retain an outperform rating on Amazon

Pierce Byrne, CFA | Investment Analyst

Core Portfolio Change - Adding Emerging markets Closing Price: £8.85

News

As of the close of business yesterday evening (31/01/2019) we have made the following changes to the core portfolio. Reducing Dalata Hotel Group by 2%, to a 2% weighting. Reducing Lloyds Banking Group by 2%, to a 2% weighting. Reducing Ryanair by 1%, to a 4% weighting. We are adding the JPMorgan Emerging Markets Trust with an initial 5% weighting.

Comment

Tying in with our house view of reducing Brexit exposure due to the risk of a No-Deal exit both increasing and failing to be adequately priced in, we are reducing three of our most significant Brexit exposed holdings. We are allocating away from Europe/UK to Emerging Markets which both reduces this risk and is an asset class we are positive on at present.

After a difficult 2018 for emerging markets we see the positive tailwinds for it to outperform in 2019. Chinese economic slowdown is of course the worry. Last nights China Caixan Manufacturing PMI of 48.3, was its lowest reading since 2016. However the Chinese government has already launched stimulus to help quell this downtrend. It is expected to further stimulate the economy to ensure its GDP rate remains above 6% in 2019 and to achieve its longer term goal of doubling GDP and incomes in the decade to 2020 (from 2010). Average growth of 6.2% in 2019 and 2020 is required to achieve this. Secondly, Chinese US trade relations is also progressing in the right direction with Trump and Xi set to meet next month, following the last two days of talks. Thirdly, the Fed has moved significantly softer in its new "patient" policy, with data dependent readings set to ensure rates fail to rise more that once this year, with expectations increasing we may actually see a cut. This, combined with a slower balance sheet run down, will put further downward pressure on the dollar. A softer Fed and subsequently a weaker dollar are supportive for global growth and emerging markets specifically as hard currency (USD) emerging market borrowers debt is devalued. Fourthly as lower oil prices is a net positive for the this emerging market index, which is majorically a net importer.

There has been sizeable flows into emerging markets this year, aiding in its 8% return. Its valuation has come back down to its longer run average (12m forward P/E of 11.5x) from 13x last year. We advise client to pick up exposure to emerging markets through JPMorgan Emerging Markets Trust (JMG LN EQUITY)

David Fahy, CFA | Investment Analyst

Providence Resources - Barryroe drilling programme progresses

Closing Price: £13.32

News

Providence Resources announced this morning that their partner in the Barryroe oil field, APEC, has nominated the 6th generation "COSLinnovater" semi-submersible drilling unit, currently deployed on the North Sea, to carry out the initial drilling of wells at the 40% Providence owned oil field which has an audited 346mmboe 2C resources.

The drilling programme is expected to start in Q3 2019 provided that all consents and regulatory approvals are in place. The focus of the drilling programme which will occur over c.12 months post Q3 2019 is to convert the 2C resources to 2P reserves therefore making the project economically viable. If successful, their 2P reserves maybe valued as much as $4+ with recent transactions being priced in the region of $4 - $9 per barrel which would imply a valuation of $1.3bn at the lower end of the range.

As a recap Providence is to receive $19.5m ($10m already received) from APEC prior to drilling, to cover previous and future operational costs related to Barryroe, APEC will supply a loan to Providence to fund 50% of the drilling costs of wells at Barryroe over the next 18 months with the loan and interest being repaid from future production cashflow and upon completion APEC can subscribe for 59.2m (10% of market cap) shares in Providence at £0.12 per share.

Providence also has a number of large oil fields off the Irish coast with a list of well-known partners including Cairn Energy, Repsol, Total and ENI. These offer future optionality with no value attributed within the Providence share price.

Comment

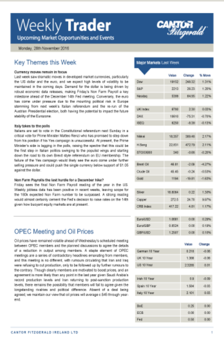
The farm out of Barryroe has always been viewed as the catalyst to create value for shareholders in Providence given that it has firmed up 2C resources. Now that the farm out has occurred and drilling programme is close to commencing, we see interest picking up in the speculative company shares.

In a blue sky scenario, Barryroe 2P resources are firmed up and APEX find additional resources viewing the project as commercially viable. Providence gets all the consents required to develop the oilfield which would create an oilfield worth over $1.3bn. Existing Providence shareholders contribution of this would be equivalent to 36% when you include the dilution. This equates to $468m relative to its current market cap of £95m.

This is a small cap, high risk investment but less risky now that Barryroe has been farmed out and funded through the drilling of 4-6 wells.

Darren McKinley, CFA | Senior Equity 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.

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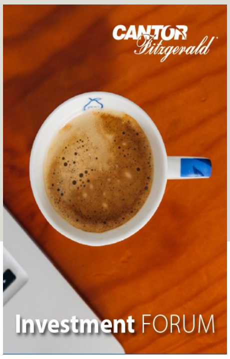

Investment Forum

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

[Click here]

Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

Amazon: Amazon is an online retailer that offers a wide range of products

Smurfit Kappa: Smurfit Kappa manufactures paper packaging products

General Electric: GE is a globally diversified technology and financial services company

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

JPMorgan Emerging Markets Investment Trust plc seeks to uncover quality stocks from across emerging markets that are also attractively valued, benefiting from an extensive network of country and sector specialists from one of the longest established emerging market teams in the industry.

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

Historical Recommendation:

Amazon: We have an Outperform recommendation for Amazon since 26/07/13, and no changes have been made since then.

Smurfit Kappa: Smurfit Kappa Group Plc is a member of our core portfolio and we have an Outperform rating on the stock since 01/01/2016

General Electric: We moved GE to Underperform in January 2017

Paddy Power Betfair: Currently outlook is Market Perform

JPMorgan Emerging Markets Investment Trust plc is on our preferred fund list

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

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