

Wednesday, 03<sup>rd</sup> April 2019

## Morning Round Up

### White House sees “headway” on US-China trade ahead of talks

The United States and China “expect to make more headway” in trade talks this week, White House economic adviser Larry Kudlow said on Tuesday as the top US business lobbying group said differences over an enforcement mechanism and the removal of US tariffs were still obstacles to a deal. “We expect to make more headway. I can’t report any of the details, but it’s a larger, grander discussion than anything we’ve had before in US-China trade relations, and there’s a certain amount of optimism,” Kudlow said in remarks at the US Chamber of Commerce. Kudlow, who directs the White House National Economic Council, acknowledged that there are still issues to be resolved, and the Trump administration will focus heavily on ways to hold China to keep its reform promises and curbing intellectual property theft and forced technology transfers and lowering tariff and non-tariff barriers. US Trade Representative Robert Lighthizer and Treasury Secretary Steven Mnuchin are due to resume talks with Chinese Vice Premier Liu He on Wednesday, just days after the two sides reported progress in talks last week in Beijing. The Chamber, the largest and most influential business lobbying group, sees increasing chances that Washington and Beijing will reach a deal to end a nine-month tariff war.

### China March services activity quickens to 14-month high

Activity in China’s services sector picked up to a 14-month high in March as demand improved at home and abroad, a new private business survey showed on Wednesday, adding to signs that government stimulus policies are gradually kicking in. But it is too early to tell if China’s economy has turned the corner, with many businesses cautious on whether there will be much improvement in a year’s time. The Caixin/Markit Services Purchasing Managers’ Index (PMI) rose to 54.4, the highest level since January 2018 and up from February’s 51.1, a four-month low. Survey respondents said activity was being buoyed by stronger demand, new state policies and improved access to financing. The findings were largely in line with those of an official gauge on the non-manufacturing sector released on Sunday, which showed services activity picked up in March as new orders rose more quickly. Construction, in particular, showed strength, likely reflecting government efforts to fast-track more infrastructure projects to kindle domestic demand.

### Oil’s run continues

As we have noted since the beginning of the [year](#), pressure from the supply side and an the over reaction regarding growth fears (demand side) since December is supportive for oil prices. These tailwinds have seen prices rise by c.40% YTD to \$63 a barrel (WTI). The same themes remain as they have done for most of the year. OPEC+ adherence to production cuts, continued adherence to US sanctions on Iran, Venezuela political turmoil and a slowdown in US shale rig count growth (lags oil by circa 4 months). On the demand side improved data from China and the increasing probability of a trade deal has also supported prices. With current prices just c.15% below last years highs it is likely we will run into some resistance as we approach the \$65 a barrel mark, that is unless a catalyst comes through. However, as always, oil is very much a momentum play hence calling a level is difficult. This is clearly evident in hedge fund positioning which is collectively increasing its net long position. We continue to expect a retracement in the second half of the year.

These higher oil prices and the lower global yield environment are supportive for the energy majors such as Royal Dutch Shell, Total and Exxon all of which were in this weeks [trader](#).

### Key Upcoming Events

10/04/2019 ECB Interest Rate Decision  
 29/03/2019 (12/04/2019) UK leaves the European Union  
 18/04/2019 Dissolvment of current EU Parliament

### Market View

Risk assets have advanced this morning after a slew of better than expected PMI data emerged from both China and Europe. Chinese Caixin Services and Composite PMI’s followed the stronger Manufacturing data last weekend by coming in well ahead of economist expectations. Along with this Europe showed some signs of life with PMI data across Germany, Spain, France and Italy beating expectations this morning. Equities have been supported further by renewed optimism that a deal will be reached between the US and China as talks resume in Washington. Retail sales and US ISM numbers will be closely watched later today.

### Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	26179	-79.29	-0.30%	12.22%
S&P	2867	0.05	0.00%	14.38%
Nasdaq	7849	19.78	0.25%	18.29%

Nikkei	21713	207.90	0.97%	8.49%
Hang Seng	29995	370.40	1.25%	16.05%

Brent Oil	69.9	0.53	0.76%	29.93%
WTI Oil	62.88	0.30	0.48%	38.47%
Gold	1292	-0.29	-0.02%	0.75%

€/\$	1.1239	0.00	0.31%	-1.99%
€/£	0.8533	0.00	0.02%	-5.07%
£/\$	1.3171	0.00	0.33%	3.27%

	Yield	Change
German 10 Year	-0.004	0.05
UK 10 Year	1.071	0.07
US 10 Year	2.5151	0.04

Irish 10 Year	0.626	0.04
Spain 10 Year	1.134	0.02
Italy 10 Year	2.50	-0.0260

Source: Bloomberg, CF Research April 2019

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**Walgreens Boots Alliance – Difficult quarter due to market and macro trends**

Closing Price: \$55.36

**News**

Walgreens Boots released results yesterday, disappointing on earnings in the quarter and forecasted earnings growth for FY19 saw the stock open at its lowest level since 2013. Revenues increased 4.6% (6.7% constant currency (cc)) to \$34.5bn (est. \$34.5bn), most of the increase was due to the acquisition of Rite Aid stores. Adjusted gross profit margin fell to 22.6% (est. 23.5% & Q218 24.7%), while adjusted operating margin also fell to 5.3% (Q218 6.3%) in the quarter. Adjusted operating income was \$1.9bn down 10.4%, while reported operating income was 23.3% lower at \$1.5bn due to cost related to its transformational cost management program and prior year tax implications related to AmerisourceBergen. Adjusted earnings per share came in below consensus at \$1.64 (est. \$1.72). Management acknowledged the quarter as the “most challenging” since the company’s formation. It also announced an increase in the expected annual savings from its transformational cost management program from €1bn to €1.5bn by FY20. Finally, management cut guidance for full year EPS growth from 7%-12% to flat for FY19.

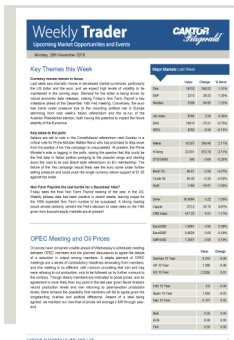
Looking at regional exposures, Retail Pharmacy USA (c. 75% of Revenue) saw organic sales growth of 1.6%. Including the acquisition of Right Aid stores sales grew 7.3% to \$26.3bn. Pharmacy sales increased on strong prescription volumes, while Retail sales also posted growth of 1.3%, however, it was weaker by 3.8% on like for like (LFL) basis. Gross profits decreased 3.5% primarily due to reimbursement impacts, while operating income was 12.6% lower at \$1.2bn. Retail Pharmacy International (c. 9% of Revenue), posted 7.1% decrease in sales (-1.2% cc), mostly due to weakness in the UK. Adjusted gross profit declines were in line with top line 8.9% (-1.2% cc). Operating income was 22.6% lower at \$192mln. Pharmaceuticals Wholesale (c. 16% of Revenue) recorded flat revenues, however, on cc basis sales grew by 9.1% due to strong expansion in emerging markets and the UK. Reported operating income was \$100mln (Q218 \$323mln (includes a \$113mln tax benefit)). On an adjusted basis operating profit in the segment fell 3.3% (+3.0% cc).

**Comment**

Yesterday’s results disappointed the market as some of the headwinds facing the sector intensified. Reimbursement pressure and generic deflation pose significant challenge to top line growth and margins. Management are focusing on increasing its cost cutting program with an expect 750 stores (previously 600) to be shut in FY19 in an effort deliver more than \$1.5bn in cost savings by FY22. As the sector adjusts to declining retail footfall, investment is focused on increasing digital capabilities to deliver a sustainable long term model. Short term the business is attempting to drive operating efficiencies to improve earnings growth in the near term. Yesterday’s move has seen valuations fall to their lowest levels in last 10 years and at its biggest discount to the S&P, at current levels the stock is trading a c. 8x blended forward earnings (versus 16.5x for the SPX). We are currently reassessing our investment case for the Walgreens Boots.

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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## Regulatory Information

### Issuer Descriptions: (Source: Bloomberg)

Walgreens Boots Alliance: Walgreens Boots Alliance operates retail drugstores that offer a wide variety of prescription and non-prescription drugs as well as general goods.

### Historical Recommendation:

Walgreens Boots Alliance: We moved our recommendation from Outperform to Under Review on the 02/04/2019

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