Daily Note

Views, news and topics from today's markets

CANTOR Fitzgerald

Tuesday, 30th April 2019

Morning Round Up

Chinese PMI misses but remains expansive

China PMI data released overnight disappointed the market by coming in below expectations. However, given the distortion from the Chinese New Year and the fact that all readings remained above 50 (expansionary) the market has taken the result better than expected with Chinese equities rising slightly. The NBS Manufacturing PMI for April came in at 50.1 (vs 50.5 last month and 50.5 expected). The Non Manufacturing PMI was stronger coming in at 54.2 (vs 54.8 last month and 54.5 expected). The Caixin Manufacturing PMI, which is generally recognised as the more accurate PMI reading, came in at 50.2 (vs 50.8 last month and 51 expected) . Hence, given the sharp upswing in March, a number of participants are viewing the numbers in an optimistic light. It is still difficult to gauge direction at present particularly given that the PBoC have stated that they may scale back stimulus should growth pick up at too quick a pace.

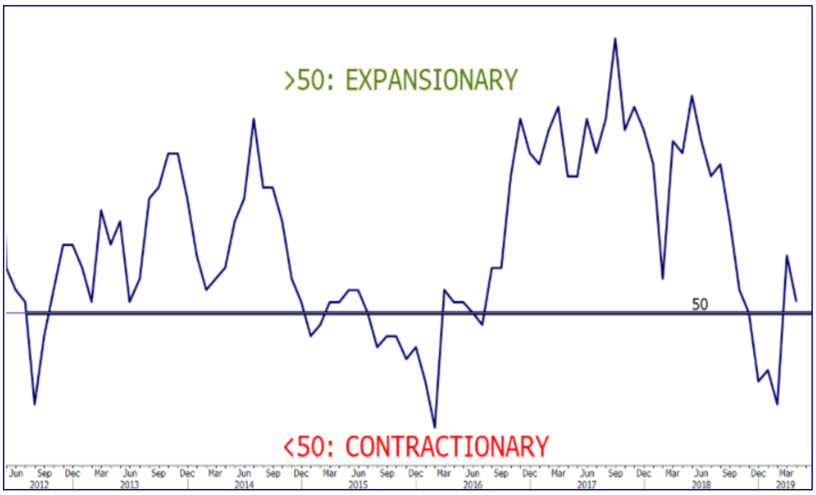
European Data slightly better than expected prior to GDP reading

Prior to the Q1 GDP reading later this morning, European data has come in slightly better than expected. In Germany, GfK consumer confidence stayed unchanged from the month prior at 10.4 (vs forecasts of 10.3). Unemployment remained unchanged at 4.9% (vs 4.9% expected). In Italy, unemployment fell to 10.2% from 10.5% the month prior (vs 10.7% expected). Spain showed signs of strength with retail sales growing by 1.7% yoy (vs 0.8% expected) , harmonised inflation of 1.6% (vs 1.5% expected) and GDP growth of 2.4% (vs 2.3% expected). European GDP, which is due to be released at 10am, is expected to show 1.1% yoy growth.

Samsung - Very weak Q1 revenue and operating profit result

Samsung reported Q1 results with revenue declining by 13% YoY to KRW52.4tn, operating profit declining by 61% and earnings per share declining by 56% to KRW752 per share. Operating profit margin declined from 25.8% in Q1 2018 to 11.9% in Q1 2019. Group return on equity declined to 8% in Q1 2019. Mobile sales declined by 6% YoY (78m smartphones sold) with Q2 expected to get worse before a recovery in the second half. Operating profit at the mobile division declined by an even more significant 40%. Semiconductor division reported a 30% drop in sales YoY and a 65% drop in operating profit. Chip demand is to increase in second half while investment in chip supply has declined significantly. Samsung trades on 12.5x earnings and 1.2x book value. Its share fell by 1.5%.

7 year China Manufacturing PMI



Source: Bloomberg, CF Research April 2019

Key Upcoming Events

01/05/2019 FOMC Decision
23/05/2019 EU Parliament Elections

Market View

European equity markets have moved lower this morning as weaker than expected earnings from Alphabet and Samsung, mixed economic readings and trade talks have left investors questioning market direction. The GDP reading from Europe will be important given the rerating in equity markets despite the clear signs of a faltering economy. Elsewhere the euro has strengthened slightly (EURUSD €1.12) as German bonds moved back into positive territory at 3bps. Oil has gained to $63.88 (WTI) after a couple of poor days following Donald Trumps tweet. Investors will look to Apple, Pfizer, GE and Mastercard who report later today.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	26554	11.06	0.04%	13.83%
S&P	2943	3.15	0.11%	17.40%
Nasdaq	8162	15.46	0.19%	23.01%
Nikkei	22259	-48.85	-0.22%	11.21%
Hang Seng	29699	-193.70	-0.65%	14.91%
Brent Oil	72.48	0.44	0.61%	34.72%
WTI Oil	63.89	0.39	0.61%	40.70%
Gold	1285	4.63	0.36%	0.16%
€/$	1.1214	0.00	0.25%	-2.21%
€/£	0.8637	0.00	-0.11%	-3.92%
£/$	1.2983	0.00	0.36%	1.80%

	Yield	Change
German 10 Year	0.036	0.03
UK 10 Year	1.188	0.03
US 10 Year	2.5288	0.00
Irish 10 Year	0.582	0.03
Spain 10 Year	1.031	0.02
Italy 10 Year	2.63	0.0400

Source: Bloomberg, CF Research April 2019

INM - Sale of company will force investors to cut their losses

Closing price: €0.104

News

Belgian/Dutch company Mediahuis has offered 10.5c per share in cash to buy Independent News and Media, the owner of the Indo, Sindo and Sunday World among others. The offer has been unanimously backed by the board of INM and has since got irrevocable undertakings from INM's two largest shareholders Denis O'Brien and Dermot Desmond (together own 45%). At 10.5c, INM trades on 9.4x earnings and 1.3x book value.

INM reported a 15% decline in profit before tax in 2018 and expectations are for a further decline of 27% this year. Management have been trying to protect profitability of the group by taking out costs as revenue falls. In addition to the operational headwinds, there is also high court proceedings ongoing related to an alleged data breach.

Mediahuis is a private company with €800m in revenue and 3,200 employees. They intend to integrate INM's 800 employees within their group and continue to distribute many of INM brands today

Comment

INM has had a challenged business model for many years now, no more exemplified then by the 15% fall in profits in 2018. Although INM has €80m of cash on its balance sheet, the annual cash flow metrics are becoming more challenging each year – thus valuing the operational business at €65m (4.3x 2019 earnings).

Given the pace of revenue decline, the deterioration in cash flow metrics and the ongoing high court proceedings – we concede that this is a fair value for the group at present and would join Dermot Desmond and Denis O'Brien in supporting this take over. Denis O'Brien acquired shares as recently as 2012 at c.30c.

The 10.5 c offer is a 44% premium to the 7c the shares traded at recently, albeit still down considerably from 2-3 years ago when it traded between 15c-20c. INM's listed life has been a challenging story and one of a "value trap", often attracting investor because of the brand names, high net cash position and strong cash flow generation. Speculation of being taking private by Denis O'Brien was always in the background.

The speed of the deterioration in cash flow generation highlights how quickly a structural change in consumer behaviour has on industry dynamics. At its peak INM was valued at €3bn and today is being sold for €145m.

Darren McKinley, CFA | Senior Equity Analyst

Alphabet - Revenue miss drives stock lower

Closing price: $1,296.20

News

Google reported Q1 earnings yesterday. Revenue missed analyst estimates, which saw the stock trade as much as 7% lower in afterhours trading. Revenue for the quarter came in at $36.4bn (est. $37.4bn) while traffic acquisition costs (TAC) were $6.86bn (est. $7.26). Ex TAC revenue was $29.48bn (est. $30bn). Operating margins decreased from 25% in Q118 (21% Q418) to 18% in this quarter. Increased operating costs was attributed to increased headcount from 85,000 in Q1 18 to 103,000. Earnings came in ahead of estimates at $11.90 (est. $10.61), excluding a €1.5bn European Union fine.

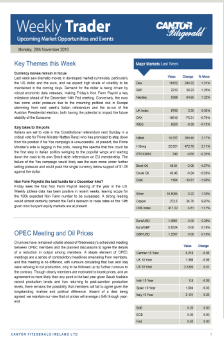
Revenue growth was the biggest disappointment with year on year (yoy) growth of 17%. Currency was a significant wiping 2% of its growth rate in the quarter. Q1 revenue growth rate slowed from 26% (Q1 18) and 23% (Q4 18). Revenue it its advertising business (84.5%) grew at 15%, while other revenues (15%) grew at 25%. Other bets revenues were $170mln up 13%.

Comment

Falling revenue growth in conjunction with rising cost is a concerning trend. The rate of the slowdown between Q418 and Q119 is also concerning. The market is also looking for more information on revenue sources such as YouTube, Search and other core platforms. However, the business continues to grow its top line significantly faster than the broader market. As growth slows to more normal levels, management need to drive profitability to maintain a premium. Alphabet current trades at 21.4x forward earnings compared to the S&P 500 at 17x. To retain that premium, management need to stabilise growth rates and margins. We have seen over the past 5 quarters both growth and margins trend lower and the market will need to see this trend reverse if it is to continue to assign it a multiple in the twenties. Our preference within the US technology sector continues to favour cloud and payment themes, however, we recognise the advertising models are still generating above trend growth rates and multiples remain attractive relative to the rest of the technology sector. We maintain our outperform rating on the stock and note the consensus price target for Alphabet is $1,334.

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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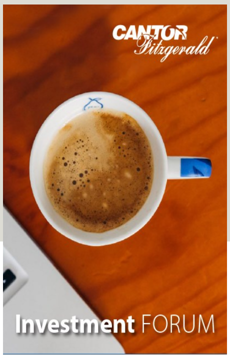

Investment Forum

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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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

INM: Independent News & Media PLC (INM) is an international media group

Alphabet: Alphabet provides web-based search, advertisement, maps, software applications, mobile operating systems, consumer content and other software services

Historical Recommendation:

INM: We updated our recommendation to Market Perform from Outperform on 19/05/17

Alphabet: Alphabet Inc is a member of our core portfolio and we have an Outperform rating on the stock since 07/01/2013

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