Daily Note

Views, news and topics from today's markets

Wednesday, 1st May 2019

Morning Round Up

Interest rates unlikely to change as the Fed meets

The Federal Open Market Committee is likely to hold interest rates unchanged at the close of its two day meeting in Washington this evening. The focus will therefore be on Jay Powell's press conference following the announcement. With market valuations back at elevated levels and mixed signalling from the US economy, the market will look for guidance on the Feds perception of the current direction of the economy. Importantly, inflation has fallen this year, reducing the probability of a hawkish tone from Powell. Again, faltering growth outside of the US will be a important factor in the address. At present, the market remains unconvinced in the current pause in the hiking cycle with a 66% probability of an interest rate cut now priced in.

US - China trade talks in focus

The latest round of trade talks between the US and China concluded this morning with US Treasury Secretary, Steve Mnuchin, referring to them as "productive meetings". The next stage of negotiations will take place in Washington next week. There have been numerous rumours of the progress made so far with reports that Donald Trump has dropped a central demand regarding commercial cyber theft and China is taking further steps to open its $44 trillion financial sector. If accurate, this is an important development from the Trump administration as it may point to watered down agreement between both sides. On the other side, should China remove some these requirements for foreign financial institutions, a generally state run sector would be open for investment. Expectations are that a trade deal will be reached in late May or early June. However, with the market now anticipating that a deal is reached the question turns to how comprehensive it is and whether Trump will shift his focus to Europe.

GE numbers beat expectations

GE released results yesterday which saw the stock move higher by 4.5%. Q1 revenue was marginal ahead of estimates at $27.3bn (est. $27.11bn), while earnings were much better than expected at 14c (est. 7c). Earnings were down 7% year over year. The Aviation segment performed well despite the ongoing issue with the Boeing 737 Max. Deliveries of its Leap engine (used in the 737 Max) increased to 424 units in Q1. Despite a stronger than expected quarter, CEO Larry Culp, maintained full year guidance, noting the performance in Q1 can be attributed to timing. The ongoing Boeing issue will be a concern for the Aviation business, which has been one of the strongest performs in GE's portfolio. We continue to advise clients to reduce exposure on pockets of strength.

5 year GE stock price

Source: Bloomberg, CF Research April 2019

Key Upcoming Events

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

Market View

With much of European and Asian markets closed today volumes are relatively light this morning. Of the markets open, sentiment is generally positive. US futures are pointing to a 25bps gain as Apple's stronger than expected results helped the technology sector following weakness from Alphabet yesterday. A combination of stronger than expected data from Europe, notably yesterday's GDP number and German inflation number, and mixed data from the US has led the euro to strengthen relative to the dollar (EURUSD $1.122). Inventors will look to the US today as it reports ISM numbers for April and the Fed meet.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	26593	38.52	0.15%	14.00%
S&P	2946	2.80	0.10%	17.51%
Nasdaq	8095	-66.47	-0.81%	22.01%
Nikkei	22259	-48.85	-0.22%	11.21%
Hang Seng	29699	-193.70	-0.65%	14.91%
Brent Oil	71.92	-0.14	-0.19%	33.68%
WTI Oil	63.48	-0.43	-0.67%	39.79%
Gold	1282	-1.65	-0.13%	-0.05%
€/$	1.1234	0.00	0.17%	-2.03%
€/£	0.8593	0.00	-0.13%	-4.41%
£/$	1.3072	0.00	0.31%	2.49%

	Yield	Change
German 10 Year	0.013	0.01
UK 10 Year	1.177	-0.01
US 10 Year	2.5017	0.00
Irish 10 Year	0.556	0.00
Spain 10 Year	1.001	-0.01
Italy 10 Year	2.56	-0.0300

Source: Bloomberg, CF Research April 2019

Pfizer - Stock gains on Q1/19 results Closing price: $40.61

News

Pfizer released a better than expected set of results yesterday afternoon, coming in ahead of expectations on both top and bottom line and raising guidance slightly for FY19. Revenue grew by 5% yoy to $13.1bn (vs expectations of $12.9bn). Net income grew by 14% to $4.67bn (vs $4.45bn). EPS grew by 10% to $0.85 (vs $0.75). The significant beat on EPS was driven by stronger than expected margins (gross margin only falling -0.74%), higher non operating income, and a lower share count. EPS guidance for the year was upgraded slightly to range between $2.83 - $2.93 from $2.82 - $2.92. Guidance for revenues was reiterated as $0.03 operational improvements were offset by unfavourable fx movements since January. During Q1/19, it returned $10.9bn to shareholders through a combination of dividends ($2bn) and share repurchases ($8.9bn). As of April 30th the remaining share repurchase authorization was $5.3bn.

Q1/19 sales were driven by the Pfizer Biopharmaceuticals Group as Eliquis (+36%), Ibrance (+25%), Prenvar (+10%) and Xeljanz (+34%) performed well. Eliquis and Prenvar were notably stronger than expectations. Upjohn, the off-patent branded and generic established medicines business, performed better than expected, particularly in China. Again there was considerable focus on its promising pipeline. Over the rest of 2019, PFE expects US approvals for tafamidis, Bavencio+Inlyta as well as for its biosimilars rituximab, bevacizumab and adalimumab. PFE expects Phase 3 readouts for PF-04965842, its JAK1 inhibitor for moderate-to-severe AD, and rivipansel for vaso-occlusive crisis from sickle cell disease.

Comment

This was a strong set of results from Pfizer, leading the stock to rise 2.6% on the day. EPS was significantly ahead of expectations and guidance was positive given adverse FX movements. The first quarter saw a number of positive product developments with five regulatory approvals. Pfizer's pipeline remains strong with a number of important readings this year, which may prove to be important catalysts. Expectations remain for growth to accelerate from 2020 onwards as newer products come to the market. Importantly, unlike the vast majority of its peers, it is relatively protected (excluding Lyrica) from generic replacement in the near future. Given the expected acceleration in earnings, attractive capital allocation and undemanding valuation (a 12m forward P/E of 13.5x), it remains a longer term outperformer in the pharma space. So far this year it, along with the broader US healthcare space, has suffered from political pressure and uncertainty (which is generally the case pre election year). Our US team hold a 12m month PT of $53. While it may not reach this price before the year end, we do see significant upside in 2019. We maintain our Outperform rating

David Fahy, CFA | Investment Analyst

Apple- Investors optimistic on Q3 guidance Closing price: $200.67

News

Apple released results after the bell yesterday, which were well received by the market. Shares in aftermarket trading were up 5%. Q2 revenues were marginally ahead of expectations at $58.02bn (est. $57.49bn), while earnings per share (EPS) also beat expectations at $2.46 (est. $2.37). Apple also announced $75bn in additional funding for its share buyback program. The real optimism steamed from its Q3 guidance, which was well ahead of expectations and implies a return to growth in Q3. Q3 revenues are expected to be between $52.5bn-$54.5bn (est. $52.2bn) with Q3 gross margin between 37%-38% (est. 38%). Q2 sales growth was negative at -5% following falling sales growth of -4.5% Q1. Product sales continue to be weaker on weaker iPhone demand with Q2 sales down -9.2%. Apple’s services business posted growth of 16%, however, this has slowed from 19% in Q1. Q2 did see revenue growth in the US but China was the down c. $2.8bn or 21%. However, management did paint an optimistic outlook for China.

Comment

Growth continues to be a challenge for Apple and despite an expected return to growth in Q3 (typically its weakest quarter), slowing trends are at the fore of investors’ concerns. The Product category is heavily reliant on iPhone sale with the segment suffering, particularly in China, against cheaper alternatives. The service category has seen growth moderate, however, the effects of new services like News+ and TV+ should see renewed growth in the segment. Apple should be able to leverage its 1.4bn user install base to make services an ever more important part of the business.

Apple’s share price performance has been strong year to date (+27%) post its profit warning in January, as risk appetite continued to improve. Its currently trading at 17x forward earnings, which is significantly higher than its 13x low back in January and its 3Y average of 14x. We continue to advise clients to reduce exposure as we see limited upside form current levels.

Pierce Byrne, CFA | Investment Analyst

AIB Group - Mixed results but still on track Closing price: €4.18

News

AIB released an encouraging set of numbers this morning, showing a strong start to 2019. Q1 net interest margin (NIM) was 2.50% up 2bps on Q4 exit NIM of 2.48%. Cost were marginally higher than Q118 on a mix of wage inflation, loan restructuring costs and increased depreciation. Management also confirmed a small net benefit from credit write backs during the quarter. Exceptional costs relating to restructuring and tracker mortgage review will be incurred in FY19.

Asset growth was positive with the performing loan book growing by €800mln in Q1 to €57.6bn, as new lending advanced 11% (18% Q118) on Q118. ROI mortgage growth has been trending lower over the past 4 quarters. This morning's release confirmed market share of 31.4% in Q1 down from 33% share in Q118 and mortgage growth of 9%. Management called out that its adjustment in fixed rate strategy is not reflected in Q1 figures, however, it is seeing a positive trend in applications. Non performing exposures (NPE) reduced to by €1.3bn to €4.8bn (7.6% of gross loans), implying €300mln in resolutions during the quarter. A second concerning trend in this morning's figures was the loan deposit ratio (LDR) at 89% (FY18 90%), continues lower.

Management issued a dollar denominated bond worth $1bn in Q1. The bond is MREL compliant, was 2.4x oversubscribed and brings its MREL issuance to an estimated 65% of regulatory requirements. Capital decreased to 17.3% (FY18 17.5%) due to accrued dividend, IFRS16 impact and increased risk weighted assets (RWA). Q1 capital figure continues to count €750mln in RWA relating to its NPE sale, which will be beneficial in Q2. The outlook remains positive and management expect to deliver on its guidance.

Comment

This morning's results confirmed strong profitability from AIB and continued progress towards balance sheet normalisation. NPE resolutions slowed to €300mln in the quarter (approx. €400mln/quarter in FY18), which is to be expected as progression through the book is achieved. We are looking for a further NPE reduction of €1.6bn-€1.8bn in FY19, as such we would expect c. €1bn of this to be achieved through a loan sale. While NIM trends continue to be positive, there are several headwinds looking forward. Continued trending lower of the LDR will weigh on the top line in a negative rate environment as excess customer deposits are held in cash, in addition to increased regulatory mandated MREL funding. Slowing mortgage growth and lower share are also concerning, however, management have reacted to this by offering a more competitive Fixed Rate offering. This morning's results show consistent underlying performance; however, we are likely to see an increase in exceptional items, higher costs and falling revenues. Irish banks remain cheap and provide an attractive yield. AIB remains our favoured name due to stronger profitability, more efficient cost management and excess capital held on the balance sheet.

Pierce Byrne, CFA | Investment Analyst

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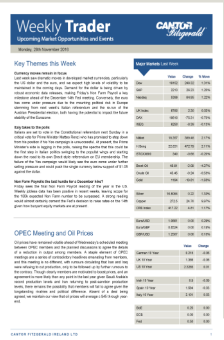

Weekly Trader

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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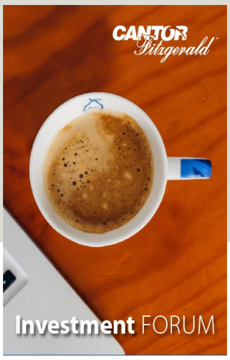

Investment Forum

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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

AIB Group: AIB Group plc attracts deposits and offers commercial banking services.

Pfizer: Pfizer Inc. operates as a pharmaceutical company. The Company offers medicines, vaccines, medical devices, and consumer healthcare products for oncology, inflammation, cardiovascular, and other therapeutic areas

Apple: Apple Inc. designs, manufactures, and markets personal computers and related personal computing and mobile communication devices along with a variety of related software, services, peripherals, and networking solutions.

Historical Recommendation:

AIB Group: AIB Group is a member of our core portfolio and we have an Outperform rating on the stock since 12/12/2018

Pfizer: We have had an outperform rating on Pfizer since 23/07/2018

Apple: We changed our rating on Apple to Market Perform from Outperform, as of 30/01/2019

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