

Thursday, 9th May 2019

Morning Round Up

Trade concerns brings volatility back to the markets

Donald Trump's claim last night that China has "broke the deal" that was being negotiated has heightened concerns that the trade war may be on the verge of escalating. A Chinese delegation will be in Washington today and tomorrow. Both sides are meeting in an attempt to broker a last minute deal prior to tomorrow's deadline, where Trump has stated that he will raise tariffs on \$200bn worth of Chinese goods to 25% from 10%. The Chinese have already responded stating that they will take retaliatory measures. Should the meeting between both sides fail to make a breakthrough, worries over global growth and heightened equity valuations will return. We advise clients to continue to be cautious when allocating at present.

PTSB release Q1 trading update

Permanent TSB released a trading update showing a strong start to the year. New mortgage lending continues to trend above the wider market at with its market share increasing from 14% to 15.1% in Q1. Total new lending increase by 25% to €0.3bn. NIM was in line with FY18 at 1.79% (FY18 1.78%) and operating costs were in line with expectations. Customer deposits increased by 3% bringing the loan deposit ratio to 98%. Management continue to make progress on non performing exposures (NPE) balances primarily due to cures and reduced default flows. Capital improve by 30bps to 14.3%. Despite encouraging Q1 performance, PTSB faces a significant challenge in adjusting its cost base to reflect its smaller balance sheet. Simply waiting for its tracker portfolio to reprice higher will not come soon enough, management need to lay out a strategy that can put PTSB on firm footing.

IFG trading in line with expectations ahead of AGM

IFG released a trading update this morning ahead of its AGM at 12 o'clock. The release confirmed the group is trading in line with expectations and there is no change to its Outlook. James Hay has seen an increase of 14bps in clients and Assets under Administration (AuA) increase 3.2% on positive market moves. Saunderson House won 63 new clients and AuA increased 4.8% since December 2018. There was not additional information provided to shareholders ahead of the vote relating to £1.93 cash offer by Epiris, which we expect to receive shareholder approval.

US 10 Year Treasury Yield



Source: Bloomberg, CF Research May 2019

Key Upcoming Events

10/05/2019 Trump Tariff Deadline
23/05/2019 EU Parliament Elections

Market View

Uncertainty over US-China trade relations prior to tomorrow's deadline has led European equity markets to drop by over 1% this morning. Asia, which is most vulnerable to the trade dispute, fell by over 2% last night. Oil has continued its decline, down to \$61.50 (WTI) this morning. Safe haven assets have gained. Yields on the US ten year have fallen to 2.44%, the Japanese yen has strengthened and gold has risen. Market direction will be driven by trade headlines for the next couple of days as China's negotiator, Liu He, meets in Washington today. Elsewhere, Kraft Heinz in the US is the standout name reporting this afternoon.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	25967	2.24	0.01%	11.32%
S&P	2879	-4.63	-0.16%	14.86%
Nasdaq	7943	-20.44	-0.26%	19.71%

Nikkei	21402	-200.46	-0.93%	6.93%
Hang Seng	28348	-655.06	-2.26%	9.68%

Brent Oil	69.73	-0.64	-0.91%	29.61%
WTI Oil	61.46	-0.66	-1.06%	35.34%
Gold	1285	4.33	0.34%	0.21%

€/£	1.118	0.00	-0.11%	-2.50%
€/£	0.8602	0.00	-0.04%	-4.31%
£/\$	1.2997	0.00	-0.07%	1.91%

	Yield	Change
German 10 Year	-0.063	-0.02
UK 10 Year	1.115	-0.02
US 10 Year	2.4423	-0.04

Irish 10 Year	0.497	-0.01
Spain 10 Year	0.955	-0.01
Italy 10 Year	2.68	0.0650

Source: Bloomberg, CF Research May 2019

BT Group - Mixed results! Commitment to 5% dividend in Q3

Closing price: £2.19

News

BT Group reported Q4/FY 2019 financial results this morning reporting revenue of £23.4bn (-1% YoY), PBT of £2.66bn (+2% YoY) and free cash flow of £2.44bn (-18% YoY). Cap-ex increased by £441m to £3.96bn which is primarily focused on fibre broadband roll out. Group final dividend of 10.8p per share is payable in September and brings the full year dividend to 15.4p (7% dividend yield). Management are guiding that dividend will be unchanged in the current financial year. Albeit a weak Q4 result, FY 2019 adjusted earnings per share increased by 6% YoY to 26.3p which would imply that dividend was 1.8x covered.

Management, led by new CEO Philip Jansen, have guided for a 2% drop in revenue in FY 2020, EBITDA of c.£7.25bn (-2%), cap-ex of £3.8bn (-5% YoY) and free cash flow of c.£2bn

Operationally, mobile and fixed churn rate continues to trend down (positive) with average revenue per customer also trending down (negative) modestly as competition within the retail channel and increased mix of sim only within mobile impact. Openreach continues to progress with its improved broadband offering, now adding 20,000 premises a week to fibre network. Management now target 3-4m with fibre broadband by 2021 and 15m by 2025. EE will launch 5G imminently and is on track to go live in 16 cities this year.

Group net debt increased by 15% to £11bn as free cash flow was used to pay down some of the groups pension deficit.

Philip Jansen, Chief Executive, commenting on the results, said “BT delivered solid results for the year, in line with our guidance, with adjusted profit growth in Consumer and Global Services offset by declines in Enterprise and Openreach.

“Since joining the company three months ago, it has become clear to me just how fundamental BT’s role is in connecting our society. While we are really well positioned in a very challenging and competitive UK market, we have a lot of work to do to ensure we remain successful and deliver long term sustainable value to our shareholders. We need to invest to improve our customer propositions and competitiveness. We need to invest to stay ahead in our fixed, mobile and core networks, and we need to invest to overhaul our business to ensure that we are using the latest systems and technology to improve our efficiency and become more agile.

Comment

We view this result as mixed with guidance around cap-ex, cash flow and EBITDA in line with expectations but with competition weighing on ARPU and increased investment likely to continue to add risk to the dividend in the medium term although management have committed to paying the 7% yield for the next year as well as paying its 5% yield in Q3 this year for 2019 financial results.

While the valuations of BT Group look attractive (8.5x earnings and 4.7x EV/EBITDA), the Openreach pension deficit is a headwind to managements cash flow and asset sale strategy hence restricting ability to create value.

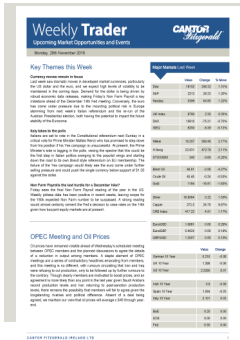
We look for further colour on the conference call as to what direction management will take but it seems to be that the new CEO is looking for an additional few months to weigh up his strategy before making drastic changes. A modest dividend cut would have been positive in our mind as it would have removed this overhang. Catalysts over the coming months would be sale of the international business and/or Openreach because we see significant value on a sum of the parts basis.

With BT Group trading at bottom of its trading range and a 5% yield due in September, we would continue to Hold BT Group shares and would consider a trade up in the name as the stock approaches £2.10. We would not recommend it as a “long term Buy” yet until we get more clarity on management’s strategy.

Our fair value for BT Group is currently £2.50 and would likely review our target price and recommendation if management either cut the dividend, sell their international division and/or meet their guidance of a return to EBITDA profit growth.

Darren McKinley, CFA | Senior Equity Analyst

Cantor Publications & Resources



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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

PTSB: Permanent TSB Group Holdings Plc provides personal financial services in the Irish market with strong market positions in life and pensions, fund management and retail banking

IFG Group: IFG is a focused financial services company. The Company offers full platform services, pension administration and independent financial advice.

BT Group: BT provides telecommunications services

Historical Recommendation:

PTSB: We have changed our outlook on PTSB to "Market Perform" from "Outperform" on the 26th of July 2017

IFG Group: We recommend accepting the IFG takeover offer

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