Daily Note

Views, news and topics from today's markets

Wednesday, 29th May 2019

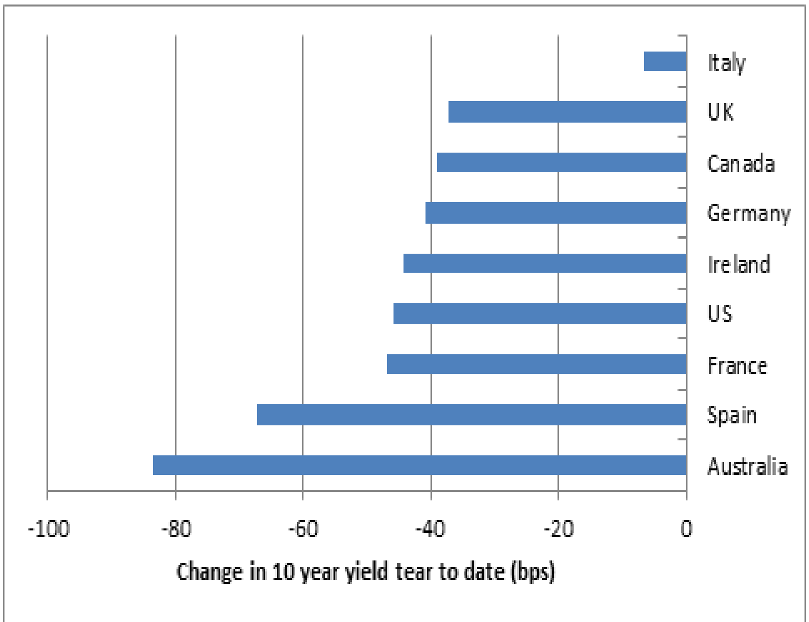
Morning Round Up

Yields tighten globally as economic fears build

The US 10-year yield is currently trading at 2.229%, which is the lowest level since September 2017. Similarly, the 2-year yield, currently at 2.081%, is also back to levels last seen in January 2018. The yield curve is also flattening with the 3 month - 10 year spread inverted at -11bps and the 2 year - 10 year spread close to the bottom of a recent trading range at 14bps. European yields are following a similar trajectory with the 10-year German yield currently trading at -16bps, only 3bps off from its low in August 2016 at -18.9%. A similar move lower in yields has been witnessed across most other European issues.

A global tightening in sovereign bond yields is indicating a flight to safer assets. There are several issues facing global markets that are causing investors to increase allocation to bond markets. Firstly, global growth concerns are tied to the outcome of a slew of political issues. The US-China trade war the most relevant to global growth. The changing tones of public rhetoric between the two economic superpowers helped drive markets higher in the first quarter and then drag markets lower so far in the second quarter. Closer to home, Brexit, fears of trade disruption with the US and political uncertainty across the region has seen Q1 optimism wean.

The net effect of such fears sees investors flock to the safety of the sovereign bond market. Continued flows out of equity markets into bonds could see yields fall even further (and generate weakness in equity markets). A reversal in the recent trend will need some resolution on trade. In the absence of such, yield will likely remain at current levels as the actual economic impact of the recent escalation in tariffs is felt across global economies. We remain cautious in our outlook for equity markets and continue to advise investors to increase allocations to the more defensive sectors. We are currently advising clients to consider allocating funds towards both the Consumer Staples sector **(Coca Cola, Danone, and Glanbia)** and the Health Care Sector **(Pfizer, Sanofi, and UnitedHealth Group)**



Source: Bloomberg, CF Research May 2019

Key Upcoming Events

01/06/2019 Chinese Tariff Deadline
28-29/06/2019 G20 Summit

Market View

Global equities are weak again this morning. Poor economic growth trends and trade concerns have seen a shift to safe haven assets. Yields across the globe have come down as a result. The US 10 year has dropped to just 2.22%, down from 3.23% six months ago. The German 10 year yield has fallen to –16bps. The Japanese yen, Swiss Franc and Gold have all strengthened this morning. Elsewhere, concerns over demand driven by the slowing global economy and trade has led oil to drop below $59 a barrel (WTI). The market will look toward US GDP data, Chinese PMI data and US PCE data this week.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	25348	-237.92	-0.93%	8.66%
S&P	2802	-23.67	-0.84%	11.79%
Nasdaq	7607	-29.66	-0.39%	14.65%
Nikkei	21003	-256.77	-1.21%	4.94%
Hang Seng	27255	-135.51	-0.49%	5.45%
Brent Oil	69.3	-0.81	-1.16%	28.81%
WTI Oil	58.42	-0.72	-1.22%	28.65%
Gold	1285	5.25	0.41%	0.16%
€/$	1.1152	0.00	-0.07%	-2.75%
€/£	0.8825	0.00	0.05%	-1.83%
£/$	1.2638	0.00	-0.12%	-0.91%

	Yield	Change
German 10 Year	-0.168	-0.01
UK 10 Year	0.907	-0.01
US 10 Year	2.2238	-0.04
Irish 10 Year	0.46	-0.01
Spain 10 Year	0.75	-0.04
Italy 10 Year	2.69	0.0070

Source: Bloomberg, CF Research May 2019

Ryanair - Cutting the price target

Closing price: €10.62

News

Following full year results last week, we are reducing our 12m price target on Ryanair from €14 to €12.50. The change comes on the back of poorer than expected guidance and the difficult macroeconomic backdrop. We maintain our Outperform rating. However, we advise clients that there may be further short term weakness driven by Brexit and/or further deterioration in the sector (which will benefit the longer term investment case).

Comment

For much of the past 12 months we have expected FY20 to be the year Ryanair returns to earnings growth after a difficult FY19. However, market conditions have failed to evolve as we expected and the upcoming summer period is set to remain challenging for airlines. With flat profits expected this year, the return to earnings growth (and a subsequent acceleration) appears to be prolonged until next year.

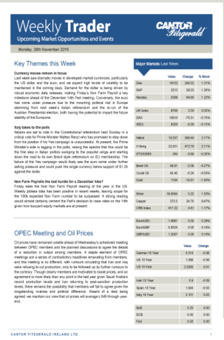
Positivity toward the sector has diminished over the past number of weeks as slowing capacity growth has been offset by a underwhelming demand for the summer period due to slowing economic growth and Brexit. This implies further fare weakness for the summer period. Despite several airline failures since last autumn the sector remains over supplied. This, combined with higher fuel costs, has been weighing on the sectors profitability with a number of loss making airlines struggling to stay afloat.

We had expected management to be cautious in its guidance for FY20. However, both cost guidance and profit guidance were poorer than we had forecast and the Boeing 737 MAX aircrafts remain an uncertainty. Despite this, management was highly optimistic in the medium term outlook for the company. It expects consolidation in the market place to be benefit Ryanair significantly. As airlines fail and capacity is taken from the market (noting Norwegian, Thomas Cook and TUI etc) the stronger airlines will see both revenue and profitability increase. We agree with this outlook and believe that Ryanair is the best placed airline to capitalise in a consolidating market place. While a number of airlines are raising capital to stay liquid Ryanair remains profitable (FY19 ROE of 18%). This longer term positive outlook is supported by the strong balance sheet position (BBB+ rated with 95% of aircraft owned, c.63% debt free), continued capacity growth and leading low cost structure. Importantly Ryanair has used the difficult period to continue to grow capacity as competitors scale back. Management is attempting to accelerate its competitor failure by pricing them out in some key markets. This has been observed in a number of routes where Norwegian and Ryanair operated. This peak capex and €700m buyback confirms managements confidence in its longer term outlook. The current fare environment is both temporary and unsustainable for the sector.

Despite the positive longer term outlook the shorter term headwinds remain. Brexit, poorer growth from European economies, higher oil prices and higher ex fuel unit costs are all near term concerns. As a result our projections for FY20 earnings have come down and are roughly in line with managements guidance. We use an FY20 EV/EBITDAR multiple 8.5x (in line with 10 year average) to achieve the PT of €12.50. Should we see an improvement in the airline space (driven by consolidation in the sector over the winter period), we will see our PT rise as the earnings outlook for FY20 improves in line with our expectations. However, given the stock moves closely with short term earnings expectations, there is potential for further weakness over the coming months. This may be driven by a weaker than expected fare environment, cost outlook, Brexit and the Boeing issue. Given the upside of the coming 12m we maintain our Outperform rating.

David Fahy, 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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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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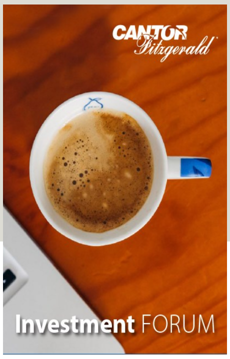

Investment Forum

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

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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

Ryanair: Ryanair Holdings plc provides low fare passenger airline services to destinations in Europe.

Historical Recommendation:

Ryanair: Ryanair was added to the Core Portfolio at inception in and have had an Outperform recommendation since then

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