

Friday, 31st May 2019

Morning Round Up

The “tariff man” targets Mexico

Donald Trump has announced he will impose a 5% tariff on Mexican goods until the country stops immigrants from entering the US, putting the new North American Trade Agreement in jeopardy. The US has stated these new tariffs are based on immigration and are therefore separate to the trade agreement. The tariffs will gradually increase from 5% until the “illegal immigrants coming through Mexico” into the US “stops”. The tariffs could rise to as high as 25% by October. The move tackles two of Trumps core policies, trade and immigration. Markets have reacted accordingly with the US 10 year treasury yield falling to 2.16% and the Mexican peso dropping by 2%. This is a further blow to US importers following the China tariff increase. Equity futures are pointing to a negative open in the US this afternoon.

Separately, China has stated its intention to restrict exports of rare earths to the US should tensions escalate further. These minerals, which are used in magnets, petroleum cracking and batteries, are critical components in numerous electronics, medicine and military applications. Approximately 80% of US rare earth imports are from China. Again we reiterate our defensive allocation as Trumps trade altercations escalate and global data continues to trend downward.

China's manufacturing PMI points to further slowdown

China's manufacturing PMI dropped to 49.4 in May, below the consensus expectation (49.9) and the second consecutive decline. Most importantly the reading below 50 shows the manufacturing economy is contracting. Renewed tariff threats from the US has led new export orders (sub component of PMI) to drop to 46.5 from 49.2. Services PMI (54.3) was better, coming in in line with expectations as the consumer economy holds up. This manufacturing reading is further confirmation of the deterioration in global economic data.

Core portfolio changes - risk reduction

Tying in with our preference for a defensive allocation, we are further reducing the cyclical (/beta) exposure of the core portfolio. Continued trade uncertainty, the consistent deterioration in global leading economic indicators, negative earnings growth and stretched valuations are all driving this decision. We are cutting our allocation to the Technology/Consumer Discretionary sectors by reducing Alphabet and Amazon by 2% each, bringing the weighting in each to 2% (both previously 4%). We are also cutting our allocation in the JP Morgan Emerging Markets Investment Trust from 5% to 0%. Emerging markets are particularly vulnerable to international trade and the global growth slowdown.

We are allocating to two new stocks. Both these stocks have proven the ability to outperform during periods of broader market drawdowns. Newmont mining, the world's largest gold miner, will increase from 0% to 5%. Newmont is highly correlated with gold (defensive asset class), has a 2% dividend yield and trades on an 8x EV/EBITDA. Greencoat Renewables, is a market leader in the Irish wind farm space with a 10% market share. It supported by both its defensive utility characteristics and the secular trend toward green energy. It has a 5.5% dividend yield, trades at 12 x earnings and has a 10% 2020 gross revenue/income yield.

Source: Bloomberg, CF Research May 2019

Key Upcoming Events

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

Market View

European equities have fallen again this morning. Trade and poorer economic data is continuing to drive negative sentiment across global financial markets. Trumps now has Mexico in his crosshairs with 5% (potentially moving to 25%) tariffs of imports unless the Mexican immigration policy improves. News from China is equally negative as it looks at plans to retaliate with rare earth exports and overnight manufacturing PMI points to economic contraction. US and German 10 year treasury yields have dropped this morning. The US 10 year yield is now 2.17% and the German 10 year has hit record lows of -20bps. Inflation data from this US will be important this afternoon.

Market Moves

	Value	Change	% Change	% Change YTD
Dow Jones	25170	43.47	0.17%	7.90%
S&P	2789	5.84	0.21%	11.25%
Nasdaq	7568	20.41	0.27%	14.05%
Nikkei	20601	-341.34	-1.63%	2.93%
Hang Seng	26882	-232.83	-0.86%	4.01%
Brent Oil	65.98	-0.89	-1.33%	22.64%
WTI Oil	56.18	-0.41	-0.72%	23.72%
Gold	1294	5.59	0.43%	0.92%
€/\$	1.1141	0.00	0.11%	-2.84%
€/£	0.8830	0.00	0.03%	-1.78%
£/\$	1.2618	0.00	0.08%	-1.07%
			Yield	Change
German 10 Year			-0.194	-0.02
UK 10 Year			0.875	-0.02
US 10 Year			2.1748	-0.04
Irish 10 Year			0.441	-0.01
Spain 10 Year			0.757	-0.01
Italy 10 Year			2.72	0.0600

Source: Bloomberg, CF Research May 2019

Total Produce - Management maintain guidance with trading update

Closing price €1.60

News

Total Produce management released a trading update this morning confirming that the group is targeting growth for 2019 with earnings growth expectations remaining unchanged. Management guided for 4-9% growth in adjusted EPS above the 13.5c reported in FY 2018.

Dole Food Company, which Total Produce now owns 45% of, is trading well and 2019 will be the first year that Dole will contribute a full year of earnings to the Total Produce group having been acquired in July 2018.

A dividend of 2.51c will be paid to shareholders on the 6th June 2019, representing a 2.5% increase on 2019. Total Produce is in a strong financial position and the Dole transaction is the most significant acquisition in the groups history.

Comment

On February 21st we moved our recommendation on Total Produce from “Buy” to “under review” as we were more cautious post the 35% rally year to date and the fact that industry peers had been reporting weaker than expected results during Q1 2019. Despite Total Produce shares subsequently correcting back to €1.50, managements superior quality once again stood out as they delivered a much better than peer FY 2018 result, delivering both revenue and earnings growth adjusted for Dole transaction costs. The recent result stood out relative to peers.

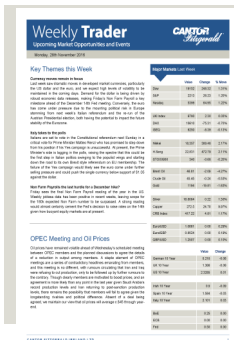
Management are now focused on delivering on synergies and deleveraging within the group with the sale of Dole’s head office and Scandinavian salad business already completed in 2018 highlighting this. The Dole acquisition should lead to margin expansion for Total Produce given the vertical integration benefits. It also gives Total Produce much greater exposure to the North American market and value added vegetables food category.

A stronger than expected Del Monte results at the end of April followed by guidance being maintained at Total Produce may imply that recent industry headwinds are abating.

We remain of the view that Total Produce is a “best in sub-industry” investment. Given our concerns about equity volatility in the short term (6-12 months), our base case is that Total Produce should trade up above €2 over the medium-long term (2-3 years) with this outcome likely to be reached sooner if Dole leverage is brought down faster than expected.

Darren McKinley, CFA | Senior Equity Analyst

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Weekly Trader

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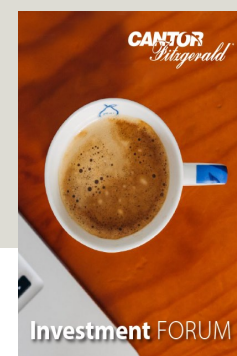
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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

Total Produce PLC : Total Produce PLC markets and distributes a wide range of branded fresh produce to pan European and National retailers and wholesaler.

Historical Recommendation:

Total Produce PLC: We changed our recommendation from Under Review to Market Perform on the 31/05/2019

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