

Wednesday, 02nd October 2019

Morning Round Up

Economic data points to contraction

A slew of economic data released yesterday continued to point to slowing economic growth. As we have noted for some time, global economic data has been trending lower, particularly in the manufacturing sector with its leading indicators sitting on decade low levels. Yesterday morning's final reading of the European manufacturing PMI came in at just 45.7, the lowest level since 2012. Notably the reading has steadily deteriorate since the end of 2017, without any major bounce backs. Again, Germany was the driver of this weakness with a reading of just 41.7. Worryingly, the manufacturing weakness appears to be beginning to weigh on the services sectors, which last week posted its weakest number since January. However, it was the economic data from the US which led to a sell off in US equities yesterday evening and Europe this morning. The US ISM manufacturing PMI released yesterday afternoon was at 10 year lows at just 47.1. Within this, new orders (47.3), prices (49.7) and employment (46.3) were all weak. Given it's historical correlation with earnings and GDP growth this number will worry investors. While this data will reaffirm both the ECB's and Fed's latest monetary softening, it is quite clear a resolution or even an easing on trade tension is necessary to spur growth. Services data and the non farm payrolls data will be influential later this week. Up until we see an improvement in the data we continue to advise clients to maintain a bias toward defensive securities.

Johnson to close Party Conference with long awaited Brexit strategy

Boris Johnson is expected to deliver the keynote speech on the last day of the Conservative Party Conference in Manchester this morning. The speech is expected to include Mr Johnson's and the UK Government's final position on Brexit. Leaked reports suggest that the proposal will include customs control points both North and South of the border, Northern Ireland to remain in an all-Ireland food zone as well as alignment on Industrial goods. After four years, Stormont would have a decision to make regarding alignment to the EU (resulting in a border through the Irish sea) or the UK (a hard border on the Island of Ireland). Irish officials have reacted negatively to the proposal, with Tánaiste Simon Coveney referring to the plan as "concerning". If the EU reject Mr Johnson's deal, which is expected to be formal submitted to the European Union today, the UK will step back from negotiations and prepare for a "no deal" exit. In this event, focus will switch to how the Government intend to circumvent the Benn Act requiring the Prime Minister to request an extension if no deal reached by October 19th. While the opposition parties will likely be manoeuvring to secure an Article 50 extension prior to calling a general election. The pound has weakened on the news trading above £0.89 briefly yesterday.

Grafton Group sell Plumbase to specialised investors

Grafton Group announced this morning the completion of the sale of Plumbase to specialised investors Plumbing and Heating Investments Ltd. The business achieved an enterprise value (EV) of £66.75m, with net cash proceeds of £60.7m received. Plumbase generated operating margin of less than 3% compared to the group's overall operating margin of 7%, which is in line with management's strategy of focusing on higher margin businesses. With £3m in operating profit in FY18, the business has achieved a valuation of c. 11x, which is marginally higher than Grafton's trailing EV/EBITDA of 10.5x. Overall, this is a positive transaction that should support stronger margins going forward at a fair price.

Key Upcoming Events

17/10/2019 ECB Leaders Summit
31/10/2019 Brexit Day

Market View

European equities have followed their US and Asian counterparts lower this morning following the weak economic data released yesterday. As a result defensive stocks are outperforming this morning with staples, real estate and utilities among the strongest sectors. Investors will look to the services and employment data released later this week for any signs of deterioration in the consumer economy. Elsewhere, prior to Boris Johnson delivering his Brexit proposals later today, the pound has weakened. Oil has snapped a six day losing streak as a surprise drop in US stockpiles and falling OPEC output offset the latest macroeconomic fears.

Market Moves

| | Value | Change | % Change | % Change YTD |
|-----------|-------|---------|----------|--------------|
| Dow Jones | 26573 | -343.79 | -1.28% | 13.91% |
| S&P | 2940 | -36.49 | -1.23% | 17.29% |
| Nasdaq | 7909 | -90.65 | -1.13% | 19.19% |

| | | | | |
|-----------|-------|---------|--------|-------|
| Nikkei | 21779 | -106.63 | -0.49% | 8.81% |
| Hang Seng | 26015 | -77.70 | -0.30% | 0.65% |

| | | | | |
|-----------|-------|------|-------|--------|
| Brent Oil | 59.12 | 0.23 | 0.39% | 9.89% |
| WTI Oil | 53.96 | 0.34 | 0.63% | 18.83% |
| Gold | 1479 | 0.32 | 0.02% | 15.36% |

| | | | | |
|------|--------|---------|--------|--------|
| €/£ | 1.0913 | -0.0020 | -0.18% | -4.83% |
| €/€ | 0.8891 | 0.0005 | 0.05% | -1.10% |
| £/\$ | 1.2275 | -0.0027 | -0.22% | -3.76% |

| | Yield | Change |
|----------------|--------|--------|
| German 10 Year | -0.534 | 0.030 |
| UK 10 Year | 0.528 | 0.058 |
| US 10 Year | 1.651 | 0.016 |

| | | |
|---------------|-------|-------|
| Irish 10 Year | 0.003 | 0.035 |
| Spain 10 Year | 0.17 | 0.021 |
| Italy 10 Year | 0.869 | 0.011 |

Flutter Entertainment - Bets big on US market via cheap acquisition of TSG

Closing price €85.62

News

Flutter Entertainment has announced this morning an all share combination with “The Stars Group” which will see TSG being acquired by Flutter for £4.95bn. TSG shareholders will be entitled to 0.2253 new shares in exchange for each TSG share. The offer represents a premium of 38.2% to Stars Group closing price on Oct 1st. Post the acquisition, Flutter will retain 54.64% of the combined group with TSG shareholders holding 45.36%.

The combined group revenue will be £3.8bn, up from £2.15bn for Flutter reported in 2018. Combined operating profit in 2019 is expected to be £588m with synergies of £140m highlighted. Flutter’s Chair, CEO and CFO to retain same roles in combined group. TSG CEO to become COO and TSG executive Chair to become Deputy Chair.

The implied valuation multiple being paid by Flutter Entertainment is 12.2x 2019 earnings – which is an extremely attractive valuation relative to Flutter. It is also less than 5x EV/EBITDA for a company offering a return on equity of 12%.

The acquisition is viewed as increasing the companies scale and exposure in key growth markets, particularly the US. Further consolidation is also positive for the industry. Regulatory hurdles need passed yet with the deal not likely to complete until H2 2020. Flutter estimates that the transaction will be c.50% accretive to earnings per share through 2022 approximately.

The combination will see Flutter add brands such as Poker Stars, Sky Bet to its Paddy Power, Betfair, Sports Bet and FanDuel brands currently. The deal increases group exposure to the poker and exchange market.

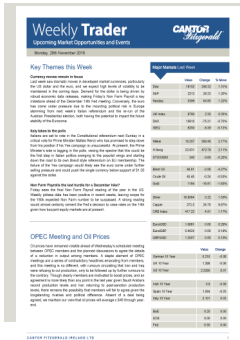
Comment

Following very strong interim results at Flutter with 9% like for like revenue growth reported and 15% EBITDA growth adjusting for taxes. Group free cash flow also surged in H1. We turned more positive on Flutter post these results but kept our preference for GVC.

We like this acquisition and we credit Peter Jackson with a strong delivery since taking over as CEO. Our recommendation is under review, having been at market perform.

Darren McKinley, CFA | Senior Equity Analyst

Cantor Publications & Resources



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Regulatory Information

Issuer Descriptions: (Source: Bloomberg)

Flutter Entertainment: Flutter Entertainment is a betting and gaming company. The Company provides online betting and gaming products.

Historical Recommendation:

Flutter Entertainment: Flutter Entertainment has been moved to under review from market perform on the 02/10/2019

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