

Deutsche Bank Markets Research

Rating

Hold

North America

United States

Company

Apple Inc.

Date

1 May 2018

Results

TMT

IT Hardware and Supply Chain

Reuters

AAPL.OQ

Bloomberg

AAPL US

Exchange

NSM

Ticker

AAPL

Price at 1 May 2018 (USD)

Price target

52-week range

169.10

165.00

181.72 - 142.27

F2Q-18 results: Better than feared

Robust cash returns and strength in Services oﬀset below-Consensus iPhone Apple's F2Q-18 sales were in line with expectations as strength in Services and Wearables oﬀset below-Consensus iPhone results. Despite numerous negative

supplier comments over the past few weeks, Apple's iPhone results weren't as bad as feared, with units only slightly lower than Street estimates. Two key highlights from the call were the strength in Services and the additional $100B in buyback authorization, which mgmt indicated would be done at a "fast" pace. We continue to be more cautious on iPhone growth in the coming quarters, but admit that the $100B buyback will create somewhat of a ﬂoor for shares. With positives and negatives largely balanced at current levels, we view valuation as fair and maintain our Hold.

Positive takeaways

Services sales growth of 31% Y/Y was robust this quarter, and well above expectations, reﬂecting broad strength across Apple's oﬀerings, including App

Store, Apple Music, iCloud and Apple Pay. Paid subscribers now total over 270M

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Key changes

TP 152.00 to ↑ 8.6%

165.00

EPS (USD) 10.88 to 11.35 ↑ 4.4%

and increased by 100M Y/Y and 30M Q/Q. Wearables (Apple Watch, Air Pods, and Beats) also beat expectations, with sales growing almost 50% Y/Y, contributing to the 38% Y/Y growth in Other Products. China was also a bright spot this quarter, with healthy demand across product categories helping to drive 21% Y/Y growth, the region's highest growth rate in 10 quarters. Finally, capital returns were a key positive, with Apple announcing a new $100B share buyback authorization and a 16% increase in the dividend.

Revenue

(USDm)

*Source: Deutsche Bank*

Price/price relative

200

150

100

50

253,185.0 to ↑ 2.2%

258,630.0

Drawbacks

Admittedly, there were few negatives in the quarter. iPhone sales of $38B and units of 52M were modestly below Street expectations, but better than feared after recent negative supplier comments. Inventory was up 73% Q/Q, something which is expected to be worked down, but a metric we would continue to monitor. Finally, while EPS beat the Street by $0.04, much of this came from lower OpEx and a lower tax rate versus guidance.

Adjusting estimates higher for buyback and raising PT $165; maintain Hold

We have raised our EPS estimates to reﬂect the additional $100B in buybacks, while our operating results only tick modestly higher. As a result of our higher EPS, we are raising our PT to $165 from $152 PT. Our target is based on 13x our updated FY-19E EPS, vs our prior 14x, which is in line with the company's historical average. Positive risks: stronger-than expected smartphone sales and

Jul '16 Jan '17 Jul '17 Jan '18

**Apple Inc. S&P 500 INDEX (Rebased)**

Performance (%) 1m 3m 12m

Absolute 0.8 0.8 15.4

S&P 500 INDEX 0.3 -6.2 10.9

*Source: Deutsche Bank*

*Please see our variance charts for F2Q-18 and F3Q-18 on p.3-4.*

share gains, and signiﬁcantly higher margins. Negatives: slower smartphone sales, and market share losses.

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| --- | --- | --- | --- | --- |
| Forecasts and ratios |  | | | |
| Year End Sep 30 | 2017A | 2018E | 2019E | 2020E |
| 1Q EPS | 3.36 | 3.89A | 4.55 | 4.98 |
| 2Q EPS | 2.10 | 2.73A | 3.00 | 3.28 |
| 3Q EPS | 1.67 | 2.17 | 2.38 | 2.56 |
| 4Q EPS | 2.07 | 2.53 | 2.78 | 2.93 |
| FY EPS (USD) | 9.21 | 11.35 | 12.80 | 13.80 |
| OLD FY EPS (USD) | 9.21 | 10.88 | 10.80 | 11.15 |
| Revenue (USDm) | 229,234.0 | 258,630.0 | 255,325.0 | 257,780.0 |
| *Source: Deutsche Bank estimates, company data* |  |  |  |  |

# Valuation

Apple has traded at an average forward P/E of 13x since 2010 with a range of 9x to 16x. We believe shares should trade in line with these historical multiples and, because of its large market cap (3-4% of the S&P 500), should trade at a modest discount to the market. Our price target is based on shares trading at 13x our FY-19E EPS.

# Risks

Company-speciﬁc positive risks to Apple include stronger-than-expected smartphone sales and share gains, signiﬁcantly higher margins, and a faster ramp of new product categories including Watch and Apple Pay. Negative risks include slower smartphone sales, market share losses in smartphones, and weaker growth in Services sales.