

Deutsche Bank Markets Research

North America

United States

TMT

IT Hardware and Supply Chain

Industry

Scribner's Slice of Apple

Date

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Periodical

A weekly take on Apple news

For the week ending June 1, 2018

With Apple's Worldwide Developer Conference kicking oﬀ on Monday, Apple- related news this week included media predictions for possible software and hardware announcements. Of note, Apple could announce a broader use of the NFC chip in iPhones and software tools to help break iPhone addiction could be included in the upcoming iOS update. In other news, a Korean source suggests all 2018 iPhone devices could feature OLED screens, a second PMIC supplier will be added for 2018 iPhones, and the App Store accounted for two-thirds of 2017 global app spend. Also, Apple saw a 20% Y/Y increase in C2H-17 national security requests, Apple has hired several former Intel employees to staﬀ an Oregon- based hardware engineering lab, Apple Music has formed a division focused on songwriting and music publishing, and Apple plans to develop an original TV series on the life of Emily Dickinson.

NFC chips in iPhone could soon be used for more than Apple Pay

Apple could be expanding the use of the near-ﬁeld communication (NFC) chip in iPhones, according to the Information. Originally introduced in iPhone 6 and 6s in 2014, NFC chips allow for the wireless transfer of sensitive data without an internet connection, thus enabling secure Apple Pay payments. While other smartphone makers have been using NFC technology more broadly, Apple has limited the use of iPhone NFC chips to Apple Pay. However, The Information reports that Apple employees are currently using their iPhones to access buildings and unlock doors at work, suggesting iPhone NFC chips have been enabled to work with smart locks. The report suggests Apple could announce an iOS update allowing the use of iPhone NFC chips for a range of "security sensitive interactions" next week at the company's upcoming Worldwide Developers Conference.

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Software tools to discourage iPhone addiction coming

Apple is reportedly planning to release a set of tools that will allow users to monitor their device usage and the time spent in certain apps, according to Bloomberg. The initiative, called Digital Health, is expected to be announced at Apple's Worldwide Developers Conference next week, and released as part of the mobile operating system update.

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Companies featured

Apple Inc. (AAPL.OQ),USD186.87 Hold

2017A 2018E 2019E

EPS (USD) 9.21 11.35 12.80

P/E (x) 14.9 16.5 14.6

EV/EBITDA (x) 7.9 9.9 9.8

*Source: Deutsche Bank*

*Our price target is based on shares trading at 13x our FY-19E EPS. Upside risks 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. Downside risks include slower smartphone sales, market share losses in smartphones, and weaker growth in Services sales.*

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Report suggests all 2018 iPhone models could feature OLED displays

Apple is reportedly planning to use OLED panels in all of the upcoming iPhone models this year, according to sources cited by South Korea's Electronic Times. Currently, only iPhone X features an OLED screen with all other iPhone models using LCD screens. However, analysts cited in a Bloomberg article cast some doubt on the Electronic Times report, given OLED supply constraints as well as the higher cost of OLED panels relative to LCD displays. (ht[tps://www.bloomberg.com/ne](http://www.bloomberg.com/news/articles/2018-05-29/asia-display-makers-dip-)ws/art[icles/2018-05-29/asia-display-makers-dip-](http://www.bloomberg.com/news/articles/2018-05-29/asia-display-makers-dip-) on-report-apple-will-go-all-oled-in-2018)

Second PMIC supplier expected for 2018 iPhone

Apple is planning to add a second iPhone power management chip (PMIC) supplier for its upcoming iPhone models, according to Dialog Semiconductor. Based on a Dialog Semi statement, Apple has cut its PMIC order volumes, resulting in a 5% reduction in Dialog Semi's FY-18 sales expectations. According to Reuters, Apple will cut its chip orders with Dialog Semi by 30% this year. (ht[tps://www](http://www.dialog-semiconductor.com/sites/default/%EF%AC%81les/).d[ialog-semiconductor.com/sites/def](http://www.dialog-semiconductor.com/sites/default/%EF%AC%81les/)aul[t/ﬁles/](http://www.dialog-semiconductor.com/sites/default/%EF%AC%81les/) press\_release\_31.05.18\_ﬁnal.pdf)

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App Store sales account for two-thirds of 2017 global app spend

In a report commemorating the App Store's 10th year, App Annie reported that worldwide App Store sales totaled $42.5B in 2017, up 31% Y/Y, and are expected to reach $53.1B in 2018. App Store sales continue to dominate the app market and accounted for two-thirds of consumer app spend globally in 2017 versus Google Play's one-third share. In contrast, Google Play remains the leader in app downloads with 70% share of worldwide downloads, compared to the App Store's 30% share. Games accounted for 31% of App Store downloads in 2017 and 75% of spend. Geographically, spend in APAC grew by 38% Y/Y and reﬂected 60% of 2017 App Store sales.

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C2H-17 transparency report reveals spike in national security requests

Apple received 16,249 national security requests related to 8,249 accounts in C2H-17, an increase of 20% over C1H-17, and more than 2.5x the amount of comparable requests in C2H-16. The company also disclosed 29,718 requests for data or information involving 309,362 devices, and plans to begin providing data on government requests to remove apps from the App Store. According to Reuters, other tech giants are also seeing an increase in data requests, with Facebook reporting a 100% increase vs. Google's 36% increase in requests from C2H-16 to C1H-17. Both companies have yet to report C2H-17 data, as they also disclose Foreign Intelligence Surveillance Act requests which require a six-month reporting delay.

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Apple reportedly hiring away Intel engineers and research staﬀ

Since November 2017, Apple has reportedly hired "close to two dozen" senior engineers and researchers from Intel and other Oregon-based tech ﬁrms,

according to Oregon Live. The new hires are working out of a hardware engineering lab located in Washington County, Oregon. While it is unclear what project the new team is working on, Apple's local job listings suggested the company was looking for individuals with design veriﬁcation experience, or the ability to ensure that product's initial design speciﬁcations are fully realized in the completed product.

[(http://www.oregonlive.com/silicon-forest/index.ssf/2018/05/](http://www.oregonlive.com/silicon-forest/index.ssf/2018/05/) apple\_quietly\_opens\_oregon\_eng\_1.html) (https://9to5mac.com/2018/05/31/apple-intel-chip-engineers/#more-535542)

Apple Music adding global music publishing division

Apple Music has formed a new internal division focused on music publishing and publishers, according to Music Business Worldwide. The group will be headed by Elena Segal, who was the legal director of iTunes International. The report suggests Apple Music's new head Oliver Schusser is focused on developing Apple's relationships with songwriters and music publishers. (ht[tps://www.musicbusinessworldwide.com/apple-music-launches-music-](http://www.musicbusinessworldwide.com/apple-music-launches-music-) publishing-division-headed-by-elena-segal)

Original TV series on the life of Emily Dickinson in development

Apple has announced plans to develop a new half-hour comedy series about the life of the poet Emily Dickinson, according to TechCrunch. The series will star Hailee Steinfeld as Dickinson and is expected to be launched next March. The show is one of several recently announced TV projects by Apple and is thought to be part of a new subscription service coming next year. [(http://dead](http://deadline.com/2018/05/hailee-steinfeld-star-dickinson-comedy-series-)l[ine.com/2018/05/hailee-steinfeld-star-dickinson-comedy-series-](http://deadline.com/2018/05/hailee-steinfeld-star-dickinson-comedy-series-) apple-emily-dickinson-1202400062/)

Apple Investment Thesis

Outlook

Apple has a dominant position in smartphones and tablets where its products represent the gold standard in both categories. These segments continue to oﬀer good growth opportunities, particularly smartphones, allowing Apple to outgrow overall IT spending. Despite healthy growth, slowing smartphone and tablet sales, as well as Apple’s already signiﬁcant revenue levels suggest growth will be more diﬃcult going forward. With puts and takes currently balanced, in our view, we consider shares as fairly valued and rate Apple a Hold.

## 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.