

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 8, 2018

Apple's Worldwide Developer Conference was the main focus of Apple-related news this week, although the updates announced to the company's four operating platforms were largely in line with expectations. In other news, Apple could cut C2H-18 iPhone supplier orders by 20% Y/Y to 80M units, C1Q-18 Indian smartphone market data suggests limited share opportunities for iPhone, and Apple Watch remained the global wearables market leader in C1Q-18. Also, Apple could be adopting new MacBook procurement processes with an eye to negotiating more favorable pricing, the App Store will now oﬀer free trials on all apps, and Apple is reportedly planning to produce two more TV series.

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OS updates, including new security/time management features, key WWDC highlights

At its annual Worldwide Developers Conference (WWDC), Apple introduced

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| updates to its four operating platforms; macOS, iOS, tvOS and WatchOS. Updates | EPS (USD) | 9.21 | 11.35 | 12.80 |
| in macOCS included enhanced security features that will make it more diﬃcult | P/E (x) | 14.9 | 17.0 | 15.1 |
| for websites to uniquely identify an individual user's device and also will add | EV/EBITDA (x)  *Source: Deutsche Bank* | 7.9 | 10.3 | 10.3 |

Companies featured

Apple Inc. (AAPL.OQ),USD193.46 Hold

2017A 2018E 2019E

protection on what personal data third-party apps receive. Apple also announced new features on iOS to limit the intrusiveness of smartphones and to help users manage their screen time across devices and apps. As expected, there were no hardware announcements at the event, and we view the software updates as more incremental than game-changing.

( [link](https://research.db.com/Research/Document?rid=85979589-ff17-4298-a13d-f3881c6d7a9c-604&amp;kid=RP0001&amp;documentType=R) )

iPhone component orders could fall by 20% Y/Y in C2H-18

Apple has reportedly told suppliers that iPhone component orders could drop by 20% Y/Y in C2H-18, according to the Nikkei. The report suggests Apple plans to launch three new iPhone models, two featuring OLED displays and one with an LCD display, with combined units expected to total 80M. Sources suggest the three models will begin shipping in September, although the two OLED devices will be ready for assembly in July vs an expected August release of the LCD iPhone model.

(https://asia.nikkei.com/Business/Companies/Apple-warns-suppliers-of-20-drop- in-new-iPhone-parts-orders)

C1Q-18 data on India smartphone market suggests limited room for iPhone Most of the phones sold in India are lower priced smartphones that cost less than

$200, according to CNN. While the high end of the market is gaining traction, with

*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.*

IDC estimating phones priced above $600 grew 68% Y/Y in C1Q-18, Samsung and Apple are seeing increasing competition from OnePlus. The Chinese brand has gained traction in India with richly featured smartphones in the $400-$600 price range, and reportedly has over 50% market share in this price range in India. Given the high share of low-cost phones in India and the signiﬁcant brand recognition of makers like OnePlus at the higher end, we believe it will be diﬃcult for Apple to gain substantial share in the Indian smartphone market. [(http://mone](http://money.cnn.com/2018/06/05/technology/oneplus-6-india-smartphone/)y[.cnn.com/2018/06/05/technology/oneplus-6-india-smartphone/](http://money.cnn.com/2018/06/05/technology/oneplus-6-india-smartphone/) index.html)

(ht[tps://www.idc.com/getdoc.jsp?containerId=prAP43810918)](http://www.idc.com/getdoc.jsp?containerId=prAP43810918))

Apple Watch remains top vendor in C1Q-18 wearables market

Global wearables shipments reached 25.1M units in C1Q-18, up 1.2% Y/Y, according to IDC. For the second straight quarter, Apple was the top selling wearables vendor with 16% unit share, a 2ppts gain Y/Y, with units growing 14% Y/Y. A top Chinese smartphone vendor was in second place with 15% share, followed by Fitbit with 9% share. Huawei and Garmin both shipped 1.3M units in the quarter and were essentially tied for fourth place. (ht[tps://www.idc.com/getdoc.jsp?containerId=prUS43900918)](http://www.idc.com/getdoc.jsp?containerId=prUS43900918))

Apple may be adopting new procurement practices

Apple is reportedly in discussions with third-party suppliers regarding the prices of non-critical parts for MacBooks, according to Digitimes. Some of the relevant parts include screws, and metallic and plastic parts required by contracted suppliers for their production of key components. The report suggests the move is part of Apple's eﬀorts to reduce the proﬁt margins of contracted supply partners and part of a larger eﬀort to expand centralized procurement to materials including copper and cobalt. (ht[tps://www](http://www.digitimes.com/news/a20180604PD202.htm)).digit[imes.com/news/a20180604PD202.htm)](http://www.digitimes.com/news/a20180604PD202.htm))

App Store now allowing free trials for all apps

In an update to its App Store guidelines, Apple will now allow all paid apps to oﬀer a free trial period. Prior to the guideline revision, free trials were only permitted for subscription-based apps. Apple revised a number of other guidelines, including those related to the use of in-app advertising, data security standards, and cryptocurrency mining.

(https://developer.apple.com/app-store/review/guidelines/) (https://9to5mac.com/2018/06/04/new-app-store-review-guidelines/)

Original TV series "Little Voices" and adaptation of "Shantaram" in the works Apple is planning to produce a new half-hour TV show called "Little Voices", produced by J.J. Abrams and Sara Bareilles, according to Variety. The 10-episode

series is expected to explore musical development and diversity in New York City. Separately, Variety reported that Apple has acquired the rights to produce a TV series based on the novel "Shantaram," Gregory David Robert's best-selling 2003 novel.

(https://variety.com/2018/tv/news/j-j-abrams-sara-bareilles-apple-little- voices-1202832614/)

(https://variety.com/2018/tv/news/shantaram-apple-series-1202835845/)

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.