

Deutsche Bank Research

North America

United States

TMT

IT Hardware and Supply Chain

Industry

Scribner's Slice of Apple

Date

17 June 2018

Periodical

A weekly take on Apple news

For the week ending June 15, 2018

In key Apple news this week, the company’s build plans suggest lower-priced LCD iPhone models may be more popular than OLED models. In other news, Apple patched security loopholes that allowed law enforcement to crack locked iPhones, and Oprah has reportedly signed an agreement with Apple to produce original TV content. Also of interest this week, Apple could be making an animated movie with Cartoon Saloon, the company banned cryptocurrency mining on its devices, next year’s Apple Watch could feature a touch-sensitive side button, and Apple and Qualcomm's long-standing legal ﬁght heads to courts in multiple countries starting next week.

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Demand for new iPhone with LCD display could exceed OLED version Production plans for Apple's upcoming 2018 iPhone models reportedly suggest that the company expects to sell more devices with LCD displays than those

featuring OLED, according to the Wall Street Journal. The report suggests that the potential popularity of new LCD devices could reﬂect greater consumer price sensitivity than the company initially expected. In addition, Apple may now be planning to make an LCD iPhone model in 2019, in contrast to prior reports that 2019 iPhones would exclusively use OLED screens. (ht[tps://www.wsj.com/articles/iphone-x-pensive-apple-looks-to-keep-phones-](http://www.wsj.com/articles/iphone-x-pensive-apple-looks-to-keep-phones-) with-cheaper-displays-1529051835)

(https://9to5mac.com/2018/06/15/2018-iphone-models-oled-lcd/#more-538461)

Apple to patch up security loopholes used by law enforcement

In an upcoming iOS update, Apple is planning to eliminate an iPhone security weakness that has allowed U.S. law enforcement agencies to crack locked iPhones, according to TechCrunch. The software patch will block the use of an iPhone's USB port an hour after the device has been locked for anything other than battery charging.

(https://techcrunch.com/2018/06/13/apple-conﬁrms-that-it-will-seal-up-law- enforcements-favorite-iphone-cracking-method/)

Oprah to create original TV content for Apple

Media celebrity Oprah Winfrey has reportedly signed a multi-year agreement with Apple to produce original TV programming content, according to Vanity Fair. Details on the types of programming and timing have not yet been disclosed. We view this as a big boost to Apple’s ongoing eﬀorts to build an extensive library

Companies featured

Apple Inc. (AAPL.OQ),USD190.70 Hold

2017A 2018E 2019E

EPS (USD) 9.21 11.35 12.80

P/E (x) 14.9 16.8 14.9

EV/EBITDA (x) 7.9 10.1 10.1

*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.*

of original TV content, which, as we have written in previous Slices, some media sources expect to debut starting next year (ht[tps://www](http://www.vanityfair.com/hollywood/2018/06/oprah-apple-multi-year-).v[anityf](http://www.vanityfair.com/hollywood/2018/06/oprah-apple-multi-year-)air[.com/hollywood/2018/06/oprah-apple-mul](http://www.vanityfair.com/hollywood/2018/06/oprah-apple-multi-year-)t[i-year-](http://www.vanityfair.com/hollywood/2018/06/oprah-apple-multi-year-) partnership-original-content)

Cartoon movie deal could be coming

Apple is reportedly close to ﬁnalizing the rights to an animated ﬁlm with Cartoon Saloon, a well-known animation studio, according to Bloomberg. Production and distribution details, including timing, for the project are unknown but the report suggests that the movie is more than a year away from release. (ht[tps://www.bloomberg.com/ne](http://www.bloomberg.com/news/articles/2018-06-14/apple-is-said-to-near-)ws/art[icles/2018-06-14/apple-is-said-to-near-](http://www.bloomberg.com/news/articles/2018-06-14/apple-is-said-to-near-) deal-for-animated-movie-in-hollywood-push)

Apple bans on-device cryptocurrency mining apps

In an update to its App Store guidelines, Apple has banned apps that mine cryptocurrency across all of its device platforms. Earlier this year, Apple removed the app Calendar 2 from the Mac App Store after it started mining cryptocurrencies on users' devices in exchange for premium features. The new guidelines allow virtual currency wallet apps, and cryptocurrency mining apps that mine in the cloud, but do not allow third-party apps that send and receive cryptocurrencies.

(ht[tps://www](http://www.theverge.com/2018/6/11/17449178/apple-app-store-).thev[erge.com/2018/6/11/17449178/apple-app-store-](http://www.theverge.com/2018/6/11/17449178/apple-app-store-) cryptocurrency-mining-ban-ios-macos/)

Apple Watch to get a touch-sensitive side button

Apple is reportedly planning to replace physical side buttons on the Apple Watch with solid state buttons which are touch-sensitive, according to Fast Company. The new buttons are expected to be announced this fall or on the 2019 version of Apple Watch.

(ht[tps://www](http://www.fastcompany.com/40583301/apple-watch-will-soon-get-touch-).f[astcompan](http://www.fastcompany.com/40583301/apple-watch-will-soon-get-touch-)y[.com/40583301/apple-watch-will-soon-get-touch-](http://www.fastcompany.com/40583301/apple-watch-will-soon-get-touch-) sensitive-solid-state-buttons)

Apple and Qualcomm heading to court starting next week

Court hearings related to the ongoing royalty payment dispute between Apple and Qualcomm are expected to start in the coming days and weeks, according to Bloomberg. The hearings being conducted most notably in the U.S., China, and Germany are expected to cover a range of patent infringement claims between the two companies. In the U.S., Qualcomm has claimed that Apple is infringing on three of its patents, and seeks a ban of the import of iPhone 7 models that don't use Qualcomm chips. The article estimates that Apple may be liable for $2.5-$4.5B in unpaid royalty payments to Qualcomm, or roughly one-ﬁfth of Qualcomm's annual sales.

(ht[tps://www.bloomberg.com/ne](http://www.bloomberg.com/news/articles/2018-06-11/apple-qualcomm-legal-)ws/art[icles/2018-06-11/apple-qualcomm-legal-](http://www.bloomberg.com/news/articles/2018-06-11/apple-qualcomm-legal-) tangle-heading-for-clarity-as-trials-begin)

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.