

Deutsche Bank Markets Research

North America

United States

TMT

IT Hardware and Supply Chain

Industry

Scribner's Slice of Apple

Date

3 November 2017

Periodical

A weekly take on Apple news

For the week ending November 3, 2017

Top of mind for investors in Apple news this week was Apple's quarterly results and the fact that the highly-anticipated iPhone X became available on Friday, with many Apple news sites reporting lines at Apple stores worldwide. The company's September quarter results were above expectations driven by double-digit sales growth in all segments except for iPhone. Also this week, reports emerged that iPhone X suppliers had been asked to increase production due to strong demand, while shortening iPhone X delivery delays pointed to improving supply. In other news, Chinese retailers rolled out discounts of up to 20% on iPhone 8 models, Qualcomm may be excluded from future iPhones and iPads, Qualcomm also ﬁled a new suit against Apple, and Apple is replacing some Apple Watch 3 devices which have defective displays. And in case you were wondering, Apple disclosed that its most popular emoji by far in the U.S. is the "face with tears of joy." LOL.

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Companies featured

Apple Inc. (AAPL.OQ),USD168.11 Hold

2017A 2018E 2019E

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Apple reports good F4Q-17 results as we wait for the main event | EPS (USD) | 9.21 | 10.45 | 9.70 |
| Apple reported above-Street F4Q-17 sales and EPS, driven by double-digit sales | P/E (x) | 14.9 | 16.1 | 17.3 |
| growth in all segments except iPhone. F1Q-18 sales guidance was a bit higher | EV/EBITDA (x) | 7.9 | 8.7 | 9.4 |
| than Street expectations, suggesting some of the supply concerns are overdone. | *Source: Deutsche Bank* |  |  |  |
| While results were solid, we believe investors' main focus is on whether Apple can sell a $1,000 premium phone in signiﬁcant quantities, something we won't have a good sense of until later this year, at the earliest. Until then, we expect bulls and bears to remain in their own camps, with this quarter's results unlikely  to sway views. |  |  |  |  |

[(http://pull.db-gmresearch.com/cgi-bin/pull/](http://pull.db-gmresearch.com/cgi-bin/pull/)

DocPull/127-11E0/7735990/4031f1de-bf97-11e7-a788-17efe23f6f57\_604.pdf)

iPhone X suppliers asked to increase production

Taiwanese suppliers for the iPhone X are reporting that Apple has asked them to double their output due to better-than-expected pre-order levels for the device, according to The Economic Daily News of Taiwan. An Apple spokesperson speaking to Reuters conﬁrmed strong customer demand for the iPhone X and noted that pre-order levels for the device were “oﬀ the charts.” The iPhone X became available in stores on Friday, with MacRumors and other Apple sites reporting long lines at stores worldwide.

[(http://www.reuters.com/article/us-apple-iphone/apple-says-iphone-x-pre-](http://www.reuters.com/article/us-apple-iphone/apple-says-iphone-x-pre-) orders-are-oﬀ-the-charts-idUSKBN1CW286) (https://money.udn.com/money/story/5612/2786157?ref=tab20171030)

Improving iPhone X wait times

*Our price target is based on shares trading at 16x 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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Some customers who pre-ordered the iPhone X on launch day (Oct 27) reportedly saw an improvement in their expected delivery times, according to Apple Insider. Several of the iPhone X's earliest pre-order day customers that were given an original delivery window of Nov 10 to Nov 17 were moved up to a Nov 3 delivery. Our checks on Apple's website on Friday showed a 3-4 week ship time, vs. the 5-6 week wait time quoted last week, suggesting supply of the iPhone X has improved.

[(http://appleinsider.com/articles/17/10/29/apple-impr](http://appleinsider.com/articles/17/10/29/apple-improves-iphone-x-delivery-)o[ves-iphone-x-delivery-](http://appleinsider.com/articles/17/10/29/apple-improves-iphone-x-delivery-) dates-for-iphone-upgrade-program-orders-impacted-by-ﬁnancing-issue)

iPhone 8 prices lowered in China

Mainland Chinese online retailers are discounting the iPhone 8 by up to 20% due to weak demand for the devices, according to Reuters. Pricing data suggest a 64GB iPhone 8 is selling for the equivalent of $722 vs. the device's $889 original price in China and $699 price in the U.S.

[(http://www.reuters.com/article/us-apple-iphone-china/ahead-of-iphone-x-](http://www.reuters.com/article/us-apple-iphone-china/ahead-of-iphone-x-) launch-china-vendors-cut-prices-of-iphone-8-models-idUSKBN1D018F)

Qualcomm chips could be excluded from upcoming iPhones and iPads

Apple is looking to discontinue the use of Qualcomm modem chips in future iPhone and iPad models, according to the Wall Street Journal. Following Apple's January lawsuit, Qualcomm stopped providing Apple with the software necessary to test chips that are used in device prototypes. The report suggests Apple is considering replacing Qualcomm's chips with ones manufactured by Intel or MediaTek. Following the report, Bloomberg reported that Qualcomm had ﬁled a new lawsuit against Apple alleging breach of contract and accusing the company of sharing proprietary data with Intel.

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Display issue in Apple Watch 3

Some owners of the Apple Watch 3 GPS devices have noted the appearance of unusual stripes on their watch's display edges when turned oﬀ. Apple is replacing defective watches, instead of repairing them. (https://9to5mac.com/2017/10/31/apple-watch-series-3-display-edge-stripes- markings/)

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 16x 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.