

NIC

— Nova Investment Club —

Newsletter

March 2019



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Foreword

This Month:

In our Macro Overview section, Analysts from both divisions will cover broad macro themes while reviewing major economic news from the past month. In our Deeper Dive section, Mariana Costa elaborates on the Chinese capital markets increased access to international investment, as MSCI plans to enlarge the country's weight in the index. Moreover, in our Regional View, Gonçalo Marques examines China's housing market amidst a growing economic slowdown.

Our Investment Banking Division will guide you through February's M&A overall activity. Read about Barrick Gold hostile offer for Newmont Mining, Morgan Stanley plans to acquire Solium Capital and Merck intentions to bid for Versum Materials. Additionally, get a detailed overview on what happened to Activision Blizzard and Under Armour, as well as consider our opinion on Lyft's upcoming IPO.

Our Financial Markets Division will present the monthly results of the NIC Fund, an active relative return fund investing across four different asset classes: Equities, Fixed Income, Commodities and Currencies. The analysts will also provide commentary on each of the four major asset classes through analysis of the past month's major market moves. The active positioning of the NIC Fund in January was slightly inferior to the benchmark.

Lastly, Vera Teixeira Wahnnon elaborates on Brexit prospects and Lisa Preußler examines the recent crisis on the Indian non-bank financial company sector. Furthermore, Rita Silva Marques analyses the US-China trade war recent developments.



The following content is original and created by the Nova Investment Club, which is run by students from Nova SBE's Master's in Finance. The reports may contain inaccurate or outdated information and should not be used as an exclusive mean for investment decisions.

Macro Overview

Monthly

March 4th, 2019

Deeper Dive

China's Capital Markets: International Capital

— p.2

Regional view

China Housing Market: Will a Bubble Pop?

— p.3

Market Moves

Market Moves

% change

	Last Close	-1W	-3M	YTD
S&P 500	2,784	3.08%	0.88%	11.08%
DJIA	25,916	4.51%	1.48%	11.10%
Nasdaq	7,533	4.35%	2.76%	13.52%
MSCI World	2,848	-4.80%	3.04%	11.11%
MSCI EM	3,934	-13.05%	8.47%	10.80%
Russell 2000	1,576	2.85%	2.76%	16.83%
Euro Stoxx 50	3,326	-3.03%	4.82%	10.82%
FTSE 100	7,112	-2.33%	1.88%	5.70%
Nikkei 225	21,603	-1.68%	-3.35%	7.93%
Hang Seng	28,812	-8.33%	8.70%	11.48%
Dollar Index	96.18	6.86%	-1.13%	0.00%
EUR/USD	1.138	-7.33%	0.59%	-0.72%
GBP/€UR	1.163	2.67%	3.24%	4.59%
GBP/USD	1.324	-4.86%	3.87%	3.83%
USD/JPY	111.8	3.72%	-1.57%	1.91%
USD/CHF	0.998	6.29%	0.02%	1.63%
Brent Crude	66.36	1.44%	13.03%	23.35%
Gold	1,310	-1.54%	7.32%	2.20%

Generic Bond Yields

change in bps

	Last Close	-1W	-3M	YTD
US 10Y Yield	2.730%	-22.1	-25.8	4.5
GER 10Y Yield	0.190%	-53.1	-12.3	-5.2
JPY 10Y Yield	-0.007%	-6.3	-9.9	-1.0
UK 10Y Yield	1.304%	-25.1	-6.0	2.7
PT 10Y Yield	1.484%	-51.2	-34.3	-23.8

*Source: Bloomberg, as of 2019-02-28

In Focus

February

China's continuing slowdown. The manufacturing sector has contracted for the third consecutive month in February. A slowing economy led to a write-down or sell-off of USD 258.0 bn "bad loans" last year. Despite the poor outlook, MSCI is set to announce that Chinese stocks' weight on the Emerging Markets index will triple by August. This index is the benchmark for more than USD 1.9 tn of funds.

Strong US signs. Inflation near the 2.00% Fed target, payroll growth of 304,000 (against forecasts of 164,000) and consumer spending growth of 2.80% YoY for 2018 indicate the US are performing well, despite global economic growth slowdown. GDP grew by 2.90% in 2018, against 2.20% in 2017.

Germany's confidence lowers. Business confidence hit 98.5, its lowest level since December 2014. The government now expects YoY GDP growth of just 1.00% in 2019, against previous expectations of 1.80%.

Pakistan and India tension. Following an attack by a Jaish-e-Mohammad suicide bomber that killed 40 Indian police in Kashmir, tensions escalated. It was the first use of Indian air power since the 1971 war between the two countries. Pakistan prime minister offered to release an Indian air force pilot as a "peace gesture".

Trump and Kim end their Hanoi summit abruptly. Mr. Trump told the press that Mr. Kim wanted all its sanctions lifted in exchange of denuclearization, which the US could not do.

Nigerian president re-elected. Africa's largest economy and most populous nation has re-elected his current leader, Muhammadu Buhari. His main opponent's party says it will not accept the result, alleging vote rigging and demanding that poles in some states be re-run.

The start of the presidential run. Bernie Sanders, 77, has announced his run for the US presidency. His campaign focuses on USD 15.0 minimum wage, Medicare for all and free college.

US pulls out of cold war-era nuclear arms treaty. The US have accused Russia of deploying midrange missiles capable of deploying nuclear weapons, prohibited by the 1987 pact.

Cuba's new constitution. The most significant reform to the country's legal framework since 1976 allows for some form of private property, sets presidential term and age limits, and potentially allows for same-sex marriage.

Cohen testifies against Trump. Once the confidant lawyer of the current US president, Michael Cohen revealed his co-operation in investigations amidst possible Russian interference on the 2016 US presidential elections.

New party shadows Brexit. 11 MPs have come together to form a new UK political group. The move came after 7 Europhile MPs resigned from the Labour Party. Meanwhile, 4 MPs from Mrs May's Conservative Party have crossed the floor to join the newly formed Independent Group.

Musk's electrical tweets. Following a tweet by Tesla's CEO regarding the number of electric vehicles produced, the US securities watchdog claimed the tweet contravened a legal statement agreed in October.

UBS fined by French authorities. The swiss bank has been fined a record EUR 3.7 bn fine in France, and was condemned to pay EUR 800.0 m in damages. UBS was found guilty of helping rich clients evade tax payments. If upheld, the fine would wipe out 1 year of profits for the firm.

Sérgio Ferrás
Financial Markets Division

Deeper Dive

China's Capital Markets: Access to International Capital



Mariana Costa
Investment Banking Division

The decision means that MSCI could send up to USD 125 bn into the Chinese market.

On the 28th of February, MSCI, the global index provider, said that it is increasing the weighting of 235 of China's large-cap "A-shares" in its indices.

A further addition of more mid-sized Chinese companies will lift the weighting to more than 3.00% by May 2020. Additionally, MSCI announced its increased weighting for domestic Chinese stocks is set to happen incrementally in three steps in May, August and November this year.

In order to integrate China's domestic stock markets with international capital, MSCI took its biggest step yet in a move that could see an estimated USD 125.0 bn entering the Chinese market during this year.

The weight of China in MSCI's flagship Emerging Markets Index, a benchmark that is taken into consideration by many investors and is tracked by USD 1.9 tn of funds, is expected to rise to 3.30% by November from the current level of 0.71%.

All the funds that measure their performance against the index have to buy the underlying stocks, which will consequently result in inflows to China. "Such inflows will be welcomed given the deterioration in China's current account position, which could even fall into deficit this year," TD Securities says.

All in all, the decision helped to drive Chinese stocks higher, with the benchmark CSI 300 rising 2.20%. That takes its gain for the year to 25.00%, trouncing the performance of every other stock market.

China's government aggressively pushed for the increased weighting. However, this move underscores how China has opened its capital markets with the US, in spite of the ongoing and growing political and trade tension.

Xi Jinping, the Chinese leader, will meet Donald Trump in April with the aim of solving the current trade war.

Chinese stocks listed offshore in Hong Kong and the US are already highly represented in the MSCI Emerging Markets Index with a 31.00% weighting. MSCI's latest decision is highly important, since it creates a stronger link between the domestic Chinese stock market, the second largest in the world, and international capital.

By the end of the calendar year it is predicted that 34.30% will be the total weighting in the MSCI index for offshore and domestic Chinese stock – by far the largest country weight.

To validate the statements above, Mr Perrin said that "The largest ChiNext names will join the index and offer an opportunity to get exposure to the most dynamic and innovative side of the Chinese economy".

However, despite the changes that were made, the fact that many Chinese stocks often have poor governance and insufficient transparency can be a problem to international investors.

Furthermore, MSCI would like to see a broader use of equity futures contracts, in order to allow offshore funds to hedge their risks in the respective market.

William Yuen, investment director at Invesco, suggested that "There is a fair probability that we can see full inclusion within five to 10 years, as China continues to adopt a more free-market mechanism and approach."

Considering everything, Remy Briand, MSCI managing director, stated that: "The strong commitment by the Chinese regulators to continue to improve market accessibility, evidenced by, among other things, the significant reduction in trading suspensions in recent months, is another critical factor that has won the support of international institutional investors."

Mariana Costa
Investment Banking Division

Regional View

China Housing Market: Will the Bubble Pop?



Gonalo Marques
Financial Markets Division

“Ghost cities are already a well-known problem (...) However, now, adding to the unsold houses, there is the problem of houses that were bought and left empty.”

February marked the beginning of the new Chinese year, the year of the pig. In the traditional culture, pigs are symbols of wealth, and with their chubby faces and big ears, they signal fortune as well. Nonetheless, none of these superstitions seems to translate into the reality of the country. Chinese economy has been struggling lately and 2019 will be no exception to that trend.

In 2018, GDP only increased by 6.60%, the lowest since 1990. The result came after a disappointing Q4, in which growth decelerated to levels of the global financial crisis period. In general, the now consumption-driven Chinese economy is being largely affected by a weaker consumer sentiment, in spite of the efforts of the PBoC to ramp up consumption.

More recently, the spending over the holiday weekend of the new year fell short of expectations, growing 8.20% *vis-à-vis* a 10.20% annual growth in 2018. This happened despite the Central Bank having injected a record RMB 570.0 bn (USD 75.0 bn), in mid-January – via open market operations to boost liquidity and promote increasing lending – amid growth fears and higher lunar new year cash demand.

Notice, however, that the PBoC has been reluctant to re-implement large-scale credit stimulus as non-performing loans continue to pile. Bad debt disposals reached a 20-year maximum, with sales to distressed asset investors totalizing RMB 1.7 tn (USD 258.0 bn) in 2018. And one of the key contributors to these poor-quality loans is precisely the housing market.

In fact, property developers are among the most indebted companies, as they face RMB 385.0 bn (USD 55.0 bn) of maturing onshore debt this year, a value almost four times the size of the offshore dollar borrowing, of about USD 14.5 bn, maturing also in 2019.

Looking to the real estate market, currently, there are around 90,000 property development companies in China. Despite the number, the market is not well distributed, as 67.00% of total sales come from the top 100 groups. Hence, naturally, small developers are the ones facing the highest pressure. Not only they suffered the most from the tighter conditions to access credit, but also they were forced to cut prices to keep up with the largest players and thus maintain the sales rhythm.

On the other hand, large players have an advantageous position in the property market, which allows them to buy up the distressed real estate debt of their rivals. While prices for tier-one cities at land auctions remain high, taking over small developers when they fail allows them to gain control of valuable assets at large discounts. But, as consolidation of the sector is expected to occur at a faster pace in the next years, the market still faces the problem of 65 million vacant apartments.

Ghost cities are already a well-known problem. These are mainly third and fourth tier cities, located in the peripheries of crowded metropolises that fail to attract businesses and residents. However, now, adding to the unsold houses, there is the problem of houses that were bought and left empty. These were mainly bought by entrepreneurs and speculators with no intention of living on them, with the unique purpose of selling them for a profit. There is also the case of single male family members buying properties, as it is traditional for grooms to gift their brides apartments.

Taking all that into account, analysts expect a challenging year of 2019, with contract-based sales predicted to fall by 5.00%, while overall selling prices are foreseen to remain relatively stable. Adding to that the weight of heavy debt burdens of property developers puts China one step closer to the implosion of the housing market bubble.

Gonalo Marques
Financial Markets Division

Macro Overview

Economic Calendar

Economic and Political Events

Brexit Events

With the 29th of March approaching, MPs are set to vote on the amended Brexit deal on the 12th of March. In case this deal is not approved, a new vote will be held to figure if Britain leaves the EU without a deal. If this one is not passed, a new vote will decide whether or not to delay Brexit.

US-China Trade Talks

Mr. Trump has set the 1st of March as the limit for US-China trade agreement. If the two biggest world economies fail to do so, the US could increase its tariffs on USD 200.0 bn of Chinese imports from 10.00% to 25.00%. Amidst developments on trade negotiations, Trump has shown willingness to postpone such surge.

Ukrainian Elections

Ukrainian people go to the polls on the 31st of March. The incumbent President, Petro Poroshenko, seeks re-election, despite his widespread disapproval in the country, following failures to tackle corruption.

Central Bank Decisions

FOMC Rate Decision

The Fed will meet on the 20th of March to decide on its short-term rate. Following concerns of a slowing economy, rates are not expected to change until the summer.

Bank of England Interest Rate Meeting

On the 21st of March the Bank of England will meet. Mark Carney, the bank's governor, has warned economic policy-makers to urge in solving what he calls the de-globalization period, both worldwide and in the UK. Rates are expected to remain at 0.75%.

ECB Monetary Policy Decision

The Governing Council of the ECB holds its monetary policy meeting on the 7th of March, in Frankfurt. ECB's board is expected to not raise its rates at least until next summer, following last year's reports of slower growth due to Brexit, Trump's protectionist plan and China's slowdown.

Inflation and Deflation

Update on Euro Zone Inflation

December inflation data for the euro area will be published on the 15th of March. Inflation in the euro area is expected to increase to 1.50%.

Germany's Inflation

Germany's inflation rate will be announced on the 28th of March. Following the biggest European economy's slowdown, YoY inflation rate is expected to pick up to 1.60%, despite having reached an 11-month low of 1.40% in January.

UK Consumer Price Index

YoY figures on consumer prices in the UK will be made public on the 16th of March. Inflation is expected to remain at 1.80%, less than one month away from Brexit.

Labour Market

US Employment Readings

On the 8th of March the US payrolls number with ADP employment change data for December and the weekly jobless claims are announced. Despite signs of economic slowdown, the labour market is expected to remain strong. The unemployment rate is expected to remain close to 4.00%.

German Labour Market

On the 1st of March, Germany announces its unemployment rate. The increase in employment continued for the thirteenth year in a row. The rate is expected to remain at the historical low of 3.40%.

Euro Zone Unemployment Data

The European Zone unemployment rate will be announced on the 1st of March. The overall unemployment rate is expected to remain at 7.80%, substantially lower than the past year value of 8.50%.

Investment Banking

M&A

Overall Activity

Global

In February, global M&A activity has fallen behind by nearly one third of the levels from last twelve months. The announced total transaction volume reached a level of USD 222.0 bn from a total of 2,538 transactions. These can be divided into Top 3 regions by transaction count, which have been Asia, North America and EMEA, with 435, 397 and 369 transactions respectively. While the number indicates a diverse allocation, the volume was mainly driven by transactions from US & Canada, with a total of USD 166.0 bn. EMEA and Asia follow behind with USD 36.0 bn and USD 18.0 bn. Moreover, it can be observed that the Top 3 sectors accounting for the biggest volume have been Healthcare, Financials and Information Technology with USD 36.0 bn, USD 36.0 bn and USD 28.0 bn. It is not a surprise that the biggest transaction this month was announced in the highest ranked region, namely the USD 28.0 bn takeover of SunTrust Banks Inc. by BB&T Corporation. In general, M&A professionals expect the level of M&A activity to grow, as factors which already helped M&A to keep strong in 2018 like tax legislation, a looser regulatory environment, a relatively strong stock market, CEOs wish to divest, and cheap financing are still present in the market.

Selected Regions

North America

Although the heavy-weight take-over of SunTrust Inc. has been announced, the largest volume per sector can be traced back to Healthcare with USD 34.0 bn. Followed by the Financials sector with about USD 31.0 bn and USD 26.0 bn in Information Tech. Furthermore, volume was also driven by the surprising announcement of the acquisition of Newmont Mining Corp. by Barrick Gold Corp. and shares-swap between Liberty Expedia Holdings and Expedia Group.

EMEA

In February, the sectors Communication Services, Real Estate and Industrials accounted for the highest volume in the region, with high announced volumes of USD 9.0 bn, USD 5.0 bn and USD 5.0 bn. The transaction volume was mainly driven by the Top 3 acquisitions, namely Sunrise Communications Group AG acquires UPC Switzerland LLC; various Asset Managers takeover ADNOC Oil Pipelines LLC and Luxinva S.A.; as well as Triton GmbH announced to buy the RPC Pooling Business of IFCO.

Asia

In the last month, besides several minor deals, the major transaction volumes in Asia were in Real Estate, Industrials and Financials with USD 4.0 bn, USD 3.0 bn and USD 2.0 bn respectively. The biggest transaction was the planned acquisition of SERVEONE Co. by Affinity Equity Partners in South Korea, for more than USD 1.0 bn. Also, the Golden Land Property Development PCL was announced to be acquired by Frasers Property PCL in Thailand, for roughly USD 1 bn.

M&A

Deals of the Month

Announced Date	Target	Buyer	Target Region	Target Business	Value (USD m)	Premium One Month Prior (%)
07 Feb 19	SunTrust Banks Inc	BB&T Corporation	US & CA	Financials	28,085.00	14.73
25 Feb 19	Newmont Mining Corporation	Barrick Gold Corporation	US & CA	Materials	23,209.06	0.721
04 Feb 19	Liberty Expedia Holdings, Inc.	Expedia Group, Inc.	US & CA	Consumer Discretionary	21,785.26	8.52
25 Feb 19	BioPharma Business of General Electric Company	Danaher Corporation	US & CA	Health Care	21,400.00	-
04 Feb 19	The Ultimate Software Group, Inc.	Hellman & Friedman LLC; JMI Management, Inc.; The Blackstone Group L.P.; GIC Pte. Ltd.; Canada Pension Plan Investment Board	US & CA	Information Technology	10,874.82	32.24
12 Feb 19	Coty Inc.	JAB Cosmetics B.V.	US & CA	Consumer Staples	10,059.70	60.91
27 Feb 19	Versum Materials, Inc.	MERCK Kommanditgesellschaft auf Aktien	US & CA	Information Technology	6,320.11	30.90
27 Feb 19	UPC Switzerland LLC	Sunrise Communications Group AG	Europe	Communication Services	6,298.30	-
13 Feb 19	Auris Health, Inc.	Ethicon US, LLC	US & CA	Health Care	5,750.00	-

Tim Borneck & Duarte Alves Pereira
Investment Banking Division

M&A: Top Deals

Barrick Gold launches hostile offer for Newmont Mining

Toronto-listed Barrick launched a hostile USD 18.0 bn all-stock offer for its closest rival Newmont, which represents a nil-premium merger at the time of announcement. Under the offer, Newmont's shareholders would receive 44.10% of the combined company.

Buyer vs Seller

Barrick Gold Corporation operates gold mines and projects in ten countries and 75.00% of its gold production comes from the Americas. Newmont Mining Corporation is an American mining company with active gold mines in Nevada, Australia, Ghana, Peru and Suriname, and it is the only gold company in the S&P's 500. CIBC Capital Markets and M. Klein and Company, Inc. are acting as financial advisors.

Industry Overview

The gold mining industry is currently in transformation, with big companies fighting to consolidate its position. In September last year, Barrick Gold agreed to buy Randgold Resources, which triggered the return of M&A to the industry. The new paradigm comes after years of punishment from investors, due to the sector's moderate returns, excessive spending and executive's overpaying.

Peers	Currency	Market Cap (CUR m)
Polyus PJSC	RUB	554,078.30
Newcrest Mining Ltd	AUD	15,741.50
AngloGold Ashanti Ltd	ZAR	58,054.81
Cia de Minas Buenaventura SAA	PEN	12,632.04
Kinross Gold Corp	CAD	4,563.34

Deal Rationale

As deal making activity in the industry intensifies, the acquisition will create the world's biggest goldminer. Barrick and Newmont would create a USD 40.0 bn company with more than 10.0 m ounces of annual production, far surpassing any of its rivals, with revenues of USD 15.6 bn and underlying earnings of USD 7.0 bn. Barrick estimates that there would be annual pre-tax synergies of USD 750.0 m from the deal with Newmont in the first five years, primarily by combining their respective gold mines in Nevada. Additionally, a nil-premium merger would offer greater benefits to shareholders than Newmont's planned acquisition of Goldcorp.

Market Reaction

Barrick Gold

With the announcement on February 25th, shares in Barrick Gold fell 1.00% to CAD 16.9 (CAD 17.2 previously), representing a slight drop in value.



Newmont Mining

Newmont Mining's shares dropped by 0.30% to USD 36.0, which means they were less affected by the announcement compared to Barrick Gold.



Future Challenges

The hostile all-stock offer for Barrick's closest rival Newmont Mining has unleashed a strong dispute between two companies whose combination would create the world's biggest gold producer. Newmont shareholders will now have to decide whether to choose Barrick's nil-premium offer or push ahead and vote in favour of the Goldcorp deal. Newmont has been one of the best-performing gold miners over the past decade and is the only gold miner in the S&P 500.

M&A: Top Deals

Morgan Stanley to acquire Solium Capital

The Canadian fintech firm Solium Capital is being targeted from Morgan Stanley in a USD 900.0 m offer. Morgan Stanley is paying a 43.00% premium for Solium. The completion of the deal is subject to relevant regulatory approvals.

Buyer vs Seller

The online stock plans administrator Solium Capital manages employee stock plans for people at over 3,000 companies, including Instacart and Levi Strauss. Meantime, 44.00% of Morgan Stanley's revenues stem from wealth management. While Morgan Stanley already operates its own version of Solium focusing on top executives, Solium is focusing on the millennial customer segment and also sells analytics tools that help companies automate share issuance, estimate compensation costs, and value their equity.

Industry Overview

The trend of financial institutions acquiring technology companies has been observable throughout the industry. While most of these acquisitions focus on application-based software, investments in stock plans administrators are relatively new. Nonetheless, banking rival Goldman Sachs is expanding its tax advisory business down the employee rank too, likely hoping to similarly profit from the millennial generation segment in the future.

Peers	Currency	Market Cap (CUR m)
Encore Capital Group Inc	USD	1.050,07
CannaRoyalty Corp	CAD	502,92
Tricon Capital Group Inc	CAD	1.592,91
OTC Markets Group Inc	USD	417,73
Burford Capital Ltd	GBp	3.887,59

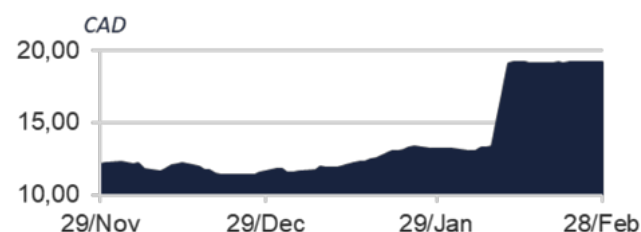
Deal Rationale

The acquisition of Solium Capital gives Morgan Stanley a boost in the war for wealth management clients. Jed Finn, chief operating officer at Morgan Stanley's wealth management business, said that owning Solium allows it to "offer our full suite of wealth management tools and advice to plan employees through Solium's platform". Moreover, the acquisition is said to move the bank's wealth management business deeper into the mass affluent category, as opposed to the higher end of the market where it is focused now.

Market Reaction

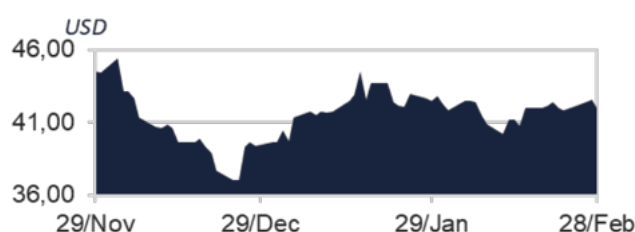
Solium Capital

After the announcement, Solium Capital's stock reacted positively, rising by over 10.00%.



Morgan Stanley

Morgan Stanley's stock fell 1.00% after the announcement of the deal, potentially due to the hefty 43.00% premium that investors are sceptical about.



Future Challenges

As the bidding comes with a 43.00% premium, the deal can be considered a bold move for Morgan Stanley. Valuing the company at more than seven times its sales over the last year – compared to Solium's peer average valuation of two to three times sales – it remains to be seen whether Morgan Stanley's plan will play out as hoped.

M&A: Top Deals

Merck to acquire Versum Materials

Versum Materials is being targeted from Merck KGaA, in an all-cash counterbid deal with an enterprise value of USD 5.9 bn. The deal is conditional on regulatory approvals and Versum's decision regarding another recent merger offer from Entegris.

Buyer vs Seller

Merck KGaA, a Germany-based pharmaceutical, chemical and life science company, has announced to acquire Versum Materials, a US-based electronic materials company providing chemicals and gases, delivery systems, services and material expertise to the global semiconductor and display industries. Merck is offering to pay USD 48.0 per Versum share, representing a 15.90% premium over the company's closing share price on the 26th of February 2019. Guggenheim Securities is supporting the deal as financial advisor and Sullivan & Cromwell LLP as legal counsel.

Industry Overview

In January 2019, the high-tech company Entegris already announced to acquire Versum in a USD 4.0 bn all-stock deal to create a big chemical supplier to the semiconductor market, now competing with the Germany-based pharmaceutical company. Merck is building a high-tech chemicals division, called Performance Materials. The Versum deal would allow Merck to further strengthen its position as a supplier for electronic materials.

Peers	Currency	Market Cap (CUR m)
WR Grace & Co	USD	5,183.66
Ingevity Corp	USD	4,795.33
Materion Corp	USD	1,169.36
Rogers Corp	USD	2,862.58
Eastman Chemical Co	USD	11,558.19

Deal Rationale

Merck's USD 48.0 a share offer would dismantle a proposed USD 3.8 bn merger between Tempe, Versum and Entegris. The German company's offer is 52.00% higher than Versum's price before the planned merger was announced last month. Merck expects the deal, which is said will reap cost synergies of about EUR 60.0 m annually, to close in the second half of 2019. Versum's shareholders and employees would immediately benefit from the all-cash deal. Nevertheless, Versum announced to review the deal conditions, proposed from Merck, but still believes in the strategic rational of the merger with Entegris.

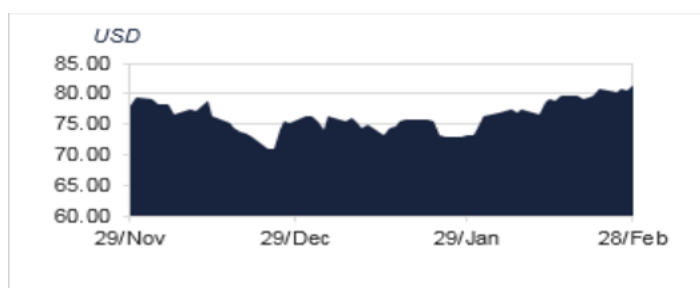
Market Reaction

Merck

Since the announcement, Merck's equity securities fell as much as 4.90% in Frankfurt after the announcement.

Versum

The news lifted Versum as much as 18.00%, putting its market value at about USD 5.3 bn.



Future Challenges

Since Merck is well-known for aggressive hostile deal-making, it would be no surprise if the deal offer is being raising again. Due to the fact that the liquid crystals business used to enjoy operating income margins of 40-50% but is now under pressure from Chinese rivals, the deal would definitely add much value to Merck's current portfolio. Nevertheless, some analysts see the deal being more expensive than expected, with Versum's proposed deal value of 13.30 times its 2018 EBITDA.

What Happened To Activision Blizzard

Activision Blizzard is an American video game company with titles such as Call of Duty and World of Warcraft in their product portfolio. By acquiring King Digital Entertainment in 2016, the company established their presence in the mobile games industry and expanded their portfolio to include the Candy Crush Saga. The firm recently reported USD 356.0 m monthly active users.

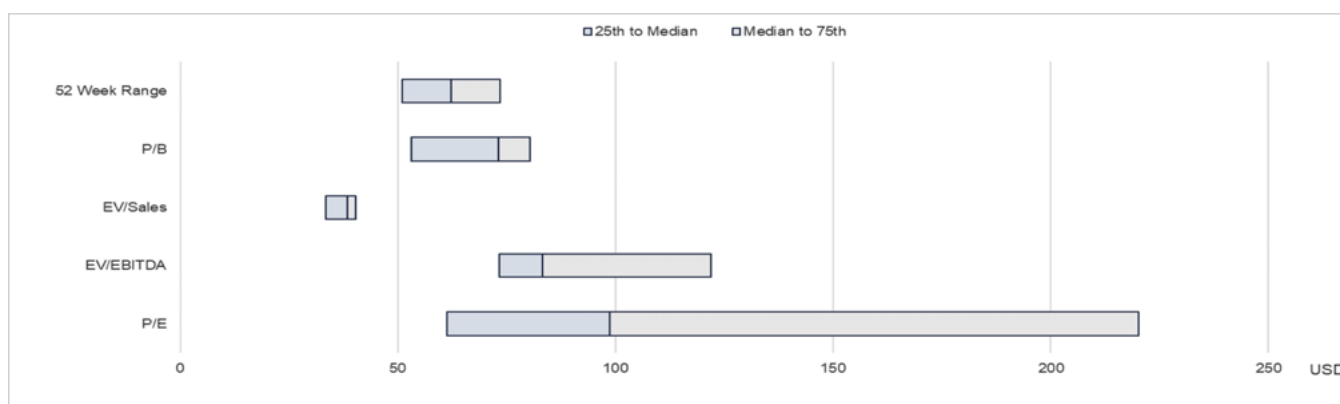
Corporate News

Activision Blizzard's share price is down 15.00% on a 3-month performance and even 50.00% on 52-week high. The more recent loss in share price has been a reaction to mixed signals from the company after presenting very solid financial numbers from 2018. Despite achieving record high results, with profits reaching USD 1.8 bn, the company adjusted expected sales downward for 2019 and laid off 800 people in the same earnings call. Considering a longer time frame, the massive sell-off in the end of September 2018 seemed to be a turning point for the stock price trajectory, when investors started reevaluating two growing concerns; an aging product portfolio with symptomatically decreasing userbases, and an increasingly threatening competitor in Tencent who currently owns the two largest video games worldwide. Analyst consensus indicates that the steep downturn has been exaggerated, with a target price of USD 54.0 (27.40% upside), and argue that the company fundamentals are rock solid.

Price (28 Feb 19, USD)	42.40
Target Price (USD)	54.00
3M Performance	-15.00%
Market Cap (USD m)	32,386.56
Enterprise Value (USD m)	30,832.56
<i>*Target Price is for 12 months</i>	



Valuation Analysis



The football field clearly depicts the share price of Activision Blizzard lagging behind comparable companies on several metrics and that it is trading below the 25th percentile of 52-week price range. Relative valuation based on EV/Sales, P/E, P/B and EV/EBITDA, specify a price closer to USD 70.0. Combining the relative valuation with the recent counter-intuitive stock price movements following the Q4 earnings release, could perhaps indicate a forthcoming correction with substantial short-term upside potential.

An important part of the dystopian look on the company's next year revenue lies in the hollow pipeline of game launches this year. Other than remakes of World of Warcraft and Warcraft 3, there have been no signals of any major releases. Revenues from Activision and Blizzard are, therefore, expected to track their decreasing userbases, while revenues from King's mobile users are expected to slightly cushion the fall with organic growth.

Peers	Currency	Market Cap (Cur m)
Electronic Arts Inc	USD	28,722.23
Take-Two Interactive Software	USD	9,960.51
Glu Mobile Inc	USD	1,301.65
Zynga Inc	USD	4,841.13
SS&C Technologies Holdings Inc	USD	15,730.96

What Happened To Under Armour

Under Armour, Inc. is an American company that manufactures footwear, sports, and casual apparel. It employs 15,000 people in 18 countries and is considered the third largest sports apparel company by sales (USD 5.2 bn, as of 2018) in the world. Despite its impressive size, UA is still far from the biggest brands: Nike (sales of USD 36.4 bn) and Adidas (sales of USD 21.2 bn).

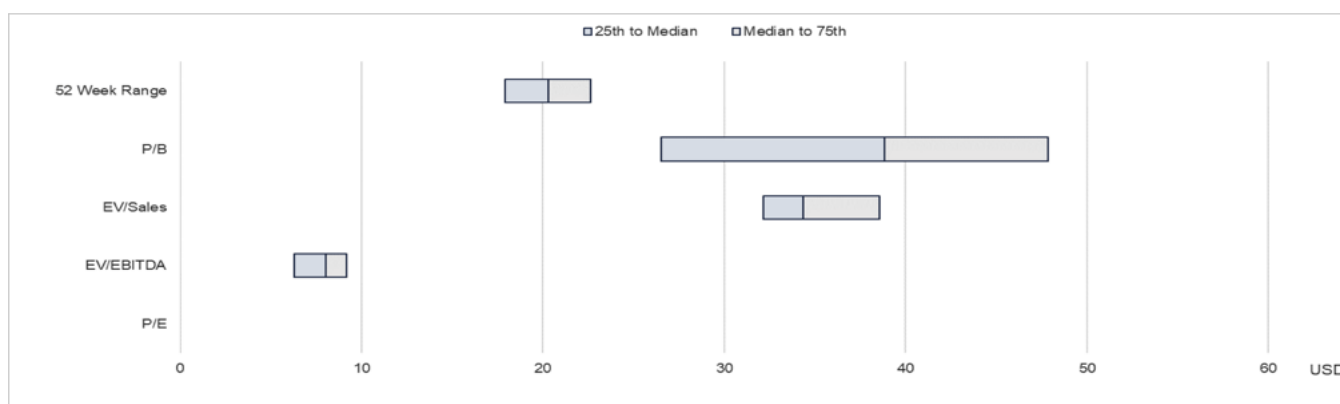
Corporate News

Under Armour's shares are up 26.77% YTD. This strong performance is mainly related to the restructuring plan that the company is undertaking since 2017. UA plans on spending approximately USD 330.0 m in facility and lease terminations, contract terminations, inventory and asset impairments in the next years. Yet, the company expects to materialize an annual saving of USD 75.0 m, starting in 2019. Gross margin has already improved by 160 bps from a year ago to 45.00%, driven predominantly by regional and channel mix, product cost improvements, lower promotional activity and a reduction in inventories of 12.00%. Additionally, the company refocused its strategy, shifting away from "athleisure", where competition is fierce, focusing its attention instead on providing the best clothes for athletes. Under Armour predicts revenue to increase between 3.00 to 4.00% in 2019, including relatively flat results for North America and low double-digit growth for its overseas business.

Price (28 Feb 19, USD)	22.55
Target Price (USD)	20.50
3M Performance	-5.57%
Market Cap (USD m)	9,517.37
Enterprise Value (USD m)	9,688.80
<i>*Target Price is for 12 months</i>	



Valuation Analysis



Under Armour closed at USD 22.6 on the 28th of February, well above its target price of USD 20.1. The 3M Performance was also quite positive, with first month losses being almost offset in the following months. Furthermore, by looking at the football field above, P/B and EV/Sales suggest that UA might be undervalued, contrarily to EV/EBITDA, which points out the opposite. In fact, in spite of the margin improvement, UA remains behind its competitors in terms of margin performance.

The global sports apparel industry is expected to grow at a CAGR of 8.00% between 2019-2023 as people care more about their health. Under Armour still struggles with capturing that growth as it competes with long-lasting brands like Nike and Adidas. However, the company has pledged to differentiate itself by improving its Direct-to-Consumer channel and by shifting attention towards the international market, which only represents 24.00% of its sales for now.

Peers	Currency	Market Cap (Cur m)
Columbia Sportswear Co	USD	7,021.65
PVH Corp	USD	8,697.43
Carter's Inc	USD	4,436.05
Oxford Industries Inc	USD	1,339.89
Hanesbrands Inc	USD	6,718.87

João Sousa Mendes
Investment Banking Division

Private Equity

Venture Capital

DCM

ECM

Spinoff

Restructuring

NIC's View On

Lyft Going Public: The First Big Ride Sharing Player to IPO



Vasco Lupi
Investment Banking Division

Lyft has already filed the paper to go public in late March. The last private valuation pointed to a target price of USD 15 bn, however, some analysts have predicted a higher price. The proposed dual class structure will give more power to the two co-founders, which has raised some concerns in relation to good governance.

The big question in investors mind is: Can Lyft transform itself from a cash burning firm to a cash producing cow?

Lyft is a ride sharing platform based in San Francisco, California. It operates mostly in the US, where it covers over 300 US Cities and, partially, Canada. According to the Second Measure Research Company, Lyft has a 28.00% market share in the US, being the biggest competitor to UBER, which dominates the landscape with nearly 70.00% of the market. Currently it has 23 m active users, which bottles down to over 1 m rides per day. In the last financing round, it raised USD 600 m for 4.00% share, valuing the firm at USD 15.1 bn, close to the USD 20.0 bn price tag optimistic analysts point to. In order to drive stock prices up, both companies will offer programs attribute their most active drivers cash bonuses which can be used to buy company stock at the listing price, according to the report. The threshold to receive the cash convertible settlement is drivers who have logged 10,000 rides on its platform, which will receive USD 1,000.

The ride sharing app has already filed the papers to list its shares on the Nasdaq, to be processed until late March. If the listing goes forward it will become the biggest IPO in 2019, opening way for a year that has been sluggish in ECM. The latest batch of hot tech companies have opted to stay private for longer than its antecessors – the Lyft IPO may increase transparency demand and push for further public listings. The approval by SEC was initially delayed by the Government shutdown, however the time frame is still the initial one – late March. The main underwriter is JP Morgan, with support of Jefferies and Credit Suisse.

Another debate lies in the dual class structure proposed – after the IPO, both co-founders, John Zimmer and Logan Green, will have voting rights greater than their economic stake. Although they will own less than 10% of the firm, their voting

rights would be slightly below the majority control, rising good-governance issues. Being the first in the two-horse race against UBER to go public will give a slight first-mover advantage. Investors, who are eager to invest in ride-hailing players, possibly will not wait for second listing, even if they consider UBER a better investment, since it has a more diversified business (UBER Eats and stake positions in Didi and Grab, other competitors). Comparable companies for the available information are similar, which will enhance the later effect.

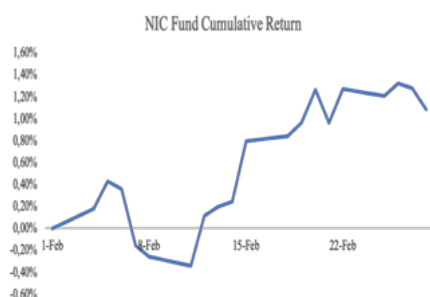
In financial terms, the firm loses money. The net loss after taxes and depreciation reached USD 373.0 m in the first half of 2018, below UBER's loss for 2018 of USD 1.8 bn, even if accounted for the calendarization. Sales for the first semester were USD 908.0 m, a growth of 88.00% YoY. Both mobility players have also faced lawsuits, the most prominent one in New York, due to their use of independent contractor classification, which can affect future labor costs. The big question in investors mind remains: Can Lyft transform itself from a cash burning firm to a cash producing cow? Some argue that scale will play a big role in increasing margins for service providers and in that sense, Uber is better positioned.

Date	Recent News
28 Feb 19	Some Uber, Lyft Drivers to Get Stock in IPOs Source: wsj.com
27 Feb 19	Lyft's IPO: The biggest thing investors should be watching for Source: bankrate.com
06 Dec 18	Why Lyft had to beat Uber to an IPO filing Source: recode.com
25 Feb 19	Lyft IPO revs up debate on dual-class share structures Source: ft.com

Vasco Lupi
Investment Banking Division

NIC Fund

NIC Fund Portfolio Overview

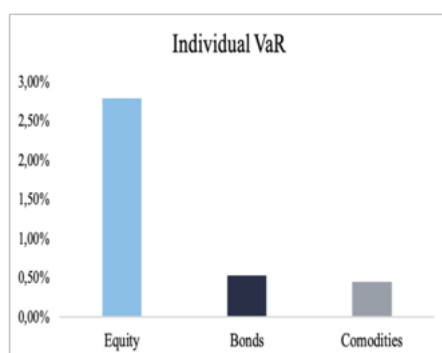


Portfolio Statistics

Cumulative Return	1.08%
Annualized Return	12.96%
Daily St. Dev	0.24%
Period St. Dev	1.12%
Annualized St. Dev	3.88%
Info Sharpe	-0.07
Skew (Daily)	0.34
Kurtosis (Daily)	-0.88

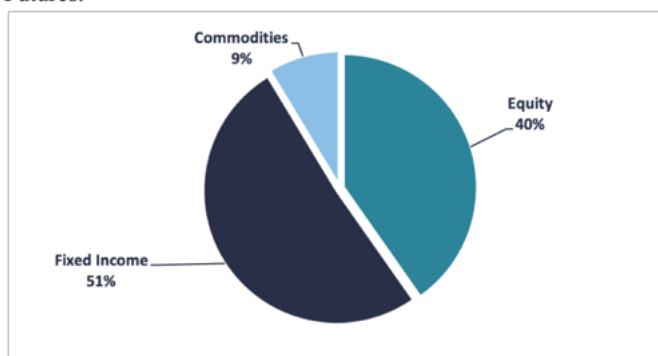
Benchmark

iShares 3-7 Year Treasury Bonds	55%
MSCI World ETF	30%
Invesco DB Commodity Index	10%
MSCI Emerging Markets ETF	5%



Portfolio Snapshot

Throughout February, the NIC Fund remained invested in Equities, Fixed Income and Commodities without any major changes to the composition from the previous month. Overall, 40% of our fund remained devoted to Equities, 51% to Fixed Income and 9% to Commodities. Yet, only 49% of the Equities were allocated to the benchmark MSCI World and MSCI Emerging Markets Indexes, while the remaining 51% were allocated primarily to fourteen specific stocks, using an equally weighted strategy. Regarding Fixed Income, we remained slightly underweighted in relation to the benchmark. Our fund is 8.64% allocated to the commodity index and it has 0.92% long position in EU Potatoes' Futures.



Return Metrics

The overall performance of the portfolio was positive, with a cumulative return of 1.08%, but stayed below the benchmark by 8 bps. After a very strong January, equities could not hold the pace they continued to rise but with steady returns the MSCI World gained 3.01%, whereas the MSCI Emerging Markets decreased by 75 bps. The Commodity Index rose 3.80% in February, showing positive signs to investors. Accordingly, as expected, Fixed Income was again the worst performer in terms of asset classes.

In terms of stock picks, the fourteen selections produced a cumulative return of 0.94%. In general, information technologies was the value driver of our equity returns in February closing with a monthly return of 10.62%, especially pushed Everbridge Inc. that closed in green territory with a 13.28% gain. Major return pullbacks came from the consumer section, closing with a loss of 5.24%.

Risk Metrics

In terms of risk, our portfolio registered a daily VaR of 2.57%, slightly above the maximum established threshold of 2.50%. This result is illustrative of the fund's high exposure to equities, namely through individual stocks.

Equities were the asset class with the highest individual VaR, which was around 2.79%. On the other hand, VaR for Fixed Income and Commodities were only 0.53% and 0.45% respectively.

NIC Fund

Assets in Brief

Asset Class	Symbol	Comments
Equity Index	URTH	One of our benchmark indices for equities, the URTH ETF tracks the MSCI World Index. Through February the index increased 2.99%, reflecting investors' lasting preference for equities, after a very bullish January.
Equity Index	EEM	The MSCI Emerging Markets ETF, the other benchmark for equities, tracks the evolution of Emerging Markets. Despite a very promising January, concerns with weak Chinese trade data and signs of an economic slowdown lead Emerging Markets closing down by 0.75%.
Equity Index	IVE	The S&P 500 Value ETF holds over 340 large capitalization US companies that exhibit value characteristics in the US equity market. The ETF is adequate for investors that weigh stability, dividends and have long-term horizons. In February, the ETF delivered a total return of 2.88%, calming down after the hottest January in 30 years. Nevertheless, it was the index that most benefited from ongoing talks by US-China trade negotiations and the fair lookout for the year of the US economy, based on a more flexible Fed.
US Equity	AMZN	In February, Amazon delivered a 0.83% return. After a very strong January Amazon had a very calm month getting back home. On February 19 th the company announced its plans to acquire the entire share capital of NetEase Koala China, a Beijing-based online retailer, from NetEase Inc. Early in the month Amazon announced to back-out of plans for their HQ2 in Queens, New York. None of these announcement have been reflected significantly in the stock price.
US Equity	DPZ	One of investor's darlings of the last year took a hit in February. Domino's Pizza missed consensus on revenue and profit numbers for Q4 2018. Shares lost 9.86% after the publication. Last year Domino's was one of the stellar performers with 20.80% in a bleak market environment.
US Equity	BAC	Bank of America closed the month with a return of 2.47%. On the 7 th of February the bank announced that it will increase its common stock repurchasing program by additional USD 2.5 bn. The repurchase should be proceeded by the 30 th of June 2019. Additionally, it disclosed an investment of a 7.01% stake of Ophir Energy Inc. an oil and gas production company based in London.
US Equity	NVDA	After a green January Nvidia closed at the end of February with a return of 6.58% and stayed close to last month's performance. At the beginning of the month Softbank's Technology announced that it sold its entire USD 100 bn stake of Nvidia, sending the stock down by 5.58% the day after. But the stock recovered throughout the month due to the pre-announcement on February 14 th , stating that Q4 non-GAAP earning will be wat USD 0.80 per share, above market expectations.
US Treasury Bonds	IEI ETF	Our benchmark bond index, IEI invests in treasuries with maturities from 3-7 years. US treasuries remained essentially flat throughout February, although the index ended slightly in red with -0.22%. The central banks are currently adopting a "wait-and-see" strategy, so happenings on the bond market are rare, guiding the market to stagnate.
Commodity	DBC ETF	Our primary commodities index, DBC tracks a basket of 14 commodities. The ETF had positive performance over the last month, rising 3.80%, mainly driven by the solid growth of oil prices and precious metals for the month.

Jan Schroff
Financial Markets Division



NIC Fund

Equities

World Equities

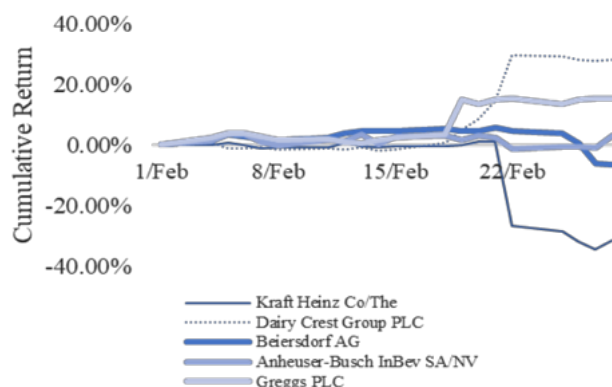
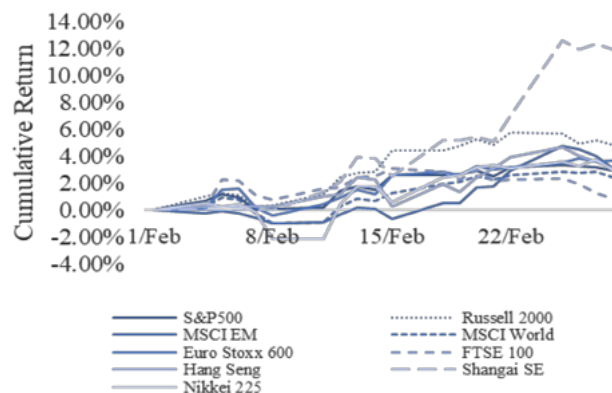
Despite a somewhat sluggish beginning of the month, all main stock indices closed February on a positive note. Shanghai stocks were by far the biggest winners of this month, posting their best week in nearly 4 years towards the end of February and closing the month with a 12.33% gain. The race was lead by the consumer stocks, which gained 27.60% in 2019. Despite weak industrial data in China, investors praised the progress made in internationalizing the A-share market, as foreign investors surpassed insurers as the largest holders of such shares. Furthermore, global index provider MSCI announced that it would quadruple the weight of mainland China shares in its global benchmark. Outside of China things were not as rosy, as the growth in global stock markets slowed in the second-half of February. Rising geopolitical tensions and slow progress in the trade war resolution were the main culprits behind that. On the bright side, investors seem to have picked more interest in American stocks, as the US equity funds ended their 11-week run of outflows.

In Depth: Ups and Downs in the Consumer Industry

The fall of Kraft Heinz was arguably the biggest equity story of the month. The company shocked the markets with a series of bad news at once: it posted weaker than expected Q4 results and lowered its guidance for 2019, while also cutting the dividends. Besides, the company wrote down almost USD 16.0 bn in goodwill and revealed that it had received a subpoena from SEC regarding its accounting practices. Investors did not take it lightly, and the stock dropped 30.50% in February. AB InBev, another holding of 3G Capital, which orchestrated the Kraft Heinz deal along with Warren Buffet, also had a disappointing month, barely closing in the green. Meanwhile, Beiersdorf reset its margin targets to account for an ambitious investments strategy that is supposed to last a few years and revive the growth. Analysts widely expect that it will result in as much as 10.00% decline in earnings in 2019. Other consumer companies performed much better. Canadian cheesemaker Dairy Crest agreed to be taken over by Saputo in the deal that valued it at 13 times EBITDA. As a result, the company outperformed the broad market and shot up over 20.00% in February.

Our Performance

We allocate significant part of our portfolio to index funds, namely MSCI EM and MSCI World. In February, the emerging markets index dropped 0.75%, corresponding to a modest 0.02% loss in our portfolio, while the global equities gained 3.01%, contributing a 0.52% gain to the NIC Fund. Among our individuals stock picks, Everbridge was the biggest winner with its 13.28% monthly spike, which corresponded to a solid portfolio gain of 0.15%. It was closely followed by BNP Paribas, which grew 9.43% in February and contributed 0.10% to the Fund. This month's biggest loser was Domino's Pizza, which fell 9.86% and dragged our portfolio down by 0.11%.



NIC Fund

Fixed Income

World Yields

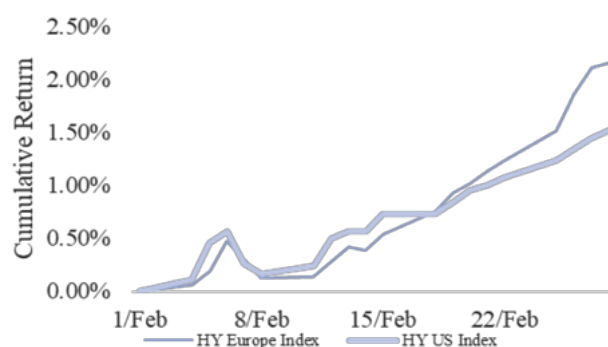
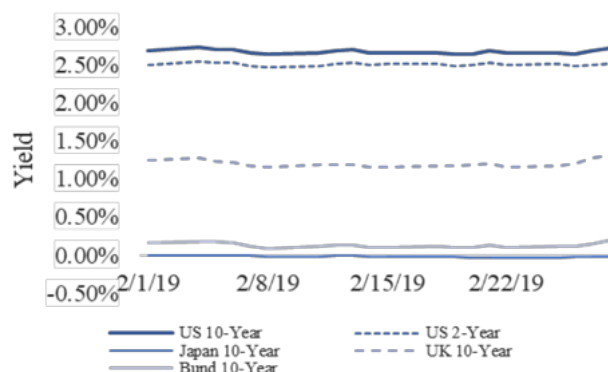
It was a quiet month for IG yields in Developed Markets. German Bunds, for example, started the month yielding 0.17% and finished up only 1 bp at 0.18%. A similar development can be observed for US 10-year rates that started at 2.69% into February and closed at 2.74%, after hovering closely around 2.70% for the whole month. The slope of the US yield curve stayed rather flat over the month, still signalling a lot of uncertainty about the short and medium-term outlook. The Fed and ECB both had no meeting this month but latest data points towards investor expectations of a more dovish path from now on. For the FOMC meeting in June, investors attach more likelihood to a step down (3.30%) as to a rate hike (0.00%). Most, however, seem to have implemented Chairman Powell's "Wait-and-See" strategy. After the chairman's statement that they will pay attention to financial-market volatility as it may threaten economic stability, some market participants argued that what we see in the Fed's scramble for course is effectively a "Powell Put", meaning downside protection for holders of financial assets. The Fed is expected to announce plans on how to move ahead with the current balance sheet runoff program which will reveal more information on their general view on future monetary policy. Looking around the world, India's Central Bank was the only major one making a move this month. Surprisingly, rates were lowered by 25 bps to 6.25%. The move might be a consequence of the higher influence of the government on India's CB. It comes in handy for ruling Premier Modi who seeks re-election and could profit from higher economic activity.

In Depth: High Yield

High Yield Bonds were able to strive alongside equities in the beginning of the year as investors seek to increase risk exposure. European and the US HY gained 2.18% and 1.54%, respectively, over the month. Although spreads have tightened now, there is still upside as ETF flows suggest net inflows in HY which can serve as a proxy for investor demand. However, Windstream's (USD 2.6 bn HY bonds outstanding) high-profile filing for bankruptcy shows that idiosyncratic risk cannot be neglected in this market. Especially because most companies have pursued a strict "Shareholder First, Debtholder Last" approach over the last years. Own shares were bought back aggressively financed by cheap debt leaving them with weaker balance sheets. We suggest to be very selective in this market segment.

Our Performance

In February, 51.10% of our portfolio was invested in fixed income. We used our benchmark ETF that tracks 3-7 year US Government Bonds and another ETF with maturities from 1-3 years to build this exposure. Together, they contributed -0.08% to our performance in February. As described in the first part, rates were slightly up over the month leading to losses in the benchmark ETF which were mitigated by a small gain in the short-term fund.



Lukas Müller
Financial Markets Division



NIC Fund

Commodities

February Round-Up

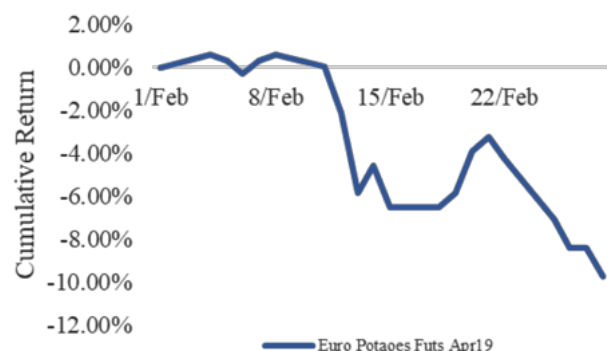
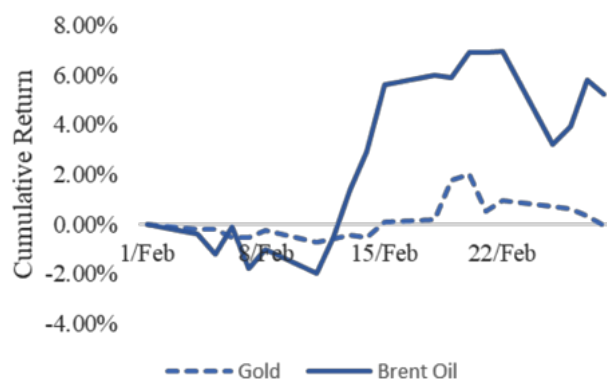
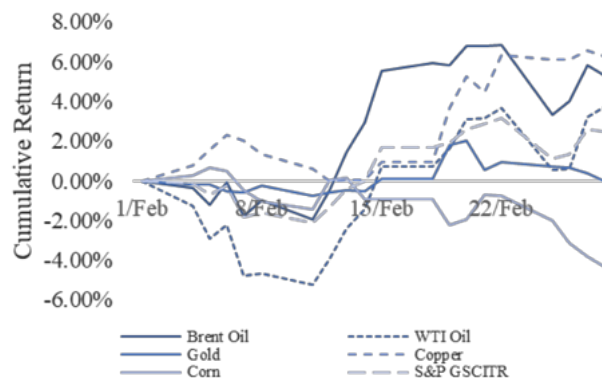
The S&P GSCI Total return index, which tracks 24 commodities, rose 2.45% in February. The positive movement was mainly driven by this month's top gainers Brent Crude Oil and WTI Oil, which were up 5.23% and 3.55% respectively. Gold finished the month flat and Corn was one of the worst performers, down 4.30%. Oil had a great bullish run at the beginning of the year rising almost 30.00% since January 1st. Wheat is among the leading losers in commodities markets in 2019 so far, with a negative performance of almost 10.00% for the year, as demand for this year's crop is expected to fall to 6-year lows. As far as gold is concerned, its price hit its highest levels in ten months in mid-February, playing the role of a safe haven for investors who fear that the US economy is reaching the end of an economic cycle or are worrisome about the possibility of an escalation of the US-China trade war. Still a surprise performance given the bullish run of equity markets in the first 2 months of the year. Although not part of the S&P GSCI Total return index, Palladium is worth mentioning since its price rose to an historical high of USD 1,550 per ounce this month, due to expectations of a supply squeeze for the year. This important component used in catalyst converters to make car engines exhaust less toxic has been rising steadily in the first quarter of 2019, fuelled by tighter regulations when it comes to emission standards in the auto industry, and it has risen sharply since its USD 200.0 an ounce levels, a decade ago.

Outlook for March

Despite the early increase in its price this year, most investors and banks still believe gold will perform well in the next couple of months. Expectations of a rate increase by the Fed are now slim and emerging markets' central banks such as Russia's or Kazakhstan's are expected to continue to buy gold to increase their reserves, pushing up supply. When it comes to oil, with Saudi Arabia deciding to reduce output, sanctions on Iran and Venezuela, and the latter country's political situation, total output may be reduced in the coming months. An outcome that can still be reversed by an increase in oil production by US producers, who hit this month a output record high of 12 m barrels a day.

Our Performance

In February, we maintained an allocation weight of 8.60% in the commodities benchmark ETF, 1.40% underweight against our benchmark weight of 10.00% of the portfolio invested in commodities. Our potato futures did not perform well this month with a decrease of 9.48% in value. Nonetheless, their total weight on our portfolio is just 0.92% and there is still time to recover from the losses before the April maturity date.



Pedro Leão
Financial Markets Division



NIC Fund

Currencies

World Currencies

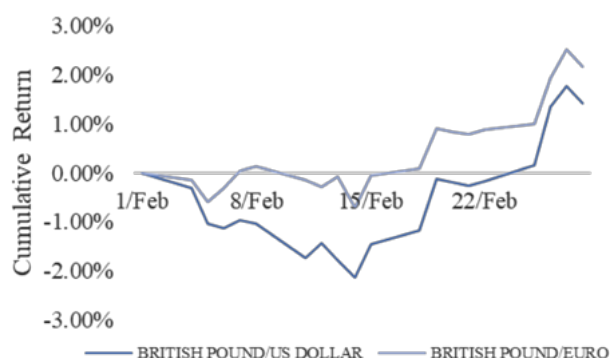
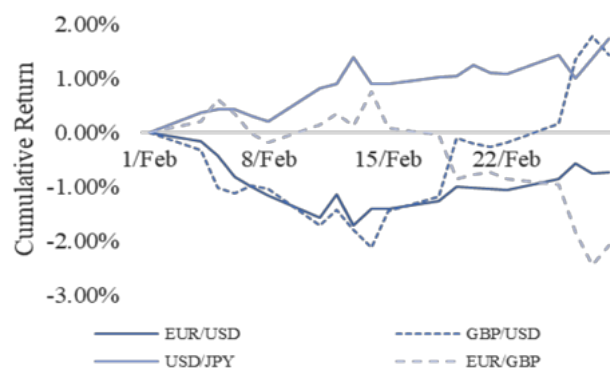
Following the best January of the past 30 years for equities, February was expected to be a modest month, without much room for additional gains. Nonetheless, it proved otherwise, particularly in the US, where some of the investors that had de-risked their portfolios considerably showed willingness to reverse it, regardless of February's higher prices. Thus, it is not surprising that the USD surged 1.73% against the JPY ("the *safe haven* currency"). Not only US macroeconomic data surpassed expectations, but also Fed's Chairman, Mr. Powell, provided increased confidence in what concerns the outlook for the US economy. Moreover, the Fed's dovish tone provided an additional stimulus and reinforced investors' trust in the greenback. Thus, the USD took the centre stage for the month. Nevertheless, in what regards the EUR, an opposing narrative took place. The EU currency devalued against major peers, having contracted 0.74% and 2.09% against the USD and GBP, respectively. Both economic and political motivations were the driving factors for the EUR downturn. Germany presented disappointing industrial data – signalling the possibility of a sluggish industrial activity recovery. Furthermore, Italy's fragility remained evident and political uncertainty kept to "haunt" the EU – as Spain runs towards a looming general election, by April 2019. Lastly, the GBP reversed the beginning of the month losses as soon as Mr. Juncker indicated the possibility of an extended deadline for Article 50. Such gains were particularly significant as the end of February approached, as Mrs. May decided to consult MPs on a *no-deal* possibility or a *decision of delay*.

In Depth: The Sterling

Following the latest news on Brexit there might be room for additional appreciation of the sterling, particularly following a market that has been consistently pricing-in the possibility of a *no deal* scenario, amidst a very much bearish tone. Despite the sluggish performance at the beginning of February, the GBP closed the month gaining 1.41% and 2.15% against the USD and EUR, respectively. Such reversed performance is suggestive of the market's recent optimism in what concerns the Brexit outcome. As Mrs. May stated: "The UK will only leave without a deal on the 29th of March if there is explicit consensus in the House for that outcome". Given that previous votes indicate that only a minority of MPs in the House of Commons would back such a result, the Parliament consult on *no-deal*, on the 13th of March, is likely to result in favour of the UK. Moreover, on the 14th of March MPs will be consulted on *decision of delay*, which could depict success in imposing alternative agendas on the government – such as a softer Brexit, a longer delay or a second referendum. All in all, the possibility of a *no-deal* Brexit, previously priced in by the markets, is fading away and the sterling is undoubtedly a promising winner.

Our Performance

Currently we do not hold any currency related assets in our portfolio.



Francisca Anselmo
Financial Markets Division



Extras

Hot Topic

A Delay to an Imminent UK-EU Divorce



Vera Teixeira Wahnnon
Investment Banking Division

“At this stage in the game the extension looks like the only way to make sure we don’t end up with no deal.”

– Edwin Morgan

After years of insistence that Brexit would happen on time, UK Prime Minister Theresa May has announced a potential delay to the UK inevitable exit from the EU. The proposed Brexit extension arises one month after May suffered the largest sitting government defeat in the history of the British Parliament, with 230 MPs voting against her proposed deal on the 15th of January. The leader of the Conservative party has committed to holding a second meaningful vote on 12th of March, buying herself more time to get other MPs into voting for her EU withdrawal agreement. If no consensus is reached at the House of Commons in favour of the revised deal, and if the Parliament rejects an exit on 29th of March, Mrs. May is set to push back the UK exit from the EU until no later than the end of June.

The delay described by the UK Prime Minister as a “short, limited extension” to the Article 50 process is appointed as the most likely outcome of the new vote taking place in March. According to the Brexit Delivery Group (BDG), Tory MPs are set to back an amendment presented by Labour MP Yvette Cooper to postpone Brexit as to prevent a no-deal scenario. To worsen Mrs. May’s chances of getting her agreement approved, the Labour leader Jeremy Corbyn is set to present his party’s own version of a Brexit deal and if rejected, a second referendum will be backed. A private briefing sent to the Labour MPs stated that the poll would only include credible Leave and Remain options, ruling out a no-deal alternative.

As parties are fiercely trying to avoid a UK departure from the EU without a deal, the likelihood of a Brexit delay is on the rise. As a result of these expectations, on February 26th, the pound hit its strongest value in seven months against the dollar of around USD 1.3254, and its highest value against

the euro in two years. However, despite the market’s observed positive outlook, investors seem to be investing less and divesting more from the pound as they wish to reduce exposure to the exchange rate’s frequent up and down swings. The exchange rate is, thus, becoming even more volatile as the number of sellers and buyers trading is dropping. The market’s predictability appears to be aligned with the Parliament’s interests, having also shifted towards a delay scenario.

In what concerns a prolonged Brexit, UK business is not as optimistic as the sterling. The rising speculation and uncertainty regarding an unanticipated no-deal after the prospective delay are causing groups to take even more dramatic measures as to minimize the impact of such outcome. The Allied Irish Banks, the largest lender in Ireland, has stocked USD 164.0 to protect the bank against a hard Brexit, and as reported by the incoming chief executive, Colin Hunt, the bank has had to put off some investments mainly in small and medium enterprises. In addition, and contrary to what would be expected, AIB increased its dividend to 17.0 cents per share based on forecasts that lending will grow next year and on the premise of a soft rather than hard Brexit. Nevertheless, businesses can benefit from the extra three months to prepare for issues related to supply chain disruption and the imposition of new tariffs, while access to the global markets is no longer a concern as the UK was granted independent membership of the government procurement agreement.

All in all, the UK-EU divorce extension is a double-edged sword: it may be exactly what the UK government and business need to better prepare for the inevitable Brexit, yet it comes with the cost of greater uncertainty about a no-deal scenario, leading to stricter actions to be taken.

Vera Teixeira Wahnnon
Investment Banking Division

Extras

Hot Topic

Too Big To Fail: The Indian NBFC Crisis



Lisa Preußler
Financial Markets Division

"India's own Lehman Moment - There's so much fickleness in the market today that nobody wants to be caught off guard. We're not over this."

"The tragedy is that housing finance companies, with 10-year home loans, were borrowing money from mutual funds that had overnight redemptions, there was a huge mismatch."

In India, general elections are imminent, while the Indian economy grew at its slowest level for more than a year due to a continued slowdown in consumption and strong investment activity.

One reason for the slowdown in consumption is the ongoing crisis in the non-bank financial company sector (NBFC), which has heavily financed India's rapid credit growth in recent years, as India's dominant state-owned banks have struggled with a growing pile of bad debt losses. They have, thus, increasingly shifted lending to the shadow banking system.

The business model of the Indian NBFCs strongly relied on the buoyant short-term credit market, driven by debt-oriented investment funds with strong inflows. As most of the loans granted were long-term, but heavily relied on short-term corporate debt – and as Friedman used to say, *ain't no such thing as free lunch* – a huge asset-liabilities mismatch emerged as sentiment in the Indian short-term debt market darkened.

The consequences of such an asset-liability mismatch could be observed during a debt market squeeze in September 2018, when one of India's largest NBFC IL&FS, a triple-A rated major Indian infrastructure and finance group, began to default on its debt as Indian market money funds ceased their funding and short-term debt could no longer be rolled over. In response, many other investors became conservative and risk-averse, freezing debt markets for many NBFCs and causing a liquidity crisis.

The scramble for liquidity led to a significant slowdown in the growth of the NBFC sector and thus in overall credit growth in India, as the Indian corporate debt market is still heavily dependent on the NBFC sector, which accounts for a third of

new lending as well as for a third of Indians home ownership loans.

The strong degree of interconnectedness of the loosely regulated NBFC sector and the associated systemic risk to the Indian economy and its future growth became increasingly apparent. In response, the Reserve Bank of India (RBI) eased the restrictions that allow banks to further promote much-needed NBFC funding.

Since there is nothing wrong with a bank buying distressed assets as long as it is in the best interest of the bank, it is wrong to do so in the best interest of a President who wants to be re-elected.

In addition, it should be critically examined whether the eased restrictions will not further increase the risk of spill over effects. Doubts in this respect are reinforced by reports of a possible rift between the RBI and the government on how best to manage the crisis.

However, one fact remains inevitable: India needs to develop a sustainable solution for the NBFC sector in order to secure the local credit market and to avoid suffering a similar experience as the US did a decade ago after the Lehman bankruptcy. India still considers itself better protected than the US back then and says that the NBFC crisis is still under control, but a catastrophic chain reaction is starting quicker than it has been controlled again and its damage is unfortunately noticeable for a long time.

Regardless of the outcome of the elections in India, the winner must be able to find an appropriate solution for the NBFC sector in order to prevent a severe downturn in the Indian economy.

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Hot Topic

Delayed Agreements



Rita Silva Marques
Investment Banking Division

"Indeed, there is no reason to turn over-optimistic. We don't expect the existing tariffs to be reduced any time soon."

– Louis Kuijs, head of Asia economics at Oxford Economics

During the last weeks, Chinese and American representatives have been vigorously involved in talks in Beijing and Washington to end trade conflict between the two before the deadline of 1st of March. At stake is one of the century's most consequent issue: the course of China's USD 14.0 tn economy.

In December of last year, the presidents of the two biggest world economies decided to pause their trade-war and negotiate an agreement by the start of March. In the absence of such an agreement, Trump had warned that he would impose additional tariffs on imports of Chinese products.

On the 24th of February, President Trump used twitter to do a surprise announcement on trade war matters. He wrote, "the U.S. has made substantial progress in our trade talks with China on important structural issues including intellectual property protection, technology transfer, agriculture, services, currency, and many other issues. As a result of these very productive talks, I will be delaying the US increase in tariffs now scheduled for March 1."

The American president also said he would meet Xi at his golf club in Mar-a-Lago, Florida, "to conclude an agreement" if "both sides make additional progress." However, no date for the summit has yet been revealed, nor has a new deadline for a tariff increase been announced.

Companies bracing for a rise in tariffs from 10% to 25% on March 1 can breathe a little easier now, even if this ultimately proves to be another delay without a firm resolution.

The "very good weekend" for the two world biggest economies lead to a very good Monday for Shanghai stocks. The benchmark Shanghai Composite jumped 5.60% in response to the news, representing the biggest daily percentage gain since July 2015. Last year, Chinese shares experienced significant losses due to concerns regarding

the country's economic slowdown and its drawn out trade war with the United States. Stocks have rallied since the start of 2019, however, partially because of increased optimism that there will soon be an end to the trade war between the world's top two economies.

But not everything is optimistic. Several experts pointed out that an easing in tensions between the two economic giants will not stop the global slowdown, which is already happening.

The International Monetary Fund projections last month estimated the global economy would grow 3.50% this year, down from 3.70% in 2018. "I think we need to take a little bit of a step back and take a look at the economic cycle," Paul Kitney, chief equity strategist at Daiwa Capital Markets, said last week "The shape of the cycle is one where we see moderation in growth in the United States this year ... we see risks of a recession in the United States growing possibly as early as the middle of 2020."

"At the same time, we have to keep in mind that the really core, critical thorny issues — which is to do with intellectual property rights protection, technology transfers, subsidies for the Chinese technological champions — those have not been addressed. So, the best we can hope for is that they will continue to talk about these into the future," he added.

The US and China might appear to be close to ending a tariff fight that hurt financial markets and dented economic activity worldwide, but that's not going to stop the slowdown already seen in the global economy. For now, companies should still prepare for the possibility that tariffs will rise to 25% at some point in the future, and wait for more developments that may flesh out when such an increase could occur.

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Thank you!

Visit www.novainvestmentclub.com for more updates.

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