Jefferies Insights

APRIL 2019

Living In A World Of Extremes

Dear Client and Employee Partners,

1. Hard Brexit or Reverse Brexit
2. Interest Rate Increases or Interest Rate Decreases
3. Red Hot Economy or Imminent Recession
4. Socialism or Hard Right
5. Sky High Energy Prices or Collapsing Oil
6. Re-elect or Impeach
7. Amazon Please Come or Stay Out of Our City!
8. Wall or No Wall
9. Technology Companies Revolutionizing How We Live or Break Them Up!
10. Open Borders or Closed Borders
11. Nationalism or Joint Cooperation
12. Tariffs or Free Trade

The list goes on and on and on....

It feels that today we live in a world of passionate extremes, with both sides believing their opinion is absolutely 100 percent right. We are not talking "mostly right," or "75 percent right," or even "90 percent right." We are talking black and white "100 percent right!" Wow, in a complex world including some of the complicated issues above, is anything really that crystal clear?

To be fair, the media is having a field day in today's world and it sure feels like they are adding a lot of fuel to this bonfire. It's really not fair to blame them because when you step back and think about it, what is their main job? Yes they want to inform and do a public good by being honest and fair, and drive for the truth. In fact, many of them do a decent job in this regard. But what is a media company? It is a "for profit" enterprise that is responsible to shareholders and other stakeholders. Their executives are operating businesses that employ lots of people and have responsibilities to meet payroll, provide careers, grow revenues and produce financial results. People today (and this probably hasn't changed and maybe never will) are entertained, educated and kept interested by reading and watching opposing sides aggressively slug it out. We are not saying all the world is a UFC match, but people get very bored watching calm, balanced and thoughtful people discuss the intricate pros and cons of grey issues. It just isn't enough fun for most people. They would much rather see two loud people duke it out publicly with absolute conviction in their diametrically opposed competing opinions.

IN THIS ISSUE

All this said, there is reason for optimism and perspective.

First, most rational people in the world will recognize that issues like those above are neither black nor white. Greyness, nuance, tradeoffs, details, compromise and factual debate are all good and healthy. Getting to the right compromise answer is much more important than espousing one's ideological and borderline "religious" belief. Just like in geography, most of the world does lie somewhere between the polar extremes. The voices of people who are "100 percent right" merely serve to sway on the margin the large population that lives in between them. On almost every economic/political issue, compromises are forged, conditions are attached, incrementalism wins the day and the life or death decision never comes to having to be decided in the manner demanded by the extremes. Yes, there can be grave mistakes that allow things to spin out of control, but in our experience even those extreme cases result in after the fact adjustments that ultimately allow for more time, which allows things to settle and better solutions to present themselves.

The point of our note today is merely to highlight that all of today's pressing issues that may seem impossible to adjudicate will most likely find their way to ultimate compromise. It can take hours, days, weeks, months, years or decades. The ones that "take decades" probably need that long runway because of their complexity and the requirement for the realities around the issues also to change. In fact, sometimes the world itself must change before these issues can be properly addressed. The concerns that take "hours, days or weeks" probably don't deserve to be on the list of critically important societal issues. It is the ones that take "months that may turn into years" which occupy the most intellectual and emotional bandwidth of people who invest in or lead companies. These are the issues that the people on the polar extremes are demanding need to be solved immediately. They also are the ones that have such critical importance that they can't sit for a decade or more to pass or the world around them to adapt.

A. Despite all the pedantic loud voices we hear, compromise most likely will rule at the end of the day. While we need to listen and learn from the passionate energy around us, we should also accept the way the world realistically works, not overindulge in the process of considering and fretting about the global large issues, and focus on the individual day-to-day and strategic pressures we face in our own complex businesses and lives. If we stay focused on what we can affect and control, and make the best choices for the companies we run and the investments we make, the world of extremes will eventually settle. We then can all sit back and wait for the very next (new) set of urgent and diametrically opposed views to present themselves. They always do.

B. While we can't readily change the reality of the macro issues and the extremes that are in contention, we can each make the world at least a little bit better and, as leaders, we can engage others to join with us in this effort. If we increase the civility and community mindedness in our own families and work units, the world will surely be a better place.

C. When faced with opportunities to express our own views on issues and choices, including electoral choices, we can dedicate the time and energy to do the real work to assure our views are based on the facts and the full picture, and not merely sound bites, emotions and personalities. The quality of our choices matter today even more than ever.

In partnership with all of you as we see and live through the greyness together,

Rich and Brian

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Economics and Strategy

A Flo Rida Market Structure

For our quarterly market strategy commentary we decided to channel a little Flo Rida by presenting the eight "lows" which best describe the current U.S. macroeconomic and financial market landscape:

1. Low inflation
2. Low unemployment
3. Low rates
4. Low curve
5. Low vol
6. Low issuance
7. Low spreads
8. Low volumes

That pretty much sums it all up, or as Flo would say: "low, low, low, low, low, low, low, low!" Additionally, in the near term, there are not really any potential catalysts for a change. Fed policy is unlikely to surprise in any way until the June summit on framework alteration. Presidential politics shouldn't start to affect markets materially until at least around the time of the first Democratic debate in the summer. Similarly, material changes in our low-inflation/low-unemployment economic landscape look highly unlikely. Grinding all these lows even lower over the next few months seems like the most probable path.

As the year progresses, however, Fed policy, Presidential politics, and the global economic data all have the potential to pop at least a few of these market characteristics off their lows. A commitment to Temporary Price Level Targeting (TPLT) by the Fed could cause inflation expectations to perk up, the curve to steepen, and rate volatility to increase. A strong showing in the debates by some of the further-left-leaning Democratic Party candidates could rattle equities, increase volatility, and even increase inflation expectations. In addition, some of the cracks we are already seeing in the global economic data may begin to widen as the long and variable lags from 250 basis points of Fed rate hikes and $600+ billion of cumulative Quantitative Tightening begin to kick in. These factors in turn could cause some shakiness around the lows in unemployment and credit spreads.

In any case, all of these lows will not simultaneously disappear, and in fact there is a decent chance they'll all remain with us for the rest of the year. But if I were to consider which ones are the most vulnerable to a flip, I would go with vol, curve, and spreads. And it would be increases in political risks and/or global economic duress that cause the change. Now if this were to happen, I suppose I would need a new song to channel. I'll work on coming up with some good choices over the next few months as we all begin to weigh the odds of an adjustment in the current "low" market structure. Sadly though, with all the politics surrounding the Fed, I doubt I will be able to go back to what I was channeling in the summer of 2014: "Turn down for what." That theme song probably only comes back after the 2020 election.

— David Zervos, Chief Market Strategist

From Despondency to Euphoria in One Quarter

Global equities have experienced a V-shaped rebound despite lukewarm data and muted earnings growth. Extremely risk averse positioning by investors and policy U-turns by the central banks have caused a rapid ascent in share prices.

The near 180-degree turn by the Federal Reserve ought to diffuse any concerns about deflation while providing global equities with a scenario of low bond yields, firm wage growth and subdued headline CPI. The missing link is earnings growth. However, judging the bottom of a growth cycle is an inexact science, especially when it never turned negative year-over-year. Oil prices remain the wild card but are not high enough to hurt Emerging Markets (EM) yet.

Investors continue to underestimate the “Reach for Yield” theme that has dominated asset allocation since 2009. Inflows into EM and high yield bonds are recovering while the dollar’s strength in blatant disregard of widening trade and fiscal deficits shows that U.S. assets still offer high enough real returns despite worries over 2019-20 growth. The Reach for Yield theme has become empowered as 1Q19 proceeded as inflationary pressures have receded.

We would expect global lead indicators and economic data to gradually bottom out through 2Q19. We feel the deflation and recession threat is overplayed while global equity financial ratios are generally in good shape.

— *Sean Darby, Global Head of Equity Strategy*

U.S. Outlook – Background on Inflation Target History

Since 1977 the Federal Reserve has conducted monetary policy with the objective of meeting the so-called “dual mandate” objectives of promoting maximum employment and stable prices. In January 2012, the FOMC announced that U.S. “inflation at the rate of 2 percent, as measured by the annual change in the price index for personal consumption expenditures, is most consistent over the longer run with the Federal Reserve’s statutory mandate.”

The Fed announcement was a classic example of bad timing. Since the 2012 announcement, inflation met the Fed’s target for the first four months only to fall below target for 54 consecutive months. All-in-all, inflation has matched or exceeded the 2% target in only 15 of 85 months that the target has been in existence. Consequently, the Fed is gearing up for a discussion of alternative frameworks for inflation. Proposals include:

1. Maintaining the current 2% target regime
2. Raising the inflation target
3. Specifying an acceptable range around the 2% target
4. Specifying a range around 2% with an adjustable inflation target option
5. Average inflation targeting
6. Price level targeting
7. Temporary price-level targeting
8. Nominal GDP targeting

The common policy implication of these proposals is that it would prompt the Fed to keep rates lower for a long period of time.

Low U.S. inflation has not always been the primary problem with inflation. During the so-called “Great Inflation” of the 1970s and 1980s, the year-over-year change in the PCE deflator averaged 420 basis points above target. By comparison with the Great Inflation, the current low-inflation environment seems like a relatively minor issue. U.S. inflation has averaged 18 basis points above the 2% target since the mid-1980s. Similarly, since 2000, inflation has averaged 14 basis points below the 2% target including the sharp deflation periods of 2008-2011 and 2015-2016. Nonetheless, the Fed is looking for a way to fine-tune the inflation framework out of concern for Fed credibility, the possible effect of missing the target on inflation expectations and fear of persistent outright deflation.

There is no compelling body of empirical research or theoretical literature that points to 2% as being an optimal inflation rate for the U.S. economy. Former Fed Chairman Ben Bernanke acknowledged as much by saying he does not see "anything magical about targeting two percent inflation." Bernanke embraced the 2% more because of "transparency and communication advantages of the approach and not as much on the specific choice of target."

Nonetheless, 2% is a target that has been widely adopted by central banks as an empirical definition of price stability, although there are differences in approaches. For example, the Fed advertises its inflation target as being symmetric around 2%, while the ECB defines price stability as a year-over-year inflation "for the euro area of below 2%."

The inflation framework discussion is taking place against the backdrop of the Fed's effort to normalize monetary policy which complicates the issue. With the benefit of a fiscal tailwind and both objectives of the dual mandate "flashing green" for most of the year, the FOMC was able to raise the fed funds rate four times and shrink the size of the balance sheet by almost $375 billion. Now that U.S. inflation has fallen back below target, the objectives of normalizing the fed funds rate and meeting the inflation objective of the dual mandate are back in conflict.

There is concern that the normalization process will stall before the fed funds rate reaches a level that will allow the Fed to make a decisive rate policy response when the next crisis and/or recession occurs. Or, as Larry Summers put it, "monetary policy of the standard form (AKA lowering the fed funds rate) will lack room to do what it usually does." Summers' opinion is based on the empirical reality that the Fed lowered the fed funds rate by an average of more than 500 basis points in response to recessions since 1960, so the fed funds rate remains more than 200 bps below the level that history suggests is likely to be necessary for Fed rate policy to be able to do "what it usually does." Summers goes so far as to suggest that one of the criterion for choosing a monetary framework is that it creates "enough room to respond to a recession...(and) foresee nominal interest rates in the range of 5% in normal times. How that is achieved seems to me to be a question of second-order importance."

This is going to be an interesting debate.

— Ward McCarthy, Chief Financial Economist

European Outlook – In a Post-QE World, ECB Stumbles Out of the Starting Block; Brexit Deadline Extended, Every Option Remains in Play; Focus on EU Elections

It didn't take long for the ECB to remind the markets that the end of QE didn't mean the end of accommodative policy. The decision at the March meeting to amend interest rate guidance and offer new Targeted longer-term refinancing operations (TLTROs) came earlier than expected, with the ECB seemingly pivoting toward a 'lower-for-longer' stance. The generosity of the new TLTROs, however, remains unclear and the details will be key in terms of the overall take-up of new bank loans. One thing to keep in mind is that if the new TLTROs are offered at rates which are higher than the ones available in 2016, there could be an argument that the deposit rate may also need to rise, and perhaps the ECB will have to revisit the idea of a tiered deposit rate system.

With regards to QE reinvestments, as expected, the amendments to the ECB Capital Key weights, coupled with historic underbuying and overbuying of bonds means that some national central banks (NCBs) continue to add to their holdings of sovereign debt, while other NCBs are not fully reinvesting the cash generated through bond redemptions and will see their balance sheets contract this year.

The data flow to start the year has been mixed, with indicators of manufacturing output and global trade soft, but measures of services activity holding up well. Overall, growth in Q1 should see some improvement on last year; nonetheless, the performance of the euro area economy had disappointed expectations over the past year. This was reflected in the ECB's latest quarterly forecasts, which saw the largest downward revision to GDP estimates since 2012.

Digging into the detail, the ECB expects growth to return to trend in the second half of the year, a view that we very much with agree with. 2019 and 2020 will be years of growing imbalances and an increasing focus of attention for the ECB.

Similarly, in terms of inflationary pressures, the ECB is confronted with mixed signals. On the one hand, the labor market has been a source of strength with wage growth accelerating over the past year, and the Phillips curve seemingly starting to reassert itself. However, stronger wages are yet to translate to higher services inflation, although measures such as 'super core' inflation and the Jefferies Deflation Monitor analysis highlight some improvement in the data. Over the coming months, however, the late timing of Easter this year compared to last will play havoc with the core inflation prints, as the annual rate potentially falls very sharply in March, before rising back up in April, and then dipping again in May. The ECB should be content to sit on its hands until the summer. However, as the composition of the ECB's Executive Board starts to evolve, so potentially could the markets view of where policy heads in 2020.

Whatever political challenges are likely to face the rest of the EU over the summer, it's difficult to imagine anything will come close to the gridlock in the UK Parliament surrounding Brexit. At the time of writing, members of Parliament are attempting to take control of the process and indicate their preference for what Brexit should look like. The final destination is yet unclear, but the delay in the proceedings likely means the UK staying in the EU at least through much of this year, and the UK taking part in EU elections. Brexit is the Great Disruptor. The complicated ecosystem that has built up in recent decades has already started to unravel. FULL REPORT

— *David Owen, Chief European Financial Economist*
— *Marchel Alexandrovich, European Financial Economist*

Actionable Ideas for Companies and Sponsors

MERGERS AND ACQUISITIONS

The New Face of Activism – Traditional Institutional Investors

2019 has seen traditional long-only institutional investors taking the step of actively embracing activism. As a new milestone in the evolution of activism, Wellington Management (~$1 trillion AUM), and a long-term 7.2% owner of Bristol Myers Squibb, issued a press release on February 27 opposing Bristol-Myers Squibb's (BMY) $74 billion buyout of Celgene (CELG). Their opposition to the transaction is several-fold including, 1) the transaction bears too much risk; 2) the transaction terms offer BMY shares to CELG shareholders at well below its implied asset value; 3) execution success is too difficult to achieve; and 4) BMY management needs to pursue alternative paths to create value.

In an even more aggressive action by a mainstream long-only institutional investor, M&G Investment Management, one of the U.K.'s largest (~$360 billion AUM) and longest established institutional investors, and a long-term 16.5% investor in Methanex, a $4.5 billion Canadian company, officially nominated an opposing slate of four board members for Methanex on Mar 25th. In a statement released by M&G, "In our 85-year investment history we have been able to fulfil our responsibility for stewardship of our investments almost exclusively through private and informal communication. Engaging in a proxy contest is extraordinary action for us, but in this situation, we feel we have no alternative but to do so."

Both Wellington's opposition and M&G's activist stance have awakened board members and CEOs across the U.S. and Europe to the fact that even the longest-term institutional shareholders are now prepared to aggressively intervene in Board decisions. These events also highlight the critical importance to Boards and management teams of consistent engagement with long-term shareholders to preempt such shareholder responses.

The Trend in Larger Take-Privates Is Gaining Significant Momentum

Capital concentration among the larger private equity funds is leading to both increased activity and increased deal size in take-privates. In 2018, the ten largest private equity funds raised $125 billion, almost a quarter of the PE capital raised, and these private equity firms are looking for larger deals in the public universe as a means of investing the large sums they need to put to work. In addition, the return requirements of private equity funds are steadily declining due to the excess supply of funds and new competitors, including pension funds, requiring lower IRRs. This has resulted in the willingness of PE funds to pay higher prices. Finally, the leverage finance new issue market remains open for highly leveraged transactions, enabling private equity funds to more effectively compete against strategics. The result of these trends is that in 2018 and 2019 YTD globally, there were 84 take-private transactions announced, and the median deal value has risen to $1.2 billion.

Family-Owned Businesses Becoming an Increasing Source of M&A Targets

Founder and family-owned businesses will be an increasing source of M&A activity, especially for financial sponsor buyers. A recent survey of 500 mid-sized family-owned businesses cited that one-third expect to transition ownership of their businesses within the next five years, and over three-quarters expect to transition within the next ten years. Because there is less inclination by the next generation to join family enterprises, these business owners are increasingly looking to outside parties when contemplating transition. This succession dynamic represents a natural point of entry for financial sponsor capital, and more than 40% of the businesses surveyed have already contemplated a sale to private equity. This trend will further accelerate as the economy moves past the peak of the business cycle and existing owners lose interest in weathering another storm.

DEBT CAPITAL MARKETS

Refinancing LIBOR Debt with EURIBOR Debt

Given the rate environment in Europe, there is an opportunity for companies with European operations and/or cash flows to significantly reduce their overall cost of debt by refinancing existing LIBOR loans with EURIBOR loans. The difference between 3-month LIBOR (~2.6%) and 3-month EURIBOR (~ -0.3%) is driving substantial savings because the equivalent LIBOR and EURIBOR term loans have recently been pricing with the similar spreads (within 25-50bps) above their applicable reference rate. Recently, Power Solutions executed a cross-border financing, pricing their pari passu EURIBOR and LIBOR based loans at E+375 and L+350, respectively. Taking in account the 0% EURIBOR Floor of the E+375 term loan, the company is paying ~235 bps less on that portion of their debt. We encourage clients to consider this refinancing alternative to achieve a lower cost of debt and a natural hedge for Euro cash flows. In addition, the execution of these refinancings is straightforward, leveraging existing documentation, and can be accomplished for transactions of €200 million or greater.

Financing with Secured Bonds Versus Term Loans

During 2019, the syndicated loan new issue market has slowed significantly, driven by the Federal Reserve change in policy away from raising rates, which has driven investors away from floating rate debt. This has been coupled with loan investors tightening documentation and widening pricing. In contrast, the high yield new issue market has been very active, with many transactions pricing at the lower end of the coupon range and with issuer-friendly terms. In addition, in today's market, a B-rated secured bond of similar maturity to its equivalent term loan would price in-line or tighter than the term loan. This change in investor demand for fixed rate bonds is supported by positive fund flows into the high yield market and away from the leveraged loan market. Year-to-date, the high yield market has experienced $8.8 billion of inflows, while the leveraged loan market has experienced $10.0 billion of outflows. The recent $4.2 billion Dun & Bradstreet LBO financing included $700 million of secured notes that priced at 6 7/8% or 135 basis points less than the equivalent $2.5 billion term loan which priced at a yield of 8.23%.

The Return of Portable Capital Structures

Since mid-March, we have seen the return of portable capital structures in the context of refinancings. This is in contrast to the previous four months where this alternative was not available to issuers, as investors were requiring indebtedness to be refinanced in the event of a change-of-control. Portability provides issuers with significant flexibility in the context of executing sale transactions especially in volatile capital markets. Recently Mirion Technologies, owned by Charlesbank Capital Partners, achieved portability for 18 months post-closing, subject to leverage no higher than closing levels. In addition, TruGreen, owned by Clayton, Dubiler & Rice, completed a refinancing with portability for 24 months post-closing. TruGreen's portability also allows pro forma leverage to be increased to 6.25x ebitda in a buyout versus the 6.1x closing leverage for the refinancing.

EQUITY CAPITAL MARKETS

Unregistered Institutional Private Offerings (U-IPOs) as a Source of Growth Capital or a Path to Monetization

Unregistered Institutional Private Offerings (U-IPO) are large ($150 million to $1 billion), pre-IPO placements of equity, that are broadly placed with traditional institutional public market investors. These investors do not require any special terms or any board seats. The only requirement is an agreement to publicly list the U-IPO security within a defined time period, typically 18 to 24 months. This listing can be achieved either through a traditional IPO or through a direct listing, leveraging the base of long-term, institutional investors that has already been established in the U-IPO.

While the U-IPO is a broadly applicable and flexible product, there are two major reasons clients choose this financing alternative. First — speed to capital — where capital can be raised for a specific need in as short a timeframe as eight weeks. This is especially important when a company is looking to meaningfully accelerate their business through near term capital deployment, either through an acquisition or organic opportunities. Second — sponsor or owner liquidity — where the issuer can sell up to 90% of an ownership stake in one offering, a far larger amount than the IPO market can typically accommodate. Jefferies is a leader in U-IPOs with a dedicated team of specialists with over 38 years of experience in this product.

Using the U.K. Investment Fund Market Across Sectors and Geographies

The U.K. is the largest fund market in Europe with over 300 funds listed in London and a market capitalization of over $200 billion. Issuers should be aware that these funds do not need to be U.K. or European-based businesses, as 20% of listed funds are focused on other markets. In addition, a diverse range of funds are listed, from specialist REITs to funds focused on healthcare royalties, renewable energy, energy efficiency, infrastructure, aircraft leasing and private equity.

Investment funds are structured as newly created companies that raise capital through an IPO to invest in a specific asset class. Fund candidates must have a differentiated investment opportunity that can attract institutional demand and demonstrate an ability to scale-up over time. These funds require a portfolio of seed assets or a clearly identified pipeline, with the objective to have the IPO proceeds fully invested within 9-12 months. There is broad investor interest in the sector, including pension funds, income funds, multi-asset managers, family offices and private banks. Yield is also an attractive aspect as 85% of listed funds pay a dividend that averages 4%. Jefferies is the #1 underwriter of U.K. investment funds since 2013, based on total equity issuance, having raised over $8 billion for our clients.

SPACs Have Become a Mainstream Source of Acquisition Capital

SPAC IPOs continue to be one of the most active areas of new issuance, despite the increased market volatility. In 2019 YTD, SPACs have accounted for 52% of all U.S. IPO activity (14 SPACs have raised $3.2 billion) and are the second largest fee pool in the U.S. equity capital markets. Issuers include private equity sponsors and alternative asset managers (36% of issuers YTD), as well as senior operating executives with public company experience (64% of issuers YTD).

SPACs are compelling to clients, as they offer economics that are significantly more attractive than traditional private equity fund economics, with limited downside and significant upside in public company. Issuers typically receive 20% of the common equity in the SPAC for an investment of approximately 3%-4% of the IPO proceeds. For example, in a $250 million SPAC, the sponsor typically receives over $60 million of common stock for a $7 million investment in warrants.

SPACs provide issuers a pool of permanent capital raised from institutional investors and a flexible acquisition strategy that can be focused on one or more industries. For private equity sponsors and other alternative asset managers, a SPAC can broaden the scope of transactions they can pursue, serving as a vehicle to complete transactions that may not otherwise fit traditional fund mandates or as a differentiating way to partner with a strong executive.

RESTRUCTURING AND RECAPITALIZATION

Incremental Financings for Stressed and Distressed Companies

For stressed and distressed issuers in need of additional liquidity to bridge to an operational turnaround or to meet seasonal working capital needs, there is an ability to utilize the various debt and lien incurrence baskets under existing credit facilities to raise significant first-in, last-out (FILO) financing behind an existing asset-based loan or an incremental term loan pari passu with the company's existing term loan.

These strategies have seen increasing use in recent quarters. Examples include: 1) Revlon, which bolstered its liquidity in 2018 via an amendment to its credit facility to provide for a FILO tranche and recently extended that facility's maturity to April 2020 as it continues to execute on the integration of Elizabeth Arden; 2) Dayton Superior, which secured a rescue loan from Solus Alternative Asset Management to help address seasonal working capital swings; and 3) Sears Canada, which raised an incremental facility of $300 million to shore up liquidity in the midst of a challenging retail environment.

MUNICIPAL FINANCE

Using Forward Delivery Bonds to Lock-in Refunding Savings

The Tax Cuts and Jobs Act of 2017 eliminated a municipal issuer's ability to issue tax-exempt advance refunding bonds more than 90 days before the call date of outstanding high coupon debt. As an alternative, municipal issuers can use forward delivery bonds to lock-in refunding savings in advance of the call date. Tax-exempt forward delivery bonds are priced in the current market but not issued until a date in the future.

Compared to bonds with a standard (up to 30 days) delivery time period, forward delivery bonds are priced with a yield premium to compensate investors for the illiquidity of their investment during the forward period and for committing funds to be used to purchase the bonds on the future delivery date. However, given current market conditions with low rates and a flat yield curve, the yield premiums for forward delivery bonds are modest—in the range of 3-6 basis points per month—and investors have been willing to accept a forward period of up to 24 months. Documentation for forward delivery transactions follows standard market formats, including an initial Official Statement for pricing and an updated Official Statement when the bonds are issued. Jefferies has recently acted as bookrunner on a number of successful tax-exempt forward delivery transactions, including for San Francisco Airport and the New York City Housing Development Corporation.

Best Research Ideas

AMERICAS

U.S. Insights – JefData: Housing Storm Largely Past and the Roof Didn't Collapse

Jefferies published a collaborative report on the U.S. housing market exploring a new Zillow dataset. Analysis of housing transactions posted to Zillow suggests that the biggest Y/Y price declines have passed and the price weakness of late is mostly limited to the most expensive homes. The U.S. is now lapping the change in SALT deductions, interest rates are well off highs, and real wages are growing at the highest rate this cycle—all reasons to believe 4Q18 was probably the worst rate of change for home prices. In addition, the current environment may also be past the worst in order misses from key homebuilders. Equity analyst Phil Ng prefers stocks with exposure to R&R (MAS, FBHS), public infrastructure and stocks that were oversold (OC, SUM). Equity analyst Jonathan Matuszewski noted strong correlation between comps at HD, LOW and FND and Y/Y home price changes. FULL REPORT

— Jefferies U.S. Equity Research

Interactive Entertainment – Game Changer: A Deep Dive on Free-to-Play Console Games like Fortnite

Jefferies took a deep dive look at the "free to play" video game model and believes it will expand the market long-term but also presents uncertainty over the near-term. The $38 billion console video game market is accelerating, and Fortnite generated a record $2.4 billion in 2018 estimated revenues, proving free to play can drive superior results vs. the $60/game model. Notably, Jefferies estimates Fortnite's EBIT margin could be 2,000 basis points better than ATVI or EA. Still, the firm notes that free to play games likely imply fewer, larger games. Jefferies believes the largest franchises such as Apex (EA), Call of Duty (ATVI), and Grand Theft Auto (TTWO) look best positioned. In addition, Jefferies highlights that ATVI trades near 4 year lows at 15.9x forward EPS and the company has Overwatch and Call of Duty that look well-positioned in light of the trends. FULL REPORT

— Timothy O'Shea, Jefferies U.S. Equity Research – Technology, Interactive Entertainment

Pharmaceutical Services – Annual Survey Says CRO Outlook Is Encouraging; Upgrade IQV

Jefferies conducted a survey among Contract Research Organizations (CROs) and found that overall R&D spend should accelerate and that respondents increasingly prefer global CROs over smaller, private players. The results also showed an improvement in sentiment toward outsourcing as measured by satisfaction and long-term outsourcing appetite. Jefferies upgraded shares of Iqvia Holdings (IQV) in conjunction with this report, and the survey results suggest IQV has increased the sales and operational intensity of the business and focused on developing and launching integrated application platforms. The company is making traction in Orchestrated Customer Engagement (OCE) for sales and marketing, and Jefferies believes this technology-oriented business will help to drive a better multiple for shares. Jefferies EPS forecasts are above consensus estimates for 2019E and 2020E. FULL REPORT

— David Windley, Jefferies U.S. Equity Research – Healthcare, Pharmaceutical Services

EMEA

Hey Big Spenders – Investment Risk in Global HPC: Unilever, Procter and Gamble, Reckitt Benckiser, Church & Dwight Most Exposed

The $600+ million of stepped-up investment by Colgate-Palmolive, Henkel and Beiersdorf for 2019 in Household & Personal Care reflects increased costs of growth and risks matching investment and/or a breakdown in pricing rationality in the big categories of oral care, laundry, and skin care. Yet Jefferies notes that current Street CY19 estimates for companies most at-risk call for 'normal' algo-type delivery (i.e., operating margins +40 basis points), while group valuation appears full at 22x next-12-month P/E (above hist. averages.). Most exposed: Unilever, Procter & Gamble, Reckitt Benckiser, Church & Dwight; Least exposed: Clorox, Kimberly-Clark, Energizer Holdings, Newell Brands. FULL REPORT

— Kevin Grundy, European HPC and Beverages Analyst
— Martin Deboo, European Food & HPC Analyst

Opportunities and Risks in Global Beer from Rising Competition

Jefferies believes the benefit to global beer stocks from outsized margin expansion and cheap debt is drawing to a close. Heightened competition in pursuit of growth is a natural consequence of this, which in turn could lead to pressure on margins. The debate in beer will shift from margin expansion to top line growth as the key driver of earnings. Jefferies upgrades Heineken and Carlsberg to Buy; downgrades AB InBev to Underperform and initiates on Royal Unibrew with an Underperform. FULL REPORT

— *Ed Mundy/Elsa Hannar, European Beverages Analysts*

ASIA

China – Telecom Services: An Updated Investor Guide to China 5G Scenarios

Continuing the discussion on China's 5G capex and China telecom services, Jefferies published an insightful piece based on: 1) assumption of no M&A; 2) reduction in estimated 5G capex by 8% (Rmb57 billion) in 2020-22 with peak capex pushed out to 2023 from 2021-22; and 3) factoring in 2G re-farming and incrementally less mobile data price pressure. Given this and China Mobile's lower 5G capex at 2.6GHz, Jefferies upgrades China Mobile to Buy and downgrades ZTE to Hold. China Unicom remains a top Buy, followed by China Tower and then YOFC. This report also explores forecasts and valuations in four other scenarios, including M&A. FULL REPORT. Additionally, Jefferies subsequently downgraded YOFC following much weaker than expected market share and ASP. FULL REPORT

— *Edison Lee, Jefferies Asia Equity Research – China Telecom Services*

India – Consumer FY20E Outlook: Chinks in the Armour

Contrary to expectations, consumer staples outperformed again in FY19 (and in eight of the last 10 years), although with higher earnings and valuation divergence with several stocks de-rating. While the overall sector de-rating hinges on broader market earnings recovery, odds are against the sector in FY20E with rising competition, peak margins, low margin of safety and low tolerance for earnings downgrades. Jefferies remains cautious and selective with a preference for companies with superior top-line driven earnings growth where margins are not looking too stretched from a medium-term perspective given benign raw material pricing and competitive intensity in the past few years. Jefferies maintains a Buy on APNT, NEST and DABUR given improving execution and growth traction, while ITC is a Buy on favorable risk-reward with a less harsh regulatory environment. FULL REPORT

— *Varun Lohchab, Jefferies Asia Equity Research – India Consumer*

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Technology, March 2019 lyft **$2,340,000,000** Initial Public Offering Joint Bookrunner	Automotive Aftermarket, February 2019 CALIBER COLLISION RESTORING THE RHYTHM OF YOUR LIFE **$2,750,000,000** Credit Facility to Finance Merger with **ABRA Auto Body Repair** Joint Lead Arranger	Consumer, January 2019 ELEMIS **$900,000,000** Sale to **L'Occitane** Joint Financial Advisor	Healthcare, March 2019 Pending bioscrip **$3,700,000,000** Merger with **Option Care Enterprises, Inc.** Joint Financial Advisor
Finance, March 2019 VIRTU FINANCIAL **$1,550,000,000** Credit Facility to Finance Acquisition of **Investment Technology Group, Inc.** Joint Lead Arranger	Industrials, February 2019 Pending ONE ROCK CAPITAL PARTNERS **$640,000,000** Acquisition of plastics distribution business from **Nexeo Solutions, Inc.** Sole Financial Advisor	Healthcare, January 2019 LABCYTE **Undisclosed** Sale to **Danaher Corporation** Sole Financial Advisor	Power, February 2019 Pending GREENCOAT UK WIND **£635,000,000** Acquisition of 49.9% stake in the **Stronelairg** and **Dunmaglass** wind farms from **SSE** Joint Financial Advisor
Healthcare, February 2019 OPKO **$200,000,000** Convertible Notes Offering Sole Bookrunner	Technology, January 2019 IMPERVA **$1,150,000,000** Credit Facility to Finance Acquisition by **Thoma Bravo** Joint Lead Arranger	Real Estate, January 2019 TRITAX BIG BOX **£250,000,000** Common Stock Offering Sole Global Coordinator and Sole Bookrunner	Energy, March 2019 Pending GOODNIGHT MIDSTREAM **$930,000,000** Sale to **TPG Capital** Joint Financial Advisor
Energy, March 2019 TALLGRASS ENERGY **$1,155,000,000** Credit Facility to Finance Acquisition by **Blackstone Infrastructure Partners** Joint Lead Arranger	Healthcare, March 2019 Epizyme **$173,000,000** Common Stock Offering Joint Bookrunner	Industrials, March 2019 Pending fxi **Undisclosed** Merger with **Innocor Inc.** Sole Financial Advisor	Real Estate/ Technology, February 2019 QTS **$322,000,000** Common Stock Offering Joint Bookrunner
Technology, March 2019 Pending careem **$3,100,000,000** Sale to **Uber** Sole Financial Advisor	Energy, February 2019 KODIAK GAS SERVICES, LLC **Undisclosed** Sale to **EQT Partners** Sole Financial Advisor	Finance, March 2019 VEIL Vietnam Enterprise Investments Limited **£154,000,000** Common Stock Offering Sole Bookrunner	Healthcare, February 2019 Pending Compassion-First Pet Hospitals **$1,215,000,000** Sale to **JAB Holdings B.V.** Sole Financial Advisor

JEFFERIES KEY FACTS & STATISTICS

(as of February 28, 2019)

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