Shock Apple downgrade worries global investors

By **Jonathan Shapiro**

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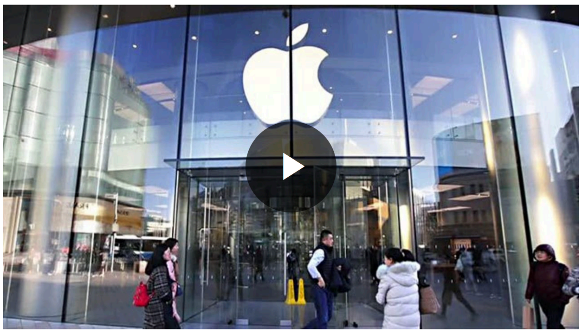
A shock revenue downgrade by United States technology giant Apple has sparked concerns among global investors that a slowdown in the Chinese economy is worse than initially feared.

The maker of the iPhone, which had a $US1 trillion market capitalisation last year, said on Wednesday that its quarterly revenues would be $US84 billion ($120 billion), substantially below its prior estimates largely as a result of a of a dramatic slowdown in Chinese sales.

The announcement, which is Apple's first pre-earnings release since 2002, stunned the market and triggered a 7.5 per cent decline in the share price in after-hours trading.



Apple on Wednesday cut its sales forecast for its latest quarter, with Chief Executive Tim Cook blaming slowing iPhone sales in China.

Lachlan MacGregor of funds management firm Alphinity Investments said that given the iPhone was the "world's largest consumer product", an unexpected slowdown in sales had widespread ramifications.

"Apple is telling us that consumers, particularly in greater China, are spending less. Taken with other weaker economic metrics out of China, this has to lead to investors being more bearish on the region generally and on consumer spending specifically," he said.

Mr MacGregor said it was not clear whether consumer spending was slowing in developed markets, as the weakness focused on China and other emerging markets.

"But this sort of news doesn't make you more bullish, and could have a flow-on impact to other areas."

Andrew Macken of global fund manager Montaka, which holds Apple stock, said the downgrade was "certainly concerning", even though it was not news that the Chinese economy was slowing.

"The apparent acceleration in the decline in recent weeks that Apple flagged this morning is a new data point that is potentially indicative of the state of the Chinese consumer," he said.

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"Perversely, the more rapidly the Chinese economy deteriorates, the greater the probability of a more significant policy response."

Less traffic in stores

Mr Macken said the key line in Apple's release was its statement that "mounting uncertainty" in financial markets was reaching consumers, which had resulted in declining traffic in its stores as the quarter progressed.

"And market data has shown that the contraction in greater China's smartphone market has been particularly sharp," Apple chief executive Tim Cook said in the letter to investors.

Graham Hay of Antipodes Partners said the announcement was further confirmation, following weak automotive sales and manufacturing data releases that the Chinese economy was slowing.

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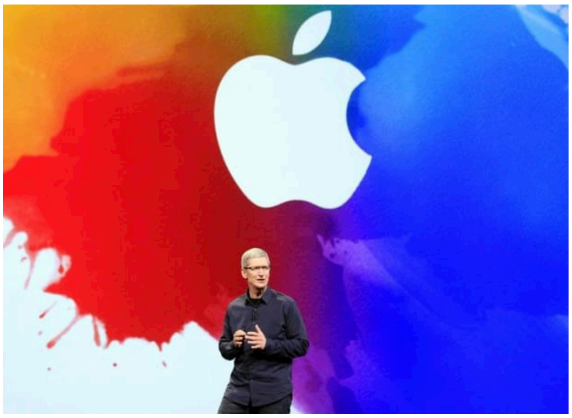
"A high-end handset is a decent discretionary item, so it is hard to escape the reality of a slowing Chinese economy," he said.

Mr Hay said a previous move by Apple to cease providing unit sales data on its handsets indicated headwinds for the company.

"The smartphone market has matured. The penetration rate has hit saturation point and for the last few years there has been an elongation of replacement cycles," Mr Hay said.

Antipodes Partners does not hold shares in Apple.



Apple CEO Tim Cook wrote in a letter to investors that "the contraction in greater China's smartphone market has been particularly sharp". **Jeff Chiu**

Mr MacGregor said the revenue shortfall was "deeper than even the bearish analysts were predicting," even if the downgrade itself had not been a surprise.

"Investors knew of the Apple production cuts, but it wasn't clear to investors if it was market-related, China or just Apple-specific, such as raising prices too fast," he said. Alphinity does not own Apple shares.

Apple is one of the largest weights in global stock market indices and the post-market decline was forecast to shave almost 100 points off the Dow Jones Industrial Index.

In fact, the post-market decline in Apple's share price wiped a staggering $US60 billion from its market capitalisation, a decline equivalent to the entire value of Australian "large caps" Westpac or CSL.

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Apple's shares already had come under pressure in the latter half of 2018 amid a broader sell-off in technology stocks and growing concerns about trade tensions between China and the United States.

The shock fall in Apple will be felt by a number of individual Australian investors who are trading more in international shares such as Apple, Amazon, Facebook and Google.

Loss of appeal

Matt Leibowitz, of global share-trading platform Stake, said Apple had been the second most popular security traded among its Australian users.

However, he noted that although Apple was the most-bought stock in November for users older than 55, it was the second most-sold stock among users aged under 35.

"The older investors see Apple as a 'safe' growth share with its cash reserves, while its general appeal to younger ones clearly dropped off," Mr Leibowitz said. "Sometimes it pays to listen to your kids."

He estimated that Apple's average daily trading volume was $10 billion compared to $6 billion for the entire ASX cash market.

While surprisingly weak China sales captured the headlines, Mr MacGregor said more attention should be paid to Mr Cook's comments "about the factors outside of China that are impacting their revenues".

"Perhaps they are downplaying how important these factors really are," he said.

Mr Cook pointed to weaker than expected upgrades of iPhones, which he attributed to macro factors, as well as fewer telecom carrier subsidies, US dollar strength increasing prices, and cheap iPhone battery replacements extending the product life.

"There has been a material shift in the length of the upgrade cycle," he said.

Mr Hay said Apple had had to achieve growth through price rises rather than volume growth.

"That has worked for the most recent cycle but they have pulled forward demand with the launch of the iPhone X in late 2016, early 2017," he said. "And they are seeing the other side of that speed bump."

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