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# Financial Newsletter

## The Financial Newsletter Team

*September Edition*



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## Foreword

With the rate of vaccinated people increasing day by day, the forecasts seem to drive the economy to a more stable path. Sectors such as hospitality, tourism, or travel have striven this pandemic since the very beginning. Even considering the increase in activity this summer, the growth appears to be slowing down, a problem for the countries that have faced the last financial crisis supported by these business areas. With this effect, the shade of unemployment emerges.

This pandemic brought numerous exposures, including the decrease in the offer curve, which has been increasing the level of the prices. To enhance with the autumn and winter coming, most of the economies around the world are concerned about the energy distribution. To note that, in the UK the energy prices have increased 250% since January.

Additionally, even with the uncertainties caused by Covid-19, and the third quarter coming to an end, the GDP in the euro area keeps climbing, and the forecasts suggest the real GDP increases more than the level it was pre-covid, about 5% YoY.

Countries in the south of the Old Continent, such as Italy and Spain, show the highest forecast recovery, projected to grow 6.2% YoY. The US real GDP is estimated to increase 6.7%, annual rate.

As a consequence of this growth in the economy, the target of 2% inflation has been a problem to deal with. Supply disruptions, increase in services' prices and energy inflation seem to be at the epicentre of this effect. However, this year the inflation is forecasted to be 2.2%, and decline to 1.5% - 1.7% in 2022-2023, in the Eurozone.

Furthermore, in our first newsletter of this year, we analyse the acquisition of MGM Growth Properties by Vici Properties, a deal that puts Vici as the top in the gaming hospitality industry.

Additionally, we also analyze "Thoughtworks", a software consultancy company that had an Initial public offering in the transact month, an offer led by Goldman Sachs and JP Morgan.

Finally, in the last section of the newsletter, we talk about the Digital Yuan, after China being the first country to ban cryptocurrencies, they release their own crypto. Even being efficient and the only crypto in the country, people cannot really see the main advantages of the Digital Yuan due to lack of education.

Have nice readings and bold investments,

*The Financial Newsletter Team*



## Macroeconomic Overview

The end of the summer brought several unexpected outcomes compared to the projected for 2021. The world is currently facing the effects of the new virus variant, Delta, and a general increase in inflation.

According to the BBC, both, US and UK saw their economic recovery slow down with the restrictions applied for the Delta variant, which "have hit spending on travel, tourism, and hospitality". These sectors, which have a powerful impact on GDP, were expected to increase in 2021. Although, despite the rise between June and August, the numbers decelerated, in September, causing impasses in several areas, for example, employment. The priority of the UK's Chancellor of the Exchequer, Rishi Sunak, has always been to protect as many jobs as possible. Therefore, he sees the recent creation of new ones as a reason to be "cautiously optimistic" (BBC, 2021).

Despite those tiny improvements, due to the job retention of the last few years, the cost of labor will decline until 2022. By 2023, it is expected to rise 1.4% (EBC, 2021).

The pandemic originated interruptions in production and supply channels, which reduced the level of supply. Due to that, the level of prices has been rising. With the beginning of the Autumn and coming Winter, along with the preoccupation of the 1st order goods supply, the world is concerned about energy distribution.

Last year, the winter in Europe and Asia was colder than intended, which reduced the gas reservations. This year, the level of stock remains low, which is already causing difficulties worldwide. In the UK, the energy prices have increased 250% since January, and seven suppliers companies, such as Hub, Money Plus, Utility Point, and People's Energy, have been forced out of business. The energy firm collapse already affected 1.5 million customers, who will see their energy bills rising by 12% from October, as the higher cap comes into force.

The previously reported event is responsible for the growth of the import deflator from -2.5%, in 2020, to 5.4%, in 2021. The fluctuation in oil and non-oil commodity prices, the increase of supply shortages' costs, and the depreciation of

the euro are reflected in this indicator (ECB & BBC, 2021).

As stated in the European Central Bank report, "HICP inflation is projected to continue to rise until the end of this year, to decline in the first half of 2022 and to gradually strengthen thereafter". The inflation will reach its peak of 3.1% by the fourth trimester, being the average in 2021 of 2.2%. Across the globe, the US attained the highest inflation rate in 13 years, 5.3% (ECB & BBC, 2021).

The American Central Bank hopes to regularize the situation by increasing the interest rates. Since this move toward higher price levels can be explained by the increment of temporary factors, the inflation level should decrease globally. In 2023, it should reach 1.5% in Europe, in agreement with the ECB report.

**Sources: BBC, ECB**

## Economic Calendar

### *Economic Outlook*

As the third quarter comes to an end, the euro area's Gross Domestic Product (GDP) continues to recover quickly, even with the many uncertainties caused by coronavirus, since restrictions in many European countries are being lifted which has aided in the economic rebound. The ECB expects for the real GDP to increase more than the level it was at pre-crisis by the end of 2021 and is currently forecasted to grow 5% YoY for the Eurozone.

The two countries in the Eurozone with the highest expected GDP YoY growth according to Eurostat are Italy and Spain. Both are forecasted to grow 6.2%.

According to the Bureau of Economic Analysis, the US real GDP for September increased by 0.1 percent from the estimate released in August. Currently the most recent annual rate released in September is 6.7%.

### *Inflation*

The strength of the current recovery in the GDP in the Eurozone has led to a slight increase in money velocity. With that, inflation went above the

ECB's target of 2%, and was roaming around 3% in August.

However, by the end of 2021, inflation is expected to average 2.2% which is still above the target due to factors such as strong increases in input costs related to supply disruptions, increases in services prices due to Covid-19 restrictions, and energy inflation. However from 2022-2023 these factors are expected to be temporary, allowing for HICP inflation to decline to rates of 1.5%-1.7% in that time period. Although, it is important to note that HICP inflation does not include food and energy prices which are expected to rise.



Figure: Euro area HICP (ECB)

In the US the Consumer Price Index (CPI) rose 5.3% YoY. The indexes for Food, shelter, and gasoline are expected to continue to rise also. Inflation continues to be troubling as bottlenecks and supply shortages continue.

### *Labour Market*

According to Eurostat, the seasonally - adjusted unemployment rate was 7.5% which was a decrease of 0.1% from July 2021 which was 7.6%. The year prior (August 2020) the unemployment rate was 8.6%, which shows that the euro area's economy is definitely recovering as the unemployment decreases. It is estimated that about 14.469 million men and women in the EU were unemployed in August 2021. When compared with last year, unemployment decreased by 1.965 million in the EU. Similar trend happened with youth unemployment. In August 2021, the youth unemployment rate was 16.2% in the EU which was a 0.2% decrease from last year which was 16.4%.

In Portugal, unemployment went from 8.2% last year to 6.4% in August 2021. A difference of 1.4%. This also shows improvement in the economy since the Covid crash which left many unemployed.

According to the U.S. Bureau of Labor Statistics, the national US unemployment rate was 5.3% in August which is down 3.2% from last year which was 8.5%.

From that data represented above, it seems that many countries' labor markets are recovering as the unemployment rates are decreasing over time.

## *Central Bank Decisions*

Despite the transitory increase in prices, the ECB is expected to not tighten any monetary policy just yet. In light of the improvement in the macroeconomic and financial conditions, the ECB announced that it will reduce the volume of net purchases of assets from the Pandemic Emergency Purchase Program (PEPP), going from around € 80 billion per month to about 60 billion euros in the fourth quarter. The ECB already bought its PEPP in August from € 88bn in July to € 65bn, ECB President Christine Lagarde stresses that these actions are not tapering.

The Federal Reserve is expected to finish tapering of bond purchases by mid 2022. The Fed has been buying \$120 billion in government bonds and mortgage-backed securities each month since to help the economy recover from the coronavirus pandemic. This was clarified at the FOMC of September as many investors expected the central bank to begin to ease on the stimulus by the end of the year.

**Sources: ECB, FED EUROSTAT, SPG GLOBAL, BEA, IMF**

## Investment Banking

### *M&A Deal of the Month: VICI Properties & MGM Growth Properties*

On the 4th of August of 2021 VICI Properties announced a \$17.2 Billion strategic acquisition of MGM Growth Properties, placing VICI in the lead of the triple net lease agreement REIT's. The deal will position VICI as the leader in the gaming hospitality industry. Upon the completion of the merger, VICI will have an enterprise value of about \$45B. The transaction will be known as "Master Transaction Agreement" in which MGP Class A shareholders will receive 1.366 shares of newly issued VICI stock in exchange for each Class A share of MGP. The MGP Class B shares, held by MGM Resorts will cease to exist. Following the consummation of the acquisition, VICI will enter in a triple-net master lease with MGM Resorts, with an annual rent of \$860M.

VICI Properties is an experiential real estate investment trust that owns one of the largest portfolios in gaming, hospitality, and entertainment destinations, including the world-renowned Caesars Palace. According to VICI's website, VICI Properties has a national and

geographically diverse portfolio in the U.S. It consists of 28 gaming facilities which add up to 47 million square feet. Their properties are leased to industry leading gaming and hospitality operators, such as: Caesars Entertainment, Inc., Century Casinos, Inc., Hard Rock International Inc., JACK Entertainment LLC and Penn National Gaming, Inc. In addition, it owns and operates four championship golf courses and 34 acres of undeveloped land adjacent to the Las Vegas Strip.

MGM Growth Properties was the leading real estate investment trust competing with VICI Properties. Just as VICI, and according to MGM's website, it engaged in the acquisition, ownership and leasing of destination entertainment and leisure resorts, with diverse ramifications such as: casino gaming, hotel, convention, entertainment, and retail offerings. MGM Growth Properties had a portfolio of 12 premium resorts in Las Vegas and in other major well-known destinations all over the United States. MGM's holdings accounted for approximately 32,400 hotel rooms, 1.5 million casino square footage, and 3.6 million convention square feet.

Due to the COVID-19 impact many hotels and casino entertainment companies realized how beneficial it would be to shift to a light asset model business. The businesses started looking for REITS with double/triple lease agreements that would offer to buy their properties. The triple net lease agreements are known by giving the tenant or lessee the responsibility over payments related to real estate taxes, building insurance and maintenance. By adopting the latter, the entertainment companies could conduct their businesses without the need of owning a property, the only downside being the payments they would have to make to their landlord, in this case VICI. Taking this strategy into account, many Hotels/Casinos adopted the latter and became asset-light companies, becoming service providers.

More recently MGM Resorts decided to adopt a light-asset model and therefore decided to sell MGM Growth Properties to VICI, making the latter the leader in the gaming, hospitality and entertainment REIT with triple net lease agreements.

One interesting aspect of the whole deal was to understand where VICI was going to obtain this much cash in



order to acquire MGM. VICI had 2 options and decided to use both. The first option was to incur more debt. With a low Debt/Equity of just 0.73, compared to the industry's 3.52, VICI could (and should) issue more debt in order to acquire new properties and further develop and refine its portfolio. Perhaps the company was waiting for an opportunity this disruptive, therefore secured a \$9.3 billion financing commitment from Morgan Stanley, J.P. Morgan and Citibank. The second option was collecting cash by the issuance of new shares, a relatively common strategy as a REIT. On September 9th VICI announced the pricing of an underwritten public offering of 100,000,000 shares of its common stock at a public offering price of \$29.50 per share. The underwriters were also granted a 30-day offer of an additional 15,000,000 shares after the underwriting considerations. By September 14, 65,000,000 of the shares were sold directly to VICI's underwriters at closing and the other 50,000,000 were directly bought by the underwriters according to forward sale agreements, more specifically: Morgan Stanley, Citigroup, J.P. Morgan and Goldman Sachs & Co LLC. In total VICI netted around \$3.39B from the latter proceedings.

Upon the completion of the transaction VICI will be one step

closer to joining the S&P 500. The main requirements to be eligible for the S&P 500 are already fulfilled by the latter and therefore it might happen soon. If so, VICI will be part of various ETF baskets which would only strengthen the company. Nonetheless the future still remains uncertain. The COVID-19 Delta variant keeps causing havoc, impairing VICI's tenants with lockdowns and safety measures, therefore indirectly affecting VICI. Another possible risk factor is how online casinos will affect VICI's clients. Present uncertainties that only the future will tell.

**Sources:** *Yahoo finance, Morningstar, S&P 500, VICI*

## *Initial Public Offering:*

### *ThoughtWorks*

Thoughtworks, a software consultancy company had an Initial public offering on September 15th, the offer was led by Goldman Sachs and JP Morgan. 36.8 million shares were issued by the company at \$21 each. The company's shares rose nearly 40% in their debut on Nasdaq to \$29 with the ticker \$TWKS. The stock price still currently continues to hover around \$29 with a market cap of \$8,980,000,000 (23/09/2021).

Thoughtworks was founded in 1933 in Chicago. The company has 48 offices located in 17 different countries and has about 9,000 workers. Thoughtworks operates in the Software & Tech Services industry, providing consulting services such as software design and delivery (digital transformation), testing, research, digital strategy, re-engineering, data science, security, and prototyping. The firm is one of the leading in this field and has worked with big name companies as their clients in different industries such as energy, health services, financial services, retail and transportation. Some of their clients include Paypal, Walmart, and Porsche to name a few.

The market Thoughtwork operates in is expected to double from \$470 billion in 2020

to \$1 trillion by 2025 according to research from MarketsandMarkets. With this expected rise, the company is expected to benefit exponentially since they provide services that are increasing in demand from other companies. One of the main services in demand is digital enterprise transformation, which is improving scalability and performance of technology by continuously updating, researching, and testing software. This is one of the critical success factors that will be very beneficial to Thoughtworks as the market grows and more and more companies become digital, therefore demanding for these types of services. Mandated stay-at-home orders due to Covid-19 demanded the need for digital transformation in many companies, this factor helped kickstart the change. Since many companies do not have the expertise to keep up and digitally transform effectively, organizations that offer services like Thoughtworks are on the rise and are something to keep an eye on.

**Sources:** *Forbes*, *Reuters*, *InvestmentU*

## Hot Topic

### *Digital Yuan*

With the craze of cryptocurrencies many nations around the world started to look at the advantages and disadvantages digital money has in every aspect of society. Many countries still don't have any regulations, others accept its widespread use and promote its use, and others disapprove of its applications/technology and ban them from their territories. El Salvador, for example, comes off as the first ever country to adopt Bitcoin as a legal tender, making it possible to use Bitcoin to pay services and products on a daily basis, however, on the other side, China was the first to ban Bitcoin and all other cryptocurrencies. The reasons are relatively unknown. The Chinese government stated that their main reasons were to protect its citizens from economic instability, saying Bitcoin and all other cryptocurrencies are extremely volatile based on speculation, therefore banning them would prevent the disruption of economic order and financial stability, as well as avoiding the threat of state monetary sovereignty. Although protecting China's economic growth is a primary concern for the Chinese Communist Party (CCP), analysts believe there's deeper

reasoning covering up the government's true intentions.

Upon the Chinese crackdown over cryptocurrencies, the Chinese government had no more competition against its own coin. Back in 2020, China announced it had begun trials to insert its own state-owned digital coin and recommended other nations to do the same. Several trialing payments were made last year in different cities across China. The primary objective of People's Bank of China (PBOC) will be to have the E-CNY ready by the winter Olympics of 2022. Overall, 2 Billion Yuens have been spent so far, around \$314M. The technology seems to be very effective and operational, nevertheless the subsequent objective will be making it mainstream. Chinese citizens can't really see the main advantages of the Digital Yuan due to lack of education, according to PBOC, and therefore refusing to adopt the new technology.

Unlike Bitcoin, the digital yuan will be a centralized network with blockchain technology, giving the People's Bank of China (PBOC) information about every transaction taking place at every second. The two main objectives of the coin were to compete with other digital currencies such as

bitcoin, stable coins, etc and to reshape China's current payment method providing a cash-like digital payment service, accessible to all with very low or any costs. However, many speculate it has other more dubious intentions. The first would be to compete against the retail payment giants (Alipay and WeChatPay) in an attempt to shift the power the latter hold. The sheer power of the data they collect is the stuff of dreams for any authoritarian government. These retail giants have information about when and where any economic agent buys or sells anything, which backed by the applications of Big Data AI and China's existing surveillance state and social credit score would allow them to, theoretically, control and plan not just the economy, but the entire population. All of these inside of the private tech giants "black boxes", out of reach to the Chinese Government. For example, the Chinese Government has been quite unhappy for a long time with Alibaba's policies and ways of doing business, and on the 6th of April of 2020 announced a \$2,8B fine over the e-commerce giant.

Perhaps, with the cryptocurrency's wide adoption, China saw a chance to take away some of the power the retail giants hold, with the introduction of the digital yuan.

Nonetheless, the main reason would be to monitor transactions, however the PBOC already has access to all the information because it has to be provided by the retail companies, according to the former leader of China's digital currency researcher, Yao Qian. Nevertheless, businesses could still conceal information, use it, or even share to other companies without government approval.

Another intention would be to shift back power to the Chinese banking system considering that to use the Digital Yuan, citizens will not be able to link it with their existing Alipay or WeChatPay account, making it necessary to create a new bank account. According to PBOC, e-CNY will have a two tiered structure in the shape of a pyramid. On top, we will have PBOC, the latter being the one that issues the digital coin. Next up, there will be the Operating Institutions (6 large state-owned banks + 2 internet banks) that will be responsible for creating and opening the wallets to allocate the digital yuan. On tier 2.5, we'll have Other banks and payment service providers such as: Alipay; and at the bottom we find the End user, in this case businesses and consumers that use the digital yuan.

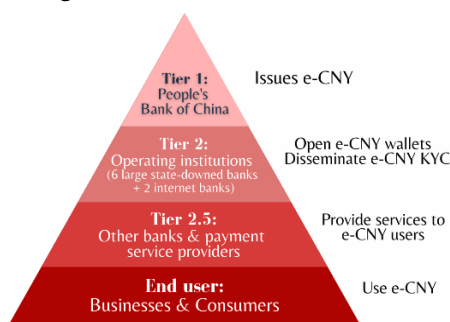
Overall, truth be told, China keeps taking major strides forward in becoming number

one super economy, reshaping what seems to be the inevitable future of the financial and economic world, cashless payment services. If a successful e-CNY roll-out takes place, a new accelerated pace of currency digitalization will happen globally.

Today's idea of money started in China and today it's also China who's waging war financially to control the next evolution of money. Perhaps this is China's attempt to replace US Dollar. China is clearly taking the matter of internationalizing the renminbi into serious effect when it gets rid of the costly trade off of removing capital controls. On the other end the reason countries choose the dollar is because of its stability, transparency and liquidity, not due to major technological uses.

For now we speculate and wait for another one of China's next cryptic moves, which if successful will pave the way for worldwide adoption of digital currencies.

**Sources: Deutsche Bank, Reuters, China Macro Economic, Ledger Insights**



**Source: Deutsche Bank Research**



## Our Team

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