

Apple (AAPL)

Highly Attractive

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## **Apple's iPhone Product Cycle is "Alive and Well" for 2018; Shares Now Back on Track After March Guidance Scare**

With Apple shares hitting all-time highs today and having a significant snap back from the dark lows we witnessed post December results/March guidance, we believe the Street is now starting to fully appreciate the massive iPhone upgrade opportunity on the horizon for FY18 with three new smart phones slated for release. Importantly we estimate Apple has roughly 350 million iPhones that are in the window of opportunity to upgrade over the next 12 to 18 months, now it's about which model and price point "strike a chord" for these customers to ultimately upgrade as the iPhone X demand has softened since reaching a supply/balance level in late December. To this point, we still expect three new iPhone releases (5.8 inch to 6.5 inch OLED designs with an LCD model) staggered over the next 6-9 months to hit the market that will help capture the underlying demand/upgrades among customers that have decided to bypass the 8/8+/X cycle this time around, with price points and features that catalyze fence sitting iPhone customers onto their next smartphone during the course of 2018 with Chinese consumers front and center. With FY18 guidance now hittable/beatable and inventory issues in the rear-view mirror given recent data points out of Asia, it appears Apple shares are now on the yellow brick road to hit the elusive trillion-dollar club (followed by Amazon which we believe will hit this mark in 2019) over the coming months in our opinion. Now all eyes are on the trifecta of a major iPhone product cycle for 2018, a ~\$300 billion buyback potentially on the horizon to be announced in April, and a multiple re-rating that we believe will move shares towards the \$200 range over the coming 3-6 months. While many of the naysayers which threw in the white towel over the last month saying the "Apple growth story is over" are now revisiting their thesis, we believe the risk/reward on shares is compelling and the iPhone upgrade thesis (albeit delayed with softer iPhone X demand) is alive and well in Cupertino with a prove me period clearly ahead for Cook & Co. **We maintain our Highly Attractive rating and \$205 price target.**

- **Catalysts ahead for Cook & Co; China a key focus.** The massive uptick in ASPs (~\$800) that Apple has experienced on the heels of a modestly

successful iPhone X launch, a services business which we forecast is on a trajectory to be a \$50 billion annual revenue stream by FY20, and an unparalleled consumer franchise which now has 1.3 billion active devices worldwide speaks to the clear tailwinds that Cook & Co. has for the foreseeable future in our opinion as it further penetrates its massive installed base. The main swing factor in our opinion is China as we estimate over a 100 million iPhone installed base in this key region, with over half of these consumers due for an upgrade during the course of FY18/1HFY19. In particular, we estimate between 60 million and 70 million Chinese iPhones will be in the “upgrade window” over the next 12 to 18 months with iPhone X/and the next launches as a major potential product catalyst in the all important Chinese market, which could see a renaissance of growth on the horizon for Cupertino. In a nutshell, while this is still a hand holding period on the name, we believe near term demand issues (iPhone X) does not change our long term bullish thesis on Apple and the underlying demand/upgrade drivers for the next 12 to 18 months remain intact with a massive product cycle underway.