

Lam Research (LRCX)

\$235.02 (As of 05/01/20)

Price Target (6-12 Months): **\$268.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/30/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: A

Summary

Lam Research reported weak fiscal third-quarter results due to disruptions in the supply chain due to COVID-19 pandemic. However, the company's equipment demand remained strong in the quarter. Rising adoption of 3D architectures drove the performance of its non-memory segments. Encouragingly, advanced packaging technology inflections remain a tailwind. Also, both etch and deposition technologies are expected to expand the company's addressable market. Lam Research has been benefiting from its transition to new data-enabled economy, wherein DRAM and NAND continue to gain from density growth. Its shares have underperformed the industry it belongs to in the past year. However, uncertainty due to the coronavirus outbreak and the ongoing U.S.-China trade war remain concerns.

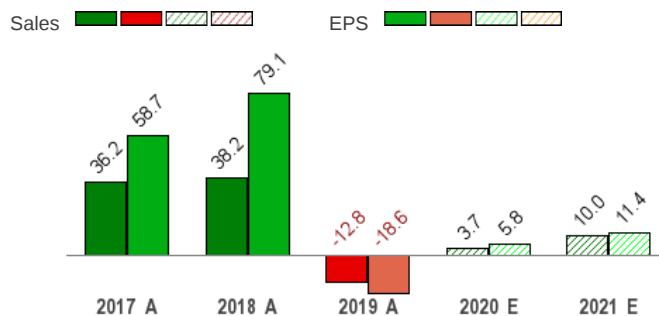
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$344.32 - \$171.04
20 Day Average Volume (sh)	2,141,293
Market Cap	\$34.1 B
YTD Price Change	-19.6%
Beta	1.34
Dividend / Div Yld	\$4.60 / 1.8%
Industry	Semiconductor Equipment - Wafer Fabrication
Zacks Industry Rank	Bottom 36% (161 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-1.0%
Last Sales Surprise	-5.6%
EPS F1 Est- 4 week change	-3.3%
Expected Report Date	07/29/2020
Earnings ESP	0.0%
P/E TTM	15.9
P/E F1	15.3
PEG F1	1.3
P/S TTM	3.6

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,646 E	2,699 E	2,842 E	2,957 E	11,015 E
2020	2,166 A	2,584 A	2,504 A	2,721 E	10,012 E
2019	2,331 A	2,523 A	2,439 A	2,361 A	9,654 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$4.19 E	\$4.16 E	\$4.52 E	\$4.88 E	\$17.14 E
2020	\$3.18 A	\$4.01 A	\$3.98 A	\$4.19 E	\$15.39 E
2019	\$3.36 A	\$3.87 A	\$3.70 A	\$3.62 A	\$14.55 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 05/01/2020. The reports text is as of 05/04/2020.

Overview

Established in 1980 and headquartered in Fremont, CA, Lam Research Corporation supplies wafer fabrication equipment and services to the semiconductor industry. Its products are used by semiconductor manufacturers in front-end and WLP processes, creating memory, microprocessors, and other logic integrated circuits for a broad range of electronic devices.

The MOS process of making integrated circuits involve the deposition of many layers of materials on a semiconductor wafer. Each layer is prepared using a pattern on a photomask, cleaning off the excess material and then exposing to light sources to change the chemical composition of the layer. The final wafer is then planarized, cut into individual die, electrical leads attached and packaged.

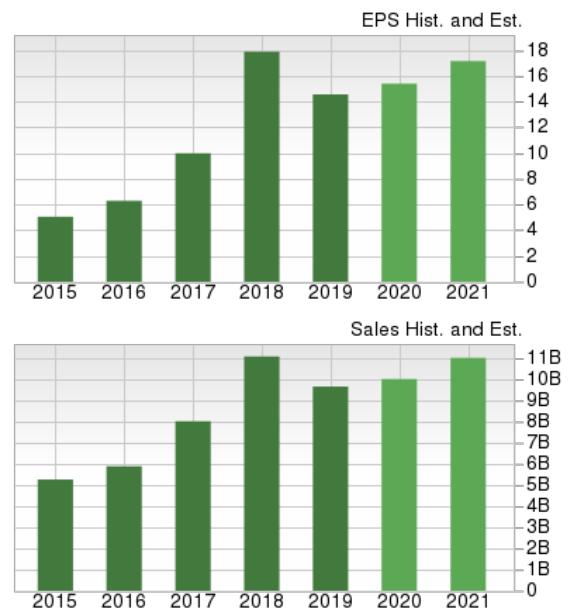
Lam's product offerings in deposition and etch address numerous critical steps in the fabrication process with the goal of reducing defect rates, improving yields, lowering costs and reducing the processing time.

In fiscal 2019, Lam served three market segments—Memory, Foundry and Logic/Integrated device manufacturing which generated 78% (up from 67% in 2018), 14% (down from 27% in 2018) and 8% (up from 6% in 2018), of its revenues, respectively.

The revenue distribution by geography in fiscal 2019 was as follows —Korea 14% (up from 35% in 2018), Taiwan 13% (down from 13% in 2018), Japan 9% (up from 17% in 2018), China 33% (up from 16% in 2018), U.S accounted for 11% (down from 7% in 2018), Europe 5% (down from 5% in 2018) and South East Asia accounted for 7% (up from 7% in 2018).

For fiscal 2019, the customers that accounted for greater than 10% of total revenues include Intel Corporation; Micron Technology, Inc.; Samsung Electronics Company, Ltd.; SK hynix Inc., and Toshiba, Inc.

Being a leading producer of specialized equipment, most of the competition comes from other large equipment makers, such as KLA-Tencor Corporation and Applied Materials, Inc.



Reasons To Buy:

- ▲ Traditionally, Lam Research has high exposure to the memory segment, which is likely to see tremendous growth over the next few years. The strength is driven by cloud computing, big data, mobile devices and IoT. These phenomena have greatly increased the volume of data on information networks that can be stored, processed and analysed to increase efficiency or drive additional sales depending on the circumstances and the business model of companies. Since storage is the starting point of this digital economy, there is a huge demand for memory chips, particularly the more efficient variety.
- ▲ Technological advancements in the areas of multi-patterning, 3D device architecture and advanced packaging technologies are playing to Lam's strengths. Technology transitions help to increase the efficiency of semiconductor manufacturing processes. Since new manufacturing techniques necessitate spending on new equipment, these changes usually lead to increased investment in manufacturing equipment. For the providers of equipment such as Lam, the challenge is to stay abreast of these changes and have the equipment on offer when customers are ready to purchase. Lam's R&D efforts have enabled it to capitalize on these trends, so it should remain a prime beneficiary, particularly since these technological inflections will be more etch and deposition intensive, which are Lam's strong points. Consequently, the company may be able to capture a larger share of total WFE spending over the next few years.
- ▲ Management expects logic and foundry demand to pick up in the second half of the year. There are twin positives in this business with not just the leading edge but also the trailing edge contributing. Management has said that IoT, auto, wearables, low-end phones, and so forth are leading to a resurgence of 28-nanometer demand. At the same time, the company has a huge installed base of more than 35K process modules and a lot of these are being upgraded. While not as strong as 3D NAND, there are technology inflections in this segment too. The transition of the DRAM market to 10nm and FinFET is resulting in a sizeable increase in multi-patterning steps. Lam has the necessary next generation products that can facilitate this transition.
- ▲ Lam Research has a strong balance sheet, with cash and short term investments of approximately \$5.4 billion at the end of fiscal third quarter versus \$4.7 billion in the prior quarter. Additionally, management returned \$163.5 million through dividend. The company regularly repurchases shares to ensure a steady share count after dilution from stock option vesting. The shareholder friendly strategy makes the stock more attractive.

Lam's exposure to memory and opportunity in logic & foundry are positives. Also, etch and deposition portfolio should gain momentum.

Reasons To Sell:

- ▼ The semiconductor equipment industry has historically been very cyclical. It fluctuates highly with respect to timing and length of the cycles. During the down cycle, there could be decreased demand from consumers. The company has a high fixed cost structure, so margins suffer substantially when sales decline. At the same time, it is mandatory for the structure to generate sales to support increases in customer demand. Additionally, Lam Research has to spend a significant amount of money on R&D to maintain its lead in innovation and generate margins that are high enough to continue this expenditure. Lam Research makes significant R&D investments focused on leading-edge deposition, plasma etch, single-wafer clean and other semiconductor manufacturing requirements.
- ▼ On the memory front, there are concerns related to oversupply and overcapacity of memory chips in the upcoming years. Yield and output seems to be improving over time as cutting-edge technologies mature, potentially leading to an oversupply situation in two years time. This could depress prices and curb equipment spending, impacting Lam's growth.
- ▼ The semiconductor capital equipment industry experiences rapid changes and is highly competitive globally. It faces significant competition from the likes of Applied Materials, Hitachi, Tokyo Electron and many more in this space. To compete effectively, considerable financial resources are required to strengthen and augment product and services portfolio as well as maintain customer service and support locations worldwide. Semiconductor manufacturers assess capital equipment suppliers, and the ability to do well in the marketplace depends upon how well the existing products are maintained and enhanced while new ones are launched to meet customer requirements on a timely basis. Also, once a semiconductor manufacturer has selected a particular supplier's equipment and qualified it for production, the manufacturer generally maintains it as long as the supplier's products perform according to specifications at the installed base. So the companies find it difficult to sell to a given customer that has qualified a competitor's equipment. At the same time, the companies have to continue to meet the expectations of their existing customers via the delivery of high-quality and cost-efficient spare parts amid competition from third-party spare parts providers. Lam Research faces significant competition in all its product and service categories.
- ▼ Lam Research derives a major portion of its revenues from outside the U.S. This is natural because a lot of the semiconductor facilities using its manufacturing equipment are located in Asian countries. However, this exposes the company to foreign currency translation impacts and poses a threat to its growth. The company also faces other risks like local legislation, monetary devaluation, exchange control restrictions and unstable political conditions, which may hamper revenue growth and impact its financial position.

The cyclical nature of the semiconductor industry, the high fixed cost structure, weakness in DRAM spending because of the prevalent decline in PCs and product concentration are negatives.

Last Earnings Report

Lam Research Q3 Earnings & Revenues Miss Estimates

Lam Research Corporation reported third-quarter fiscal 2020 non-GAAP earnings of \$3.98 per share, which missed the Zacks Consensus Estimate of \$4.02. Also, the figure decreased 1% sequentially.

Adjusted revenues decreased 3.1% sequentially but increased 2.6% year over year to \$2.50 billion. The reported revenues missed the Zacks Consensus Estimate by 5.6%.

Following the weaker-than-expected fiscal third-quarter results, its share price rose 2.1% in after-hours trading.

Top Line in Detail

China, Korea and Taiwan accounted for 32%, 23% and 21% of the company's total fiscal third-quarter revenues, respectively. On the contrary, Japan, the United States, Europe and Southeast Asia accounted for 10%, 9%, 3% and 2%, respectively.

Operating Details

Non-GAAP gross margin came in at 46.3%, which expanded 60 basis points (bps) sequentially.

Non-GAAP operating expenses were \$486.5 million, reflecting an increase of 3.5% sequentially. As a percentage of sales, both research & development expenses and selling, general & administrative costs decreased.

Adjusted operating margin was 26.9%, down 20 bps sequentially. The increase was primarily due to higher-than-expected expenses.

Balance Sheet & Cash Flow

At the end of the fiscal third quarter, cash and cash equivalents, and short-term investments increased to \$5.6 billion from \$4.9 billion in the fiscal second quarter.

Cash flow from operating activities was \$541.4 million, up from \$307.9 million in the fiscal second quarter. Capital expenditures were \$51.4 million, down from \$62.1 million in the fiscal second quarter.

During the quarter, Lam Research paid dividends of \$163.5 million.

Guidance

The company did not provide any guidance for the June quarter due to risks and uncertainties related to the COVID-19 crisis.

Quarter Ending **03/2020**

Report Date	Apr 22, 2020
Sales Surprise	-5.62%
EPS Surprise	-1.00%
Quarterly EPS	3.98
Annual EPS (TTM)	14.79

Recent News

On March 16, 2020, Lam Research provided business update on account of the coronavirus outbreak. The company has temporarily stopped on-site work at its Fremont and Livermore locations for three weeks effective March 17, 2020.

On Mar 3, 2020, Lam Research unveiled Sense.i platform which is a plasma etch technology and system solution. The company aims to offer unparalleled system intelligence and high-density architecture to the chipmakers with the help of the new platform.

Valuation

Lam Research shares are down 12.7% in the year-to-date period but up 23.5% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 2% and 1.9% in the Zacks Computer & Technology sector in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is up 30.5% and the sector is up 7.4%

The S&P 500 index is down 8.8% in the year-to-date period and 3.3% in the past year.

The stock is currently trading at 14.71X forward 12-month earnings, which compares to 22.56X for the Zacks sub-industry, 23.05X for the Zacks sector and 20.81X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.35X and as low as 7.86X, with a 5-year median of 12.89X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$268 price target reflects 17.1X forward 12-month earnings.

Valuation Multiples - LRCX					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	14.71	22.56	23.05	20.81
	5-Year High	18.35	22.56	23.05	20.81
	5-Year Low	7.86	12.36	16.71	15.19
	5-Year Median	12.89	17.19	19.23	17.44
P/S F12M	Current	3.31	6.21	3.32	3.14
	5-Year High	4.38	6.45	3.59	3.44
	5-Year Low	1.6	3.63	2.32	2.54
	5-Year Median	2.55	4.83	3.09	3.01
EV/EBITDA TTM	Current	12.92	26.19	10.85	10.83
	5-Year High	17.31	30.6	12.84	12.87
	5-Year Low	4.04	9.4	7.56	8.28
	5-Year Median	7.38	19.73	10.61	10.78

As of 04/30/2020

Industry Analysis Zacks Industry Rank: Bottom 36% (161 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Agilent Technologies, Inc. (A)	Neutral	3
Analog Devices, Inc. (ADI)	Neutral	3
Advanced Energy Industries, Inc. (AEIS)	Neutral	4
Applied Materials, Inc. (AMAT)	Neutral	3
ASML Holding N.V. (ASML)	Neutral	3
KLA Corporation (KLAC)	Neutral	4
Lam Research Corporation (LRCX)	Neutral	3
MKS Instruments, Inc. (MKSI)	Neutral	3

Industry Comparison Industry: Semiconductor Equipment - Wafer Fabrication				Industry Peers		
	LRCX	X Industry	S&P 500	AMAT	ASML	MKSI
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	B	-	-	B	F	C
Market Cap	34.12 B	41.34 B	20.61 B	43.06 B	117.15 B	5.05 B
# of Analysts	9	7	14	10	3	5
Dividend Yield	1.96%	1.27%	2.11%	1.79%	0.89%	0.87%
Value Score	B	-	-	B	F	C
Cash/Price	0.14	0.11	0.06	0.08	0.04	0.10
EV/EBITDA	13.28	18.42	11.87	11.99	33.30	16.87
PEG Ratio	1.27	1.30	2.47	1.16	1.68	NA
Price/Book (P/B)	7.52	6.72	2.67	4.97	8.48	2.48
Price/Cash Flow (P/CF)	14.48	16.55	10.66	14.17	35.55	14.62
P/E (F1)	15.27	19.42	19.01	12.54	38.31	18.31
Price/Sales (P/S)	3.55	3.45	2.10	2.87	8.76	2.56
Earnings Yield	6.55%	5.26%	5.05%	7.98%	2.61%	5.46%
Debt/Equity	1.11	0.58	0.72	0.54	0.31	0.43
Cash Flow (\$/share)	17.63	5.81	7.01	3.51	8.11	6.86
Growth Score	C	-	-	C	F	C
Hist. EPS Growth (3-5 yrs)	31.25%	26.99%	10.88%	35.63%	22.72%	33.93%
Proj. EPS Growth (F1/F0)	5.77%	7.04%	-7.32%	22.99%	5.71%	11.15%
Curr. Cash Flow Growth	-25.33%	-30.45%	5.92%	-35.58%	-4.32%	-27.42%
Hist. Cash Flow Growth (3-5 yrs)	23.38%	14.24%	8.55%	13.90%	14.58%	24.72%
Current Ratio	4.47	2.72	1.23	2.36	2.72	4.51
Debt/Capital	52.64%	36.54%	43.84%	35.25%	23.60%	30.11%
Net Margin	21.81%	20.32%	11.08%	18.83%	21.83%	9.99%
Return on Equity	47.82%	28.82%	16.44%	36.15%	21.49%	13.76%
Sales/Assets	0.78	0.72	0.54	0.79	0.55	0.58
Proj. Sales Growth (F1/F0)	3.71%	10.04%	-1.42%	16.37%	0.98%	6.90%
Momentum Score	A	-	-	A	B	D
Daily Price Chg	-8.83%	-7.65%	-2.39%	-8.58%	-5.03%	-7.15%
1 Week Price Chg	-4.43%	-3.59%	-1.74%	-2.74%	-1.29%	-0.41%
4 Week Price Chg	15.74%	16.19%	17.07%	14.89%	16.64%	28.83%
12 Week Price Chg	-21.09%	-21.24%	-18.53%	-21.38%	-6.82%	-11.86%
52 Week Price Chg	23.42%	18.55%	-9.82%	13.68%	40.06%	12.04%
20 Day Average Volume	2,141,293	1,467,079	2,641,413	8,873,357	792,864	388,603
(F1) EPS Est 1 week change	1.97%	0.00%	0.00%	0.00%	0.00%	-0.12%
(F1) EPS Est 4 week change	-3.26%	-4.76%	-6.62%	-4.35%	-5.16%	-14.66%
(F1) EPS Est 12 week change	-8.53%	-12.63%	-13.28%	-0.93%	-16.73%	-17.42%
(Q1) EPS Est Mthly Chg	-9.33%	-7.41%	-11.97%	-5.48%	46.51%	-15.17%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	C
Momentum Score	A
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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