

MKS Instruments (MKS)

\$77.80 (As of 04/02/20)

Price Target (6-12 Months): **\$82.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/04/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: C

Growth: D

Momentum: C

Summary

MKS Instruments is benefiting from the stabilization of revenues in the company's Light & Motion and Vacuum & Analysis segments. Moreover, the improving semiconductor market, as indicated by strong logic and foundry spending, and memory capital expenditure bode well for the company's prospects. MKS Instruments is also benefiting from a lean cost structure. Moreover, the Electro Scientific Industries acquisition strengthened the company's offerings in optics, photonics and laser markets. However, the company's results are affected by headwinds in the advanced market segment, stemming from the United States-China trade war-related tariffs. Moreover, a decline in the equipment and solutions segment is hurting growth prospects. Notably, shares have underperformed the industry in the past year.

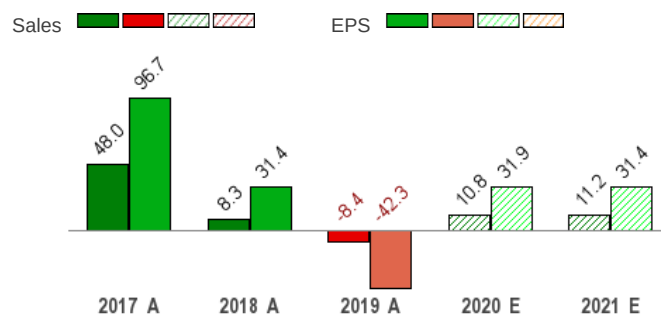
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$122.30 - \$66.87
20 Day Average Volume (sh)	537,789
Market Cap	\$4.3 B
YTD Price Change	-29.3%
Beta	1.46
Dividend / Div Yld	\$0.80 / 1.0%
Industry	Electronics - Manufacturing Machinery
Zacks Industry Rank	Top 24% (61 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	13.2%
Last Sales Surprise	5.9%
EPS F1 Est- 4 week change	-3.2%
Expected Report Date	05/04/2020
Earnings ESP	-7.2%
P/E TTM	17.2
P/E F1	13.1
PEG F1	1.1
P/S TTM	2.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	559 E	596 E	591 E	596 E	2,342 E
2020	515 E	517 E	530 E	544 E	2,106 E
2019	464 A	474 A	462 A	500 A	1,900 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.64 E	\$1.82 E	\$1.89 E	\$1.89 E	\$7.83 E
2020	\$1.30 E	\$1.34 E	\$1.47 E	\$1.58 E	\$5.96 E
2019	\$1.12 A	\$1.09 A	\$1.12 A	\$1.20 A	\$4.52 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 04/02/2020. The reports text is as of 04/03/2020.

Overview

Massachusetts-based MKS Instruments, Inc. is a global provider of instruments, subsystems and process control solutions that measure, monitor, deliver, analyze, power and control critical parameters of advanced manufacturing processes.

MKS solutions are used in pressure measurement and control, flow measurement and control, gas and vapor delivery, gas composition analysis, residual gas analysis, leak detection, control technology, ozone generation and delivery, RF & DC power, reactive gas generation, vacuum technology, lasers, photonics, sub-micron positioning, vibration control, and optics.

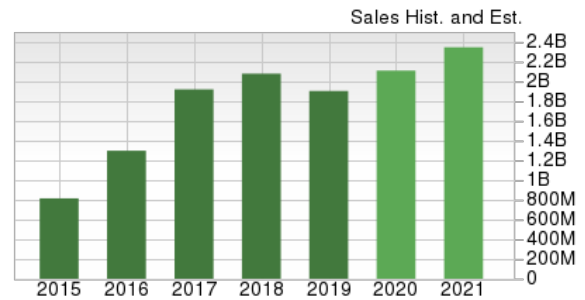
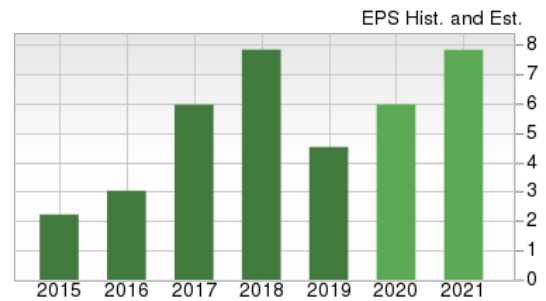
Total revenues in 2019 were \$1.9 billion. The company has six product groups: Analytical and Controls Solutions; Power, Plasma and Reactive Gas Solutions; Vacuum Solutions; Photonics; Optics; and Laser Products.

Since the acquisition of Electro Scientific Industries (ESI) (February 2019), MKS Instruments has been reporting results via three business segments as discussed below:

The Vacuum and Analysis segment (56% of 2019 revenues) provides a wide range of components, instruments, software and subsystems. The Analytical and Controls Solutions, the Power, Plasma and Reactive Gas Solutions and the Vacuum Solutions are included under this segment.

The Light and Motion (35.3% of 2019 revenues) offers several components, instruments and subsystems. The Photonics, Optics and Laser product groups are included under this segment.

Equipment & Solutions segment (8.7% of 2019 revenues) includes a portfolio of industrial laser-based component and micromanufacturing test systems used for processing materials.



Reasons To Buy:

- ▲ MKS Instruments' is expected to gain from solid demand for laser-based solutions for advanced industrial manufacturing, including solar market applications and flexible PCB. The company won a number of orders in this space in China and Korea, which bodes well for top-line growth.
- ▲ MKS Instruments' has solid growth prospects in the semiconductor market due to its exposure to 3D NAND, DRAM and logic- based devices. The company continues to develop innovative solutions for 5-nm logic devices, 3D NAND stacks of 128 layers and beyond and next-generation DRAM structures. Moreover, broad exposure to almost 85% of WFE spending including deposition, etch, lithography, metrology and inspection presents significant growth opportunity over the long term.
- ▲ Moreover, rapid adoption of 5G technology presents significant growth opportunity for MKS Instruments over the next few years. This is due to the fact that implementation of 5G will require upgraded wireless infrastructure and new mobile devices. This will require increased data processing and storage capabilities, which is positive for the company's semiconductor and laser diode testing businesses.
- ▲ The acquisition of Electro Scientific Industries (ESI) expands MKS Instruments' total addressable market by nearly \$2.2 billion. The deal also strengthens its lasers, photonics and optic product portfolio.

Robust semiconductor portfolio, increasing demand for solutions related 5G and the Electro Scientific Industries (ESI) buyout are key catalysts.

Reasons To Sell:

- ▼ Notably, a significant portion of sales now originates from Asia (especially South Korea, Japan, Israel, China and Taiwan) post ESI acquisition. Since, the company conducts businesses in major foreign currencies, unfavorable movement in foreign currency exchange rates often adversely impact sales. Moreover, the uncertainty regarding the resolution of the ongoing U.S.-China trade war doesn't bode well for MKS Instruments.
- ▼ A significant portion of MKS Instruments revenue comes from a handful of customers. Top 10 customers contributed 33% to the company's top line in 2019. Loss of any of these top customers can significantly hurt revenues.
- ▼ The acquisitions of Newport and ESI have negatively impacted the company's balance sheet in the form of high level of goodwill and intangible assets, which totaled \$1.62 billion or almost 47.5% of total assets as of Dec 31, 2019.

Sluggish semiconductor capital equipment spending as well as foreign currency exchange rate volatility are concerns.

Last Earnings Report

MKS Instruments' Q4 Earnings Beat, Revenues Rise Y/Y

MKS Instruments reported fourth-quarter 2019 adjusted earnings of \$1.20 per share, which beat the Zacks Consensus Estimate by 13.2% but slumped 22.1% year over year. The decline was primarily due to lower operating margin.

Revenues of \$499.7 million beat the consensus mark by 5.9% and increased 8.5% year over year, driven by increased demand in the semiconductor market.

Products revenues (85.4% of total revenues) were \$426.5 million, up 6% from the year-ago quarter. Services revenues (14.6%) increased 25.8% year over year to \$73.2 million.

Quarter Ending **12/2019**

Report Date	Jan 28, 2020
Sales Surprise	5.90%
EPS Surprise	13.21%
Quarterly EPS	1.20
Annual EPS (TTM)	4.53

Quarter Details

Revenues from the semiconductor market (54.3% of total revenues) increased 15.7% year over year to \$271.4 million. Sequentially, revenues increased 22%, driven by strong logic and foundry spending as well as the recovery of memory capital expenditure.

Revenues from advanced markets (45.7% of total revenues) were \$228.3 million, up 1% from the year-ago quarter. The slight increase was due to stabilization of the company's light and motion business.

Segment-wise, Vacuum and Analysis (56% of total revenues) revenues were \$279.8 million, up 8.4% year over year, driven by strong volume orders for RF generators.

Light and Motion division revenues (35.3% of total revenues) were \$176.5 million, down 12.8% year over year.

Equipment & Solutions segment revenues (8.7% of total revenues) were \$43.3 million.

Operating Details

In the fourth quarter, MKS Instruments' adjusted gross margin contracted 230 basis points (bps) on a year-over-year basis to 43.3%.

Adjusted EBITDA decreased 12.2% year over year to \$107.9 million. Adjusted EBITDA margin was 21.6%, significantly down from 26.7% reported in the year-ago quarter.

Research & development (R&D) and sales, general & administrative (SG&A) expenses, as a percentage of revenues, expanded 130 bps and 170 bps, respectively.

Management stated that the company has been successful in saving \$13 million on an annual basis and is on track to achieve \$15 million of cost synergies annually.

MKS Instruments reported non-GAAP operating income of \$92.1 million, down 15.7% year over year. Adjusted operating margin was 18.4%, down from 26.7% reported in the year-ago quarter.

Balance Sheet & Cash Flow

As of Dec 31, 2019, MKS Instruments had cash and short-term investments of 524 million compared with \$475 million as of Sep 30, 2019.

Secured term-loan debt outstanding as of Dec 31 was \$892 million.

MKS Instruments paid out dividends worth \$11 million during the reported quarter.

First-Quarter Guidance

For the first quarter of 2020, MKS Instruments anticipates revenues between \$495 million and \$545 million. Management expects strong semiconductor capital spending to continue. Moreover, advanced market is expected to witness stable revenues and a modest increase in equipment solution revenues.

Non-GAAP gross margin is expected between 43% and 45%.

Non-GAAP operating expenses are expected in the \$128-\$136 million range. R&D expenses are expected between \$43 million and \$46 million, while SG&A expenses are anticipated in the \$85-\$90 million range.

Non-GAAP earnings are expected between \$1.14 and \$1.49 per share.

Recent News

On Feb 11, 2020, MKS Instruments announced a quarterly cash dividend of 20 cents per share. The dividend was paid out on Mar 6 to shareholders of record as of Feb 24, 2020.

Valuation

MKS Instruments shares are down 29.3% in the year-to-date period and 21.1% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are down 26.9% and 14.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are down 7.5% and 4.9%, respectively.

The S&P 500 index is down 23.2% in the year-to-date period and 14.1% in the past year.

The stock is currently trading at 11.73X forward 12-month earnings, which compares to 14.92X for the Zacks sub-industry, 18.94X for the Zacks sector and 15.37X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.58X and as low as 7.14X, with a 5-year median of 15.29X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$82 price target reflects 12.37X forward 12-month earnings.

The table below shows summary valuation data for MKSI

Valuation Multiples - MKSI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	11.73	14.92	18.94	15.37
	5-Year High	25.58	23.12	22.02	19.34
	5-Year Low	7.14	10.44	16.85	15.18
	5-Year Median	15.29	18.43	19.3	17.44
P/S F12M	Current	1.92	1.87	2.97	2.7
	5-Year High	3.26	2.57	3.59	3.43
	5-Year Low	1.46	1.45	2.3	2.54
	5-Year Median	2.27	2.05	3.05	3
EV/EBITDA TTM	Current	10.15	11.29	9.95	9.15
	5-Year High	16.89	16.71	12.84	12.88
	5-Year Low	4.32	5.51	7.59	8.27
	5-Year Median	10.46	10.56	10.61	10.78

As of 04/02/2020

Industry Analysis Zacks Industry Rank: Top 24% (61 out of 254)



Top Peers

Advanced Energy Industries, Inc. (AEIS)	Outperform
Coherent, Inc. (COHR)	Outperform
Applied Materials, Inc. (AMAT)	Neutral
AMETEK, Inc. (AME)	Neutral
Entegris, Inc. (ENTG)	Neutral
KLA Corporation (KLAC)	Neutral
Lam Research Corporation (LRCX)	Neutral
Teradyne, Inc. (TER)	Neutral

Industry Comparison Industry: Electronics - Manufacturing Machinery				Industry Peers		
	MKSI Neutral	X Industry	S&P 500	AEIS Outperform	AME Neutral	COHR Outperform
VGM Score	D	-	-	B	C	C
Market Cap	4.27 B	952.37 M	17.16 B	1.73 B	16.29 B	2.33 B
# of Analysts	5	3	13	5	9	3
Dividend Yield	1.03%	0.00%	2.5%	0.00%	1.01%	0.00%
Value Score	C	-	-	B	F	C
Cash/Price	0.12	0.26	0.06	0.18	0.02	0.14
EV/EBITDA	13.32	12.43	10.80	19.25	13.05	11.89
PEG Ratio	1.06	7.40	1.74	NA	2.79	NA
Price/Book (P/B)	2.10	1.24	2.33	2.56	3.18	1.79
Price/Cash Flow (P/CF)	11.35	13.90	9.11	15.13	13.58	9.66
P/E (F1)	12.76	14.75	14.73	13.49	18.11	22.14
Price/Sales (P/S)	2.25	1.34	1.81	2.20	3.16	1.71
Earnings Yield	7.66%	6.58%	6.71%	7.42%	5.53%	4.52%
Debt/Equity	0.43	0.19	0.70	0.61	0.44	0.30
Cash Flow (\$/share)	6.86	1.50	7.01	2.98	5.23	10.00
Growth Score	D	-	-	C	A	D
Hist. EPS Growth (3-5 yrs)	33.93%	31.25%	10.92%	14.90%	11.36%	25.03%
Proj. EPS Growth (F1/F0)	31.95%	115.43%	1.02%	37.21%	-6.31%	-26.24%
Curr. Cash Flow Growth	-27.42%	-11.44%	5.93%	-35.66%	23.89%	-46.32%
Hist. Cash Flow Growth (3-5 yrs)	24.72%	21.58%	8.55%	8.19%	10.17%	18.56%
Current Ratio	4.51	3.53	1.24	2.71	1.42	4.38
Debt/Capital	30.11%	15.87%	42.33%	37.83%	30.75%	23.27%
Net Margin	7.39%	4.16%	11.67%	8.23%	16.70%	1.76%
Return on Equity	12.67%	5.27%	16.70%	13.49%	20.14%	6.46%
Sales/Assets	0.56	0.56	0.54	0.65	0.56	0.63
Proj. Sales Growth (F1/F0)	10.85%	10.96%	1.54%	65.88%	-6.31%	-5.20%
Momentum Score	C	-	-	B	C	A
Daily Price Chg	0.83%	0.00%	1.45%	2.27%	1.83%	-3.10%
1 Week Price Chg	6.98%	20.13%	12.29%	39.43%	12.06%	14.80%
4 Week Price Chg	-21.74%	-25.02%	-21.33%	-26.89%	-20.19%	-26.08%
12 Week Price Chg	-29.34%	-33.37%	-28.56%	-36.85%	-29.86%	-43.95%
52 Week Price Chg	-20.72%	-22.62%	-22.55%	-14.54%	-15.38%	-37.42%
20 Day Average Volume	537,789	348,415	4,257,668	377,556	2,764,363	285,279
(F1) EPS Est 1 week change	-3.24%	0.00%	-0.04%	0.00%	-1.62%	0.00%
(F1) EPS Est 4 week change	-3.24%	-4.11%	-4.30%	0.00%	-9.20%	0.00%
(F1) EPS Est 12 week change	-2.36%	-5.74%	-5.47%	1.70%	-11.08%	3.33%
(Q1) EPS Est Mthly Chg	-8.84%	0.00%	-5.91%	0.00%	-25.98%	0.00%

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	C
Growth Score	D
Momentum Score	C
VGM Score	D

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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