

MKS Instruments (MKS)

\$105.79 (As of 06/15/20)

Price Target (6-12 Months): **\$111.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/04/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:B

Value: C

Growth: B

Momentum: C

Summary

MKS Instruments gains traction from stable Vacuum & Analysis and Equipment & Solutions segment revenues. Moreover, the improving semiconductor market bodes well for the company's prospects. MKS Instruments is also benefiting from a lean cost structure. Additionally, the Electro Scientific Industries acquisition strengthened the company's offerings in optics, photonics and laser markets. However, the advanced market segment revenues are expected to be negatively impacted by university and research lab closures due to the coronavirus. Management stated that order rates remain strong in the second quarter. Nonetheless, lockdowns around the world due to the pandemic are expected to hurt the top line in the period. Notably, shares have underperformed the industry on a year-to-date basis.

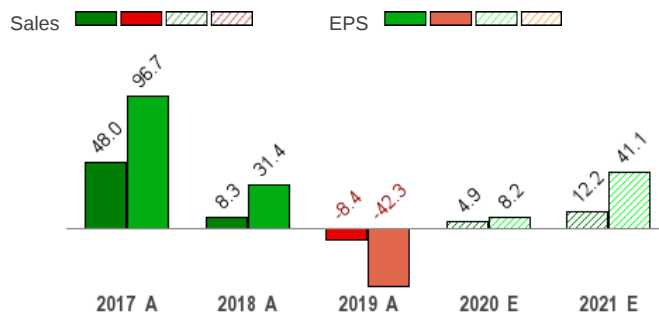
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$122.30 - \$66.87
20 Day Average Volume (sh)	310,592
Market Cap	\$5.8 B
YTD Price Change	-3.8%
Beta	1.49
Dividend / Div Yld	\$0.80 / 0.8%
Industry	Electronics - Manufacturing Machinery
Zacks Industry Rank	Top 38% (95 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	24.2%
Last Sales Surprise	4.8%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	08/04/2020
Earnings ESP	0.0%
P/E TTM	21.4
P/E F1	21.6
PEG F1	1.8
P/S TTM	3.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	524 E	560 E	571 E	582 E	2,238 E
2020	536 A	489 E	485 E	484 E	1,994 E
2019	464 A	474 A	462 A	500 A	1,900 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.46 E	\$1.71 E	\$1.84 E	\$1.89 E	\$6.90 E
2020	\$1.54 A	\$1.16 E	\$1.20 E	\$1.21 E	\$4.89 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 06/15/2020. The reports text is as of 06/16/2020.

Overview

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.

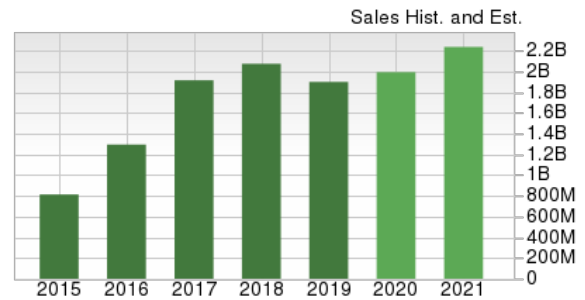
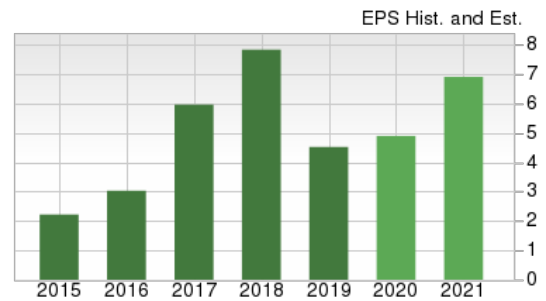
Total revenues in 2019 were \$1.9 billion. The Massachusetts-based company has six product groups: Analytical and Controls Solutions; Power, Plasma and Reactive Gas Solutions; Vacuum Solutions; Photonics; Optics; and Laser Products.

Since the acquisition of Electro Scientific Industries (ESI) in 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' has witnessed strong demand for its solutions that are being used to fight coronavirus. The company's valves and pressure measurement solutions are currently used in the sterilization of personal protective equipment. While its optical filters are deployed in diagnostic systems for coronavirus, gradings are incorporated in blood analyzers. The company gains from solid demand for laser-based solutions for advanced industrial manufacturing, including solar market applications and flexible PCB. The company anticipates revenues from advanced markets to remain stable in the second quarter.
- ▲ MKS Instruments' has solid growth prospects in the semiconductor market due to increasing demand for advanced memory and logic chips. Moreover, strong demand for power solutions has been a major growth driver in the semiconductor end-market. Adoption of Ozone Solutions for Atomic Layer Deposition, which serves both logic and memory manufacturing, bodes well for MKS Instruments. The company continues to see strong order rates in the second quarter. 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. Moreover, the company reached its previously announced annualized cost synergies target of \$15 million within 14 months of the acquisition, well ahead of its original estimation of 18-36 months post acquisition.
- ▲ MKS Instruments' liquidity position is strong. As of Mar 31, 2020, the company had cash and short-term investments worth \$503 million. In comparison, secured term-loan as of the March quarter-end was \$840 million. However, schedule term loan payments for the next 12 months are only \$9 million. Moreover, total debt to total capital was 28.9% as of Mar 31, 2020, better than the industry average of 33.9%. Further, times interest earned were 6.5X as of Mar 31, 2020, higher than the industry's 5.8X. The company also had \$100 million of incremental borrowing capacity under an asset-based line of credit, subject to certain borrowing-based requirements. Its strong cash position is expected to support dividend payouts in the near term.

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

Reasons To Sell:

- ▼ MKS Instruments generates a significant portion of sales from Asia (especially South Korea, Japan, Israel, China and Taiwan) post ESI acquisition. Hence, the uncertainty regarding the final resolution of the ongoing U.S.-China trade war doesn't bode well for the company. Moreover, coronavirus outbreak in MKS Instruments' top five operating markets (United States, South Korea, China, Japan and Germany) is expected to hurt top-line in near term.
- ▼ Moreover, coronavirus outbreak negatively impacted MKS Instrument's research end-market. As university and research laboratories globally remain closed due to lockdowns and physical distancing, demand for instruments sees a sudden collapse. This along with supply-chain issues in the semiconductor space is expected to hurt MKS Instruments' top-line growth at least in the near term.
- ▼ Since, the company conducts businesses in major foreign currencies, unfavorable movement in foreign currency exchange rates often adversely impact sales. The company generated more than 56% of first-quarter revenues from markets outside the United States.
- ▼ 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 \$1.60 billion or almost 46.2% of total assets as of Mar 31, 2020.

Adverse impact of Coronavirus, forex volatility, customer concentration and higher level of goodwill in balance sheet are major concerns.

Last Earnings Report

MKS Instruments' Q1 Earnings Top, Revenues Rise Y/Y

MKS Instruments reported first-quarter 2020 adjusted earnings of \$1.54 per share, which beat the Zacks Consensus Estimate by 24.2% and also increased 28.3% year over year.

Revenues of \$535.7 million surpassed the consensus mark by 4.8% and also improved 15.6% year over year, driven by buoyant demand for the semiconductor market.

Products revenues (86.1% of total revenues) were \$461.2 million, up 8.1% from the year-ago quarter. Services revenues (13.9%) inched up 1.8% year over year to \$74.5 million.

Quarter Ending 03/2020

Report Date	Apr 28, 2020
Sales Surprise	4.76%
EPS Surprise	24.19%
Quarterly EPS	1.54
Annual EPS (TTM)	4.95

Quarterly Update

Revenues from the semiconductor market (58.4% of total revenues) jumped 41.9% year over year to \$312.6 million owing to increased demand.

Revenues from advanced markets (41.6% of total revenues) were \$223.1 million, down 8.3% from the year-ago quarter. The top line was negatively impacted by university and research lab closures due to the coronavirus (COVID-19).

Segmentwise, Vacuum and Analysis (59.6% of total revenues) revenues surged 36.2% year over year to \$319.3 million.

Equipment & Solutions segment revenues (9.5% of total revenues) were \$51 million, up 44.9% year over year.

Light and Motion division revenues (30.9% of total revenues), however, decreased 14.7% year over year to \$165.4 million.

Operating Details

In the first quarter, MKS Instruments' adjusted gross margin contracted 190 basis points (bps) on a year-over-year basis to 44.7%.

Adjusted EBITDA increased 20.2% year over year to \$129.7 million. Adjusted EBITDA margin expanded 90 bps on a year-over-year basis to 24.2%.

Research & development and sales, general & administrative expenses, as a percentage of revenues, declined 110 bps and 150 bps on a year-to-date basis, respectively.

MKS Instruments reported non-GAAP operating income of \$110 million, up 19.4% year over year. Adjusted operating margin expanded 70 bps on a year-over-year basis to 20.5%.

Balance Sheet & Cash Flow

As of Mar 31, 2020, MKS Instruments had cash and short-term investments of \$503 million compared with \$524 million as of Dec 31, 2019.

Secured term-loan principal outstanding as of Mar 31, 2020 was \$840 million. The company also had \$100 million of incremental borrowing capacity under an asset-based line of credit, subject to certain borrowing base requirements.

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

Q2 Guidance

For the second quarter of 2020, MKS Instruments anticipates revenues between \$450 million and \$520 million. Management stated that order rates will remain strong in the second quarter. However, lockdowns around the world due to the coronavirus are expected to impact second-quarter revenues.

Non-GAAP earnings are expected between 90 cents and \$1.38 per share.

Recent News

On May 14, 2020, MKS Instruments announced a quarterly cash dividend of 20 cents per share. The dividend will be paid on Jun 5 to shareholders of record as of May 25, 2020.

Valuation

MKS Instruments shares are down 3.9% in the year-to-date period but up 47.3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are up 1.5% and 7%, in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are up 41.2% and 22.7%, respectively.

The S&P 500 index is down 4.8% in the year-to-date period but up 6.2% in the past year.

The stock is currently trading at 18.2X forward 12-month earnings, which compares to 22.61X for the Zacks sub-industry, 24.56X for the Zacks sector and 21.92X 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 15.27X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$111 price target reflects 19.11X 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	18.2	22.61	24.56	21.92
	5-Year High	25.58	23.12	24.56	22.11
	5-Year Low	7.14	10.44	16.72	15.23
	5-Year Median	15.27	18.56	19.28	17.49
P/S F12M	Current	2.76	2.61	3.73	3.41
	5-Year High	3.26	2.64	3.73	3.44
	5-Year Low	1.46	1.45	2.32	2.53
	5-Year Median	2.28	2.09	3.11	3.02
EV/EBITDA TTM	Current	12.67	14.68	12.09	11.25
	5-Year High	16.89	16.71	12.72	12.85
	5-Year Low	4.32	5.51	7.57	8.25
	5-Year Median	10.67	10.63	10.75	10.82

As of 06/15/2020

Industry Analysis Zacks Industry Rank: Top 38% (95 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Advanced Energy Industries, Inc. (AEIS)	Neutral	3
Applied Materials, Inc. (AMAT)	Neutral	3
AMETEK, Inc. (AME)	Neutral	3
Coherent, Inc. (COHR)	Neutral	5
Entegris, Inc. (ENTG)	Neutral	4
KLA Corporation (KLAC)	Neutral	3
Lam Research Corporation (LRCX)	Neutral	3
Teradyne, Inc. (TER)	Neutral	3

Industry Comparison Industry: Electronics - Manufacturing Machinery				Industry Peers		
	MKSI	X Industry	S&P 500	AEIS	AME	COHR
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	2	-	-	3	3	5
VGM Score	B	-	-	B	B	D
Market Cap	5.81 B	1.15 B	21.70 B	2.49 B	20.25 B	3.50 B
# of Analysts	5	3	14	5	8	3
Dividend Yield	0.76%	0.00%	1.95%	0.00%	0.82%	0.00%
Value Score	C	-	-	C	C	D
Cash/Price	0.09	0.25	0.06	0.14	0.06	0.11
EV/EBITDA	17.69	17.37	12.55	27.26	15.62	17.52
PEG Ratio	1.80	1.84	2.96	NA	3.57	NA
Price/Book (P/B)	2.83	1.85	2.99	3.64	3.80	3.99
Price/Cash Flow (P/CF)	15.43	26.26	11.61	21.78	16.87	14.41
P/E (F1)	21.63	28.49	21.21	23.47	24.99	57.27
Price/Sales (P/S)	2.95	1.91	2.26	2.58	3.99	2.71
Earnings Yield	4.62%	3.31%	4.43%	4.26%	4.00%	1.75%
Debt/Equity	0.40	0.29	0.76	0.60	0.51	0.44
Cash Flow (\$/share)	6.86	1.43	7.01	2.98	5.23	10.00
Growth Score	B	-	-	B	A	C
Hist. EPS Growth (3-5 yrs)	30.00%	25.70%	10.87%	11.18%	13.12%	12.84%
Proj. EPS Growth (F1/F0)	8.27%	28.45%	-10.58%	13.52%	-15.69%	-57.49%
Curr. Cash Flow Growth	-27.42%	-17.54%	5.46%	-35.66%	23.89%	-46.32%
Hist. Cash Flow Growth (3-5 yrs)	24.72%	18.65%	8.55%	8.19%	10.17%	18.56%
Current Ratio	4.53	3.80	1.29	2.84	1.88	4.28
Debt/Capital	28.56%	22.21%	45.06%	37.55%	33.98%	30.41%
Net Margin	9.99%	4.07%	10.54%	7.02%	18.48%	-32.25%
Return on Equity	13.64%	5.41%	16.08%	15.06%	18.77%	4.99%
Sales/Assets	0.58	0.57	0.55	0.70	0.52	0.63
Proj. Sales Growth (F1/F0)	4.96%	4.13%	-2.59%	55.24%	-14.41%	-15.41%
Momentum Score	C	-	-	C	C	F
Daily Price Chg	1.72%	1.12%	0.98%	0.82%	0.71%	2.02%
1 Week Price Chg	-8.81%	-6.54%	-7.25%	-11.68%	-9.62%	-9.57%
4 Week Price Chg	8.68%	8.34%	5.45%	5.61%	6.00%	3.13%
12 Week Price Chg	44.11%	54.67%	39.81%	68.35%	51.66%	53.85%
52 Week Price Chg	47.22%	17.82%	-4.47%	27.85%	4.54%	19.79%
20 Day Average Volume	310,592	284,415	2,587,370	282,424	1,232,911	162,977
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.00%	-0.52%	-59.92%
(F1) EPS Est 12 week change	-20.60%	-23.34%	-15.39%	-18.57%	-16.99%	-59.92%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.00%	-116.51%

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	C
Growth Score	B
Momentum Score	C
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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