

NETGEAR, Inc. (NTGR)

\$31.79 (As of 07/23/20)

Price Target (6-12 Months): **\$33.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/06/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: C

Growth: B

Momentum: C

Summary

NETGEAR delivered impressive second-quarter 2020 results, with the top and the bottom line surpassing the respective Zacks Consensus Estimate. With a market share of nearly 49% in both U.S. retail Wi-Fi products and switch markets, the company is well poised to benefit from robust networking solutions. It maintains a competitive edge with new product launches, based on Wi-Fi 6 standards and aims to leverage latest technological innovations to boost growth. With an accretive subscriber base, NETGEAR caters to the networking demands for small and medium-sized enterprises. However, it faces headwinds in APAC region due to lower product sales. It operates in a highly-competitive and dynamic environment. Due to COVID-19 uncertainties, NETGEAR withdrew its prior guidance for 2020 and has not provided any definitive outlook for the third quarter.

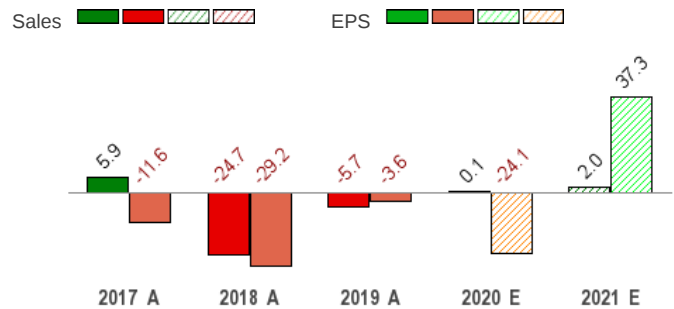
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$36.87 - \$15.01
20 Day Average Volume (sh)	452,411
Market Cap	\$935.2 M
YTD Price Change	29.7%
Beta	1.08
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Computer - Networking
Zacks Industry Rank	Top 37% (92 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	134.8%
Last Sales Surprise	16.9%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	10/28/2020
Earnings ESP	9.9%
P/E TTM	18.3
P/E F1	22.4
PEG F1	NA
P/S TTM	0.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	241 E	233 E	260 E	286 E	1,020 E
2020	230 A	280 A	256 E	275 E	1,000 E
2019	249 A	231 A	266 A	253 A	999 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.40 E	\$0.32 E	\$0.55 E	\$0.66 E	\$1.95 E
2020	\$0.21 A	\$0.54 A	\$0.47 E	\$0.56 E	\$1.42 E
2019	\$0.60 A	\$0.28 A	\$0.65 A	\$0.34 A	\$1.87 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 07/23/2020. The reports text is as of 07/24/2020.

Overview

Incorporated in January 1996 and headquartered in San Jose, CA, NETGEAR, Inc. is a global telecommunications firm that offers innovative networking and Internet connected products for seamless networking, broadband access and network connectivity. The company's products are built on variety of proven technologies such as wireless (Wi-Fi and LTE), Ethernet and powerline, with a focus on reliability and ease-of-use. These products are available in multiple configurations to address the evolving needs of customers in each geographic region where it operates. Leveraging its technological expertise, high volume manufacturing and engineering infrastructure, NETGEAR designs its products and services to meet the specific needs of consumer, business and service provider markets. The company customizes various elements of the software interface and product design, including component specification, physical characteristics such as casing, design and coloration to meet the individual needs of its clients.

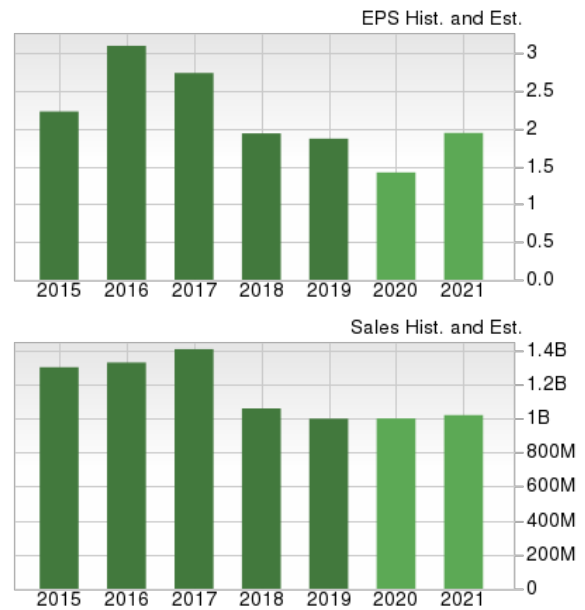
On Dec 31, 2018, NETGEAR completed the spin-off of the Arlo business through a distribution of 62,500,000 shares of Arlo Technologies stock to NETGEAR's shareholders. Prior to that, the company owned approximately 84.2% of Arlo's stock. Following the completion, the company no longer owns any shares of Arlo.

NETGEAR currently operates and reports under two segments: Connected Home, and Small and Medium Business (SMB).

Connected Home (accounting for 82.1% of net revenues in second-quarter 2020): Generating the lion's share of revenues, this segment offers high-performance, dependable and easy-to-use LTE and WiFi Internet networking solutions for consumers.

SMB (17.9%): Focused on small and medium-sized businesses, this segment comprises affordable business networking, storage and security solutions for enterprise-class functionality for small and medium-sized businesses.

The company conducts business across three geographic regions: Americas, Europe, Middle-East and Africa (EMEA) and Asia Pacific (APAC).



Reasons To Buy:

- ▲ NETGEAR continues to capitalize on technology inflections, create new categories and build recurring service revenues to maintain its market leadership position and drive future growth. The company's revenues have been driven by the rapid increase in Internet connected devices such as smart phones, laptops, tablets and the advent of Smart Home and Internet of Things devices, which have boosted the need for robust networking solutions. An increased market demand for Smart Home and Internet-connected products such as Smart TVs, game consoles, HD streaming players, security cameras, thermostats and smoke detectors continues to drive innovations in networking. NETGEAR continues to focus on introducing products into growth areas which form the basis of Smart Homes as it strives to be the provider of industry-leading networking and smart connected products for consumers, business and service provider markets.
 - ▲ NETGEAR intends to maintain a competitive edge with new product launches, which hinge on affordability, reliability and ease of use, for consumer, business and service provider markets.
 - ▲ NETGEAR is confident to retain a competitive edge in new product introductions, based on the Wi-Fi 6 standards. In the last reported quarter, the company generated net revenues of \$280.1 million, up 21.3% from the prior-year quarter's figure. The year-over-year improvement was primarily driven by solid demand for CHP products in the wake of growing work-from-trend due to the COVID-19 pandemic. The company is excited to be part of AT&T's commitment to be the first to introduce mobile 5G services in the United States, and intends to launch more 5G related products in 2020. Its adjusted operating margin was 7.5% compared with 4.4% in the year-ago quarter driven by higher operating income. Furthermore, it has released Meural Canvas II. Notably, Meural is the world's leading smart digital canvas. NETGEAR also announced an exciting new Meural content partnership with National Geographic.
 - ▲ With an exponential growth in data traffic, consumers, businesses and service providers need a complete set of wired and wireless networking and broadband products that are tailored to their specific needs and budgets. The company's products are designed with an industrial appearance, including metal cases, the ability to mount the product within standard data networking racks as well as unique mounting solutions for other uses and targeting the business market. These products typically include higher port counts, higher data transfer rates and other performance characteristics designed to meet the needs of a business user, providing a competitive edge to outsmart its rivals. Notably, the number of registered app users recorded in second-quarter 2020 was 6.4 million, up from 5.1 million on a sequential basis. The company ended the quarter with 293,000 paid subscribers.
 - ▲ The company continues to introduce new products and services that hinge on affordability, reliability and ease of use. In order to capitalize on the increasing demand for cloud-based applications for small and medium-sized enterprises, NETGEAR is introducing next generation commercial products. These include PoE switches, Multi-gigabit Ethernet switches, high capacity local and remote unified storage, small to medium capacity campus wireless LAN, and security appliances. These products are likely to augment the effectiveness and efficiency of its hybrid cloud access network and strengthen its position in the market. In the last reported quarter, NETGEAR shipped nearly 3.7 million units, including 2.7 million nodes of wireless products. Although the consensus estimate has remained unchanged at \$1.95 for fiscal 2021, the same has inched up 1.4% for fiscal 2020 in the past 60 days. This reflects on bullish sentiments for the stock.
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Reasons To Sell:

- ▼ NETGEAR's business continues to be affected by geopolitical and economic conditions, and changes in the overall demand for networking and smart home product. The company's operating results are likely to be impacted by introduction of new products by competitors, slow growth in the networking product, personal computer and Internet infrastructure. A seasonal shift in end market demand for products, particularly in Connected Home business segment, is expected to impair growth. Moreover, the outbreak of coronavirus in China, an important region for its supply chain and end market sales, as well as in other countries doesn't bode well for near-term growth.
- ▼ Although NETGEAR witnessed robust developments in the Americas and EMEA regions owing to solid demand for CHP products, the company is facing headwinds in APAC that is likely to negatively impact its revenues. In second-quarter 2020, APAC revenues came in at \$29.4 million, down 3.7% year over year, due to lower sales in the region. Moreover, the company's decision to split into two independent companies involves a fair amount of risk, which may lead to decline in the top line, earnings dilution and lower cash flow in the long term. The company has incurred high costs related to the separation of the Arlo business.
- ▼ The company functions in a rapidly evolving and fiercely competitive market and expects competition to intensify on price. Furthermore, it depends on a limited number of third-party manufacturers for substantially all of its manufacturing needs, primarily based in low-cost countries like China and Vietnam. With potential trade restrictions on China, NETGEAR is likely to lose its cost advantage and products can become pricier. The company's business is highly seasonal. It experiences increased sales in the third and fourth fiscal quarters primarily due to seasonal demand from consumer markets relating to the beginning of the school year and holiday season. This leads to volatility in cash flow and reduces the predictability of earnings.
- ▼ NETGEAR operates in a highly competitive and dynamic environment. Hence, its future success depends on its ability to develop new products that have broad market acceptance. In order to differentiate its products, the company has to continually invest in research and development activities, which strain its margins. In addition, high technological obsolescence of its product portfolio has led to lower return on capital. In the last reported quarter, SMB segment generated net revenues \$50 million, down 21% year over year due to reduced demand triggered by the virus outbreak. However, Connected Home segment generated net revenues of \$230 million, up 37.3% year over year owing to robust product demand in retail and service provider channels.
- ▼ Due to the COVID-19 pandemic, NETGEAR has not given any definitive financial guidance for the third quarter of 2020 and full-year 2020. With a significant shift in its business operations, the company predicts supply-chain disruptions due to the ongoing pandemic situation. Channel inventory is anticipated to decline in the future as the company is witnessing a change in demand from retail to online platforms. Markedly, NETGEAR anticipates that its CHP business is likely to get hampered with the growing uncertainties pertaining to the COVID-19 pandemic. The company's most profitable business segment, SMB, might also face financial difficulties in the near term if the ongoing situation does not get stabilized.
- ▼ As of Jun 28, 2020, the company had \$252.6 million in cash and equivalents with \$270.9 million of total current liabilities compared with respective tallies of \$210 million and \$234 million in the previous quarter. Although the company has favorable cash and cash equivalents with reduced long-term debt, NETGEAR's dividend payout rate has reduced sequentially compared with 47.8% of the sub-industry. The rate has declined in the past few quarters, which indicates that the company is sharing less of its earnings with stockholders. It has a favorable debt-to-capital ratio of 0.04 compared with 0.29 of the sub-industry coupled with conducive cash ratio. As stated earlier, the company has withdrawn its previous guidance for 2020 and it remains to be seen how NETGEAR handles its business operations in the near future amid disruptions caused by COVID-19 pandemic.

NETGEAR's business is highly seasonal and causes volatility in cash flow. The company operates in a dynamic environment that further strains its margins. It has withdrawn its prior guidance for 2020 due to COVID-19 crisis.

Last Earnings Report

NETGEAR Q2 Earnings Beat Estimates, Revenues Up Y/Y

NETGEAR delivered impressive second-quarter 2020 results, with the top and the bottom line surpassing the respective Zacks Consensus Estimate. Further, earnings and revenues increased significantly on a year-over-year basis despite coronavirus-induced turmoil.

Net Income

GAAP earnings from continuing operations in the reported quarter were \$6 million or 20 cents per share compared with \$0.8 million or 3 cents per share in the year-ago quarter. The year-over-year improvement was primarily driven by higher revenues. Non-GAAP net income from continuing operations was \$16.3 million or 54 cents per share compared with \$8.9 million or 28 cents per share in the year-earlier quarter. The bottom line beat the Zacks Consensus Estimate by 31 cents.

Revenues

NETGEAR generated net revenues of \$280.1 million, up 21.3% year over year driven by solid demand for CHP products in the wake of growing work-from-trend due to the COVID-19 pandemic. The top line surpassed the consensus estimate of \$240 million. The company shipped nearly 3.7 million units, including 2.7 million nodes of wireless products in the second quarter of 2020.

Region wise, net revenues from the Americas were \$202.2 million (72.2% of net revenues), up 28.7% year over year. EMEA (Europe, Middle East and Africa) revenues were \$48.4 million (17.3%), up 12.2% year over year. Significant growth in both the regions can be attributed to higher demand of CHP products in retail and service provider channels. However, APAC (Asia Pacific Region) revenues fell 3.7% to \$29.4 million (10.5%) due to lower sales in the region. The number of registered app users in the quarter was 6.4 million. NETGEAR ended the quarter with 293,000 paid subscribers. The company tapped new service subscribers with considerable growth in parental control and cybersecurity protection services.

Segmental Performance

Connected Home, which includes Nighthawk, Orbi, Nighthawk Pro Gaming and Meural brands, generated net revenues of \$230 million, up 37.3% year over year owing to robust product demand in retail and service provider channels. Markedly, NETGEAR continues to hold about 49% market share in U.S. retail WiFi products, which include mesh, routers, gateways and extenders.

Net revenues from **SMB** declined 21% year over year to \$50 million due to reduced demand stemming from the virus outbreak. However, on the product front, ProAV switching and PoE Plus lines performed well in the market. Markedly, the company continues to hold about 49% market share in U.S. retail switch market.

Other Details

Adjusted gross margin increased to 29.6% from 28.8% due to higher revenues. Non-GAAP operating margin was 7.5% compared with 4.4% in the year-ago quarter thanks to higher operating income.

Cash Flow & Liquidity

During the second quarter, NETGEAR generated \$63.2 million of cash from operating activities. As of Jun 28, the company had \$252.6 million in cash and equivalents with \$270.9 million of total current liabilities. It repurchased approximately 315,000 shares in the reported quarter at an average price of \$23.78 per share for \$7.5 million.

2020 Outlook

Due to uncertainties related to the COVID-19 pandemic, NETGEAR has not provided any definitive financial guidance for the third quarter of 2020 and full-year 2020. The company witnessed a significant shift in its business operations and predicts supply-chain disruptions due to the ongoing pandemic situation. Although the channel inventory levels have depleted in the second quarter, the company witnessed a significant development in Wi-Fi 6 offerings with a strong online presence. As channel partners migrate to efficient operating structures, the company is witnessing a change in demand from retail to online platforms. With a sturdy growth potential, the company continues to have accretive subscriber base and solid product demand owing to a rise in work-from-home trend. Backed by a robust liquidity position, NETGEAR is poised to witness recurring top-line growth.

Moving Forward

NETGEAR is confident that it will maintain its leadership in new product introduction, based on the Wi-Fi 6 standards. The company witnessed higher shipments of 5G mobile hotspots and launched two new PoE+ switches. It aims to emerge as a pioneer of best-in-class networking technologies like WiFi 6 and Pro AV, thereby benefiting from advanced technological innovations. In order to ramp up the availability of its products, the company is committed to help customers with superior performance and emerge as the biggest contributor in these crucial times. NETGEAR intends to capitalize on technology inflections, create new categories, build recurring service revenues and boost its paid subscriber base to drive the momentum in 2020.

Quarter Ending 06/2020

Report Date	Jul 22, 2020
Sales Surprise	16.90%
EPS Surprise	134.78%
Quarterly EPS	0.54
Annual EPS (TTM)	1.74

Recent News

On Jul 14, 2020, NETGEAR announced the launch of two 16-port Gigabit Ethernet PoE+ Smart Managed Pro Switches — GS716TP and GS716TPP — to reinforce widespread adoption of advanced connectivity solutions. These innovative devices support small and medium-sized organizations with best-in-class features and performance. Specifically designed for converged networks, these PoE+ Smart Managed Pro Switches enable network segregation with advanced configuration and control.

On Jun 30, NETGEAR announced the launch of the new entrant, Orbi WiFi 6 AX4200 Tri-band Mesh Systems (RBK752/753), following the enormous success from Orbi WiFi 6 AX6000 Tri-band Mesh System (RBK852). The newest addition to the Orbi Mesh System comes with a two and three pack router and satellite system that offers consistent WiFi coverage to large-sized homes spanning over an area of up to 5,000 square feet. This is likely to make the Orbi technology more accessible to a broader spectrum of audience by catering to the WiFi needs of almost every household.

Valuation

NETGEAR shares are down 4.5% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 16.9% over the past year, but stocks in the Zacks Computer and Technology sector are up 27.6% in the same time frame.

The S&P 500 Index is up 9.8% in the past year.

The stock is currently trading at 18.5X trailing 12-month EV/EBITDA, which compares to 9.52X for the Zacks sub-industry, 13.3X for the Zacks sector and 12.19X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 20.24X and as low as 3.51X, with a 5-year median of 8.67X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$33 price target reflects 21.15X trailing 12-month book value.

The table below shows summary valuation data for NTGR

Valuation Multiples - NTGR					
		Stock	Sub-Industry	Sector	S&P 500
EV/EBITDA TTM	Current	18.5	9.52	13.3	12.19
	5-Year High	20.24	13.94	13.35	12.86
	5-Year Low	3.51	4.87	7.59	8.25
	5-Year Median	8.67	7.29	10.88	10.88
P/B TTM	Current	1.56	5.11	6.1	4.49
	5-Year High	3.27	6.16	6.12	4.56
	5-Year Low	0.76	1.84	3.16	2.83
	5-Year Median	1.88	2.93	4.39	3.71
P/S F12M	Current	0.93	3.65	4.01	3.62
	5-Year High	1.58	4.3	4.01	3.62
	5-Year Low	0.46	2.36	2.32	2.53
	5-Year Median	1.02	3.33	3.14	3.02

As of 07/23/2020

Industry Analysis Zacks Industry Rank: Top 37% (92 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Allot Communications Ltd. (ALLT)	Neutral	3
Cisco Systems, Inc. (CSCO)	Neutral	2
Digi International Inc. (DGII)	Neutral	3
Extreme Networks, Inc. (EXTR)	Neutral	3
Infinera Corporation (INFN)	Neutral	3
Lantronix, Inc. (LTRX)	Neutral	3
NetScout Systems, Inc. (NTCT)	Neutral	3
Radcom Ltd. (RDCM)	Neutral	3

Industry Comparison Industry: Computer - Networking				Industry Peers		
	NTGR	X Industry	S&P 500	EXTR	INFN	NTCT
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	C	-	-	B	F	C
Market Cap	935.23 M	122.42 M	22.58 B	555.37 M	1.46 B	1.99 B
# of Analysts	4	3	14	3	7	2
Dividend Yield	0.00%	0.00%	1.81%	0.00%	0.00%	0.00%
Value Score	C	-	-	B	F	C
Cash/Price	0.25	0.17	0.06	0.37	0.22	0.19
EV/EBITDA	15.38	15.34	13.13	20.52	-8.28	15.29
PEG Ratio	NA	3.18	3.04	NA	NA	3.18
Price/Book (P/B)	1.54	1.71	3.15	33.38	3.95	1.02
Price/Cash Flow (P/CF)	21.20	10.32	12.33	7.99	NA	10.32
P/E (F1)	21.98	22.35	22.09	24.32	NA	15.91
Price/Sales (P/S)	0.91	1.72	2.41	0.56	1.09	2.23
Earnings Yield	4.47%	4.11%	4.30%	4.11%	-5.64%	6.28%
Debt/Equity	0.05	0.14	0.76	27.66	1.58	0.27
Cash Flow (\$/share)	1.50	0.39	7.01	0.58	-0.06	2.61
Growth Score	B	-	-	B	D	C
Hist. EPS Growth (3-5 yrs)	-16.21%	-6.10%	10.82%	-10.04%	NA	-16.21%
Proj. EPS Growth (F1/F0)	-23.93%	11.54%	-9.01%	714.30%	26.91%	7.64%
Curr. Cash Flow Growth	102.04%	23.87%	5.47%	-31.93%	-196.51%	-4.98%
Hist. Cash Flow Growth (3-5 yrs)	-24.73%	17.48%	8.55%	5.33%	NA	15.50%
Current Ratio	2.66	2.21	1.31	1.06	1.68	1.65
Debt/Capital	4.38%	15.67%	44.41%	96.51%	61.26%	21.18%
Net Margin	1.35%	-1.67%	10.46%	-12.46%	-27.26%	-0.31%
Return on Equity	2.29%	2.46%	15.13%	-25.79%	-37.47%	3.83%
Sales/Assets	1.11	0.89	0.54	1.04	0.85	0.29
Proj. Sales Growth (F1/F0)	0.12%	0.00%	-2.06%	-3.60%	3.09%	0.77%
Momentum Score	C	-	-	F	F	D
Daily Price Chg	6.79%	0.00%	-0.20%	0.22%	2.90%	-0.11%
1 Week Price Chg	17.10%	4.07%	3.82%	9.96%	4.07%	7.17%
4 Week Price Chg	28.44%	8.45%	6.02%	8.45%	32.65%	9.98%
12 Week Price Chg	32.57%	21.96%	10.03%	35.88%	26.52%	1.55%
52 Week Price Chg	-4.45%	3.70%	-2.89%	-34.56%	113.70%	3.70%
20 Day Average Volume	452,411	19,387	2,026,477	986,495	3,070,940	384,488
(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%	0.15%	-22.22%	-1.13%	0.00%
(F1) EPS Est 12 week change	0.00%	-2.46%	-3.24%	NA	-50.00%	-4.92%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	NA	-0.39%	0.00%

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	C

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.

Disclosures

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ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

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