

Semtech Corporation (SMTC)

\$26.99 (As of 03/16/20)

Price Target (6-12 Months): **\$23.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 03/11/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:F

Value: F

Growth: D

Momentum: F

Summary

Semtech reported decent fiscal fourth-quarter results on diversification strategy. However, the company continues to be negatively impacted by mounting competition in the semiconductor space and slowing demand in China. The resultant pricing pressure continues to affect its margins and profitability. Moreover, seasonality in the consumer segment is a matter of concern. Nonetheless, Semtech's strong performance in industrial and communications markets continues to drive top-line growth. Additionally, product differentiation, operational flexibility, and a specific focus on fast-growing segments and regions continue to be its key growth drivers. However, the stock has underperformed the industry it belongs to in the past year.

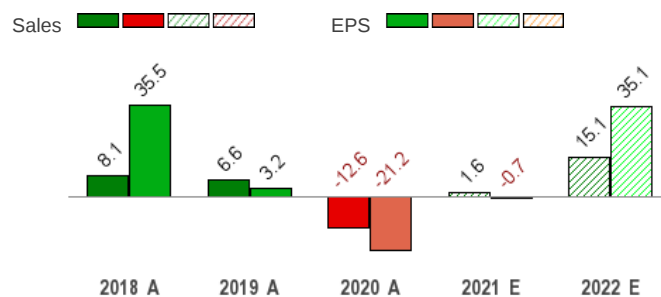
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$56.13 - \$26.03
20 Day Average Volume (sh)	795,076
Market Cap	\$1.8 B
YTD Price Change	-49.0%
Beta	1.94
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Semiconductor - Analog and Mixed
Zacks Industry Rank	Bottom 24% (192 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	14.3%
Last Sales Surprise	2.6%
EPS F1 Est- 4 week change	-26.9%
Expected Report Date	06/03/2020
Earnings ESP	0.0%
P/E TTM	17.6
P/E F1	17.9
PEG F1	1.5
P/S TTM	3.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	151 E	157 E	165 E	161 E	641 E
2021	129 E	136 E	145 E	147 E	557 E
2020	131 A	137 A	141 A	138 A	548 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	\$0.45 E	\$0.50 E	\$0.54 E	\$0.51 E	\$2.04 E
2021	\$0.31 E	\$0.36 E	\$0.42 E	\$0.43 E	\$1.51 E
2020	\$0.34 A	\$0.38 A	\$0.41 A	\$0.40 A	\$1.52 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 03/16/2020. The reports text is as of 03/17/2020.

Overview

Headquartered in Flynn Road Camarillo, CA, Semtech Corporation designs, manufactures and markets a wide range of analog and mixed-signal semiconductors for commercial applications.

The product line comprises Signal Integrity Products, Protection Products, Power and High-Reliability Products, Wireless and Sensing Products, and Systems Innovation Group.

The company's devices are used in a variety of applications including computer, communications, industrial, military-aerospace and automotive. The company also provides a limited amount of wafer foundry services to other electronic component manufacturers.

Semtech has manufacturing facilities in Irvine, Camarillo and San Diego in California, Reynosa in Mexico and Neuchâtel in Switzerland.

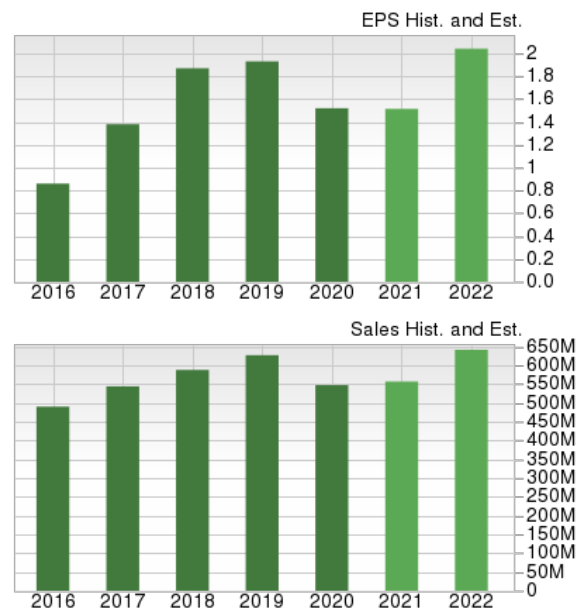
In fiscal 2020, the company generated \$547.5 billion in revenues, which was derived from four end markets—Enterprise Computing (31% of fiscal 2020 revenue), Industrial and Other (26%), High-End Consumer (26%), Communications (18%).

In Enterprise Computing market, the company caters to the demand for products needed in data centers, monitors, desktops, notebook, passive optical networks, servers and other computer peripherals.

In Communications market, Semtech takes care of the needs of wireless LAN, base stations, cable modems, optical networks, carrier networks, switches and routers. It also caters to the demand for equipment required in other communication infrastructures.

The company serves the requirements needed in tablets, wearables, digital video recorders, handheld products, wireless charging, set-top boxes, smartphones, digital televisions, monitors and displays in high-end Consumer market.

Further, equipment requirements in smart grid, wireless charging, military and aerospace, medical, security systems, automotive, industrial and home automation analog and digital video broadcast equipment, video-over-IP solutions, automated meter reading and Internet of Things are taken care by Semtech in its Industrial end-market.



Reasons To Sell:

- ▼ Semtech's end markets, especially the high-end consumer and industrial, experience **seasonality**. These end markets experience weaker demand in the first and fourth quarters, relative to second and third quarters. The seasonality causes considerable fluctuations in revenues and profits and makes forecasting difficult.
- ▼ Semtech operates in an intensely **competitive market** where its success depends on new product development capacity, capacity to recruit and retain industry experts and marketing efficiency. Some of the major competitors of the company include ON Semiconductor, Texas Instruments, Maxim Integrated Products, Broadcom Limited, Microsemi Corporation, Cypress Semiconductor Corp and Monolithic Power Systems. The market is characterized by lower entry barriers and frequent technological improvements that increase the chances of price competition. Pricing pressure makes Semtech susceptible to reduced sales and lower margins.
- ▼ The nature of business makes Semtech vulnerable to **foreign exchange risk**. A significant part of the company's assets exist in non-U.S. dollar-denominated currencies such as the Swiss franc, euro, British pound sterling, Canadian dollars, Mexican peso and Japanese yen. Thus, appreciation or depreciation of the U.S. dollar versus these foreign currencies could impact the company's financial results.

Major headwinds for Semtech are seasonality, a competitive market and foreign exchange risk.

Risks

- Semtech has a **specific focus on fast-growing segments and regions**. The company has been targeting analog/mixed signal sub-segments of some of the most potential and fast growing end markets. The enterprise computing, industrial, communications and high-end consumer markets are characterized by a number of trends such as increasing bandwidth over high-speed networks, growing need for more efficient energy management in home and industrial settings, increasing electronic system requirements for mobile devices, rising demand for Internet connectivity to low power sensors and propagation of green standards. All these trends are driving demand for Semtech's products.
 - Semtech **acquired AptoVision**, a privately held company that provides algorithms for transporting video over Internet protocol (IP). The acquisition is expected to strengthen Semtech's position in the video over IP Pro AV space in the long-term. This market is expected to expand significantly over the years to come driven by an increase in video consumption and distribution across a large number of industrial applications including education, transport, medical and retail.
 - The company carries on **product differentiation and price competition** simultaneously. While there is continuous focus on creating new, unique and proprietary products that add performance and value, they are priced competitively. Semtech continues to attain design wins with new and existing customers, which in turn underscores its strong growth potential. Further, outsourcing provides operational flexibility to Semtech. The company outsources the major part of its manufacturing so that it can better focus on designing, developing and marketing functions. The company's primary wafer foundries are located in the U.S. China and Israel. Outsourcing leads to capital efficiency and technological flexibility and at the same time reduces investment risk.
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Last Earnings Report

Semtech Q4 Earnings & Revenues Surpass Estimates

Semtech Corporation's fiscal fourth-quarter 2020 non-GAAP earnings of 40 cents per share surpassed the Zacks Consensus Estimate by 5 cents. However, the reported earnings decreased 2.4% sequentially and 27.3% year over year.

Non-GAAP revenues of \$138 million decreased 2.1% sequentially and 13.8% from the prior-year quarter. The decrease was due to softer demand from industrial and consumer end markets, partially offset by stronger demand from enterprise computing and communications end markets.

Revenues surpassed the Zacks Consensus Estimate by 2.6% and came at the higher end of the guided range of \$130-\$140 million.

Its key growth drivers are product differentiation, operational flexibility, and specific focus on fast-growing segments and regions.

Let's delve into the numbers in detail:

Revenues by End Market

Sales to the enterprise computing end market—which represented 32% of its total revenues—increased on a sequential basis, driven by a strong rebound in PON demand. Also, communications end market increased sequentially, representing 10% of the total revenues.

However, revenues from the industrial market decreased from the prior-year quarter and represented 31% of total net revenues.

Also, sales to the high-end consumer market represented 26% of total revenues and decreased sequentially due to lower smartphone demand. Roughly 18% of high-end consumer revenues were attributable to mobile devices and 8% to other consumer systems.

Revenues by Product Group

Signal Integrity Product Group revenues contributed 43% to total sales. The reported figure increased 1% sequentially. The sequential increase was driven by stronger demand from data center and base station segments.

Revenues from Protection Product Group represented 27% of the total revenues. The figure was down 6% sequentially due to weak smartphone demand.

However, management expects prospects for protection platforms in mobile devices, displays and accessories to remain positive in the near term as 5G smartphones integrate higher performance interfaces and more advanced photography devices.

Revenues from Wireless and Sensing Product Group, which contributed 30% to total revenues, decreased 2% sequentially.

Bookings

Bookings, which accounted for roughly 37% of shipments, decreased on a sequential basis during the quarter. The book-to-bill ratio was above 1.

Margins and Net Income

Non-GAAP gross margin was 61.5%, down 10 basis points (bps) sequentially and 60 bps from the year-ago quarter.

Semtech's adjusted selling, general and administrative expenses increased 4.6% year over year to \$29.8 million. However, product development and engineering expenses decreased 1% from the year-ago quarter to \$24.1 million.

As a result, its operating margin of 22.5% was down 150 bps sequentially and 640 bps year over year.

Balance Sheet & Cash Flow

Semtech ended the quarter with cash and cash equivalents of \$293.3 million versus \$283.1 million in the fiscal third quarter. Accounts receivables were \$61.9 million, up from \$61.4 million in the fiscal third quarter. Long-term debt was \$194.7 million, up from \$179.1 million in the fiscal third quarter.

During the quarter, cash flow from operations was \$45.3 million, capital expenditure amounted to \$2.6 million and free cash flow totaled \$42.6 million.

During the quarter, the company repurchased 0.5 million shares for \$27.6 million.

Guidance

For fiscal first-quarter 2021, management expects revenues in the range of \$125-\$135 million.

Non-GAAP gross profit margin is expected within 61-62%. Management projects SG&A expenses within \$28-\$29 million, and research and development costs in the range of \$24-\$25 million. Non-GAAP earnings per share are expected in the range of 30-36 cents.

Quarter Ending 01/2020

Report Date	Mar 11, 2020
Sales Surprise	2.56%
EPS Surprise	14.29%
Quarterly EPS	0.40
Annual EPS (TTM)	1.53

Recent News

On **Nov 14, 2019**, Semtech rolled out new BlueRiver audio visual processor (AVP) chipset which enables a new generation of lower cost peripherals and integration directly into end-products. Further, the new chipset is capable of driving growth of SDVoE-enabled products.

Valuation

Semtech shares are down 44% in the past six-month period and 50.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are down 30.6% and 15.6% in the past six-month period, respectively. Over the past year, the Zacks sub-industry and the sector are down 23.7% and 12.3%, respectively.

The S&P 500 index is down 20.3% in the past six-month period and 16.6% in the past year.

The stock is currently trading at 16.5X forward 12-month earnings, which compares to 17.16X for the Zacks sub-industry, 18.62X for the Zacks sector and 15.84X for the S&P 500 index.

Over the past five years, the stock has traded as high as 53.62X and as low as 12.91X, with a 5-year median of 25.4X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$23 price target reflects 14.02X forward 12-month earnings.

The table below shows summary valuation data for SMTC

Valuation Multiples - SMTC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	16.5	17.12	18.45	15.72
	5-Year High	53.62	22.8	22.01	19.34
	5-Year Low	12.91	13.42	16.85	15.18
	5-Year Median	25.4	18.12	19.3	17.42
P/S F 12M	Current	3.01	3.55	3.06	2.9
	5-Year High	6.34	4.52	3.58	3.43
	5-Year Low	1.9	2.81	2.3	2.54
	5-Year Median	3.71	3.69	3.06	3
EV/EBITDA TTM	Current	13.27	9.86	10.46	10.05
	5-Year High	26.53	14.57	12.84	12.88
	5-Year Low	6.8	8.18	7.6	8.31
	5-Year Median	15.43	11.75	10.6	10.79

As of 03/16/2020

Industry Analysis Zacks Industry Rank: Bottom 24% (192 out of 253)



Top Peers

Analog Devices, Inc. (ADI)	Neutral
Broadcom Inc. (AVGO)	Neutral
Cypress Semiconductor Corporation (CY)	Neutral
Monolithic Power Systems, Inc. (MPWR)	Neutral
MACOM Technology Solutions Holdings, Inc. (MTSI)	Neutral
Maxim Integrated Products, Inc. (MXIM)	Neutral
Texas Instruments Incorporated (TXN)	Neutral
ON Semiconductor Corporation (ON)	Underperform

Industry Comparison Industry: Semiconductor - Analog And Mixed				Industry Peers		
	SMTC Underperform	X Industry	S&P 500	ADI Neutral	MTSI Neutral	TXN Neutral
VGM Score	F	-	-	F	B	D
Market Cap	1.79 B	4.07 B	16.36 B	30.64 B	1.13 B	87.33 B
# of Analysts	7	8.5	13	12	7	12
Dividend Yield	0.00%	0.00%	2.63%	2.98%	0.00%	3.85%
Value Score	F	-	-	D	D	D
Cash/Price	0.13	0.13	0.06	0.02	0.16	0.05
EV/EBITDA	13.79	13.04	10.54	13.75	-5.75	12.56
PEG Ratio	1.53	1.29	1.46	1.42	NA	1.98
Price/Book (P/B)	2.64	2.64	2.26	2.62	3.86	9.81
Price/Cash Flow (P/CF)	22.89	12.98	8.80	11.21	16.56	14.41
P/E (F1)	18.40	17.72	13.18	17.62	36.83	18.51
Price/Sales (P/S)	3.27	2.90	1.78	5.33	2.42	6.07
Earnings Yield	5.59%	5.63%	7.56%	5.67%	2.69%	5.40%
Debt/Equity	0.29	0.55	0.70	0.41	2.33	0.60
Cash Flow (\$/share)	1.18	2.91	7.01	7.42	1.03	6.49
Growth Score	D	-	-	D	A	B
Hist. EPS Growth (3-5 yrs)	11.89%	13.72%	10.85%	19.53%	-41.02%	20.28%
Proj. EPS Growth (F1/F0)	-0.38%	-1.37%	5.72%	-8.32%	260.10%	-3.63%
Curr. Cash Flow Growth	-44.69%	-12.47%	6.15%	-9.88%	-30.98%	-4.66%
Hist. Cash Flow Growth (3-5 yrs)	-10.07%	22.53%	8.55%	24.75%	-8.89%	8.82%
Current Ratio	4.67	2.78	1.24	1.08	4.34	4.13
Debt/Capital	22.35%	36.52%	42.57%	28.87%	69.99%	37.32%
Net Margin	7.16%	3.29%	11.64%	21.06%	-83.56%	34.83%
Return on Equity	9.30%	12.19%	16.74%	15.38%	-15.36%	56.21%
Sales/Assets	0.52	0.48	0.54	0.27	0.39	0.81
Proj. Sales Growth (F1/F0)	1.75%	1.64%	3.50%	-6.24%	1.53%	-1.27%
Momentum Score	F	-	-	D	B	D
Daily Price Chg	-22.91%	-16.27%	-12.67%	-16.62%	-13.20%	-11.83%
1 Week Price Chg	-7.31%	-12.91%	-11.01%	-6.74%	-17.95%	-6.29%
4 Week Price Chg	-46.47%	-41.85%	-32.63%	-29.27%	-42.29%	-29.28%
12 Week Price Chg	-48.16%	-37.31%	-30.17%	-30.18%	-37.36%	-27.27%
52 Week Price Chg	-50.36%	-17.09%	-23.26%	-23.77%	-10.38%	-14.85%
20 Day Average Volume	795,076	948,753	3,457,426	4,176,163	584,272	7,939,034
(F1) EPS Est 1 week change	-16.08%	-0.17%	0.00%	-0.42%	0.00%	-0.49%
(F1) EPS Est 4 week change	-26.88%	-1.95%	-0.48%	-1.13%	0.00%	-1.09%
(F1) EPS Est 12 week change	-26.88%	-5.41%	-0.93%	-1.25%	NA	1.37%
(Q1) EPS Est Mthly Chg	-22.73%	-8.77%	-0.60%	-3.55%	0.00%	-1.97%

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	F
Growth Score	D
Momentum Score	F
VGM Score	F

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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