

## ARM Holdings

Price 964.00p

Q1 results with no surprises, FY16 guidance in line with Street's expectations

Fair Value 1340p (+39%)

BUY

Bloomberg	ARM.LN
Reuters	ARM.L
12-month High / Low (p)	1,201 / 848.5
Market Cap (GBPm)	13,577
Ev (BG Estimates) (GBPm)	12,591
Avg. 6m daily volume (000)	3,552
3y EPS CAGR	15.5%

	1 M	3 M	6 M	31/12/15
Absolute perf.	-4.6%	0.0%	-1.2%	-7.2%
Semiconductors	-0.1%	9.9%	2.6%	-2.6%
DJ Stoxx 600	2.2%	4.9%	-4.1%	-4.5%

YEnd Dec. (GBPm)	2015	2016e	2017e	2018e
Sales	968.3	1,170	1,301	1,448
% change		20.8%	11.2%	11.3%
EBITDA	542	648	734	829
EBIT	499.8	593.2	673.9	761.6
% change		18.7%	13.6%	13.0%
Net income	429.0	510.0	584.9	659.7
% change		18.9%	14.7%	12.8%

	2015	2016e	2017e	2018e
Operating margin	51.6	50.7	51.8	52.6
Net margin	44.3	43.6	45.0	45.6
ROE	18.9	18.6	18.5	17.8
ROCE	34.9	40.8	46.9	52.7
Gearing	-36.0	-45.8	-53.8	-60.7

(p)	2015	2016e	2017e	2018e
EPS	30.20	35.99	41.27	46.55
% change	-	19.2%	14.7%	12.8%
P/E	31.9x	26.8x	23.4x	20.7x
FCF yield (%)	0.0%	0.0%	0.0%	0.0%
Dividends (p)	7.60	11.24	13.94	14.49
Div yield (%)	0.8%	1.2%	1.4%	1.5%
EV/Sales	13.4x	10.8x	9.4x	8.1x
EV/EBITDA	23.9x	19.4x	16.6x	14.2x
EV/EBIT	25.9x	21.2x	18.1x	15.4x

ARM Holdings has reported Q1 2016 results in line with consensus expectations and company guidance. Q1 sales came in at USD398m or GBP276m, up 2.6% sequentially, with normalised operating margin at 49%, and EPS at 8.2p. This was broadly in line with the consensus forecast for sales of GBP271m and adjusted EPS at 8.1p. The group also added a comment on FY16 sales, which are expected to be in line with the current street figure at USD1,615m, up +9%. Note that ARM again proved its resilience to the slowing smartphone market thanks to its growing diversification.

## ANALYSIS

- While Q1 top-line growth was in line with expectations, EPS was above forecasts.** The company reported Q1 revenues of USD398m, or GBP276m up +2.6% seq. (+21.3% yoy), 2% above consensus expectations. Gross margin came in at 96.7%, flat compared to Q4 (at 96.5%), and operating expenses came out at GBP133m (up from GBP124m in Q4-15). As a result, normalised EBIT was 4% above the consensus figure at GBP134m (cons. GBP129m/BG ests. GBP136m), and EPS was also 2% above at 8.2p (cons. 8.07p / BG ests. 8.28p). Normalised cash generation stood at GBP81m in Q1-16, down from GBP112m in Q4-15. As a result, the net cash position at the end of Q1-16 was GBP1,006m compared with GBP951m at the end of Q4-15.
- Licencing sales grew by +11% seq. in dollar terms in Q1 and royalties by +17%.** Q1 licencing revenues accounted for USD148m of which USD135m from the processors business and USD13m from the physical IP activity. Overall, the royalties business was the most dynamic with sequential growth of +17% seq. in dollar term. Royalties revenues grew to USD216m, of which USD192m from the processors business and USD24m from physical IP. Software & tools and services revenues came out at USD20m and USD14m respectively, compared with USD17m and USD15m achieved in Q4.
- FY16 sales expected to be in line with Street's expectations.** Despite the cautious message regarding current economic conditions that could possibly lead customers to lower spending and impact the entire semiconductors industry, the group is nevertheless guiding on FY16 revenue in line with current Street's expectations in dollar terms, i.e. at a level close to USD1,615m (BG ests. FY16 sales at USD1,662m, up +12%). Over FY16, we believe that the group should strongly benefit from a positive move of USD/GBP exchange rate. This should also help to boost GBP revenue.
- Taking benefit from diversification.** While many expected to see disappointing figures due to a slowdown in the smartphone market, we note that ARM again proved its resilience thanks to a growing diversification. Many highlighted the risk of a slowdown in licence revenues but the group continued to benefit from the emergence of IoT which is said to drive upward the number of licensees while more companies need access to ARM technologies. While IoT chips come with a lower average selling price, they should also help generate incremental royalties revenue in the future.

## VALUATION

- We are making no change to our estimates at this point and will wait for further details from today's conference call (see details below).
- Based on our estimates, ARM's shares are trading on 2016e P/E of 26.8x, well below its 5y historical average of 39.3x.

## NEXT CATALYSTS

- Today: Q1 results conference call (10:30am CET, +44 (1) 452 555 566, ID: 82498894).
- 28th April 2016: Annual General Meeting.
- 27th July 2016: Q2 results



### Actual Q1-16 vs. Consensus

[GBPm]	BG ests. 1Q16	Consensus 1Q16	1Q16 Actual	Actual vs. Cons.
Net revenue	269	271	276	1.8%
% change (seq)	+0.0%	+0.7%	+2.6%	186bp
% change (yoy)	+18.3%	+19.1%	+21.3%	220bp
Gross Margin	96.2%	96.1%	96.7%	
Adj. EBIT	136	129	134	4.2%
% of revenue	50.7%	47.6%	48.7%	
Dil. EPS (in p.)	8.28	8.07	8.20	1.6%

Sources: Thomson Reuters I.B.E.S.; Bryan Garnier & Co. ests.

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